立法會
Legislative Council

LC Paper No. CB(1)1270/13-14
(These minutes have been seen by the Administration)

Ref : CB1/BC/3/13

Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2013

Second meeting on
Monday, 24 February 2014, at 10:45 am
in Conference Room 2A of the Legislative Council Complex

Members present	**:**	Hon WONG Ting-kwong, SBS, JP (Chairman) Hon James TO Kun-sun Hon CHAN Kam-lam, SBS, JP Hon Andrew LEUNG Kwan-yuen, GBS, JP Hon Starry LEE Wai-king, JP Hon CHAN Kin-por, BBS, JP Hon Alan LEONG Kah-kit, SC Hon Charles Peter MOK Hon Kenneth LEUNG Hon SIN Chung-kai, SBS, JP
Public officers attending	**:**	Mr Eddie CHEUNG Deputy Secretary for Financial Services and the Treasury (Financial Services) 2 Mr CHIU Kwok-kit, JP Deputy Commissioner of Inland Revenue (Technical) Ms Polly LUI Acting Assistant Commissioner of Insurance (Policy and Development) Miss Lily CHAN Senior Insurance Officer (Policy and Development)

Mr Manuel NG
Acting Senior Government Counsel
Department of Justice

Clerk in attendance : Ms Connie SZETO
Chief Council Secretary (1)4

Staff in attendance : Mr Timothy TSO
Assistant Legal Adviser 2

Ms Angel SHEK
Senior Council Secretary (1)4

Action

I Meeting with the Administration

Follow-up to issues arising from previous meeting

(LC Paper No. CB(1)905/13-14(01)	—	List of follow-up actions arising from the discussion at the meeting on 28 January 2014
LC Paper No. CB(1)905/13-14(02)	—	Administration's written response to the issues arising from the discussion at the meeting held on 28 January 2014)

Other relevant papers

(LC Paper No. CB(3)291/13-14	—	The Bill
LC Paper No. CB(1)790/13-14(01)	—	Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to Members)
File Ref: L/M (19) in G6/90/4C (2011) Pt. 5	—	Legislative Council Brief
LC Paper No. LS22/13-14	—	Legal Service Division Report

LC Paper No. CB(1)790/13-14(02) — Background brief on Inland Revenue (Amendment) (No. 3) Bill 2013 prepared by the Legislative Council Secretariat)

Discussion

The Bills Committee deliberated (Index of proceedings attached at **Appendix**).

Follow-up actions to be taken by the Administration

2. In response to members' enquiries at the meeting, the Administration agreed to provide the following information –

(a) the number of Mainland enterprises which had formed captive insurers to enhance their risk management, and the estimated number of Mainland enterprises which would be attracted to set up captive insurers in Hong Kong as a result of the proposed tax concession; and

(b) details of the regulatory regime and measures to assess and monitor market risks of the local captive insurance industry, in particular the measures to mitigate risks arising from insolvency of captive insurers.

(*Post-meeting note*: The Administration's written response was issued to members on 27 February 2014 vide LC Paper No. CB(1)1009/13-14(02).)

II Any other business

Way forward

3. The Chairman concluded that the Bills Committee had completed scrutiny of the Bill. The Administration would provide supplementary information on issues arising from the discussions at the meeting.

4. Members supported the Administration's proposal to resume the Second Reading debate on the Bill at the Council meeting of 19 March 2014. Both the Bills Committee and the Administration would not propose Committee Stage amendments to the Bill. The Chairman said that he would give a verbal report on the Bills Committee's deliberations to the House Committee at its meeting on 28 February 2014.

5. There being no other business, the meeting ended at 11:46 am.

Council Business Division 1
Legislative Council Secretariat
16 April 2014

Appendix

Proceedings of the
Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2013
Second meeting on Monday, 24 February 2014, at 10:45 am
in Conference Room 2A of the Legislative Council Complex

