

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance (Chapter 112)

INLAND REVENUE (AMENDMENT) (NO. 6) BILL 2017

INTRODUCTION

A At the meeting of the Executive Council on 21 November 2017, the Council ADVISED and the Chief Executive ORDERED that the Inland Revenue (Amendment) (No. 6) Bill 2017 (“the Bill”), at **Annex A**, should be introduced into the Legislative Council (“LegCo”).

JUSTIFICATIONS

2. Base Erosion and Profit Shifting (“BEPS”) refers to exploitation of the gaps and mismatches in tax rules by multinational enterprises (“MNEs”) to artificially shift profits to low or no-tax locations where there is little or no economic activity. The Organisation for Economic Co-operation and Development (“OECD”) has estimated that global tax revenue losses due to BEPS range from USD100 billion to USD240 billion a year. The OECD released a package of 15 action plans in October 2015 to counter BEPS. In June 2016, Hong Kong indicated its commitment to implementing the BEPS package.

3. A consultation exercise we conducted in late 2016 revealed broad support for our proposed implementation strategy, which focuses on the codification of the transfer pricing principles into the Inland Revenue Ordinance (Cap. 112) (“IRO”) and the four minimum standards of the BEPS package, i.e. imposing country-by-country (“CbC”) reporting requirements, improving the cross-border dispute resolution mechanism, countering harmful tax practices and preventing treaty abuse, as well as measures of direct relevance to their implementation. The majority of respondents also agreed that we should uphold Hong Kong’s simple and low tax regime; that a pragmatic approach should be adopted so as to minimise the compliance burden on businesses, particularly small and medium enterprises; and that the changes should be implemented in a progressive manner. We issued a report on the outcome of the consultation

in July 2017. The key elements of the legislative proposals are set out below.

Transfer Pricing Regulatory Regime

4. Transfer pricing refers to the setting of prices for transactions of goods, services and intangible property between associated enterprises. The internationally agreed standard for setting transfer prices is the arm's length principle. At present, the Inland Revenue Department ("IRD") relies on the general provisions in the IRO and its Departmental Interpretation and Practice Notes ("DIPNs") to deal with transfer pricing issues. IRD has all along been applying the arm's length principle to transactions between associated enterprises in accordance with the OECD's guidelines.

5. We propose to codify the OECD's transfer pricing rules into the IRO so that the transactions between associated enterprises in Hong Kong will be taxed on the basis that they are effected at arm's length. The proposed fundamental transfer pricing rule ("fundamental rule") requires an adjustment of the profits or losses of an enterprise where the actual provision made or imposed between two associated persons¹ departs from the provision which would have been made between independent persons and that has created a tax advantage.

6. We propose to apply the fundamental rule to cases where the affected persons are associated, including transactions of assets and services as well as financial and business arrangements between different parts of an enterprise, such as between head office and a permanent establishment. Given the unique nature of intellectual property ("IP") and the lack of comparables, we propose to introduce specific provisions in the IRO to ensure that a person carrying out the functions of development, enhancement, maintenance, protection or exploitation for an IP in Hong Kong will be taxed on the basis of that person's contribution in carrying out such functions.

7. To ensure compliance with the fundamental rule, we propose to introduce an administrative penalty relating to transfer pricing. Noting that transfer pricing is not an exact science and having regard to international practices, we propose to set the administrative penalty at a level lower than the existing one for other non-compliances under section 82A of the IRO. Specifically, the taxpayer will be liable to an administrative penalty by way

¹ Two persons are associated where one person is directly or indirectly participating in the management, control or capital of the other person, or a third person is so participating in the same of both persons.

of additional tax not exceeding the amount of tax undercharged (vis-à-vis an amount trebling the tax undercharged, as currently imposed for incorrect return and other matters under section 82A of the IRO). That said, we will not rule out the possibilities of imposing more stringent penalty or initiating criminal prosecutions on blatant cases in accordance with relevant provisions of the IRO.

8. IRD has been implementing an advance pricing arrangement (“APA”) regime which seeks to provide enterprises with an opportunity to reach prior agreement with IRD on the method of applying the arm’s length principle to major or material transactions or arrangements between associated enterprises. With the implementation of statutory transfer pricing rules, we anticipate a rising demand for APAs, particularly for high-value transactions within large enterprise groups. We therefore propose to put in place a statutory APA regime to cater for unilateral, bilateral and multilateral APAs². We will set out the key provisions in the IRO and elaborate the details in the DIPNs of IRD.

Transfer Pricing Documentation and CbC Reporting

Master File and Local File

9. We propose to mandate the relevant enterprises in Hong Kong to prepare the transfer pricing documentation, namely master file, local file and CbC report³. This three-tier standardised approach requires an enterprise to articulate consistent transfer pricing position and provide the tax administration with useful information for assessing transfer pricing risks.

10. As regards the preparation of master file and local file, we propose to provide exemption so as to minimise compliance burden on the business sector. Specifically, an enterprise engaging in transactions with associated

² Unilateral APAs involve agreement between the taxpayer and one tax administration. Meanwhile, taxpayers may also enter into APAs with more than one tax administration, i.e. bilateral or multilateral APAs, through the mutual agreement procedure under Comprehensive Avoidance of Double Taxation Agreements (“CDTAs”).

³ A **master file** gives high-level overview of the group of enterprises, including the global business operations, transfer pricing policies and global allocation of income. A **local file** provides detailed transactional transfer pricing information specific to the enterprise in each jurisdiction, including details of material related party transactions or arrangements undertaken by the enterprise and associated enterprises involved, amount involved in those transactions or arrangements and transfer pricing analysis with respect to those transactions or arrangements. A **CbC report** sets out the amounts of revenue, profits and tax paid as well as certain indicators of economic activity such as number of employees, stated capital, retained earnings and tangible assets for each jurisdiction in which an MNE group operates.

enterprises will **not** be required to prepare a master file and a local file if they can meet **either one** of the following exemption criteria –

(a) Exemption based on size of business

An enterprise which satisfies **any two** of the conditions below will **not** be required to prepare a master file and a local file –

- (i) total annual revenue not more than HK\$200 million;
- (ii) total assets not more than HK\$200 million; and
- (iii) not more than 100 employees.

(b) Exemption based on value of related party transactions

If the amount of a category of related party transactions for the relevant accounting period is **below** the prescribed threshold, an enterprise will **not** be required to prepare a local file **for that particular category of transactions** –

- (i) transfers of properties (other than financial assets and intangibles): HK\$220 million;
- (ii) transactions in respect of financial assets: HK\$110 million;
- (iii) transfers of intangibles: HK\$110 million; and
- (iv) any other transactions (e.g. service income and royalty income): HK\$44 million.

If an enterprise is fully exempted from preparing a local file (i.e. its related party transactions of **all categories** are **below** the prescribed thresholds), it will **not** be required to prepare a master file either. This exemption criterion follows the Mainland's exemption threshold for related party transactions.

11. In line with the prevailing retention requirement for business records under section 51C of the IRO, relevant enterprises will be required to retain master files and local files for not less than seven years after the end of the relevant accounting period. The information to be included in the master files and local files are specified in the Bill, whilst the operational details will be set out in a DIPN of IRD as appropriate.

CbC Reporting

12. As mandated by the OECD, MNEs with annual consolidated group revenue not less than EUR750 million (or HK\$6.8 billion) would be required to file CbC reports. We propose to impose the primary obligation of filing CbC reports on the ultimate parent entities of MNEs that are resident in Hong Kong. Constituent entities of MNEs in Hong Kong could be subject to a **secondary filing obligation** if the ultimate parent entity is in a jurisdiction that does not require the filing of CbC reports or does not exchange such reports with Hong Kong. In such circumstances, an MNE group may also be allowed, under the **surrogate filing arrangement**, to authorise a constituent entity in Hong Kong to file CbC reports to IRD on behalf of the group for exchange with other jurisdictions. The proposed filing requirement will apply to an accounting period commencing on or after 1 January 2018. Given that some jurisdictions have implemented CbC reporting since 2016, we will introduce a **voluntary filing arrangement** whereby the ultimate parent entity of an MNE group that is resident in Hong Kong would be allowed to voluntarily submit its CbC reports in respect of an accounting period commencing between 1 January 2016 and 31 December 2017 to IRD for exchange with other jurisdictions, with a view to relieving the constituent entities of the MNE group in overseas jurisdictions of the secondary filing obligation for that accounting period.

13. Modelled on the arrangements for financial institutions in respect of the Automatic Exchange of Financial Account Information in Tax Matters, which has already been put in place in Hong Kong by legislation, we propose to allow a reporting entity to engage a service provider to furnish a CbC report and give relevant notifications on its behalf. Penalty and offence provisions are made in respect of matters such as failing to file reports or notifications, providing misleading, false or inaccurate information, or omitting information in CbC reports furnished by the reporting entity. Some of the penalty and offence provisions will also apply to the service providers engaged by the reporting entity. We propose to ride on the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (“Multilateral Convention”)⁴ as the main platform for exchanging CbC reports with other jurisdictions. Signatory

⁴ The multilateral route is more efficient and effective than the bilateral approach that Hong Kong has relied on so far. The Central People’s Government has given in-principle approval for extending the application of the Multilateral Convention to Hong Kong. We introduced into LegCo on 18 October 2017 an amendment bill for, amongst others, empowering the Chief Executive in Council to give effect to the Multilateral Convention in Hong Kong. The bill is currently under scrutiny by LegCo.

jurisdictions of the Multilateral Convention and the relevant competent authority agreements need to observe requirements in respect of protection of personal data, confidentiality and appropriate use of the information exchanged. The OECD will conduct reviews to ensure compliance with such requirements. IRD may also suspend exchange of information if there is significant non-compliance by another tax authority.

