

**立法會**  
*Legislative Council*

LC Paper No. CB(1)94/17-18  
(These minutes have been seen  
by the Administration)

Ref : CB1/BC/8/16/2

**Bills Committee on Inland Revenue (Amendment) (No. 4) Bill 2017**

**Minutes of the first meeting**  
**held on Thursday, 20 July 2017, at 2:30 pm**  
**in Conference Room 2B of the Legislative Council Complex**

**Members present** : Hon Kenneth LEUNG (Chairman)  
Hon James TO Kun-sun  
Hon Charles Peter MOK, JP  
Dr Hon KWOK Ka-ki  
Hon IP Kin-yuen  
Hon CHAN Chun-ying

**Members absent** : Hon WONG Ting-kwong, GBS, JP  
Dr Hon Junius HO Kwan-yiu, JP

**Public Officers attending** : **Agenda item II**

Financial Services and the Treasury Bureau

Ms Mable CHAN, JP  
Deputy Secretary (Financial Services)1

Miss Carrie CHANG  
Principal Assistant Secretary (Financial Services)1

Miss Renita AU  
Assistant Secretary (Financial Services)(1)1

Inland Revenue Department

Miss HUI Chiu-po  
Senior Assessor (Research)1

Department of Justice

Ms Amy CHAN  
Senior Assistant Law Draftsman (Acting)

**Clerk in Attendance :** Ms Sharon CHUNG  
Chief Council Secretary (1)2

**Staff in attendance :** Ms Winnie LO  
Assistant Legal Adviser 7

Miss Rita YUNG  
Senior Council Secretary (1)2

Ms Christina SHIU  
Legislative Assistant (1)2

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Action

**I. Election of Chairman**

Election of Chairman

Mr James TO, the member who had the highest precedence among members of the Bills Committee present at the meeting, presided at the election of Chairman of the Bills Committee.

2. Mr James TO invited nominations for the chairmanship of the Bills Committee. Dr KWOK Ka-ki nominated Mr Kenneth LEUNG, and the nomination was seconded by Mr IP Kin-yuen. Mr Kenneth LEUNG accepted the nomination.

3. There being no other nomination, Mr Kenneth LEUNG was declared Chairman of the Bills Committee. Mr LEUNG then took the chair.

4. Members agreed that there was no need to elect a Deputy Chairman.

Action

**II. Meeting with the Administration**

(LC Paper No. CB(3)737/16-17	— The Bill
File Ref.: ASST/3/1/5/1C(2017)Pt.6	— Legislative Council Brief
LC Paper No. LS91/16-17	— Legal Service Division Report
LC Paper No. CB(1)1328/16-17(01)	— Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to Members)
LC Paper No. CB(1)1328/16-17(02)	— Background brief prepared by the Legislative Council Secretariat
LC Paper No. CB(1)1328/16-17(03)	— Letter from Assistant Legal Adviser to the Administration dated 13 July 2017)

5. With the aid of a powerpoint presentation, the Administration briefed members on the Inland Revenue (Amendment) (No. 4) Bill 2017 ("the Bill").

*(Post-meeting note: A soft copy of the powerpoint presentation materials was circulated to members vide LC Paper No. CB(1)1336/16-17(01) by email on 21 July 2017.)*

Discussion

6. The Bills Committee deliberated (index of proceedings in the **Appendix**).

Follow-up actions to be taken by the Administration

7. The Administration was requested to provide the following information:
- (a) elaboration on the rationale for imposing the following conditions on the profits tax exemption for onshore privately offered open-ended fund companies ("OFCs"):
    - (i) Condition 2: The OFC must be "non-closely held";
    - (ii) Condition 3: The OFC must invest in permissible asset classes specified by the Securities and Futures Commission,

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but with a degree of flexibility (i.e. 10% de minimis limit);  
and

- (iii) Condition 4: Transactions of the OFC must be carried out through or arranged by a qualified person.
- (b) the rationale for not offering profits tax exemption to onshore privately offered funds/OFCs under the current taxation regime;
- (c) projection of the financial and economic implications of the extension of profits tax exemption to onshore privately offered OFCs, such as the number of privately offered OFCs expected to be established in Hong Kong, the number of jobs expected to be created in the financial services industry, etc; and
- (d) with reference to the Departmental Interpretation and Practice Notes of the Inland Revenue Department and the proposed section 20AJ(3), elaboration on the taxability of carried interest (including the dividends derived from it) received by fund executives.

