

Clerk to Bills Committee  
Legislative Council Secretariat  
Legislative Council Complex  
1 Legislative Council Road  
Central, Hong Kong

1 June 2018

Dear Sir

**Inland Revenue (Amendment) (No. 3) Bill 2018 (the Bill)**

On behalf of ACCA (Association of Chartered Certified Accountants) Hong Kong, we would like to submit our views in relation to the abovementioned Bill.

In general, the provisions in the Bill appear to be complicated in the way it is drafted. This makes it difficult for taxpayers to understand and hence imposes a perception that taxpayers are discouraged to claim any super deduction of research and development (R&D) expenses. This will ultimately defeat the whole purpose of the proposed incentive of encouraging more R&D activities in Hong Kong.


In respect of the application of the proposed provisions, we would like to highlight the following:

**R&D expenditure paid / incurred under subcontracting arrangements**

We note that under the current Inland Revenue Ordinance (IRO) provisions as well as the proposed provisions in the Bill, R&D expenditure if paid to subcontractors other than designated research institutions is not eligible for either normal deduction under the current IRO or enhanced deduction under the Bill.


We are of the view that the scope of enhanced tax deduction for R&D expenditure should be expanded to include R&D activities subcontracted to group companies or unrelated parties regardless of whether they are designated research institution so far as the R&D activities are conducted by the subcontractors in Hong Kong. This helps achieve the ultimate aim of the proposed incentive and can encourage more investments in R&D activities to support the diversification of Hong Kong's economic structure.

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In addition, we reiterate our proposal in our Budget Proposal submitted to the Financial Secretary that normal tax deduction should also be allowed for R&D expenditure paid to subcontractors, no matter whether the R&D activities are conducted in-house by the taxpayer or outsourced to a third party which may not be an approved research institute or designated local research institution.

### **Co-ownership of IP rights under a Cost Sharing Arrangement (CSA)**

The Bill requires that any rights generated from the R&D activities have to be “fully vested” in the person claiming a tax deduction on the expenditure incurred on the R&D activities. However, under a CSA on R&D where a company jointly conducts R&D with other companies within a group, the resulting rights will usually be co-owned by all the participants under the CSA.

We consider that under this scenario, with the underlying rationale of the proposed incentive, the R&D expenditure incurred by the taxpayer under the CSA should be allowed for the enhanced deduction. However, we are of the view that clarification is required on whether under this scenario, the condition of “fully vested” can still be met.

### **Director remuneration**

Under section 12(5) of the Bill, expenditure in relation to an employee excludes any remuneration of a director, which includes any salaries, wages and any other benefits. We are unsure about the rationale of such restriction as under commercial practice, an individual can play a dual role as a director for decision making as well as an employee engaged in the R&D activities.

As such, we recommend that such condition be revisited and an appropriate proportion of the expenditure related to an individual who is a director but engaged in the R&D activities be allowed in the qualifying expenditure.

**One of the main purposes test**

Under section 14 of Schedule 45 in the Bill, the “one of the main purposes” test is introduced to disallow any deduction where the main purpose or one of the main purposes of an arrangement is to enable the person to obtain the deduction.

We consider that the general anti-avoidance rule under section 61A of the IRO should be sufficient to address any abuse of the claim under Schedule 45, and hence this may not be required in the proposed provisions to avoid any complication of the law.

Should there be any questions, please do not hesitate to contact the undersigned at 2973 1113.

Yours faithfully



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