Dispute Resolution Mechanism

14. Jurisdictions may at times have divergent views on the interpretation and application of BEPS measures. We anticipate that there will be more treaty-related disputes requiring resolution via the mutual agreement procedure (“MAP”)⁵ or arbitration. To ensure effective and efficient resolution of these disputes in a timely manner, we propose to put in place a statutory dispute resolution mechanism to replace the current mechanism which relies on administrative rules in the DIPNs of IRD. The statutory dispute resolution mechanism will encompass the following features –

- (a) a taxpayer may present a case for MAP and/or arbitration under the relevant CDTA;
- (b) the Commissioner of Inland Revenue (“the Commissioner”) may give a notice requiring the taxpayer to provide information regarding the case;
- (c) the Commissioner may request the taxpayer to reimburse or pay any costs and reasonable expenses incurred in the course of the MAP and arbitration; and
- (d) the Commissioner must give effect to any solution unilaterally arrived at by the Commissioner or agreement reached with the other tax authority concerned in the course of the MAP or arbitration, and any decision delivered by arbitrators in the case of arbitration.

Double Taxation Relief

15. With the implementation of statutory transfer pricing rules and continued expansion of the CDTA network, we envisage that more claims

⁵ Under MAP, where a taxpayer considers that the actions of one or both contracting parties result in taxation not in accordance with the CDTA, he is allowed to present the case to the tax authority of his resident jurisdiction. If the case cannot be resolved **unilaterally** by the tax authority of the resident jurisdiction, the tax authorities of both sides will endeavour to resolve the case by **mutual agreement**.

for relief from double taxation⁶ by way of tax credit will be lodged in the future. We propose to enhance the current tax credit system by –

- (a) extending the period for claiming tax credit from two years to six years⁷;
- (b) requiring a taxpayer to minimise its foreign tax liability by making full use of all other available relief under CDTAs and the local legislation of foreign jurisdictions before resorting to tax credits; and
- (c) mandating taxpayers to notify IRD of any adjustment to their foreign tax payments which may result in tax credit granted being excessive.

Amendments to preferential tax regimes

16. The OECD has all along reviewed preferential tax regimes relating to income from geographically mobile activities (such as financial and other service activities) of all participating jurisdictions. In determining whether a preferential tax regime fails to meet the international standards on countering BEPS, the OECD would take into account a number of factors, including whether the regime is ring-fenced from the domestic economy⁸ and whether it meets the substantial activities requirement⁹. Meanwhile, the European Union (“EU”) released a list of “non-cooperative” tax jurisdictions on 5 December 2017 and fair taxation is one of the evaluation criteria¹⁰. For non-cooperative tax jurisdictions identified by the OECD and the EU, they could be subject to defensive

⁶ At present, Hong Kong provides for relief from juridical double taxation in relation to CDTA states by way of tax credit under section 50 of the IRO. Juridical double taxation occurs where the profits of a Hong Kong enterprise arising from its operation in a CDTA state are adjusted upwards without a corresponding downward adjustment in the same enterprise’s profits from its operation in Hong Kong.

⁷ The extended period for claiming tax credit would be the same as the current time limit for correction of assessment due to error or omission under section 70A of the IRO.

⁸ Ring-fencing occurs when the applicability of a preferential regime is limited to foreign transactions. In such circumstances, the tax base of the jurisdictions from which the geographically mobile activities are attracted will be eroded, whilst the domestic tax base of the jurisdiction providing the regime will not be affected.

⁹ To meet the substantial activities requirement mandated by the OECD, a jurisdiction should provide tax concessions only to qualifying taxpayers who undertake core income generating activities in that jurisdiction.

¹⁰ On 5 December 2017, the EU published a list of non-cooperative tax jurisdictions. 17 jurisdictions were included in the list for failing to meet the EU’s requirements on fair taxation, tax transparency and implementation of anti-BEPS standards. The list will be updated at least once a year.

measures in both tax and non-tax areas. The measures include imposition of withholding tax, non-deductibility of cost, etc. It is essential for Hong Kong to meet the requirements of the OECD and the EU so as to maintain our reputation as an international financial centre.

17. To meet our commitments made to the OECD and the EU, we propose to amend three tax regimes which were introduced to promote the development of corporate treasury centres (“CTC”), professional reinsurance and captive insurance. At present, only profits derived from foreign transactions are entitled to the half-rate concessions under these regimes. We propose to revise these three tax regimes by extending the half-rate concessions to profits derived from domestic transactions. The revised regimes will become effective from the year of assessment 2018/19 onwards.

18. As regards the substantial activities requirement, the OECD expects that qualifying taxpayers should employ an appropriate number of full-time qualified employees and at least incur a specified amount of operating expenditure in the jurisdiction that offers the tax concessions. In this connection, we propose to incorporate the substantial activities requirement in the tax regimes for CTC, professional reinsurers, captive insurers, ship owners, aircraft lessors and aircraft leasing managers. After the relevant bureaux have consulted their stakeholders on the detailed arrangement, the Commissioner will specify the detailed thresholds (i.e. minimum number of full-time qualified employees and minimum amount of operating expenditure), which are applicable to all taxpayers who enjoy the tax concessions, in a notice to be published in the Gazette. Such notice is a piece of subsidiary legislation, which will be subject to negative vetting by the LegCo.

OTHER OPTIONS

19. We must amend the IRO in order to give effect to the proposals above. There is no other viable option.

THE BILL

20. The main provisions of the Bill are as follows –

(a) **Clause 9** adds a new Part 8AA to the IRO to the effect as follows –

- (i) Apart from defining relevant terms, Division 1 applies Part 8AA to determining property tax, salaries tax and profits tax and requires the Part to be read in a way that best secures consistency between its effect and the effect given to Articles 7 and 9 of the Model Tax Convention on Income and on Capital (“Model Tax Convention”) approved by the OECD;
 - (ii) New Division 2 of the new Part 8AA incorporates the international transfer pricing rules. A person’s tax liability under the IRO is to be determined on the basis that the person’s transactions with an associated person are effected at arm’s length. A person who would have a Hong Kong tax advantage if taxed on the basis of a non-arm’s length provision (“advantaged person”) will have income adjusted upwards or loss adjusted downwards¹¹. Similarly, the income of an enterprise attributable to its permanent establishment in Hong Kong is to be determined as if the permanent establishment were a distinct and separate enterprise. Schedule 17G (added by Clause 10) contains rules for determining whether a person has a permanent establishment in Hong Kong;
 - (iii) Division 3 of the new Part 8AA provides that, after adjustment to tax assessment is made on the advantaged person to reflect the arm’s length provision, corresponding relief may be applied for by the disadvantaged person (which means the person who would suffer a tax disadvantage if taxed on the basis of the non-arm’s length provision) to avoid double taxation. Similar relief applies in relation to transactions between parts of an enterprise in different territories; and
 - (iv) Under Division 4 of the new Part 8AA, a person and the Commissioner may, by an APA, agree in advance on a method for resolving pricing issues for the purposes of the above transfer pricing rules. The new Schedule 17H (added by Clause 10) supplements Division 4 by providing for an application for an APA and fees payable for the application;
- (b) **Clause 13** adds a new section 15BA to the IRO to provide for adjustments to taxable profits or allowable losses to reflect any appropriation from or into trading stock or any acquisition or

¹¹ The expression *provision* is broadly equivalent to the expression *condition made or imposed* in Article 9 of the Model Tax Convention.

disposal of trading stock other than in the course of trade at market value;

- (c) **Clause 14** adds a new section 15F to the IRO. A person who has contributed in Hong Kong to the development, enhancement, maintenance, protection or exploitation of an IP will be taxed on such part of the sum accruing in respect of its exhibition or use or related rights as is attributable to the contribution even if the sum accrues to the person's associate;
- (d) **Clauses 16 and 17** add a new Part 9A and a new Schedule 17I to the IRO to provide for requirements for transfer pricing documentation –
 - (i) Division 2 of the new Part 9A (i.e. the new section 58C) requires a Hong Kong entity of a group in the extended sense to prepare, for each accounting period, a master file and a local file and to retain the files for 7 years. More specifically, the term “group in the extended sense” essentially means a collection of enterprises (whether all or any of them are local enterprises) required to prepare consolidated financial statements for financial reporting purposes under applicable accounting principles but is taken to cover a single enterprise in a territory if the enterprise carries on business through a permanent establishment in another territory;
 - (ii) The new Schedule 17I specifies criteria for exemption from the requirement to keep files based on size of revenue and assets and number of employees of the entity concerned or the value of controlled transactions (as defined in that Schedule). It also specifies information about the group and the entity itself that must be contained in the master file and local file; and
 - (iii) Division 3 of the new Part 9A gives effect to the OECD's CbC reporting requirements –
 - (1) Under the new section 58D, the requirements for filing a CbC return only apply to a reportable group (which means an MNE group whose annual consolidated group revenue reaches the specified threshold amount);
 - (2) The new sections 58E(1) and 58F set out requirements for the ultimate parent entity or other entities of a

reportable group to file CbC returns for each accounting period beginning on or after 1 January 2018 if the ultimate parent entity has, or the other entities have, a Hong Kong connection. As a transitional measure, the new section 58E(2) provides for voluntary filing of a CbC return by an ultimate parent entity resident in Hong Kong for an accounting period beginning on or after 1 January 2016 but before 1 January 2018;