*(Post-meeting note: The Administration's response was issued to members vide LC Paper CB(1)1446/16-17(02) on 29 September 2017.)*

Invitation of public views

8. Members agreed to the following arrangements for inviting written submissions on the Bill:

- (i) issue invitation letters to relevant professional organizations and the 18 District Councils; and
- (ii) post a notice on the website of the Legislative Council ("LegCo") to invite public views.

*(Post-meeting note: On 4 August 2017, letters were sent to DCs and relevant professional organizations, and a notice was posted on the LegCo website.)*

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**III. Any other business**

9. There being no other business, the meeting ended at 4:09 pm.

Council Business Division 1  
Legislative Council Secretariat  
23 October 2017

## Bills Committee on Inland Revenue (Amendment) (No. 4) Bill 2017

**Proceedings of the first meeting  
on Thursday, 20 July 2017, at 2:30 pm  
in Conference Room 2B of the Legislative Council Complex**

Time marker	Speaker	Subject(s)	Action required
<i>Agenda Item I - Election of Chairman</i>			
000408 – 000510	Mr James TO Dr KWOK Ka-ki Mr IP Kin-yuen Mr Kenneth LEUNG	Election of Chairman  Mr Kenneth LEUNG was elected Chairman of the Bills Committee.	
<i>Agenda Item II - Meeting with the Administration</i>			
000511 – 001329	Chairman Administration	Briefing by the Administration on the Inland Revenue (Amendment) (No. 4) Bill 2017 ("the Bill")	
001330 – 002415	Chairman Mr James TO Administration	<p>At the request of Mr James TO, the Administration agreed to provide written information on:</p> <p>(a) the rationale for imposing the following conditions on the profits tax exemption for onshore privately offered open-ended fund companies ("OFCs"):</p> <p style="margin-left: 40px;">(i) Condition 2: The OFC must be "non-closely held" ("NCH");</p> <p style="margin-left: 40px;">(ii) Condition 3: The OFC must invest in permissible asset classes specified by the Securities and Futures Commission ("SFC"), but with a degree of flexibility (i.e. 10% de minimis limit); and</p> <p style="margin-left: 40px;">(iii) Condition 4: Transactions of the OFC must be carried out through or arranged by a qualified person.</p> <p>(b) the rationale for not offering profits tax exemption to onshore privately offered funds/OFCs under the current taxation regime; and</p> <p>(c) projection of the financial and economic implications of the extension of profits</p>	Administration (paragraphs 7 (a) to 7 (c) of the minutes refer)

Time marker	Speaker	Subject(s)	Action required
		<p>tax exemption to onshore privately offered OFCs, such as the number of privately offered OFCs expected to be established in Hong Kong, the number of jobs expected to be created in the financial services industry, etc.</p> <p>In response to Mr James TO's enquiry, the Administration advised that currently there was no onshore privately offered OFC in Hong Kong.</p>	
002416 – 003024	Chairman Mr CHAN Chun-ying Administration	<p>Mr CHAN Chun-ying raised the following enquiries:</p> <p>(a) whether the Inland Revenue Department ("IRD") would consider issuing certificate of resident status to OFCs which were eligible for profits tax exemption; and</p> <p>(b) the timetable for reviewing the ownership requirement under the NCH condition in future.</p> <p>The Administration's response that:</p> <p>(a) An onshore privately offered OFC would be granted profits tax exemption if it could meet the relevant conditions which included that its central management of control should be exercised in Hong Kong and that its regulated activities should be carried out or arranged in Hong Kong by or through a qualified person. If an OFC could meet these conditions, it would generally be regarded as a tax resident of Hong Kong (upon application by the OFC).</p> <p>(b) The proposed tax regime for OFCs, being an onshore scheme for activities within a defined scope with real economic substance in Hong Kong and necessary safeguards, should not be regarded as a harmful tax practice by the Organisation for Economic Co-operation and Development.</p> <p>(c) The Government would review the effectiveness of the proposed profits tax</p>	

