

立法會
Legislative Council

LC Paper No. CB(1)813/17-18
(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 second meeting
held on Tuesday, 13 February 2018, at 9:30 am
in Conference Room 2A of the Legislative Council Complex

- Members present** : Hon Kenneth LEUNG (Chairman)
Hon James TO Kun-sun
Hon WONG Ting-kwong, GBS, JP
Hon IP Kin-yuen
Dr Hon Junius HO Kwan-yiu, JP
Hon CHAN Chun-ying
- Member attending** : Hon WU Chi-wai, MH
- Members absent** : Hon Charles Peter MOK, JP
Dr Hon KWOK Ka-ki
- Public officers attending** : **Agenda item I**
Financial Services and the Treasury Bureau

Mr Chris SUN, 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

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

Miss HUI Chiu-po
Senior Assessor (Research)1

Department of Justice

Ms Françoise LAM
Senior Assistant Law Draftsman

Ms Amy CHAN
Senior Assistant Law Draftsman (Acting)

Clerk in attendance : Ms Doris LO
Chief Council Secretary (1)2

Staff in attendance : Ms Rachel DAI
Assistant Legal Adviser 2

Miss Rita YUNG
Senior Council Secretary (1)2

Action

I. Meeting with the Administration

Matters arising from the meeting on 20 July 2017

(LC Paper No. CB(1)1446/16-17(01) — List of follow-up actions
arising from the discussion
at the meeting on
20 July 2017

Action

LC Paper No. CB(1)1446/16-17(02) — Administration's response to issues raised by members at the meeting on 20 July 2017)

Submissions received from organizations and the Administration's response

(LC Paper No. CB(1)1405/16-17(01) — Submission dated 22 August 2017 from Hong Kong Bar Association

LC Paper No. CB(1)1405/16-17(02) — E-mail dated 25 August 2017 from The Hong Kong Society of Financial Analysts

LC Paper No. CB(1)1405/16-17(03) — Submission dated 31 August 2017 from PricewaterhouseCoopers Limited

LC Paper No. CB(1)1405/16-17(04) — Submission dated 1 September 2017 from The Hong Kong Association of Banks

LC Paper No. CB(1)1405/16-17(05) — Submission dated 4 September 2017 from The Hong Kong Institute of Chartered Secretaries

LC Paper No. CB(1)1405/16-17(06) — Submission dated 4 September 2017 from Joint Liaison Committee on Taxation

LC Paper No. CB(1)1405/16-17(07) — Submission dated 29 August 2017 from Democratic Alliance for the Betterment and Progress of Hong Kong

LC Paper No. CB(1)1405/16-17(08) — Submission dated 4 September 2017 from Deloitte Advisory (Hong Kong) Limited (Restricted to Members)

Action

- LC Paper No. CB(1)1405/16-17(09) — Submission dated 4 September 2017 from Hong Kong Investment Funds Association
- LC Paper No. CB(1)1405/16-17(10) — Submission dated 5 September 2017 from Hong Kong Institute of Certified Public Accountants
- LC Paper No. CB(1)41/17-18(01) — Submission dated 25 August 2017 from The Taxation Institute of Hong Kong
- LC Paper No. CB(1)415/17-18(01) — Administration's response to the submissions received from organizations)

Clause-by-clause examination of the Bill

- (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
- LC Paper No. CB(1)1335/16-17(01) — Administration's response to Assistant Legal Adviser's letter dated 13 July 2017 [LC Paper No. CB(1)1328/16-17(03)]

Action

Draft amendments to the Bill proposed by the Administration

(LC Paper No. CB(1)574/17-18(01) — Draft amendments to the Bill proposed by the Administration)

The Bills Committee deliberated (index of proceedings attached at the **Annex**).

2. At 9:58 am, the Chairman suspended the meeting to invite participants of the meeting to observe a one-minute silence in mourning to express their deep condolences to the victims of the traffic accident on Tai Po Road occurred on 10 February 2018. The meeting resumed at 10:01 am.