- (3) The new section 58G empowers an assessor to require an entity to file a CbC return; and
 - (4) The new section 58H sets out requirements for filing a notification containing information relevant for determining the obligation for filing a CbC return;
- (e) **Clause 8** (in so far as it adds a new section 50AAB to the IRO) enables effect to be given to solutions resulting from the MAP and/or arbitration under CDTAs, resolving disputes arising under the agreements. The solutions can be agreed between the Commissioner and competent authorities of the territories concerned. The new section also provides for the Commissioner's related powers in requiring information and in seeking reimbursement for costs and reasonable expenses incurred;
 - (f) **Clauses 3 to 7 and Clause 8** (in so far as it adds a new section 50AA to the IRO) make miscellaneous amendments relating to existing unilateral double taxation relief and tax credit allowed under CDTAs;
 - (g) **Clauses 19 to 22** amend sections 80, 82 and 82A of the IRO and add new sections 80G to 80J to the IRO to provide for offences and additional tax for failure to comply with the requirements under new sections 50AA and 50AAB, and Parts 8AA and 9A, or for providing misleading, false or inaccurate information or omitting to provide information in connection with those provisions;
 - (h) **Clause 23** amends the fees for an application for advance ruling under section 88A of the IRO; and
 - (i) **Clauses 24 to 32** amend the requirements relating to certain preferential tax regimes so as to meet the international standards promulgated by the OECD –

- (i) **Clauses 24 to 26 and 29 to 30** amend the IRO to revise the preferential tax regimes to extend the profits tax concessions to authorized captive insurers, professional reinsurers and CTCs in respect of their domestic profits. The application of the anti-abuse provisions in section 16 of the IRO is also extended to situations where profits tax concessions are claimed under section 14B or 14D of the IRO; and
- (ii) **Clause 32** adds a new section 26AB to the IRO to provide that profits tax concessions under sections 14B, 14D, 14H, 14J and 23B of the IRO are available only if the threshold requirement is met. The Commissioner is empowered to prescribe the threshold requirement by a notice published in the Gazette.

LEGISLATIVE TIMETABLE

21. The legislative timetable is as follows –

Publication in the Gazette	29 December 2017
First Reading and commencement of Second Reading debate	10 January 2018
Resumption of Second Reading debate, committee stage and Third Reading	To be notified

IMPLICATIONS OF THE PROPOSAL

22. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. The proposal will not affect the binding effect of the existing provisions of the IRO and its subsidiary legislation. It has no environmental, gender, family, productivity or sustainability implications. The economic, financial and civil service implications of the proposal are set out in **Annex B**.

B

PUBLIC CONSULTATION

23. We conducted a consultation exercise from 26 October to 31 December 2016 on the legislative proposals to implement the BEPS package. A total of 26 written submissions from 23 organisations and

three individuals were received. During the consultation period, we also organised two engagement sessions with key stakeholders. There is broad support for the Government's proposal to introduce measures for complying with various BEPS-related requirements. We briefed the LegCo Panel on Financial Affairs on the legislative proposals in December 2016 and Panel members raised no objection to our proposals.

PUBLICITY

24. We will issue a press release on 27 December 2017. A spokesperson will be available to answer media and public enquiries.

BACKGROUND

25. The BEPS package was first launched by the Group of Twenty ("G20") and the OECD in 2013. The ultimate objective of the BEPS package is to restore public confidence in tax systems and level the playing field for businesses through international cooperation. G20 and the OECD have called on all countries and jurisdictions to join an inclusive framework for implementing the BEPS package. As at 14 December 2017, 110 jurisdictions, including Hong Kong, have joined the inclusive framework.

ENQUIRIES

26. Enquiries on this Brief can be addressed to Mr Stephen Lo, Principal Assistant Secretary for Financial Services and the Treasury (Treasury) at 2810-2317.

Financial Services and the Treasury Bureau
27 December 2017

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance
(Chapter 112)

INLAND REVENUE (AMENDMENT) (NO. 6) BILL 2017

ANNEXES

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Annex B	Economic, Financial and Civil Service Implications of the Proposal

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A BILL

To

Amend the Inland Revenue Ordinance to codify rules on transfer pricing to require income or loss from provision between associated persons (or between parts of the same enterprise in different territories) to be computed, for tax purposes, on an arm's length basis; to provide for an advance pricing arrangement regime under which how the rules apply may be agreed before transactions take place; to require documentation relating to transactions; to enable effect to be given to mutual agreements made with other jurisdictions under arrangements for relief from double taxation; to enhance the current provisions for double taxation relief; to adjust fees in respect of an application for advance ruling; to revise the requirements relating to profits tax concessions so as to meet the international standards promulgated by the Organisation for Economic Co-operation and Development; and for related purposes.

Enacted by the Legislative Council.

Part 1

Preliminary

1. Short title

This Ordinance may be cited as the Inland Revenue (Amendment) (No. 6) Ordinance 2017.

2. Enactments amended

- (1) The Inland Revenue Ordinance (Cap. 112) is amended as set out in Part 2.
- (2) The Inland Revenue Rules (Cap. 112 sub. leg. A) are amended as set out in Part 3.

Part 2

Amendments to Inland Revenue Ordinance

Division 1—Amendments Relating to Double Taxation

3. **Section 8 amended (charge of salaries tax)**

- (1) Section 8(1A)(c)—

Repeal

“territory outside Hong Kong”

Substitute

“non-DTA territory (as defined by section 48A)”.

- (2) After section 8(1B)—

Add

“(1C) Subsection (1A)(c) has effect subject to section 50AA.”.

4. **Section 16 amended (ascertainment of chargeable profits)**

- (1) Section 16(1)(c), before “tax of”—

Add

“subject to subsection (2J),”.

- (2) Section 16(1)(c)—

Repeal

“elsewhere”

Substitute

“in a non-DTA territory (as defined by section 48A)”.

- (3) Section 16(1)(c)—

Repeal the colon

Substitute a semicolon.

- (4) Section 16(1)(c)—

Repeal the proviso.

- (5) After section 16(2I)—

Add

“(2J) Subsection (1)(c) has effect subject to section 50AA.”.

5. **Section 48A added**

Before section 49—

Add

“48A. Interpretation of Part 8

In this Part—

double taxation arrangements (雙重課稅安排) means arrangements that—

- (a) are made with the government of a territory outside Hong Kong with a view to affording relief from double taxation; and
(b) have effect under section 49(1) or (1A);

DTA territory (有安排地區) means a territory outside Hong Kong with which double taxation arrangements have been made;

DTA territory resident person (有安排地區居民人士) means a person who is resident for tax purposes in a DTA territory;

Hong Kong resident person (香港居民人士) means a person who is resident for tax purposes in Hong Kong;

non-DTA territory (無安排地區) means a territory outside Hong Kong that is not a DTA territory;

resident for tax purposes (稅務居民) in relation to any double taxation arrangements, has the meaning given by the provisions of the arrangements relating to the determination of resident status.”.

6. Section 49 amended (arrangements for relief from double taxation and exchange of information)

(1) Section 49(1), after “this Ordinance”—

Add

“in accordance with subsection (1C)”.

(2) Section 49(1A)(a), after “this Ordinance”—

Add

“in accordance with subsection (1C)”.

(3) After section 49(1B)—

Add

“(1C) Arrangements specified in an order made under subsection (1) or (1A) have effect despite any provision in any enactment so far as the arrangements provide for—

- (a) affording relief from tax charged under this Ordinance;
- (b) taxing income, profits or gains of DTA territory resident persons arising in, or derived from sources in, Hong Kong;
- (c) taxing chargeable gains accruing to DTA territory resident persons on the disposal of assets in Hong Kong;
- (d) determining income, profits or gains to be attributed to DTA territory resident persons;

(e) determining income, profits or gains to be attributed to permanent establishments in Hong Kong of DTA territory resident persons; or

(f) determining income, profits or gains to be attributed to Hong Kong resident persons who have special relationships with DTA territory resident persons.

(1D) In subsection (1C)—

permanent establishment (常設機構) has the meaning given by section 50AAC(4);

special relationship (特殊關係) has the meaning given by subsection (1E).

(1E) A person has a special relationship with another person—

(a) if both persons are individuals and one of the persons is—

- (i) the other person’s spouse;
- (ii) a relative of the other person;
- (iii) a relative of the other person’s spouse; or
- (iv) the spouse of a person who falls within subparagraph (ii) or (iii); or

(b) if—

- (i) one of the persons is not an individual or both persons are not individuals; and
- (ii) the 2 persons are in a relationship by virtue of which the participation condition is met under section 50AAG.

(1F) In subsection (1E)—

relative (親屬), in relation to a person, means the parent, child, brother or sister of the person, and, in deducing such a relationship—

- (a) an adopted child is regarded as a child of both the natural parents and the adopting parents; and
- (b) a step child is regarded as a child of both the natural parents and any step parent.”.

7. Section 50 amended (tax credits)

(1) Section 50—

Repeal subsection (1)

Substitute

“(1) This section has effect if, under double taxation arrangements, tax payable in respect of any income in the DTA territory concerned is to be allowed as a credit against tax payable in respect of that income in Hong Kong.