Time marker	Speaker	Subject(s)	Action required
		<p>exemption in enhancing Hong Kong's competitiveness as a fund domicile for OFCs at an appropriate juncture in future, and, if necessary, might consider adjusting the NCH condition as the circumstances might warrant. There was no specific timetable for reviewing the ownership requirement under the NCH condition at the moment.</p>	
003025 - 003419	Chairman Mr CHAN Chun-ying Administration	<p>Mr CHAN Chun-ying enquired about the taxability of performance fees and carried interest paid out to investment managers in the form of dividends.</p> <p>The Administration's response that:</p> <p>(a) Section 26(a) of the Inland Revenue Ordinance (Cap. 112) ("IRO") provided for profits tax exemption for dividends received from corporations.</p> <p>(b) The proposed new section 20AJ(3) included an express provision to the effect that if an OFC was not exempt from the payment of tax, the consideration or remuneration that a person received (including consideration or remuneration in the form of dividends) for providing any services directly or indirectly to the OFC would be chargeable to tax.</p>	
003420 - 003719	Chairman Administration	<p>The Chairman sought elaboration on an OFC's eligibility for profits tax exemption where the OFC's investments in "non-permissible asset classes" exceeded the 10% de minimis limit.</p> <p>The Administration's response that:</p> <p>(a) Profits of an OFC derived from transactions in "non-permissible asset classes" (if any) would be subject to tax.</p> <p>(b) If the 10% de minimis limit was not exceeded, only profits derived from the transactions in "non-permissible asset classes" would be chargeable to profits tax.</p>	



Time marker	Speaker	Subject(s)	Action required
		(c) If the 10% de minimis limit was exceeded, the tax exemption for the OFC would be lost, i.e. all profits would be wholly chargeable to profits tax.	
003720 - 004625	Chairman Administration	The Chairman requested the Administration to provide written information to elaborate, with reference to the Departmental Interpretation and Practice Notes issued by IRD and the proposed section 20AJ(3), on the taxability of carried interest (including the dividends derived from it, and the subsequent income derived from the holding or disposal of such dividends) received by fund executives.	Administration (paragraph 7(d) of the minutes refers)
004626 - 004852	Chairman Administration	<p>The Chairman sought elaboration on the definition of "permissible asset classes" for an OFC.</p> <p>The Administration's response that:</p> <p>(a) SFC would specify in its OFC Code the asset classes that privately offered OFCs would be allowed to invest in. The investment scope should largely align with SFC's Type 9 (asset management) regulated activity, i.e. mainly securities and futures, as well as that for offshore funds (e.g. offshore hedge funds) as set out in Schedule 16 to IRO.</p> <p>(b) To enjoy profits tax exemption, an OFC must have its profits-producing activities carried out through or arranged in Hong Kong by corporations or authorized financial institutions licensed or registered under the Securities and Futures Ordinance (Cap. 571) ("SFO") to carry out Type 9 regulated activity.</p>	
004853 - 005421	Chairman Administration	The Chairman pointed out that while OFCs were not permitted to invest in shares of local private companies, they were allowed to invest in shares of overseas private companies which could own assets in Hong Kong. He enquired whether this might give rise to tax leakage.	

