

立法會
Legislative Council

LC Paper No. CB(4)756/15-16
(These minutes have been seen
by the Administration)

Ref : CB4/BC/2/15

Bills Committee on Inland Revenue (Amendment) (No. 4) Bill 2015

Minutes of the third meeting
held on Monday, 29 February 2016, at 4:30 pm
in Conference Room 2A of the Legislative Council Complex

Members present : Hon Kenneth LEUNG (Chairman)
Hon CHAN Kam-lam, SBS, JP
Hon Jeffrey LAM Kin-fung, GBS, JP
Hon Andrew LEUNG Kwan-yuen, GBS, JP
Hon WONG Ting-kwong, SBS, JP
Hon Alan LEONG Kah-kit, SC
Hon NG Leung-sing, SBS, JP
Hon Dennis KWOK
Hon Christopher CHEUNG Wah-fung, SBS, JP
Hon SIN Chung-kai, SBS, JP

Public officers attending : Agenda item II

Financial Services and the Treasury Bureau

Mr Jackie LIU
Principal Assistant Secretary (Financial Services)

Ms Jenny LEE
Assistant Secretary (Financial Services)

Miss Tanna CHONG
Assistant Secretary (Financial Services)

Inland Revenue Department

Mr CHIU Kwok-kit, JP
Deputy Commissioner (Technical)

Mr Allen NG Ka-wing
Senior Assessor (Research)

Ms CHAN Shun-mei
Senior Assessor (Special Duties)

Hong Kong Monetary Authority

Miss Kyle HUNG
Senior Manager (Market Development)

Miss Theresa KWAN
Senior Manager (Banking Policy)

Department of Justice

Miss Betty CHEUNG
Senior Assistant Law Draftsman

Mr Peter SZE
Senior Government Counsel

Miss Christine WONG
Government Counsel

Clerk in attendance : Mr Daniel SIN
Chief Council Secretary (4)3

Staff in attendance : Miss Carrie WONG
Assistant Legal Adviser 4

Mr Joey LO
Senior Council Secretary (4)8

I. Confirmation of minutes of meeting

(LC Paper No. CB(4)602/15-16 -- Minutes of meeting held on 12 January 2016

The minutes of the meeting held on 12 January 2016 were confirmed.

II. Meeting with the Administration

Follow-up to issues arising from previous meeting

(LC Paper No. CB(4)647/15-16(01) -- Administration's responses to written submissions

LC Paper No. CB(4)534/15-16(01) -- Summary of major views received during the drafting stage of the Bill and the Government's responses

LC Paper No. CB(4)647/15-16(02) -- Administration's response to Assistant Legal Adviser's letter dated 25 February 2016

LC Paper No. CB(4)534/15-16(02) -- Assistant Legal Adviser's letter dated 25 January 2016 to the Administration

LC Paper No. CB(4)655/15-16(01) -- List of follow-up actions arising from the discussion at the meeting on 26 January 2016

LC Paper No. CB(4)510/15-16(01) -- List of follow-up actions arising from the discussion at the meeting on 12 January 2016

LC Paper No. CB(4)628/15-16(01) -- Submission from Hong Kong Bar Association dated 1 February 2016 (English version only)

Clause-by-clause examination of the Bill

Clause 1 to 27

- LC Paper No. CB(3)206/15-16 -- The Bill
- LC Paper No. CB(4)491/15-16(01) -- Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to members)

Other relevant papers

- File Ref: B&M/2/1/66C -- Legislative Council Brief
- LC Paper No. LS19/15-16 -- Legal Service Division Report
- LC Paper No. CB(1)409/15-16(01) -- Background brief on Inland Revenue (Amendment) (No. 4) Bill 2015 prepared by the Legislative Council Secretariat)

Discussion

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

Clause-by-clause examination of the Bill

3. The Bills Committee had completed clause-by-clause examination of the Bill. Members noted that the Administration proposed to move Committee Stage amendments ("CSAs") to delete the proposed section 17H under Clause 14 which made it clear that the proposed sections 17E and 17G did not prevent the operation of the "arm's length" and "separate enterprise" principles in other circumstances. After passage of the Bill, the Administration would explain that in the Departmental Interpretation and Practice Notes ("DIPNs") to be issued by the Inland Revenue Department.