(1A) In this section—

(a) *foreign tax* (外地稅款) means—

- (i) any tax—
 - (A) that is payable in respect of any income in a DTA territory; and
 - (B) that is, under the double taxation arrangements concerned, to be allowed as a credit against tax payable in respect of that income in Hong Kong; or
- (ii) any tax that would have been payable under the laws of a DTA territory but for relief—
 - (A) given under the laws of the territory with a view to promoting investment or

industrial, commercial, economic, scientific, educational or other development in the territory; and

(B) provided for in the double taxation arrangements concerned;

(b) *tax* (稅款), in relation to Hong Kong, means tax chargeable under this Ordinance; and

(c) *income* (收入), in relation to a DTA territory, includes profits and gains within the meaning of the double taxation arrangements concerned.

(1B) For the purposes of this section, *foreign tax* within the meaning of subsection (1A)(a)(ii) is treated as having been payable under the laws of the DTA territory concerned.”.

(2) Section 50(2), proviso—

Repeal

“resident in Hong Kong”

Substitute

“a Hong Kong resident person”.

(3) Section 50(3)—

Repeal

“arrangements having effect under section 49”

Substitute

“double taxation arrangements”.

(4) Section 50(4)—

Repeal

“arrangements having effect under section 49”

Substitute

“double taxation arrangements”.

- (5) Section 50(6)—

Repeal

“arrangements for the time being in force under section 49”

Substitute

“double taxation arrangements for the time being in force”.

- (6) Section 50—

Repeal subsection (9)

Substitute

- “(9) A claim for an allowance by way of credit may only be made before—

- (a) the end of 6 years after the end of the year of assessment; or
- (b) the end of 6 months after the date on which an assessment is made imposing liability or additional liability to tax in respect of the income on which foreign tax has been assessed,

whichever is the later.

- (9A) If a person makes a claim under subsection (9) for an allowance by way of credit and an assessor refuses to allow a credit pursuant to the claim, the assessor must give the person a written notice of the refusal and the person has the same rights of objection and appeal under Part 11 as if the notice were a notice of assessment.”.

- (7) Section 50—

Repeal subsection (10).

8. Sections 50AA and 50AAB added

Part 8, after section 50—

Add

“50AA. General provisions on relief from double taxation

- (1) This section applies if, in respect of tax (*foreign tax*) payable in a territory outside Hong Kong (*foreign territory*) on any income, profits or gains (*relevant income*), a person is entitled to any of the following relief (each of which is referred to in this section as *relief from double taxation*)—

- (a) if the foreign territory is a non-DTA territory—

- (i) relief under section 8(1A)(c) by way of exclusion of any amount of the relevant income; or
- (ii) relief under section 16(1)(c) by way of deduction of any amount of the foreign tax;

- (b) if the foreign territory is a DTA territory—relief under section 50 by way of credit and deduction of any amount of the foreign tax.

- (2) The amount of any relief from double taxation granted must not exceed the amount of the relief that would be granted had all foreign tax minimization steps been taken.

- (3) For the purposes of subsection (2)—

- (a) all foreign tax minimization steps are taken only if all reasonable steps are taken under—

- (i) the laws of the foreign territory; and
- (ii) if the foreign territory is a DTA territory—the double taxation arrangements concerned,

to minimize the amount of foreign tax payable in the foreign territory in respect of the relevant income; and

- (b) the reasonable steps mentioned in paragraph (a) include—
 - (i) claiming, or otherwise securing the benefit of, relief, deductions, reductions or allowances; and
 - (ii) making elections for tax purposes.
- (4) For the purposes of subsections (2) and (3), a question as to the steps which it would have been reasonable for a person to take is to be determined on the basis of what the person might reasonably be expected to have done in the absence of the relief from double taxation.
- (5) If—
 - (a) relief from double taxation has been granted to a person; and
 - (b) subsequently, the amount of the relief becomes excessive as a result of an adjustment to the amount of the foreign tax under the laws of the foreign territory,

the person must give the Commissioner written notice of the adjustment within 3 months after the adjustment is made.
- (6) If the amount of the relief from double taxation becomes excessive or insufficient by reason of an adjustment to the amount of the foreign tax or tax payable in Hong Kong, an assessment, additional assessment or claim to which the adjustment gives rise may be made before—
 - (a) the end of 2 years from the time when all assessments, adjustments and other determinations have been made, whether in the foreign territory or in Hong Kong, that are material in determining

whether any, and if so what, relief is to be granted; or

- (b) the expiry of the time limit for making an assessment, additional assessment or claim for relief under this Ordinance,

whichever is the later.

50AAB. Mutual agreement procedure and arbitration under double taxation arrangements

- (1) This section applies if a person (*taxpayer*) presents a case for mutual agreement procedure under double taxation arrangements made in relation to a DTA territory, with or without an issue in the case also being referred for arbitration under the arrangements.
- (2) The Commissioner may give a notice to the taxpayer requiring the taxpayer to provide information regarding the case that is in the possession, custody or control of the taxpayer.
- (3) The Commissioner may request the taxpayer—
 - (a) 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
 - (b) to reimburse the Commissioner for the costs and expenses.
- (4) Any amount payable or reimbursable under subsection (3) is recoverable as a civil debt due to the Government.
- (5) Subsection (6) applies if, for a case presented for mutual agreement procedure—
 - (a) the Commissioner arrives at a solution unilaterally;

- (b) the competent authorities of Hong Kong and the DTA territory reach a mutual agreement; or
- (c) after the case or an issue in the case is referred for arbitration—
 - (i) a solution is arrived at by the Commissioner unilaterally, or a mutual agreement is reached between the competent authorities of Hong Kong and the DTA territory, before a decision is delivered by the arbitrators; or
 - (ii) a decision is delivered by the arbitrators.
- (6) The Commissioner must give effect to the solution, agreement or decision (*MAP solution*) by making any adjustment (other than in relation to any additional tax, fines and penalties imposed under Part 14) that is appropriate as a result of the MAP solution, despite any provision in this Ordinance.
- (7) If the Commissioner considers it appropriate to do so having regard to a MAP solution, the Commissioner may adjust any additional tax imposed under Part 14 unless the Board of Review or the court has delivered a decision, opinion, determination or direction in respect of the assessment of the additional tax.
- (8) The Commissioner may decide the way in which an adjustment under subsection (6) or (7) is to be made, including by way of discharge or repayment of tax, the allowance of credit against tax payable in Hong Kong, or the making of an assessment.
- (9) In this section—
arbitrator (仲裁員) means a person who is appointed by mutual agreement between the competent authorities of

Hong Kong and the DTA territory concerned to conduct arbitration;

competent authority (主管當局) has the meaning given by the double taxation arrangements concerned.”.

Division 2—Amendments Relating to Transfer Pricing: Addition of New Part 8AA and Schedules 17G and 17H

9. Part 8AA added

After Part 8—

Add

“Part 8AA

Transfer Pricing Rules, Relief and Advance Pricing Arrangement

Note (with no legislative effect) providing an overview of Part 8AA—

1. Apart from defining relevant terms, Division 1 applies Part 8AA to determining property tax, salaries tax and profits tax and requires the Part to be read in a way that best secures consistency between its effect and the effect given to Articles 7 and 9 of the Model Tax Convention on Income and on Capital approved by the Organisation for Economic Co-operation and Development. The expression *provision* is broadly equivalent to the expression *condition made or imposed* in Article 9.
2. Division 2 incorporates the international transfer pricing rules and has the following effect—
 - (a) a person’s tax liability under this Ordinance is to be determined on the basis that a provision made or imposed between the person and the person’s associated person is made or imposed on an arm’s length basis;

- (b) in other words, a person who would have a Hong Kong tax advantage if taxed on the basis of a non-arm's length provision (*advantaged person*) will have income adjusted upwards or loss adjusted downwards;
 - (c) similarly, the income or loss of a non-Hong Kong resident person attributable to the person's permanent establishment in Hong Kong are to be determined as if the permanent establishment were a distinct and separate enterprise.
3. Division 3 provides that, after adjustment to tax assessment is made on the advantaged person to reflect the arm's length provision, corresponding relief may be applied for by the disadvantaged person (that is, the person who would suffer a tax disadvantage if taxed on the basis of the non-arm's length provision) to avoid double taxation. Similar relief applies in relation to transactions between parts of the same enterprise in different territories.
4. Under Division 4, a person and the Commissioner may, by an advance pricing arrangement, agree in advance on a method for resolving issues arising from Division 2.