Legislative timetable

3. The Bills Committee completed scrutiny of the Inland Revenue (Amendment) (No. 4) Bill 2017 ("the Bill"). The Bills Committee raised no objection to the resumption of the Second Reading debate on the Bill at the Council meeting of 21 March 2018. The Chairman informed members that he would report verbally the deliberations of the Bills Committee to the House Committee on 23 February 2018. The deadline for giving notice to move amendments to the Bill was 12 March 2018.

II. Any other business

4. There being no other business, the meeting ended at 11:01 am.

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

**Proceedings of the second meeting
on Tuesday, 13 February 2018, at 9:30 am
in Conference Room 2A of the Legislative Council Complex**

Time marker	Speaker	Subject(s)	Action required
<i>Agenda Item I - Meeting with the Administration</i>			
000413 – 000647	Chairman	Opening remarks	
000648 – 001134	Chairman Administration	Briefing by the Administration on its response to issues raised by members at the meeting on 20 July 2017 [LC Paper No. CB(1)1446/16-17(02)] and the draft amendments to the Bill proposed by the Administration [LC Paper No. CB(1)574/17-18(01)]	
001135 – 001808	Chairman Mr CHAN Chun-ying Administration	Briefing by the Administration on its response to the submissions received from organizations [LC Paper No. CB(1)415/17-18(01)]	
001809 – 002221	Chairman Administration	<p>The Chairman enquired about the taxability of the profits of onshore privately offered open-ended fund companies ("subject OFCs") in the following circumstances:</p> <p>(a) a subject OFC engaged in direct trading or direct business undertaking in Hong Kong; or</p> <p>(b) a subject OFC invested in private companies engaging in direct trading or direct business undertaking in Hong Kong.</p> <p>The Administration responded that:</p> <p>(a) a subject OFC would only be taxed on its profits from (i) direct trading or direct business undertaking in Hong Kong in assets of a non-Schedule 16A class (i.e. non-qualifying transactions); and (ii) investment in private companies that could not meet the requirements under the proposed new section 20AH; and</p> <p>(b) the no-tainting arrangement was that the tax-exempt profits of the subject OFC would not be tainted even if profits tax had to be paid under the above circumstances.</p>	

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002222 – 003109	Chairman Mr CHAN Chun-ying Administration	<p>Mr CHAN Chun-ying expressed concern about whether the proposed new section 20AJ(3) would avoid double taxation in all the circumstances under which the investment managers were remunerated for providing services to OFCs.</p> <p>The Chairman sought clarification on whether dividends paid to investment managers by a subject OFC for their provision of professional services would be tax-deductible for the subject OFC.</p> <p>The Administration responded that:</p> <p>(a) the proposed new section 20AJ(3) did not affect the general tax principles that were currently applicable in determining whether carried interest or performance fees were taxable;</p> <p>(b) it also did not affect the current treatment of expense deduction, i.e. the consideration or remuneration (e.g. management/performance fees) paid to investment managers and charged in the accounts of an OFC as an expense would be allowed for tax deduction for the OFC to the extent that it had been incurred for producing chargeable profits; and</p> <p>(c) accordingly, the issue of double taxation would not arise.</p>	
003110 – 003232	Chairman Mr WU Chi-wai	<p>Mr WU Chi-wai was concerned about the views expressed in the written submissions from certain organizations (as set out in paragraph 31 of the Administration's response to the submissions received from organizations (LC Paper No. CB(1)415/17-18(01)), i.e. the proposed tax regime for subject OFCs might be considered to have a ring-fencing feature and thus a harmful tax practice by the Organisation for Economic Co-operation and Development ("OCED").</p>	
003233 – 003508	Chairman	<p>Suspension of the meeting for a one-minute silence in mourning for the victims of the traffic accident on Tai Po Road occurred on 10 February 2018</p>	
003509 – 004039	Chairman Mr WU Chi-wai Administration	<p>The Administration's response to Mr WU Chi-wai's concern that:</p>	