Follow-up actions

4. The Bills Committee noted that the Administration would propose other CSAs to improve the drafting of the Bill. The Administration would prepare the draft CSAs for consideration by the Bills Committee. The Inland Revenue Department would issue DIPNs shortly after the passage of

the Bill, and forward them to the Joint Liaison Committee on Taxation for reference.

5. The Chairman said that the Administration's proposed CSAs would be circulated to members for consideration. If members considered it necessary, a meeting would be convened at 8:30 am on Monday, 14 March 2016 to discuss the CSAs.

Legislative timetable and date of next meeting

6. The Bills Committee completed scrutiny of the Bill. Members noted that the Clerk would also liaise with the Administration to ascertain when the Administration intended to resume Second Reading debate of the Bill. A written report of the Bill, together with the Administration's proposed CSAs would be submitted to the House Committee.

(Post-meeting note: The Administration's proposed CSAs were circulated to members vide LC Paper No. CB(4)685/15-16(01) on 7 March 2016.)

III. Any other business

7. There being no other business, the meeting closed at 6:30 pm.

Council Business Division 4
Legislative Council Secretariat
22 March 2016

**Proceedings of the third meeting of
Bills Committee on Inland Revenue (Amendment) (No. 4) Bill 2015
on Monday, 29 February 2016, at 4:30 pm
in Conference Room 2A of the Legislative Council Complex**

Time marker	Speaker	Subject(s)	Action required
Agenda item I – Confirmation of minutes of meeting			
000000 – 000237	Chairman Administration	Confirmation of minutes of meeting on 12 January 2016 (LC Paper No. CB(4)602/15-16)	
Agenda item II – Meeting with the Administration			
000238 – 000758	Chairman Administration	Briefing by the Administration (LC Paper No. CB(4)647/15-16(01) and LC Paper No. 647/15-16(02))	
000759 – 000928	Chairman Administration	<p>Submission from Ernst & Young Tax Services Limited on application of the "subject to tax" condition under the proposed section 16(2I) (LC Paper No. CB(4)667/15-16(01))</p> <p>The Administration agreed that, after the passage of the Bill, the Inland Revenue Department ("IRD") would issue Departmental Interpretation and Practice Notes ("DIPNs") to explain the interpretation and application of the "subject to tax" condition.</p>	The Administration to follow up as per paragraph 4 of the minutes
000929 – 001450	Chairman Administration Assistant Legal Adviser 4 ("ALA4")	<p>Clause-by-clause examination of the Bill</p> <p><u>Long Title</u></p> <p>The Chairman's enquiry and the Administration's response on the proposed treatment of regulatory capital securities ("RCS") under the Bill.</p> <p>The Administration advised that, with the proposed new Schedule 9 added to the Stamp Duty Ordinance (Cap. 117), no stamp duty would be levied for transactions involving RCSs.</p> <p>In view of paragraph 14.4.10 of "Drafting Legislation in Hong Kong – A Guide to Styles and Practices" issued by the Law Drafting Division of the Department of Justice, ALA4 enquired whether "related and" should be added before "consequential amendments" in the long title.</p> <p>The Administration advised that Part 3 of the Bill provided for consequential amendments to the</p>	

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		<p>Inland Revenue Rules (Cap. 112, sub. leg. A) (Division 1) and related amendments to the Stamp Duty Ordinance ("SDO") (Cap. 117) (Division 2), in connection with the proposed tax treatment of RCS. As the amendments contained in Division 2 of Part 3 of the Bill were covered in the long title by the expression "to amend SDO to give stamp duty relief in relation to RCS", it was not necessary to add "related and" before "consequential amendments" in the long title.</p>	
001451 – 001632	Chairman Administration	<p><u>Clause 1</u></p> <p>Short title</p> <p>The Chairman enquired whether IRD could issue DIPNs in time to tie in with the commencement of the Bill, and whether the Joint Liaison Committee on Taxation would be consulted on the draft DIPNs.</p> <p>The Administration advised that IRD was preparing the draft DIPNs and would forward it to the Joint Liaison Committee on Taxation shortly after the passage of the Bill.</p>	The Administration to follow up as per paragraph 4 of the minutes
001633 – 001650	Chairman Administration	<p><u>Clause 2</u></p> <p>Enactments amended</p>	
001651 – 004130	Chairman Administration	<p><u>Clause 3</u></p> <p>Section 14C to Section 14F added</p> <p>The Chairman's enquiry and the Administration's response on the definition of "associated corporation" under IRO.</p> <p>The Administration advised that the definition of "associated corporation" under the proposed section 14C adopted the same scope as other definitions of "associated corporation" (e.g. the existing section 2(2)).</p> <p>The Chairman's enquiry and the Administration's response on "any activity other than a corporate treasury activity" under the proposed section 14D(3)(b).</p> <p>The Administration advised that, for the purpose of</p>	