Division 1—Preliminary

50AAC. Interpretation of Part 8AA

(1) In this Part—

actual provision (實際條款)—

- (a) except in relation to section 50AAN, has the meaning given by section 50AAF(1); and
- (b) in relation to section 50AAN, has the meaning given by section 50AAN(1);

advance pricing arrangement (預先定價安排) has the meaning given by section 50AAP(1);

affected person (當事人)—

- (a) except in relation to section 50AAN, has the meaning given by section 50AAF(1); and
- (b) in relation to section 50AAN, has the meaning given by section 50AAN(1);

arm's length provision (獨立交易條款)—

- (a) except in relation to section 50AAN, has the meaning given by section 50AAF(1); and
- (b) in relation to section 50AAN, has the meaning given by section 50AAN(1);

associated enterprise (相聯企業) has the meaning given by subsection (2)(a);

associated person (相聯人士) has the meaning given by subsection (2)(a);

business (業務) has the meaning given by section 2(1) and includes the performance of professional services and of other activities of an independent character;

double taxation arrangements (雙重課稅安排) has the meaning given by section 48A;

DTA territory (有安排地區) has the meaning given by section 48A;

DTA territory resident person (有安排地區居民人士) means a person who is resident for tax purposes in a DTA territory;

enterprise (企業) means a person who carries on a trade, profession or business;

foreign tax (外地稅項) means any tax that is—

- (a) chargeable in a territory outside Hong Kong; and
- (b) of substantially the same nature as Hong Kong tax;

Hong Kong resident person (香港居民人士) means a person who is resident for tax purposes in Hong Kong;

Hong Kong tax (香港稅項) means any tax imposed by this Ordinance other than additional tax charged under section 82A;

income (收入) includes profits or gains;

independent enterprise (獨立企業) has the meaning given by subsection (2)(b);

independent person (獨立人士) has the meaning given by subsection (2)(b);

non-DTA territory (無安排地區) has the meaning given by section 48A;

non-DTA territory resident person (無安排地區居民人士) means a person who is resident for tax purposes in a non-DTA territory;

non-Hong Kong resident person (非香港居民人士) means a person who is not a Hong Kong resident person;

permanent establishment (常設機構) has the meaning given by subsection (4);

potential advantage (潛在利益) has the meaning given by section 50AAJ;

recognized pension fund (認可退休基金), in relation to a territory, means an entity or arrangement established in the territory—

- (a) that is treated as a separate person under the taxation laws of the territory; and
- (b) either—
 - (i) that is established and operated exclusively or almost exclusively to administer or provide retirement benefits and ancillary or incidental

benefits to individuals and that is regulated as such by the territory or one of its political subdivisions or local authorities; or

- (ii) that is established and operated exclusively or almost exclusively to invest funds for the benefit of entities or arrangements that meet the description in subparagraph (i);

resident for tax purposes (稅務居民)—

- (a) in relation to Hong Kong, means—
 - (i) an individual who ordinarily resides in Hong Kong;
 - (ii) an individual who stays in Hong Kong—
 - (A) for a period or a number of periods amounting to more than 180 days during a year of assessment; or
 - (B) for a period or a number of periods amounting to more than 300 days in 2 consecutive years of assessment if one of the years is the year of assessment concerned;
 - (iii) a company incorporated in Hong Kong or, if incorporated outside Hong Kong, normally managed or controlled in Hong Kong;
 - (iv) a recognized pension fund of Hong Kong; or
 - (v) any other person, or a trust, constituted under the laws of Hong Kong or, if otherwise constituted, normally managed or controlled in Hong Kong;
- (b) in relation to a DTA territory, has the meaning given by the provisions relating to the

determination of resident status under the double taxation arrangements concerned;

(c) in relation to a non-DTA territory—

(i) means a person who, under the laws of the territory, is liable to tax in the territory by reason of the person's domicile, residence, place of management or any other criterion of a similar nature; and

(ii) includes the territory, the government of the territory and any political subdivision and local authority of the territory as well as a recognized pension fund of the territory;

transaction (交易) and *series of transaction* (一系列交易) have the meanings given by section 50AAI.

(2) For the purposes of this Part—

(a) a person is taken to be associated with another person if, as between them, the participation condition is met under section 50AAG; and a reference to associated person or associated enterprise is to be read accordingly; and

(b) a person is taken to be independent of another person if, as between them, the participation condition is not met under section 50AAG; and a reference to independent person or independent enterprise is to be read accordingly.

(3) In this Part—

(a) an income means a positive or nil amount of income;

(b) a loss means a positive or nil amount of loss;

(c) a nil amount of income is a smaller amount of income than any other amount of income; and a reference to larger amount of income is to be read accordingly; and

(d) a nil amount of loss is a smaller amount of loss than any other amount of loss; and a reference to a larger amount of loss is to be read accordingly.

(4) For the purposes of this Part—

(a) Schedule 17G has effect for determining whether a non-Hong Kong resident person has a permanent establishment in Hong Kong; and

(b) a reference to a permanent establishment in Hong Kong, in relation to a non-Hong Kong resident person, is to be read accordingly.

(5) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend Schedule 17G.

50AAD. Application of Part 8AA

(1) This Part applies in determining a person's liability for property tax, salaries tax and profits tax.

(2) In so far as this Part relates to a provision made or imposed as between 2 persons by means of a transaction or series of transactions, subsection (1) has effect—

(a) regardless of whether either person is, or both persons are, chargeable to foreign tax; and

(b) if either person is, or both persons are, chargeable to foreign tax—regardless of whether the foreign tax is chargeable in a DTA territory.

- (3) In so far as this Part relates to a non-Hong Kong resident person who has a permanent establishment in Hong Kong, subsection (1) has effect—
- (a) regardless of whether the person is chargeable to foreign tax in respect of income attributable to the permanent establishment or of other income; and
 - (b) if the person is so chargeable to foreign tax—regardless of whether the foreign tax is chargeable in a DTA territory.
- (4) Subsections (2) and (3) do not apply to sections 50AAN and 50AAO.

50AAE. Consistency with OECD rules

- (1) This Division is to be read in the way that best secures—
- (a) consistency between—
 - (i) the effect given to sections 50AAF, 50AAG, 50AAM and 50AAN; and
 - (ii) the effect that, in accordance with the OECD rules, is to be given to double taxation arrangements that incorporate the associated enterprises article or any rules in the same or equivalent terms as that article; and
 - (b) consistency between—
 - (i) the effect given to sections 50AAK and 50AAO; and
 - (ii) the effect that, in accordance with the OECD rules, is to be given to double taxation arrangements that incorporate the business profits article or any rules in the same or equivalent terms as that article.
- (2) In this section—

associated enterprises article (相聯企業條文) means the rules contained in Article 9 of the Model Tax Convention;

business profits article (營業利潤條文) means the rules contained in Article 7 of the Model Tax Convention;

OECD rules (《經合組織規則》) means—

- (a) the commentary on the associated enterprises article or the business profits article (as the case requires); and
 - (b) the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations published by the Organisation for Economic Co-operation and Development on 10 July 2017.
- (3) For the purposes of subsection (2), a reference to an article of the Model Tax Convention and to the commentary on the article means the article in the Model Tax Convention on Income and on Capital as approved by the Organisation for Economic Co-operation and Development on 15 July 2014 and to the commentary on the article approved on the same date.
- (4) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend the definitions in subsections (2) and (3).

Division 2—Computation of Income or Loss**Subdivision 1—Provision between Associated Persons****50AAF. Rule 1: Arm's length principle for provision between associated persons**

- (1) If the following circumstances happen—

- (a) a provision (*actual provision*) has been made or imposed as between 2 persons (each an *affected person*) by means of a transaction or series of transactions;
 - (b) the participation condition is met under section 50AAG;
 - (c) the actual provision differs from the provision that would have been made or imposed as between independent persons (*arm's length provision*); and
 - (d) the actual provision confers a potential advantage in relation to Hong Kong tax on an affected person (*advantaged person*),
- then, for the purposes of Hong Kong tax, 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*.)
- (2) The cases in which a provision made or imposed as between 2 persons is to be taken to differ from the provision that would have been made or imposed as between independent persons include a case in which provision is made or imposed as between 2 persons but no provision would have been made or imposed as between independent persons. References in this Part to arm's length provision are to be read accordingly.
 - (3) An assessor may give a notice to the advantaged person requiring the person to prove, within a reasonable time stated in the notice and to the assessor's satisfaction, that the amount of the person's income or loss as stated in the person's tax return is the arm's length amount.

- (4) A notice may be given under subsection (3) whether or not any assessment has already been made on, or any computation of loss has already been issued in respect of, the advantaged person.
- (5) If the advantaged person fails to prove to the assessor's satisfaction that the amount of the person's income or loss as stated in the person's tax return is the arm's length amount, the assessor must estimate an amount as the arm's length amount and, taking into account the estimated amount—
 - (a) make an assessment or additional assessment on the person; or
 - (b) issue a computation of loss, or revise a computation of loss resulting in a smaller amount of computed loss, in respect of the person.
- (6) For all purposes of this Ordinance, the estimated amount under subsection (5) is taken to be the arm's length amount unless the advantaged person proves that another amount is a more reliable measure of the arm's length amount.

50AAG. Interpretation: *participation condition*

As between affected persons, the participation condition is met if, at the time of the making or imposition of the actual provision—

- (a) one of the affected persons was participating in the management, control or capital of the other affected person within the meaning of section 50AAH; or
- (b) the same person or persons was or were participating in the management, control or capital

of each of the affected persons within the meaning of section 50AAH.

