

Hon Kenneth Leung
Chairman
The Bills Committee
Legislative Council
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

Attention: Clerk of Bills Committee

20 February 2018

Dear Sir

Inland Revenue (Amendment) (No.6) Bill 2017 (“the Bill”)

The international tax landscape has been evolving rapidly through the collaborative effort of different international bodies, such as the Group of Twenty (“G20”) and the Organisation for Economic Co-operation and Development (“OECD”) who called for cooperation among its member states to counter Base Erosion and Profit Shifting (BEPS) of enterprises.

To reinforce Hong Kong as an international financial centre and being a responsible member of the international community, ACCA (the Association of Chartered Certified Accountants) shares the view that Hong Kong has to put in place a tax system in line with international tax practices, incorporating clear and proper guidelines and documentations on transfer pricing.

We are delighted that many of our recommendations in our previous submissions on the general Transfer Pricing policy in 2015 and on measures to counter BEPS in 2016 have been taken into account in the Bill.

While we support the overall scheme of introducing measures to counter BEPS, we have the following comments:

1. Scope of transfer pricing

Under section 50AAD(1), it stipulates that the transfer pricing provisions apply in determining a person’s liability for property tax, salaries and profits tax.

A simple and effective tax system has been contributing to the long term success of the economy of Hong Kong. While we support the incorporation of transfer pricing rules in Hong Kong tax laws to put Hong Kong in line with international tax practices, we should maintain the underlying principle for a 'simple and effective' tax system. Moreover applying transfer pricing rules to salaries and property taxes is expected to create unnecessary compliance burden to small and medium enterprises which are usually owned by individuals who are involved in their management. Oftentimes these owner-managers receive a small amount of salaries or even no salaries at all, especially at the start-up stage of the business.

The tax implications / disputes on transfer pricing often arise from complex transactions between associated business entities, not small and medium domestic businesses. To avoid overly complicating the overall tax system of Hong Kong and to help ensure a smooth implementation of the transfer pricing rules at its start, we suggest excluding salaries tax and property tax in the transfer pricing regime. We trust that this practice should comply with the minimum standards required by the OECD.

2. Relief for foreign tax payable in non-DTA and DTA territory

According to Section 50AA(1), where foreign tax payable in a non-DTA territory outside Hong Kong on any income, profits or gains (relevant income), a person is entitled to the relief under section 8(1A)(c) by way of exclusion of any amount of the relevant income (for salaries tax purposes) or section 16(1)(c) by way of deduction of any amount of the foreign tax (for profits tax purposes). However, where foreign tax payable is in a DTA territory, relief is only available by way of credit and deduction of any amount of the foreign tax under section 50.

The purpose of having tax treaties in place is to allocate taxing rights between two jurisdictions and to deal with double taxation issues when arises. Whether to exercise the taxing rights allocated is at the discretion of the jurisdiction. The relief by the way of credit agreed in tax treaties is to handle the situation where double taxation arises to avoid taxpayers being taxed twice on the same income in two different tax jurisdictions. Hence the treatments under the domestic law (that is the Inland Revenue Ordinance) should always be available to taxpayers with or without treaties. The restriction proposed by the Bill will make the tax position of a person in Hong Kong who pays foreign tax in DTA territory worse off in any case as compared to a person who pays foreign tax in non-DTA territory.

For these reasons, we recommend the same reliefs be available for foreign tax payable in DTA and non-DTA territory.

3. Exemption for tax neutral transactions

We are pleased that the thresholds for exempting enterprises from the preparation of local file and master file purposes under section 58(4) are raised in response to our submission in 2016. However, we reiterate our view that tax neutral transactions between domestic related parties with same tax profiles should also be exempt. Without any group relief available under Hong Kong tax laws, such transactions between domestic companies generally will only be tax neutral to both the taxpayers and the government and will not result in any overall tax benefits. Excluding these transactions will help reduce an undue compliance burden on taxpayers.

4. Sums derived from intellectual property by non-Hong Kong resident associates

The proposed section 15F stipulates that the part of the relevant sum that is attributable to the person's value creation contributions in Hong Kong (attributable amount) is to be regarded as a trading receipt arising in or derived from Hong Kong by a person from a trade, profession or business carried on in Hong Kong and the person is accordingly chargeable to profits tax in respect of the attributable amount.

However, the proposed section 50AAF, the arm's length principle applicable to all types of transactions between associated persons including those related to the value creation functions related to intellectual property, should be able to be used by the tax administration to deal with abusive situations. Moreover there are unpredictable situations arising from the application of the proposed section 15F. To avoid duplication and further complication, we recommend that the proposed section 15F be removed in the Bill.

5. The range of the arm's length amount

Under Section 50AAF Rule 1(1), the advantaged person's income or loss is to be computed as if the arm's length provision had been made or imposed instead of the actual provision. The amount of income or loss computed in accordance with this subsection is referred to as 'the arm's length amount'.

We are of the view that the ultimate agreeable transfer price can be subjective, which can depend on specific facts and other available comparable data. As a result, any agreeable transfer price could fall within a reasonable range rather than being a specific amount. As such, we recommend that the wordings be revised to reflect an amount acceptable within a range based on an arm's length principle instead of a

specific amount which is literally interpreted with the word “the” in the current wordings.

6. Timeline for preparing the master file and local file

According to the proposed section 58C(2), the Hong Kong entity must prepare the master file and local file within 6 months after the end of each accounting period of the entity. The tax filing deadline for a majority of Hong Kong companies with a December year end currently is 15 August, which is seven and half months from the year end date. We consider that the deadline of preparing master file and local file should not be earlier than the tax filing deadline in order to ensure proper and consistent data in all documents.

7. Reimbursement of expenses for mutual agreement procedure (MAP) and arbitration under double taxation arrangement

Under 50AAB(3), if a taxpayer presents a case for mutual agreement procedure under double taxation arrangements made in relation to a DTA territory, with or without arbitration, the Commissioner may request the taxpayer to pay any costs and reasonable expenses incurred by the Commissioner in relation to the mutual agreement procedure and, if an issue in the case is further referred for arbitration, in relation to the arbitration; or to reimburse the Commissioner for the costs and expenses.

We suggest that a cap of the costs and expenses be imposed in relation to the mutual agreement procedure in order to enable tax certainty to taxpayers for their business planning purposes.

8. Data for the Country-by-country Reporting

According to Section 58E(1), a Hong Kong ultimate parent entity of a reportable group is required to file country-by-country returns (CbC).

Multinational business groups often have subsidiaries operating in different jurisdictions, where these subsidiaries may, under local legislative requirements, compile their financial statements in accordance with their local accounting standards which may have some variations from the International Financial Reporting Standards (IFRS). In order to assist the Hong Kong ultimate parent entities of multinational business groups in converting the accounting information from different countries for the preparation of their CbC returns, it would be helpful if the Inland Revenue Department will issue a DIPN or guidance on its website in this regard.

Should there be any questions, please do not hesitate to contact the undersigned at 2973 1108.

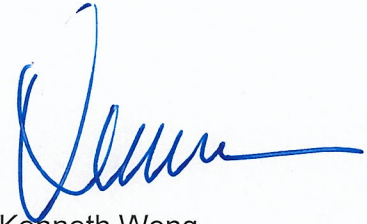
Yours faithfully



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