Time marker	Speaker	Subject(s)	Action required
		<p>(a) the proposed tax regime for the subject OFCs was for activities within a defined scope with real economic substance in Hong Kong and necessary safeguards; and</p> <p>(b) therefore the Administration was of the view that the proposed tax regime should not be regarded as a harmful tax practice by OECD.</p>	
004040 – 004306	Chairman Mr WU Chi-wai Administration	Mr WU Chi-wai enquired whether stamp duty would be payable in respect of the transactions in securities carried out by the subject OFCs. The Administration replied in the affirmative.	
004307 – 005259	Chairman Mr James TO Administration	<p>Mr James TO considered it incumbent upon the Administration to ensure that the proposed tax regime for the subject OFCs, in particular with regard to the deeming provisions for residents, would not be in violation of the latest international standards.</p> <p>The Administration responded that:</p> <p>(a) in essence, the deeming provisions should be aimed at residents, in view that non-residents generally might not be subject to Hong Kong tax under a double tax agreement in the absence of a permanent establishment;</p> <p>(b) the proposed tax regime for the subject OFCs was in keeping with the prevailing international standards under the Base Erosion and Profit Shifting package of OECD and the European Union; and</p> <p>(c) that said, the Administration would continue to monitor the latest developments in the international community.</p> <p>Mr James TO enquired about the estimated loss in tax revenue if the deeming provisions for residents were removed.</p> <p>The Administration responded that it could not project the number of subject OFCs that would be established in Hong Kong given that the OFC was a new fund structure. Hence, it would not be able to estimate the loss in tax revenue if the deeming provisions for residents were to be removed.</p>	

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<p>Clause-by-clause examination of the Bill [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))] [Draft amendments to the Bill proposed by the Administration (LC Paper No. CB(1)574/17-18(01))]</p>			
005300 – 005941	Chairman Administration	<p>The Bills Committee continued clause-by-clause examination of the Bill, and considered the draft amendments to the Bill proposed by the Administration.</p> <p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AG — Sub-funds of open-ended fund companies</i></p> <p>Proposed amendment to the new section 20AG(4) consequential to the proposed removal of the 10% de minimis rule</p> <p><i>20AH — Certain profits of certain open-ended fund companies exempt from payment of tax</i></p> <p>Proposed amendments to the new section 20AH to (a) plug a technical loophole in the Bill to prevent tax leakage and (b) address the international community's concern about ring-fencing</p> <p>Members raised no queries.</p>	
005942 – 011211	Chairman Assistant Legal Adviser 2 ("ALA2") Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AI — Interpretation of section 20AH: meaning of non-closely held</i></p> <p><u>New section 20AI(2)</u></p> <p>ALA2 enquired about the purpose of the requirement that the specified requirements in relation to the "non-closely held" ("NCH") condition should be met "in good faith".</p> <p>The Administration responded that:</p> <p>(a) the term "in good faith" was intended to guard against notional but not genuine compliance of the ownership requirement for an NCH OFC to facilitate the Inland Revenue Department's assessment of the arrangements between investors and nominees; and</p>	