50AAH. Interpretation: *participation*

- (1) A person (*person A*) is participating in the management, control or capital of another person (*person B*) at a particular time only if, at that time, person B is—
 - (a) a corporation, partnership, trustee (whether incorporated or unincorporated) or a body of persons; and
 - (b) controlled by person A.
- (2) For the purposes of subsection (1)(b), person B is controlled by person A if—
 - (a) person A has the power to secure that the affairs of person B are conducted in accordance with the wishes of person A—
 - (i) because person A has more than half of the direct or indirect beneficial interest in or in relation to person B or any other corporation, partnership, trustee (whether incorporated or unincorporated) or a body of persons;
 - (ii) because person A is, directly or indirectly, entitled to exercise or control the exercise of more than half of the voting rights in or in relation to person B or any other corporation, partnership, trustee (whether incorporated or unincorporated) or a body of persons; or
 - (iii) because of powers conferred on person A by the constitutional document regulating person B or any other corporation, partnership,

trustee (whether incorporated or unincorporated) or a body of persons; or

- (b) person B is accustomed or under an obligation (whether express or implied, and whether or not enforceable or intended to be enforceable by legal proceedings) to act, in relation to person B's investment or business affairs, in accordance with the directions, instructions or wishes of person A.
- (3) In applying subsection (2), if person A has a direct beneficial interest in person B, the extent of the beneficial interest of person A in person B is—
 - (a) if person B is a corporation that is not a trustee of a trust estate—the percentage of the issued share capital (however described) of the corporation held by person A;
 - (b) if person B is a partnership that is not a trustee of a trust estate—the percentage of the income of the partnership to which person A is entitled;
 - (c) if person B is a trustee of a trust estate—the percentage in value of the trust estate in which person A is interested; or
 - (d) if person B is an entity that does not fall within any of paragraphs (a), (b) and (c)—the percentage of person A's ownership interest in the entity.
- (4) In applying subsection (2), if person A has an indirect beneficial interest in, or is indirectly entitled to exercise or control the exercise of voting rights in, person B through another person (*interposed person*), the extent of the beneficial interest or voting rights of person A in person B is—

- (a) if there is only one interposed person—the percentage arrived at by multiplying the percentage representing the extent of the beneficial interest or voting rights of person A in the interposed person by the percentage representing the extent of the beneficial interest or voting rights of the interposed person in person B; or
 - (b) if there is a series of 2 or more interposed persons—the percentage arrived at by multiplying the percentage representing the extent of the beneficial interest or voting rights of person A in the first interposed person in the series by—
 - (i) the percentage representing the extent of the beneficial interest or voting rights of each interposed person (other than the last interposed person) in the series in the next interposed person in the series; and
 - (ii) the percentage representing the extent of the beneficial interest or voting rights of the last interposed person in the series in person B.
- (5) For the purposes of subsection (4)—
- (a) subsection (3) applies in determining the extent of the beneficial interest of person A in an interposed person as if references to person B in subsection (3) were references to an interposed person;
 - (b) subsection (3) applies in determining the extent of the beneficial interest of an interposed person in person B as if references to person A in subsection (3) were references to an interposed person; and
 - (c) subsection (3) applies in determining the extent of the beneficial interest of an interposed person

(*interposed person X*) in another interposed person (*interposed person Y*) as if—

- (i) references to person A in subsection (3) were references to interposed person X; and
 - (ii) references to person B in subsection (3) were references to interposed person Y.
- (6) In applying subsections (1) and (2), the rights and powers attributed to person A include all the rights and powers of persons other than person A so far as they are required, or may be required, to be exercised in any one or more of the following ways—
- (a) on behalf of person A;
 - (b) under the direction of person A;
 - (c) for the benefit of person A.
- (7) For the purposes of this section, a reference to the exercise of the voting rights in a corporation is to be read as a reference to the exercise of the voting rights at general meetings of the corporation.

50AAL Interpretation: *transaction and series of transactions*

- (1) In this Part, transaction includes any operation, scheme, arrangement, understanding and mutual practice (whether express or implied, and whether or not enforceable or intended to be enforceable by legal proceedings).
- (2) References in this Part to a series of transactions include a number of transactions each entered into (whether or not one after the other) in pursuance of, or in relation to, the same matter.
- (3) A series of transactions is not prevented from being regarded as a series of transactions by means of which a

provision has been made or imposed as between any 2 persons, even if one or more of the following applies—

- (a) there is no transaction in the series to which both those persons are parties;
- (b) the parties to any arrangement or scheme in pursuance of which the transactions in the series are entered into do not include one or both of those persons;
- (c) there is one or more transactions in the series to which neither of those persons is a party.

50AAJ. Interpretation: potential advantage in relation to tax

An actual provision confers a potential advantage in relation to Hong Kong tax or foreign tax on a person if, disregarding this Division, making or imposing the actual provision, instead of the arm's length provision, would in relation to Hong Kong tax or foreign tax (as the case requires) have either or both of the following effects—

- (a) a smaller amount would be taken to be the amount of the person's income;
- (b) a larger amount would be taken to be the amount of the person's loss.

Subdivision 2—Permanent Establishment in Hong Kong

50AAK. Rule 2: Separate enterprises principle for attributing income or loss of non-Hong Kong resident person

- (1) Without limiting section 14, a non-Hong Kong resident person who has a permanent establishment in Hong Kong is regarded as carrying on a trade, profession or business in Hong Kong for the purposes of charging profits tax.

- (2) The income or loss of the person that is attributable to the permanent establishment of the person are those that the permanent establishment would have made in circumstances where it were a distinct and separate enterprise that—

- (a) engaged in the same or similar activities under the same or similar conditions; and
- (b) dealt wholly independently with the person.

(The amount of income or loss of the person that is attributed to the permanent establishment in accordance with this subsection is referred to as the *arm's length amount*.)

- (3) In applying subsection (2), account is to be taken of the functions performed, assets used and risk assumed by the person—
 - (a) through the permanent establishment; and
 - (b) through the other parts of the person.
- (4) In applying subsection (2), it is assumed that the permanent establishment—
 - (a) has the same credit rating as the person; and
 - (b) has the equity and loan capital that it could reasonably be expected to have in the circumstances set out in that subsection.
- (5) In applying subsection (2), transactions between the permanent establishment and any other part of the person are treated as taking place on the terms that would have been agreed between parties dealing at arm's length.

- (6) No deduction is to be allowed for costs and expenses in excess of those that would have been incurred on the assumptions set out in subsection (4).
- (7) An assessor may give a notice to the person requiring the person to do the following within a reasonable time stated in the notice—
 - (a) to state the amount of income or loss attributed to the permanent establishment that has been taken into account in the amount of the person's income or loss as stated in the person's tax return; and
 - (b) to prove to the assessor's satisfaction that the amount of income or loss so attributed is the arm's length amount.
- (8) A notice may be given under subsection (7) whether or not any assessment has already been made on, or any computation of loss has already been issued in respect of, the person.
- (9) If the person fails to prove to the assessor's satisfaction that the amount of income or loss attributed as mentioned in subsection (7)(a) is the arm's length amount, the assessor must estimate an amount as the arm's length amount and, taking into account the estimated amount—
 - (a) make an assessment or additional assessment on the person; or
 - (b) issue a computation of loss, or revise a computation of loss resulting in a smaller amount of computed loss, in respect of the person.
- (10) For all purposes of this Ordinance, the estimated amount under subsection (9) is taken to be the arm's length

amount unless the person proves that another amount is a more reliable measure of the arm's length amount.

Division 3—Relief Consequential on Transfer Pricing Adjustment

50AAL. Interpretation: *relevant activities*

- (1) In this Division—
relevant activities (有關活動), in relation to a person (*person A*) who is one of the persons as between whom any provision is made or imposed, means activities that—
 - (a) are within subsection (2); and
 - (b) are not within subsection (3).
- (2) The activities within this subsection are those of person A's activities that comprise the activities in the course of which, or with respect to which, the provision is made or imposed.
- (3) The activities within this subsection are any of person A's activities carried on—
 - (a) separately from the activities mentioned in subsection (2); or
 - (b) for the purposes of a different part of person A's business.

50AAM. Corresponding relief not involving foreign tax

- (1) This section applies if, in the circumstances set out in section 50AAF(1)—
 - (a) the affected person on whom a potential advantage in relation to Hong Kong tax is conferred by the actual provision (*advantaged person*) has income arising from the relevant activities assessed to, or

- has loss so arising computed for the purposes of Hong Kong tax on the basis of the arm's length provision; and
- (b) the other affected person (*disadvantaged person*) has income or loss arising from the relevant activities to be computed for the purposes of Hong Kong tax.
- (2) On a claim by the disadvantaged person, the disadvantaged person's income or loss arising from the relevant activities is to be computed for the purposes of Hong Kong tax 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*.)
- (3) In applying subsection (2), the way in which the disadvantaged person's income or loss is to be computed on the basis of the arm's length provision must be consistent with the way in which the advantaged person's income has been assessed, or the advantaged person's loss has been computed, on that basis.
- (4) If—
- (a) the disadvantaged person makes a claim seeking to have its income or loss computed for the purposes of Hong Kong tax on the basis of the arm's length provision under subsection (2); but
- (b) the disadvantaged person's income has already been assessed to, or the disadvantaged person's loss has already been computed for the purposes of, Hong Kong tax other than on that basis,
- an assessor must revise the assessment, or computation of loss, to reflect the arm's length provision.

