

Inland Revenue (Amendment) Bill 2015

The Administration's Responses to Questions Raised by the Legal Adviser of the Legislative Council in the letter of 10 April 2015

This paper sets out the Administration's responses to the questions raised by the Legal Adviser of the Legislative Council in the letter of 10 April 2015.

Clause 4

- (a) Paragraph (b) of the definition of *capital commitment* in the proposed section 20AC(6) (i.e. in respect of which the originator may make capital calls from time to time according to the terms of agreement) means that the originator may make calls from time to time for payment of the capital, which has not been paid or satisfied by an investor, under a capital commitment according to the terms of agreement governing the operation of the fund. We consider it not necessary to define the term "capital calls" as it only carries the literal meaning, i.e., calls or requests for capital, and such calls are invariably governed by the contractual terms laid down in an agreement governing the operation of the fund.
- (b) The definition of 資本認繳 in the proposed section 20AC(6) starts by the introductory words "就某基金而言，指符合以下說明的認繳", which are then followed by the descriptions of the commitment in paragraphs (a) and (b) of the definition. It is therefore not necessary to add the words "認繳" again after "形式的" in paragraph (a) of the definition.

Clause 5

- (a) The inclusive definitions for *trade* and *business* are found in section 2 of the Inland Revenue Ordinance ("IRO"). For the purpose of profits tax, the term "business" carries a wider meaning as compared with the term "trade", and the term "business" covers all forms of "trade". Carrying on business usually calls for some activities on the part of whoever carries it on, although depending on the nature of the business, the activities may be intermittent with long intervals of quiescence

in between (e.g. the holding of a property by a company to collect an annual rent is business but not trade). See *American Leaf Blending Co Sdn Bhd v Director-General of Inland Revenue* 1979 AC 676 at 684D. Insofar as trading is concerned, the concept connotes an active occupation with frequent transactions, short period of ownership, supplementary work to enhance value of goods and profits motive, etc. Therefore, we consider it not necessary to add the word “trade” after “business”.

- (b) Under the Inland Revenue (Amendment) Bill 2015 (“the Bill”), to qualify for tax exemption, one of the conditions that an offshore private equity fund has to meet is that a portfolio company held by it should be a private company incorporated outside Hong Kong (i.e. an *excepted private company*). Therefore, it is necessary for the term *private company* to cover companies incorporated outside Hong Kong to reflect our policy intention.

The definition of *private company* under section 11 of the Companies Ordinance (Cap. 622) may not be applicable to companies incorporated outside Hong Kong, as the companies legislation in the overseas jurisdictions may not adopt the same meaning for a private company. If we provide in the definition of *private company* that “the prohibition is imposed by and contained in the articles of association of the company or otherwise of the Companies Ordinance”, this may render some private companies incorporated outside Hong Kong not eligible for tax exemption. Indeed, this point has been raised by the industry during consultation and the current definition has taken into account the industry’s views.

- (c) As explained in (a) above, trading as a concept connotes an active occupation with frequent transactions, short period of ownership, supplementary work to enhance value of goods and profits motive, etc.

Under the proposed section 20ACA(2), a special purpose vehicle means a corporation, partnership, trustee of a trust estate or any other entity, inter alia, that does not carry on any trade or activities except for the purpose of holding, directly or indirectly, and administering one or more excepted private companies. The use of the word “trade” is appropriate in this context to reflect

our policy intention that the special purpose vehicle should not engage in active occupation with frequent transactions, but should only hold or administer the excepted private companies.