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		<p>(b) similar wordings (i.e. the Latin equivalent "bona fide") could be found in the Inland Revenue Ordinance (Cap. 112) ("IRO"), such as the provision relating to profits tax exemption for publicly offered funds under section 26(1A)(a), etc.</p> <p><u>New section 20AI(5)</u></p> <p>The Chairman enquired how the relevant thresholds to be met by a subject OFC for determining whether it was NCH as set out in Schedule 16B were determined.</p> <p>The Administration responded that the relevant thresholds were set taking into account views received during industry consultations and with reference to data provided by the industry relating to privately offered funds.</p> <p><u>New section 20AI(6)</u></p> <p>Proposed amendments to clearly state that sovereign wealth funds should fall within the definition of "qualified investor"</p> <p>The Chairman queried if it was too stringent to require an institutional investor to meet all the conditions set out in paragraph (a) of the definition of "qualified investor" in the new section 20AI(6) in order to be regarded as a qualified investor in relation to an OFC.</p> <p>The Administration responded that:</p> <p>(a) in general terms, a "qualified investor" referred to certain specified types of institutional investors, including organizations established for non-profit-making purposes, pension funds, publicly offered funds and governmental entities; and</p> <p>(b) the conditions set out in paragraph (a) of the definition of "qualified investor" in the new section 20AI(6) largely aligned with those for determining non-profit-making active non-financial entities as promulgated by OECD. A similar concept had been added to IRO in the context of automatic exchange of financial account information for tax purposes.</p>	

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011212 – 011712	Chairman ALA2 Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AJ — Supplementary provisions for section 20AH</i></p> <p>Proposed amendments to the new section 20AJ consequential to the proposed removal of the 10% de minimis rule</p> <p>ALA2 enquired how a failure of an OFC to meet the NCH condition could be regarded as "temporary".</p> <p>The Administration responded that:</p> <p>(a) basically the term "temporary" should mean not being "long-term" or "permanent"; and</p> <p>(b) flexibility was allowed under the new section 20AJ(1)(b) to give the Commissioner of Inland Revenue the discretion to decide whether an OFC should be regarded as having met the NCH condition, after taking into account all the relevant circumstances including whether the failure was temporary.</p>	
011713 – 012320	Chairman Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AK — Assessable profits of open-ended fund companies regarded as assessable profits of resident person</i></p> <p>The Chairman enquired about the implementation of the deeming provisions:</p> <p>(a) whether the resident person concerned was required to proactively make declaration on the deemed assessable profits; and</p> <p>(b) the handling of tax assessment under the proposed new section 20AK(7) where a resident person was liable to tax in respect of the profits of an OFC by having an indirect beneficial interest in the company through one or more interposed person(s) and one or more of these interposed person(s) was a non-resident person.</p> <p>The Administration responded that:</p> <p>(a) in the tax return form, there would be an item which required declaration of deemed</p>	

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		<p>assessable profits of resident persons derived from OFCs (now applicable to offshore funds); and</p> <p>(b) the proposed new section 20AK(7) aimed to avoid double taxation such that a resident person, who had an indirect beneficial interest in the OFC through an interposed person or through a series of two or more interposed persons, could be discharged from the person's liability to tax in respect of the profits in case any of the interposed person was a resident who was also liable to tax in respect of the profits of the OFC.</p>	
012321 – 012611	Chairman Administration	<p><u>Clause 4 — Sections 20AG to 20AL added</u></p> <p><i>20AL — Losses from section 20AH(1) transactions and non-Schedule 16A transactions</i></p> <p>Proposed amendments to the new section 20AL consequential to the proposed changes to the new section 20AH</p> <p>Members raised no queries.</p>	
012612 – 012651	Chairman Administration	<p><u>Clause 5 — Schedule 15B added</u></p> <p>Members raised no queries.</p>	
012652 – 013030	Chairman Administration	<p><u>Clause 6 — Schedules 16A and 16B added</u></p> <p>Proposed amendments to the new Schedule 16A to remove the ring-fencing feature in the Bill such that investments in both local and overseas private companies would be considered as qualifying transactions for profits tax exemption.</p> <p>The Chairman urged the Administration to review if similar ring-fencing feature existed in the current tax regime for offshore privately offered funds and make appropriate legislative amendments as soon as possible.</p>	
013031 – 013306	Chairman ALA2 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>Discussion on drafting issues</p>	

Time marker	Speaker	Subject(s)	Action required
013307 – 013458	Chairman	The Bills Committee completed the scrutiny of the Bill. Legislative timetable	

Council Business Division 1
Legislative Council Secretariat
17 April 2018