- (5) A claim under subsection (2) must be made in writing and may only be made before—
- (a) the end of 6 years after the end of the relevant year of assessment;
- (b) the end of 6 months after the date on which an assessment is made imposing liability or additional liability to Hong Kong tax on the advantaged person or the disadvantaged person taking into account the income or loss arising from the relevant activities; or
- (c) the end of 6 months after the date on which a computation of loss, or a revised computation of loss resulting in a smaller amount of computed loss, in respect of the relevant activities is issued to the advantaged person or disadvantaged person,
- whichever is the latest.
- (6) For the purposes of subsection (2) or (4), an assessor may give a notice to the disadvantaged person requiring the disadvantaged person to prove, within a reasonable time stated in the notice and to the assessor's satisfaction, that the amount of the disadvantaged person's income or loss as stated in the disadvantaged person's claim under subsection (2) is the arm's length amount.
- (7) A notice may be given under subsection (6) whether or not any assessment has already been made on, or any computation of loss has already been issued in respect of, the disadvantaged person.
- (8) If the disadvantaged person fails to prove to the assessor's satisfaction that the amount of the disadvantaged person's income or loss as stated in the disadvantaged person's claim is the arm's length

- amount, the assessor may estimate an amount as the arm's length amount and, taking into account the estimated amount—
- (a) make or revise an assessment on the disadvantaged person; or
 - (b) issue or revise a computation of loss in respect of the disadvantaged person.
- (9) If an assessor refuses to revise the disadvantaged person's assessment under subsection (4)—
- (a) the assessor must give a written notice of the refusal to the disadvantaged person; and
 - (b) the disadvantaged person has the same rights of objection and appeal under Part 11 as if the notice of refusal were a notice of assessment.
- (10) For all purposes of this Ordinance, the estimated amount under subsection (8) is taken to be the arm's length amount unless the disadvantaged person proves that another amount is a more reliable measure of the arm's length amount.
- (11) If an assessment on, or computation of loss in respect of, a disadvantaged person has been made, issued or revised under this section, the disadvantaged person must—
- (a) take reasonable steps to ensure the disadvantaged person has knowledge about any adjustment to the advantaged person's assessed income or computed loss arising from the relevant activities (*adjustment on advantaged person*); and
 - (b) give the Commissioner written notice of the adjustment on advantaged person within 3 months after the adjustment is made if the adjustment—

- (i) renders the disadvantaged person's assessed income arising from the relevant activities insufficient for the purposes of Hong Kong tax; or
 - (ii) renders the disadvantaged person's computed loss arising from the relevant activities excessive for the purposes of Hong Kong tax.
- (12) Subject to subsection (13), the following may be made or issued after the adjustment on advantaged person is made—
- (a) a corresponding adjustment to the disadvantaged person's assessed income or computed loss arising from the relevant activities;
 - (b) an assessment or additional assessment on, or computation or revised computation of loss in respect of, the disadvantaged person to reflect the corresponding adjustment.
- (13) An adjustment to assessed income and an assessment or additional assessment made under subsection (12) may only be made before—
- (a) the end of 2 years from the time when the adjustment on advantaged person is made; or
 - (b) the expiry of the time limit for making an assessment or additional assessment under this Ordinance,
- whichever is the later.

50AAN. Corresponding relief involving foreign tax: disadvantaged person

- (1) This section applies if—

- (a) a provision (*actual provision*) has been made or imposed as between 2 persons (each an *affected person*) by means of a transaction or series of transactions;
 - (b) the participation condition is met under section 50AAG;
 - (c) the actual provision differs from the provision that would have been made or imposed as between independent persons (*arm's length provision*);
 - (d) the actual provision confers a potential advantage in relation to foreign tax in a DTA territory on an affected person (*advantaged person*);
 - (e) the advantaged person has income arising from the relevant activities assessed to, or has loss so arising computed for the purposes of, foreign tax in the DTA territory and the assessment or computation relates to determining what the arm's length provision is; and
 - (f) the other affected person (*disadvantaged person*) has income or loss arising from the relevant activities to be computed for the purposes of Hong Kong tax.
- (2) If—
- (a) a claim is made by the disadvantaged person pursuant to the provisions relating to mutual agreement procedure under the double taxation arrangements concerned; and
 - (b) a MAP solution within the meaning of section 50AAB is arrived at and it includes a determination of what the arm's length provision is (*MAP arm's length provision*),

- the disadvantaged person's income arising from the relevant activities is to be assessed to, or the disadvantaged person's loss so arising is to be computed for the purposes of, Hong Kong tax as if the MAP arm's length provision had been made or imposed instead of the actual provision.
- (3) If a disadvantaged person's income or loss has been assessed or computed under subsection (2), the disadvantaged person must—
- (a) take reasonable steps to ensure the disadvantaged person has knowledge about any adjustment made after the date of the MAP solution to the advantaged person's assessed income or computed loss for the purposes of foreign tax in the DTA territory (*advantaged person's foreign tax-related adjustment*); and
 - (b) give the Commissioner written notice of the advantaged person's foreign tax-related adjustment within 3 months after the adjustment is made if—
 - (i) the adjustment relates to a determination of the arm's length provision (*newly determined arm's length provision*); and
 - (ii) computing the disadvantaged person's income or loss for the purposes of Hong Kong tax on the basis of the newly determined arm's length provision, instead of the MAP arm's length provision, will result in—
 - (A) a larger amount being computed as the disadvantaged person's income arising from the relevant activities; or

- (B) a smaller amount being computed as the disadvantaged person's loss arising from the relevant activities.
- (4) Subject to subsection (5), the following may be made or issued after the advantaged person's foreign tax-related adjustment is made—
- (a) a corresponding adjustment to the disadvantaged person's assessed income or computed loss arising from the relevant activities;
 - (b) an assessment or additional assessment on, or computation or revised computation of loss in respect of, the disadvantaged person to reflect the corresponding adjustment.
- (5) An adjustment to assessed income and an assessment or additional assessment made under subsection (4) may only be made before—
- (a) the end of 2 years from the time when the advantaged person's foreign tax-related adjustment is made; or
 - (b) the expiry of the time limit for making an assessment or additional assessment under this Ordinance,
- whichever is the later.

50AAO. Corresponding relief involving foreign tax: non-Hong Kong resident person's permanent establishment

- (1) This section applies if—
- (a) a non-Hong Kong resident person has income or loss, attributable to a permanent establishment in Hong Kong of the person, to be computed for the purposes of Hong Kong tax; and

- (b) the person's income has been assessed to, or the person's loss has been computed for the purposes of, foreign tax in a DTA territory and the assessment or computation relates to determining what amount of the person's income or loss is attributable to the permanent establishment in Hong Kong.
- (2) If—
- (a) a claim is made by the person pursuant to the provisions relating to mutual agreement procedure under the double taxation arrangements concerned; and
 - (b) a MAP solution within the meaning of section 50AAB is arrived at and it includes a determination of what amount of the person's income or loss is attributable to the permanent establishment in Hong Kong (*MAP attribution*),
- the person's income is to be assessed to, or the person's loss is to be computed for the purposes of, Hong Kong tax in a way that is consistent with the MAP attribution.
- (3) If a non-Hong Kong resident person's income or loss has been assessed or computed under subsection (2), the person must—
- (a) take reasonable steps to ensure the person has knowledge about any adjustment made after the date of the MAP solution to the person's assessed income or computed loss for the purposes of foreign tax in the DTA territory (*foreign tax-related adjustment*); and
 - (b) give the Commissioner written notice of the foreign tax-related adjustment within 3 months after the adjustment is made if—

- (i) the adjustment relates to a determination of the amount of the person's income or loss attributable to the person's permanent establishment in Hong Kong (*newly determined attribution*); and
 - (ii) computing the person's income or loss for the purposes of Hong Kong tax on the basis of the newly determined attribution, instead of the MAP attribution, will result in—
 - (A) a larger amount of the person's income being attributed to the person's permanent establishment in Hong Kong; or
 - (B) a smaller amount of the person's loss being attributed to the person's permanent establishment in Hong Kong.
- (4) Subject to subsection (5), the following may be made or issued after the foreign tax-related adjustment is made—
- (a) a corresponding adjustment to the person's income or loss attributed to the person's permanent establishment;
 - (b) an assessment or additional assessment on, or computation or revised computation of loss in respect of, the person to reflect the corresponding adjustment.
- (5) An adjustment to assessed income and an assessment or additional assessment made under subsection (4) may only be made before—
- (a) the end of 2 years from the time when the foreign tax-related adjustment is made; or

- (b) the expiry of the time limit for making an assessment or additional assessment under this Ordinance,
- whichever is the later.

Division 4—Advance Pricing Arrangement

50AAP. Advance pricing arrangement may be made

- (1) On application by a person and if the Commissioner considers appropriate, the Commissioner may make an arrangement (*advance pricing arrangement*) with the person relating to how the person's income or loss is to be computed under section 50AAF or 50AAK for a fixed period of time.
- (2) The advance pricing arrangement must specify—
 - (a) the name of the person to which the arrangement applies;
 - (b) the transactions covered by the arrangement, if applicable;
 - (c) the period covered by the arrangement;
 - (d) the methodology as agreed between the Commissioner and the person for determining the income or loss of the person;
 - (e) the critical assumptions on which the agreed methodology is based;
 - (f) the person's obligations under the arrangement, including obligations for providing reports on the matters, and at the intervals, as specified in the arrangement; and
 - (g) any other terms as agreed between the Commissioner and the person.

- (3) The Commissioner may refuse to make an advance pricing arrangement—
- (a) if—
 - (i) the arrangement is to apply to any provision made or imposed as between any persons any of whom (*specified person*)—
 - (A) has income or loss to be computed for the purposes of Hong Kong tax; but
 - (B) is not the person, or one of the persons, making the application for the arrangement; and
 - (ii) the specified person fails or refuses to join in the application; or
 - (b) if any fee payable under Schedule 17H for the application for the arrangement, or any deposit for the fee payable under that Schedule, is not paid.
- (4) Subsection (3) does not limit the grounds on which the Commissioner may refuse to make an advance pricing arrangement.
- (5) The Commissioner may make an advance pricing arrangement for a period that covers a period earlier than the date of the arrangement but—
- (a) liability for tax is not to be increased under this subsection after the expiry of the time limit for making an assessment or additional assessment under this Ordinance; and
 - (b) liability for tax is not to be reduced under this subsection after the expiry of the latest of the time limits for raising an objection or applying for relief or revision of assessment (as applicable) under this

Ordinance or any relevant double taxation arrangements.