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		<p>subsection (3)(b), in determining whether a corporation had carried out any activity other than a corporate treasury activity, only those activities that had generated income to the corporation were to be taken into account.</p> <p>The Chairman commented that corporate treasury centres ("CTCs") which were housed in holding companies with functions of holding investments and receiving dividend income on behalf of the group might not be able to enjoy the profits tax concession. He said that holding companies did not predominantly perform a CTC function and might not be able to satisfy the safe harbour rule as proposed under section 14E. He enquired if holding companies could be treated as qualifying CTCs if they chose not to receive dividend from the group companies.</p> <p>The Administration advised that dividend income was not subject to tax in Hong Kong. If a holding company was also performing some CTC functions, it could benefit from the profits tax concession provided that it satisfied the criteria for being a "qualifying CTC" in the proposed section 14D(2) (Clause 3). In particular, under the proposed section 14E and Part 3 of the proposed Schedule 17B (Clause 6), the Administration proposed a safe harbour rule which allowed corporations having 75% or more of their profits derived from, and 75% or more of their assets used to carry out, corporate treasury activities to be subject to the half-rate profits tax (in respect of the qualifying profits). This would help strike a reasonable balance to ensure that companies carrying out predominantly corporate treasury activities would meet the proposed qualifying criteria.</p> <p>The Chairman's enquiry and the Administration's response on the computation of the aggregate value of "corporate treasury asset".</p> <p>The Administration referred to the proposed section 14E(9) (Clause 3) and advised that, in computing the aggregate value of the corporate treasury assets of a corporation, if a corporate treasury asset was used partly to carry out a corporate treasury activity and partly for another purpose, only the part of the value of the asset that was proportionate to the extent to which the asset was used to carry out a</p>	

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		<p>corporate treasury activity was to be taken into account.</p> <p>The Chairman enquired if the Commissioner of Inland Revenue's ("the Commissioner") determination of whether a corporation was a qualifying CTC for a year of assessment under the proposed section 14F would only be valid for that particular year of assessment.</p> <p>The Administration confirmed that, for a particular year of assessment, the Commissioner's determination under the proposed section 14F(1) would only be valid for that year of assessment.</p>	
004131 – 004300	Chairman Administration	<p><u>Clause 4</u></p> <p>Section 19CA amended (treatment of losses: concessionary trading receipts)</p> <p>Members raised no query.</p>	
004301 – 004322	Chairman Administration	<p><u>Clause 5</u></p> <p>Schedule 8 amended (rate of profits tax in respect of a corporation)</p> <p>Members raised no query.</p>	
004323 – 005010	Chairman Administration	<p><u>Clause 6</u></p> <p>Schedule 17B added</p> <p>The Chairman's enquiry and the Administration's response on whether the meaning of corporate treasury service described in section 1(1) of Schedule 17B reflected the current industry practice, and whether the services listed under section 1(1)(a)-(k) (in Part 1) of Schedule 17B were based on any international standard.</p> <p>The Administration advised that the meaning of corporate treasury service was formulated in consultation with the treasury industry and accounting profession. There was no international standard. The Secretary for Financial Services and the Treasury ("SFST") would be empowered to amend the meaning of corporate treasury service as prescribed in Schedule 17B by way of subsidiary legislation, if necessary.</p>	