Time Marker	Speaker	Subject(s)	Action Required
000101 – 000222	Chairman	Introductory remarks	
000223 – 000701	Administration	Briefing by the Administration on its written response to the issues arising from the discussions at the meeting held on 28 January 2014 (LC Paper No. CB(1)905/13-14(02))	
000702 – 001756	Mr James TO Administration Chairman	Mr TO enquired about – (a) the Administration's considerations for maintaining the current proposal to reduce the profits tax of the business of insurance of offshore risks of captive insurers to one half of the normal tax rate for corporations (which was currently at 16.5%) notwithstanding the greater tax concessions granted by some other jurisdictions; and (b) the estimated amount of tax revenue forgone as a result of the proposed tax concession. The Chairman considered that it would be difficult to assess the impact of the proposal on the tax revenue as the Administration could not estimate accurately at this stage the number of enterprises to be attracted to form captive insurers in Hong Kong. The Administration advised that – (a) the proposal was meant to extend the current profits tax concession (i.e. one-half of the normal corporation tax rate of 16.5%) provided to reinsurers' business of offshore risks to captive insurers. The Administration would keep in view market developments in considering whether further measures were necessary in future; and	

Time Marker	Speaker	Subject(s)	Action Required
		(b) due to the small base of only two captive insurers currently domiciled in Hong Kong, it was difficult to project at this stage the growth in the number of captive insurers in Hong Kong or the amount of tax revenue forgone. Mr TO enquired about how a captive insurer's insurance business of "offshore risks" could be distinguished from those of "onshore risks" technically (e.g. in common law, case law, practice notes issued by the Inland Revenue Department ("IRD"), relevant insurance policies) in view of the term "offshore risks" not being legally defined. The Administration advised that – (a) whether an insured risk was located outside Hong Kong (i.e. offshore risks) was a question of fact to be decided on a case by case basis. In general, if the contract of insurance was made in Hong Kong or the proposals of the contract of insurance were made to a corporation in Hong Kong, the premiums arising from the contract of insurance would be regarded as premiums from insurance business in Hong Kong and therefore chargeable to tax. If these premiums were related to "offshore risks", the proposed concessionary tax rate would apply; and (b) "offshore risks" was already a concept used in granting the existing profits tax concession for reinsurers' business of offshore risks. So far, IRD had not encountered any problem in the assessment of profits tax on "premiums from reinsurance of offshore risks". In reply to the Chairman, the Administration advised that the concept of "offshore risks" pertaining to reinsurance business and captive insurance business was essentially the same.	

Time Marker	Speaker	Subject(s)	Action Required
001757 – 002700	Mr SIN Chung-kai Ms Starry LEE Chairman Administration	Mr SIN and Ms LEE enquired about – (a) the criteria for granting the proposed profits tax concession in respect of captive insurance business, and not other businesses which had also sought tax concessions in the past; (b) measures to attract enterprises to set up captive insurers in Hong Kong; and (c) the projected growth in the number of captive insurers domiciled in Hong Kong as a result of the proposed tax concession. The Administration advised that – (a) the proposal was a positive response to the insurance industry's suggestion raised since 2009 that Hong Kong should consider offering tax concessions to attract enterprises to choose Hong Kong as the domicile for captive insurers, given Hong Kong's edges of a sound legal system, robust regulatory regime, a simple and transparent tax system, the tax incentives currently offered by some other jurisdictions, as well as the potential market in Asia where captive insurance was still novel to many enterprises. In particular, with its proximate location to the Mainland, Hong Kong would benefit from the anticipated growth in the use of captive insurance by Mainland enterprises. Similar tax concession was accorded to reinsurance business of offshore risks; (b) apart from the proposed tax concession, regulatory concessions were granted to captive insurers (e.g. lower capital requirements and fees). Concerted efforts from the Administration and the Hong Kong Federation of Insurers ("HKFI") were taken to promote Hong Kong as an insurance hub and to attract enterprises to set up captive insurers in Hong Kong. For instance, a workshop on captive insurance was jointly organized by the Administration and	

Time Marker	Speaker	Subject(s)	Action Required
		HKFI during the Asian Financial Forum 2014. Relevant information was also disseminated to Mainland/foreign enterprises through the Hong Kong Economic and Trade Offices. Moreover, the Administration also promoted Hong Kong as a domicile of captive insurers to large Mainland enterprises in 2013. Further incentives for developing captive insurance would be considered in future in the light of industry's feedback and developments in other jurisdictions; and (c) since announcement of the proposed tax incentive in the 2013-2014 Budget, the Insurance Authority ("IA") had received about ten enquiries concerning the establishment of captive insurers in Hong Kong.	
002701 – 003546	Chairman Mr Kenneth LEUNG Mr CHAN Kin-por Administration	In response to Mr LEUNG, the Administration advised that there were currently over 6 000 captive insurers established in the world with majority of them domiciled in Bermuda and British Virgin Islands ("BVI"). As regards Singapore, there were about 50 captive insurers at present, mostly set up by enterprises in nearby areas (e.g. New Zealand, Australia and Japan). In view of global concerns about low transparency in the company and trust law regimes of Bermuda and BVI, Mr LEUNG enquired whether the Administration would strategically seek to compete with these jurisdictions as a desirable domicile for captive insurers. Mr CHAN remarked that, compared to Bermuda and BVI, Singapore was a more vigorous competitor to Hong Kong in the development of captive insurance business in the region given Singapore's more attractive profits tax concession for captive insurers. (*Post-meeting note*: As advised by the Administration after the meeting, the prominent domiciles for captive insurers should be Bermuda and Cayman Islands.)	