- (d)(i) The term “activities” used in the proposed section 20ACB is generic and cover “business activities” and “trading activities”, though the activities themselves might not constitute the “business” or “trade” itself. In general, conduct having the character or essence of a business or trade would involve capital, dealings with other persons, plant and machinery, etc. We consider adding the word “trade” or “business” in front of “activities” would not bring in further clarity.
- (ii) It is our policy intention that a “permanent establishment” covers a fixed place of business through which activities of the company are wholly or partly carried on. As this is a threshold commonly used in taxation to decide whether a non-resident should be subject to taxation in the source jurisdiction (i.e. the jurisdiction from which the profit is derived or sourced), we consider the provision in the present form sufficiently clear.
- (iii) Under the proposed section 20ACB(1), for a private company, a permanent establishment is a fixed place of business through which activities of the company are carried on (including a branch and a place of management), and the word “including” does not preclude the determination of any other place of business (e.g. an office, a factory, a workshop) being a permanent establishment. Subsections (1) and (2) of the proposed section 20ACB together provide how a permanent establishment is to be determined. The description “place of management” refers to a place where a business or trade is being managed. While an office, a factory or a workshop are normally a fixed place of business, they may not necessarily be a place where the business or trade is being managed.

The Inland Revenue Department will provide in more detail, if necessary, its interpretation of the definition in the Departmental Interpretation and Practice Notes.

- (e) In formulating the meaning of “permanent establishment” in the proposed section 20ACB, we have made reference to Article 5 of the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention on Income and

Capital. We consider it appropriate to adopt the term “慣常”, which is the common Chinese translation of “habitually” in double tax treaties.

Clauses 7 and 8

(a)&(b) We amended the IRO in 2006 to provide for profits tax exemption to offshore funds, and the scope of *associate* in relation to the tax exemption regime was defined under section 20AE (i.e. the deeming provision stipulating that a resident person (alone or jointly with his associates) holding a beneficial interest of 30% or more in a tax-exempt offshore fund will be deemed to have derived assessable profits in respect of profits earned by the fund from specified transactions and incidental transactions in Hong Kong.)

Sections 14A and 16EC(8) of the IRO were later amended in 2011, and when compared with the existing definition in section 20AE(10), the scope of *associate* in relation to these two sections was expanded to include the following -

- (i) if it is a natural person, a corporation controlled by a relative of the natural person;
- (ii) if it is a natural person, a corporation controlled by a relative of the partner, who is also a natural person, of the natural person; and
- (iii) if it is a partnership, a corporation controlled by a partnership in which the partnership is partner.

Under the Bill, in amending section 20AE to apply the deeming provision to offshore private equity funds, and adding a similar anti-abused provision in respect of assessable profits of special purpose vehicles, we have aligned the scope of *associate* with the re-defined definitions in sections 14A and 16EC(8). Also, given that offshore private equity funds are generally structured as limited partnership, we consider it appropriate to cover also the following persons in the definition of *associate* –

- (i) if it is a corporation, a partnership in which the corporation is a partner; and

- (ii) if it is a partnership, an “associated partnership” of the partnership.

Clause 8

We consider that there is no difference in meaning and effect between the expressions “某非居港者的實益權益的持有情況屬真正的財產權分散” (in section 28AE(8) of IRO) and “某非居港者的實益權益屬被真正地分散持有” (in the proposed section 28AF(7) of IRO). The latter expression is adopted in the Bill to achieve better language flow and easier comprehension.

Clause 10

The expressions “前者” and “後者” have been widely used in the statutes to facilitate the referencing of particular persons or entities in a provision. **Annex** contains some examples on the use of the expressions.

Financial Services and the Treasury Bureau
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Annex

Chapter:	238	Title:	FIREARMS AND AMMUNITION ORDINANCE	Gazette Number:	L.N. 193 of 2000
Section:	8	Heading:	Possession of arms and ammunition in transit	Version Date:	26/05/2000

(2) Sections 13 and 14 do not apply to the possession of or dealing in arms or ammunition by a person whose possession or dealing is limited to arms or ammunition-

- (a)
- (b) which are brought into Hong Kong on board an aircraft ("the first aircraft") to be transported as cargo to some other place in another aircraft ("the second aircraft"), if-
 - (i) the arms or ammunition are recorded as cargo in the manifest of the first aircraft and the manifest of the second aircraft; and
 - (ii)