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		<p>The Chairman's enquiry and the Administration's response on the adjustment to the prescribed profits and asset percentages for the purpose of satisfying the safe harbour rule in Schedule 17B.</p> <p>The Administration proposed that SFST be empowered under the Bill (the proposed section 14C(5) (Clause 3)) to amend the prescribed percentages for the safe harbour rule in Schedule 17B by way of subsidiary legislation as situations warranted.</p> <p>In response to the Chairman, the Administration explained that if a company failed to meet the prescribed profits or asset percentage for the safe harbour rule under the proposed section 14E, it might apply for a determination from the Commissioner under the proposed section 14F.</p>	
005011 – 005458	Chairman Administration	<p><u>Clause 7</u></p> <p>Section 15 amended (certain amounts deemed trading receipts)</p> <p>The Chairman's enquiry and the Administration's response on the treatment of interest income of a financial institution under Cap. 112.</p> <p>The Administration advised that, in order to maintain a symmetric tax treatment for interest income, section 15(1)(ia) and (1a) was introduced to stipulate clearly that the "operation test" was applicable in the determination of the source of interest income, as well as relevant gains or profits, arising from the carrying on in Hong Kong by a corporation (other than a financial institution) of its intra-group financing business. Clause 7 sought to amend section 15 of Cap.112 to add the new section 15(1)(ia) and (1a) to deem certain sums received by or accrued to a corporation (other than a financial institution) from its intra-group financing business as having a Hong Kong source regardless of whether the moneys concerned were made available outside Hong Kong. Similar situations for a financial institution had been dealt with by the existing section 15(1)(i) and (l).</p>	

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005459 – 010334	Chairman Administration ALA4	<p><u>Clause 8</u></p> <p>Section 16 amended (ascertainment of chargeable profits)</p> <p>The Chairman's enquiry and the Administration's response on the application of the "subject to tax" condition.</p> <p>The Administration advised that "subject to tax" meant that tax had been paid or would be paid, whether by deduction or otherwise. IRD would explain the operation of this provision through DIPNs with examples, with reference to those scenarios described in the submission from Ernst & Young Tax Services Limited tabled at the meeting (LC Paper No. CB(4)667/15-16(01)).</p> <p>ALA4 pointed out that the "main purpose, or one of the main purposes" test under the proposed section 16(2CC) was more stringent than the "sole or dominant purpose" test under the existing section 61A and enquired why the more stringent text was proposed.</p> <p>The Administration advised that in order to align with the latest international practices, the Administration intended to adopt the "main purpose test" for section 16(2CC) to prevent tax avoidance schemes shifting losses to Hong Kong, even though the "main purpose test" might be regarded as more stringent (from some taxpayers' perspectives) than the "sole or dominant purpose test" under the existing section 61A.</p>	The Administration to follow up as per paragraph 4 of the minutes
010335 – 010350	Chairman Administration	<p><u>Clause 9</u></p> <p>Schedule 8 amended (rate of profits tax in respect of a corporation)</p> <p>Members raised no query.</p>	
010351 – 010407	Chairman Administration	<p><u>Clause 10</u></p> <p>Schedule 17A amended (specified alternative bond scheme and its tax treatment)</p> <p>Members raised no query.</p>	

Time marker	Speaker	Subject(s)	Action required
010408 – 010614	Chairman Administration	<p><u>Clause 11</u></p> <p>Section 2 amended (interpretation)</p> <p>Members raised no query.</p>	
010615 – 010918	Chairman Administration	<p><u>Clause 12</u></p> <p>Section 15 amended (certain amounts deemed trading receipts)</p> <p>The Chairman's enquiry and the Administration's response on tax treatment of income arising from deep discount RCS.</p>	
010919– 011230	Chairman Administration	<p><u>Clause 13</u></p> <p>Section 16 amended (ascertainment of chargeable profits)</p> <p>The Chairman's enquiry and the Administration's response on the eligibility for deduction of distributions in respect of RCSs issued by a non-bank holding company.</p>	
011231 – 014706	Chairman Mr SIN Chung-kai Administration	<p><u>Clause 14</u></p> <p>Sections 17A to 17H added</p> <p>The Chairman's enquiry and the Administration's response on tax treatment of Additional Tier 1 capital instrument and Common Equity Tier 1 capital instrument ("CET1").</p> <p>The Administration advised that, unlike Additional Tier 1 or Tier 2 capital instruments, CET1 capital instruments were equity rather than debt in nature and therefore did not fall within the meaning of RCSs. Under the proposed section 17A(2)(b), the definition of RCS did not include an instrument which provided for an issuer converting, or having an option to convert, the instrument into a CET1 capital instrument after a certain period of time.</p> <p>The Chairman's enquiry and the Administration's response on the definition of "specified connected person" under the proposed section 17D.</p> <p>The Chairman's enquiry and the Administration's response on the application of the "arm's length</p>	