Time marker	Speaker	Subject(s)	Action required
		<p>The Administration's response that:</p> <p>(a) In order to enhance Hong Kong's attractiveness as a location for domiciliation of funds, an appropriate degree of flexibility would be allowed for the investment scope of OFCs.</p> <p>(b) Relevant measures had been proposed to prevent abuse or round-tripping by a resident person disguising as an OFC to take advantage of the proposed profits tax exemption.</p>	
005422 - 005550	Chairman Administration	<p>The Chairman enquired about the composition of an OFC board of directors.</p> <p>The Administration's response that:</p> <p>(a) An investor of an OFC could be a director of the OFC.</p> <p>(b) To ensure that a tax-exempt OFC was not controlled by a small number of investors or by the originator and originators' associates, an OFC must have a minimum number of investors and the participation interests of various types of investors must meet relevant percentage caps and levels.</p>	
005551 - 005855	Chairman Administration	<p>Discussion on the implementation of the OFC regime in overseas jurisdictions, in particular the number of jobs created.</p> <p>The Administration's advice that:</p> <p>(a) The corporate fund structure was common in other major fund jurisdictions, for example the United Kingdom and Luxembourg.</p> <p>(b) Currently there was no onshore OFC in Hong Kong.</p> <p>(c) It was expected that the tax exemption proposal would enhance Hong Kong's competitiveness as a location for domiciliation of funds.</p>	

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		(d) Fund creation activities would drive demand for professional services such as fund management and investment advice, as well as legal, accounting, administration and other ancillary services, in addition to sales and marketing.	
005856 - 010321	Chairman Mr CHAN Chun-ying Administration	<p>The Chairman enquired about the public consultation conducted by the Administration on the Bill.</p> <p>The Administration's response that:</p> <p>(a) From January to April 2016, the Administration had consulted the industry on the concept of extending profits tax exemption to onshore privately offered OFCs.</p> <p>(b) The industry had been consulted again in March 2017 on the legislative proposal.</p> <p>Invitation of public views</p> <p>Arrangements for the next meeting</p>	
<p><b>Clause-by-clause examination of the Bill</b>                      [The Bill (LC Paper No. CB(3)737/16-17)]                      [Marked-up copy of the Bill prepared by the Legal Service Division (LC Paper No. CB(1)1328/16-17(01))]</p>			
010322 - 010840	Chairman Assistant Legal Adviser 7 ("ALA7")	<p><u>Clause 1 — Short title and commencement</u></p> <p>ALA7 sought information on the estimated commencement date of section 53(8) of the Securities and Futures (Amendment) Ordinance 2014 (related to the commencement date of item 8, which involved over-the-counter ("OTC") derivative products, of the new Schedule 16A).</p> <p>The Administration's response that:</p> <p>(a) SFO had been amended in 2014 to provide for a regulatory framework for the OTC market in Hong Kong. The regulatory regime was being implemented in stages in tandem with the making of the necessary subsidiary legislation.</p>	

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		<p>(b) So far, nine pieces of subsidiary legislation had been passed to implement mandatory reporting and clearing obligations under the regime.</p> <p>(c) The next stage would involve the implementation of regulation of intermediaries engaging in OTC derivatives activities. SFC would consult the market before finalizing the relevant subsidiary legislation and expected it to be in place after the OFC regime had come into operation, i.e. after the second quarter of 2018.</p>	
010841 – 010923	Chairman Administration	<p><u>Clause 2 — Inland Revenue Ordinance amended</u></p> <p><u>Clause 3 — Section 20AB amended (interpretation of sections 20AC, 20ACA, 20AD, 20AE and 20AF and Schedules 15 and 15A)</u></p> <p>Members raised no queries.</p>	
010924 – 011200	Chairman Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AG — Sub-funds of open-ended fund companies</i></p> <p>The Chairman enquired about the handling of loss sustained by a sub-fund of an OFC.</p> <p>The Administration responded that any loss sustained by a sub-fund was not available for set off against any assessable profits of another sub-fund of an OFC.</p>	
011201 – 013036	Chairman ALA7 Mr CHAN Chun-ying Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AH — Certain profits of certain open-ended fund companies exempt from payment of tax</i></p> <p><u>New section 20AH(2)(c)</u></p> <p>The Chairman and ALA7 sought elaboration on the basis for setting the 10% de minimis limit for OFCs to invest in "non-permissible asset classes" in order to enjoy the proposed profits tax exemption.</p>	

