

Inland Revenue (Amendment) (No. 4) Bill 2017

Proposed extension of profits tax exemption to
onshore privately offered open-ended fund companies
("OFCs")

20 July 2017



Hong Kong's Fund Industry

- A fast growing sector: combined fund management business in Hong Kong amounted to \$18,293 billion at end-2016
 - Publicly offered funds (March 2012 to March 2017): total number authorised by the Securities and Futures Commission (“SFC”) grew by 11% to 2 203; number domiciled in Hong Kong grew by 90% to 735
 - Hedge funds (privately offered funds) (2010 to 2014): number managed by SFC-licensed managers grew by 45% to 778



The OFC Regime

- To promote further development of the industry: introduction of the OFC regime
 - Securities and Futures (Amendment) Ordinance 2016 (“2016 Amendment Ordinance”) passed by LegCo in June last year
 - Put in place the legal framework for OFC as a form of fund vehicle
- Must register with the SFC, the principal regulator of OFCs
 - SFC to set out the operational and procedural details in subsidiary legislation and code
 - Must have an investment manager licensed or registered for the SFC’s Type 9 (asset management) regulated activity
 - Investment scope should align with Type 9 regulated activity



Existing Taxation Regime

- OFCs are subject to the current taxation regime applicable to funds as follows -

	Offshore	Onshore
Publicly offered	Exempted	Exempted
Privately offered	Exempted	Not exempted

- Onshore privately offered OFCs are not tax-exempt under the existing taxation regime. They may choose to stay offshore because of the disparity in tax treatment
- Financial Secretary announced in the 2017-18 Budget that profits tax exemption would be extended to onshore privately offered OFCs



Proposal – Key Points

Four Conditions

1. Onshore

- Central management and control must be exercised in Hong Kong

2. Non-closely held (“NCH”) – an eligible OFC should not be closely held

- A minimum number of investors required (so that the OFC is not controlled by a small number of investors)
- A threshold of participation interest imposed (so that the OFC is not controlled by a small number of investors)
- A minimum investment amount for various types of investors required (so that fund has a reasonable size)

3. Can only invest in permissible asset classes specified by the SFC, but with a degree of flexibility (10% *de minimis* limit)

4. Transactions carried out through or arranged by a qualified person (as required by the 2016 Amendment Ordinance) in Hong Kong



Safe Harbour Rules

- To cater for actual operational needs, we propose to implement safe harbour rules
- OFCs can seek exemption from Commissioner of Inland Revenue from meeting the NCH condition and/or the 10% *de minimis* limit:
 - during winding down of activities and investments
 - due to temporary and out-of-control circumstances
 - due to market fluctuations or circumstances that significantly reduce the value or amount of assets



Anti-abuse Measures

- With defined investment scope
- A resident person who, alone or jointly with his associates, holds direct and/or indirect beneficial interest of 30% or more in a tax-exempt OFC will be deemed to have derived assessable profits (same arrangement for the offshore fund tax regime)
- Consideration or remuneration received by an investment manager would be chargeable to profits tax



Way Forward

- Upon passage of the bill, the profits tax exemption will be implemented in tandem with the commencement of the OFC regime (currently planned for 2018)



Thank You