章：	238	標題：	《火器及彈藥條例》	憲報編號：	L.N. 193 of 2000
條：	8	條文標題：	對過境槍械及彈藥的 管有	版本日期：	26/05/2000

(2) 如任何人管有或經營的槍械或彈藥只限於下述者，則第13及14條並不適用於該等管有或經營—

- (a)
- (b) 由一架飛機(“前者”)帶進香港，再由另一架飛機(“後者”)運往其他地方的槍械或彈藥，而—
 - (i) 在前者的貨單上及在後者的貨單上，該等槍械或彈藥均記錄為貨物；及
 - (ii)

Chapter:	553	Title:	ELECTRONIC TRANSACTIONS ORDINANCE	Gazette Number:	L.N. 131 of 2004
Section:	6	Heading:	Electronic signatures, digital signatures, etc.	Version Date:	01/07/2004

(1) Where-

- (a) a rule of law requires the signature of a person ("the first mentioned person") on a document or provides for certain consequences if the document is not signed by the first mentioned person; and
- (b) neither the first mentioned person nor the person to whom the signature is to be given ("the second mentioned person") is or is acting on behalf of a government entity,

an electronic signature of the first mentioned person satisfies the requirement if-

- (c) the first mentioned person uses a method to attach the electronic signature to or logically associate the electronic signature with an electronic record for the purpose of identifying himself and indicating his authentication or approval of the information contained in the document in the form of the electronic record;
- (d)
- (e) the second mentioned person consents to the use of the method by the first mentioned person.

章：	553	標題：	《電子交易條例》	憲報編號：	L.N. 131 of 2004
條：	6	條文標題：	電子簽署、數碼簽署等	版本日期：	01/07/2004

(1) 凡一

- (a) 任何法律規則規定須由任何人(“前者”)在某文件簽署，或規定該文件未由前者簽署則會有某些後果；及
- (b) 前者及將會獲提供該簽署的人(“後者”)均既非政府單位亦非代表任何政府單位行事，

則在以下情況下，前者的電子簽署即屬符合該規定一

- (c) 前者使用某方法使該電子簽署與某電子紀錄相連或在邏輯上相聯，以識別自己和顯示自己認證或承認包含於以該電子紀錄形式存在的該文件內的資訊；
- (d)
- (e) 後者同意前者使用該方法。

Chapter:	602	Title:	Race Discrimination Ordinance	Gazette Number:	L.N. 166 of 2009
Section:	27	Heading:	Discrimination in provision of goods, facilities or services	Version Date:	10/07/2009

(1) It is unlawful for any person (“the first-mentioned person”) concerned with the provision (for payment or not) of goods, facilities or services to the public or a section of the public to discriminate against another person (“the second-mentioned person”) who seeks to obtain or use those goods, facilities or services—

- (a) by refusing, or deliberately omitting to provide, the second-mentioned person with any of them; or
- (b) by refusing or deliberately omitting to provide the second-mentioned person with goods, facilities or services of the like quality, in the like manner and on the like terms as are normal in the first-mentioned person’s case in relation to other members of the public or (where the second-mentioned person belongs to a section of the public) to other members of that section

章：	602	標題：	《種族歧視條例》	憲報編號：	L.N. 166 of 2009
條：	27	條文標題：	在提供貨品、設施或服務方面的歧視	版本日期：	10/07/2009

(1) 從事向公眾人士或部分公眾人士提供貨品、設施或服務(不論是否為此而收取款項)的人(“前者”),如藉以下做法歧視任何謀求獲得或使用該等貨品、設施或服務的另一人(“後者”),即屬違法—

- (a) 拒絕向後者提供或故意不向後者提供任何該等貨品、設施或服務;或
- (b) 前者在正常情況下,會按某方式及某些條款向其他公眾人士,或(如後者屬於某部分的公眾人士)向屬該部分的其他公眾人士,提供具有某種品質或質素的貨品、設施或服務,然而前者拒絕按相同方式及相同條款(或故意不按相同方式及相同條款)向後者提供具有相同品質或質素的該等貨品、設施或服務。