Time Marker	Speaker	Subject(s)	Action Required
		The Administration advised that – (a) the insurance industry considered Hong Kong had the potential to become an attractive domicile of captive insurers given its advantages of a robust regulatory regime, simple and transparent tax system, and proximity to Mainland cities; and (b) the Administration's intention was not to compete with particular places as a desirable domicile, but to attract enterprises to form captive insurers in Hong Kong to enhance their risk management. At the request of Mr LEUNG, the Administration agreed to provide information on the number of Mainland enterprises which had formed captive insurers and the estimated number of Mainland enterprises which would be attracted to set up captive insurers in Hong Kong. Mr CHAN remarked that – (a) while it would be difficult to project the number of Mainland enterprises that would be attracted to form captive insurers in Hong Kong at this stage, the prospect was certainly favourable given the large number of Mainland enterprises that might need to form captive insurers to manage their risks; and (b) as there might be great fluctuation in the assessable income of captive insurers for taxation purpose, it was difficult to assess the potential loss in tax revenue from captive insurers as a result of the proposal.	 The Administration to take action as per paragraph 2(a) of the minutes.
003547 – 004530	Mr SIN Chung-kai Mr James TO Administration Chairman	Mr SIN enquired about the market and regulatory risks arising from the local captive insurance industry, and the measures to assess and monitor such risks. The Chairman considered that, compared to other lines of insurance business (e.g. motor	

Time Marker	Speaker	Subject(s)	Action Required
		third party insurance), the impact on the public arising from the insolvency of a captive insurer would be relatively small because captive insurers underwrote exclusively the risks of its parent/group companies or their associated companies, and such risks did not involve the general public. Mr TO opined that insolvency of captive insurers domiciled in Hong Kong might pose reputational risks to the Government or even responsibility to establish funds to meet the defaulted claims. The Administration advised that – (a) captive insurance was a risk management measure employed by enterprises, and the insured risks could be diversified through reinsurance. A captive insurer could not write life insurance nor other statutory lines of business involving the general public; and (b) captive insurers were subject to IA's prudential supervision, with requirements on capital adequacy to meet the maximum amount of claims borne by the captive insurers. IA monitored captive insurers' compliance and the market risks arising from their business through regular monitoring of their operation and solvency position, etc. At the request of Mr SIN, the Administration agreed to provide supplementary information on the details of Hong Kong's regulatory regime on captive insurers.	 The Administration to take action as per paragraph 2(b) of the minutes.
004531 – 010029	Mr James TO Mr CHAN Kin-por Administration Chairman	Mr TO reiterated the need to provide a definition of "offshore risks" in the Bill and/or IRD's practice notes to facilitate tax assessment. He cautioned that there could be different interpretations and even abuses of the concept arising from, for instance, risk distribution or shifting through insurance/reinsurance agreements, or other legal instruments/arrangements such as mergers.	

Time Marker	Speaker	Subject(s)	Action Required
		The Chairman considered that the arrangements to transfer risks by a captive insurer should have no impact on its liabilities to the policyholder(s). The oversight by IA would ensure prudent supervision of captive insurers' business. Mr CHAN considered that the market risks posed by captive insurers would not be large as they underwrote exclusively the risks of their parent/group companies or their associated companies, and the risk exposure of the captive insurer would be reduced by reinsurance arrangements. Besides, insurance policies underwritten by captive insurers in Hong Kong were subject to IA's authorization. The Administration responded that the concept of "offshore risks" was clear having regard to its established usage in past tax assessments and the "territorial source" principle of taxation. After all, whether an insured risk was located outside Hong Kong remained a question of fact to be decided case-by-case, IRD would monitor the situation and review the need to provide a definition of "offshore risks" in light of operation of the tax concessionary regime.	
010030 – 010230	Chairman Administration	Follow-up arrangements and legislative timetable	

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