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		<p>The Administration's response that:</p> <p>(a) In setting the 10% de minimis limit, feedback from the industry received during the public consultation on the proposed OFC regime in 2014 had been taken into account.</p> <p>(b) The 10% de minimis limit should be met at all times during the basis period for a year of assessment for the exemption of profits tax. It might not be practical for an OFC to calculate the 10% de minimis limit for each day during the year of assessment. In practice, the OFC could rely on the yearly audited financial statements to ascertain whether the 10% de minimis limit was met for a year of assessment.</p> <p>Mr CHAN Chun-ying said that the industry generally welcomed the proposed 10% de minimis limit, which allowed a certain degree of flexibility in investing in "non-permissible asset classes".</p> <p>Discussion on drafting issues</p>	
013037 – 013233	Chairman Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AH — Certain profits of certain open-ended fund companies exempt from payment of tax</i></p> <p><u><i>New section 20AH(5)</i></u></p> <p>The Chairman enquired about the taxability of the profits of an OFC if it had not become NCH within 24 months after the day on which it accepted its first investor.</p> <p>The Administration responded that in the above-mentioned case, the profits tax exemption was to be regarded as never having been granted and the OFC would be chargeable to tax for the whole of the 24-month start-up period.</p>	

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013234 – 013719	Chairman ALA7 Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AH — Certain profits of certain open-ended fund companies exempt from payment of tax</i></p> <p><u><i>New section 20AH(6)</i></u></p> <p>The Chairman enquired about the eligibility for profits tax exemption in cases where an OFC failed to satisfy the NCH condition temporarily (e.g. certain investors redeeming their shares and exiting the fund in a short period of time).</p> <p>The Administration responded that to cater for the actual operation circumstances that an OFC might encounter, safe harbour rules would be introduced. Under these rules, an OFC might claim tax exemption even if it failed to meet the NCH condition under certain special circumstances. The safe harbour rules were set out in the new section 20AJ.</p> <p>ALA7 referred members to her letter to the Administration dated 13 July 2017 (LC Paper No. CB(1)1328/16-17(03)) seeking clarification in relation to the disapplication of profits tax exemption in cases where cessation of a trade, profession or business in Hong Kong of an OFC was involved.</p> <p>Briefing by the Administration on its reply to ALA7's enquiry as set out in LC Paper No. CB(1)1335/16-17(01)</p>	
013720 – 013804	Chairman	The Bills Committee would continue the clause-by-clause examination of the Bill at the next meeting.	
013805 – 014224	Chairman Mr CHAN Chun-ying Administration	<p><u>New Schedules 16A and 16B (under clause 6)</u></p> <p>Mr CHAN Chun-ying sought elaboration on section 2 of Schedule 16B (the criteria for determining whether an OFC that had one or more qualified investors was NCH), in particular the requirement that "the participation interest of the originators and their associates does not exceed 30% of the</p>	

Time marker	Speaker	Subject(s)	Action required
		<p>OFC's issued share capital" (section 2(e)).</p> <p>The Administration's response that:</p> <p>(a) "Qualified investors" referred to certain specified types of institutional investors, including organizations established for non-profit-making purpose, pension funds, publicly offered funds and governmental entities.</p> <p>(b) The "originator" of an OFC referred to the person who originated or sponsored the OFC, and had the power to make investment decisions on behalf of the OFC.</p> <p>(c) The criteria set out in section 2(e) of Schedule 16B aimed to ensure that an OFC was not controlled by the originator and the originators' associates.</p>	
014225 – 014328	Chairman	Closing remarks	