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		<p>principle" contained in the proposed section 17E in respect of RCS transactions between a financial institution and its associates.</p> <p>The Chairman's enquiry and the Administration's response on whether, under the proposed section 17F, the deduction of interest on RCSs was only denied to the extent that the instruments were not funded through an external issue.</p> <p>The Administration advised that interest deduction would be allowed to the extent to which the money paid by, or on behalf of, the specified connected person of the issuer for the issue of RCSs, was funded through an external issue of RCSs, debentures or debt instruments, where the externally issued instruments were not held by or for the benefit of a specified connected person of an issuer.</p> <p>The Chairman requested the Administration to, after the passage of the Bill, issue DIPNs to explain the operation of the proposed section 17G, and to explain the operation of the various proposed amendments. The Administration agreed to the request.</p> <p>Mr SIN Chung-kai's enquiry and the Administration's response on whether the concerns raised by deputations at the meeting on 26 January 2016 had been addressed.</p> <p>The Administration advised that taking into account the concerns expressed by deputations at the meeting held on 26 January 2016 over the interpretation of the proposed section 17H, the Administration would consider proposing Committee Stage amendments to remove the proposed section 17H and all references to the section from the Bill. As regards the concerns raised by the deputations in relation to the need for the proposed sections 17F and 17G, the deputations were satisfied with the Administration's explanation.</p>	<p>The Administration to follow up as per paragraph 4 of the minutes</p>
014707 – 014830	Chairman Administration	<p><u>Clause 15</u></p> <p>Schedule 6 amended</p> <p>Members raised no query.</p>	

Time marker	Speaker	Subject(s)	Action required
014831 – 014900	Chairman Administration	<p><u>Clause 16</u></p> <p>Schedule 16 amended (specified transactions)</p> <p>Members raised no query.</p>	
014901 – 014930	Chairman Administration	<p><u>Clause 17</u></p> <p>Section 89 amended (transitional provisions)</p> <p>Members raised no query.</p>	
014931 – 015306	Chairman Administration	<p><u>Clause 18</u></p> <p>Schedule 36 added</p> <p>The Chairman's enquiry and the Administration's response on the effective date of the profits tax concession granted to qualifying CTCs.</p> <p>The Administration advised that, for the purposes of the proposed sections 14D(1) and 14E(5), in computing the qualifying profits and corporate treasury profits of a corporation, sums received by or accrued to the corporation before 1 April 2016 were not to be taken into account. Section 15(1)(ia) and (la) would not apply to sums received or accrued before the commencement date of the Bill.</p> <p>The Chairman's enquiry and the Administration's response on whether any application for advance ruling had been received by IRD.</p>	
015307 – 015330	Chairman Administration	<p><u>Clause 19</u></p> <p>Cross-heading before rule 3 amended</p> <p>Members raised no query.</p>	
015331 – 015400	Chairman Administration	<p><u>Clause 20</u></p> <p>Rule 3 amended (banks; Hong Kong branch offices)</p> <p>Members raised no query.</p>	

Time marker	Speaker	Subject(s)	Action required
015401 – 015450	Chairman Administration	<u>Clauses 21 and 22</u> Cross-heading before rule 5 amended Rule 5 amended (profit of Hong Kong branch offices) Members raised no query.	
015451 – 015511	Chairman Administration	<u>Clause 23</u> Rule 7 added Members raised no query.	
015512 – 015520	Chairman Administration	<u>Clause 24</u> Section 19 amended (contract notes, etc. in respect of sale and purchase of Hong Kong stock) Members raised no query.	
015521 – 015530	Chairman Administration	<u>Clause 25</u> Section 63 amended (regulations) Members raised no query.	
015531 – 015600	Chairman Administration	<u>Clause 26</u> First Schedule amended Members raised no query.	
015601 – 015620	Chairman Administration	<u>Clause 27</u> Schedule 9 added Members raised no query.	
Agenda item III – Any other business			
015621 – 020108	Chairman Mr SIN Chung-kai Administration	Follow-up actions Legislative timetable Date of next meeting	The Administration to follow up as per paragraph 4 of the minutes