50AAQ. Sections 50AAF and 50AAK to be applied in accordance with advance pricing arrangement

- (1) This section applies if—
- (a) an advance pricing arrangement has been made in respect of a person for a period specified in the arrangement (*specified period*); and
 - (b) the person is required under this Ordinance to provide a return for a year of assessment (*year of assessment*) that includes all or part of the specified period.
- (2) The person must disclose in the return for the year of assessment—
- (a) the existence of the advance pricing arrangement;
 - (b) whether or not the person has relied on the arrangement in preparing and providing the return; and
 - (c) any material change to the facts and circumstances specified in the arrangement.
- (3) If the person has disclosed in the return for the year of assessment that the person has relied on the advance pricing arrangement in preparing and providing the return, then, subject to section 50AAR, the Commissioner is to apply sections 50AAF and 50AAK in relation to the person in accordance with the arrangement for the year of assessment.
- (4) The Commissioner may, if the Commissioner considers appropriate, apply the principles developed in an

advance pricing arrangement to a period earlier than the date of the arrangement but—

- (a) liability for tax is not to be increased under this subsection after the expiry of the time limit for making an assessment or additional assessment under this Ordinance; and
- (b) liability for tax is not to be reduced under this subsection after the expiry of the latest of the time limits for raising an objection or applying for relief or revision of assessment (as applicable) under this Ordinance or any relevant double taxation arrangements.

50AAR. Advance pricing arrangement may be revoked, cancelled or revised

- (1) The Commissioner may revoke, cancel or revise an advance pricing arrangement made in respect of a person if—
 - (a) any condition or critical assumption specified in the arrangement has not been met or is no longer met;
 - (b) the person has failed to comply with the person's obligations under the arrangement; or
 - (c) in connection with the application pursuant to which the arrangement was made, the person is found to have—
 - (i) made an incorrect statement;
 - (ii) provided incorrect information; or
 - (iii) omitted to make a statement or provide information,

and the statement or information is material to the application.

- (2) If the Commissioner revokes an advance pricing arrangement, the arrangement is to be treated as having never been made.
- (3) If the Commissioner cancels an advance pricing arrangement, the arrangement is to cease to apply from a date that the Commissioner determines.
- (4) If the Commissioner revises an advance pricing arrangement, the revision is to take effect from a date that the Commissioner determines.
- (5) Any revocation, cancellation or revision of an advance pricing arrangement because of a matter referred to in subsection (1) does not affect any criminal liability that may arise in respect of the matter.

50AAS. Obligation to notify breach of critical assumption, etc.

A person in respect of whom an advance pricing arrangement is made—

- (a) must notify the Commissioner of a breach of any critical assumption specified in the arrangement within a reasonable time after the breach; and
- (b) must provide the Commissioner from time to time with all reports and other information that the person may be required to provide under the arrangement.

50AAT. Record keeping

A person in respect of whom an advance pricing arrangement is made for a period (*specified period*) must retain, for a period of not less than 7 years after the end of the specified period, all the records and data—

- (a) relied on in concluding the arrangement;
- (b) used in applying for the arrangement; and
- (c) referred to in any reports and other information provided to the Commissioner under the arrangement.

50AAU. Advance pricing arrangement and double taxation arrangements

- (1) If an advance pricing arrangement being applied for—
 - (a) either—
 - (i) is to cover a transaction in respect of which an applicant for the arrangement or an associated person of the applicant is likely to be liable to tax in a DTA territory; or
 - (ii) relates to the attribution of income or loss to a permanent establishment in Hong Kong of an applicant for the arrangement and the applicant is likely to be liable to tax in a DTA territory; and
 - (b) is relevant to the question how the applicant or the associated person is to be taxed (whether in Hong Kong or the territory) so as to accord with the double taxation arrangements concerned,
the Commissioner may resolve the question with the competent authority of the territory through the mutual agreement procedure mentioned in section 50AAB before making the advance pricing arrangement.
- (2) If a mutual agreement referred to in section 50AAB is not consistent with the terms of an advance pricing arrangement already made, the Commissioner must revise the arrangement so far as may be necessary for

enabling effect to be given to the mutual agreement in relation to the subject matter of the arrangement.

50AAV. Application for advance pricing arrangement and application fees

- (1) Schedule 17H provides for an application for an advance pricing arrangement and for fees payable for the application.
- (2) The Secretary for Financial Services and the Treasury may by order amend Schedule 17H.

50AAW. Protection of public officer

No liability is to rest on the Government, the Commissioner or any other public officer in respect of the exercise of any power or performance of any duty in good faith in relation to an advance pricing arrangement or an application for the arrangement.”.

10. Schedules 17G and 17H added

After Schedule 17F—

Add

“Schedule 17G

[ss. 50AAC & 58B &
Sch. 42]

Meaning of *Permanent Establishment* in Hong Kong

Part 1

Preliminary

1. Interpretation

- (1) An expression used in this Schedule, and defined or otherwise explained in Part 8AA, has the same meaning as in that Part.
- (2) In this Schedule—
company (公司) means any body corporate or any entity that is treated as a body corporate for tax purposes.

2. Interpretation: *closely related, closely related person and closely related enterprise*

- (1) For the purposes of this Schedule, a person (*person A*) is closely related to another person (*person B*) if, based on all the relevant facts and circumstances—
 - (a) person A has control of person B;
 - (b) person B has control of person A; or
 - (c) person A and person B are both under the control of the same other person or enterprise.
- (2) Also, a person (*person A*) is taken to be closely related to another person (*person B*) if—
 - (a) person A possesses directly or indirectly more than the specified interest in person B;
 - (b) person B possesses directly or indirectly more than the specified interest in person A; or

- (c) another person possesses directly or indirectly more than the specified interest in each of person A and person B.

(3) In subsection (2)—

specified interest (指明權益), in relation to a person, means—

- (a) 50% of the beneficial interest in the person; or
- (b) if the person is a company, 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company.
- (4) A reference to closely related person or closely related enterprise is to be read accordingly.

Part 2

Permanent Establishment of DTA Territory Resident Person

3. Permanent establishment of DTA territory resident person

Whether a DTA territory resident person has a permanent establishment in Hong Kong is to be determined in accordance with the relevant provisions under the double taxation arrangements concerned.

Part 3

Permanent Establishment of Non-DTA Territory Resident Person

4. Permanent establishment constituted by fixed place of business

- (1) Subject to sections 5, 6 and 7 of this Schedule, an enterprise that is a non-DTA territory resident person has a permanent establishment in Hong Kong if it has a fixed place of business in Hong Kong through which the business of the enterprise is wholly or partly carried on.
- (2) For the purpose of subsection (1), a fixed place of business includes, but is not limited to—
 - (a) a place of management;
 - (b) a branch;
 - (c) an office;
 - (d) a factory;
 - (e) a workshop; and
 - (f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.
- (3) For the purpose of subsection (1), a building site or construction or installation project is a permanent establishment of an enterprise (*subject enterprise*) only if—
 - (a) the subject enterprise has carried on activities at the site or project for a period of more than 12 months; or
 - (b) all of the following apply—

- (i) the subject enterprise has carried on activities at the site or project for a period that exceeds, or 2 or more periods that in the aggregate exceed, 30 days;
 - (ii) connected activities have been carried on at the site or project by one or more closely related enterprises of the subject enterprise for one or more different periods that each exceeds 30 days;
 - (iii) all the periods referred to in subparagraphs (i) and (ii) in the aggregate exceed 12 months.
- (4) In determining whether different activities are connected for the purposes of subsection (3)(b)(ii), regard is to be had to the facts and circumstances of the case, including in particular—
- (a) whether the contracts covering the different activities were concluded with the same person or closely related persons;
 - (b) whether the conclusion of additional contracts with a person is a logical consequence of a previous contract concluded with the person or closely related persons;
 - (c) whether the activities would have been covered by a single contract absent tax planning considerations;
 - (d) whether the nature of the work involved under the different contracts is the same or similar; and
 - (e) whether the same employees are performing the activities under the different contracts.

5. Preparatory or auxiliary activities not constitute permanent establishment

- (1) This section applies subject to section 6 of this Schedule.
- (2) If the 1st or 2nd set of conditions are met in relation to an enterprise, the enterprise is not regarded under section 4(1) of this Schedule as having a permanent establishment in Hong Kong even if it has a fixed place of business in Hong Kong through which the business of the enterprise is carried on.
- (3) The 1st set of conditions are—
 - (a) the activity carried on for the enterprise through the place consists solely of one of the following—
 - (i) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandize belonging to the enterprise;
 - (ii) the maintenance of a stock of goods or merchandize belonging to the enterprise solely for the purpose of storage, display or delivery;
 - (iii) the maintenance of a stock of goods or merchandize belonging to the enterprise solely for the purpose of processing by another enterprise;
 - (iv) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandize, or collecting information, for the enterprise;
 - (v) the maintenance of a fixed place of business solely for the purpose of carrying on any other activity for the enterprise; and

- (b) in relation to the business of the enterprise as a whole, the activity is of a preparatory or auxiliary character.
- (4) The 2nd set of conditions are—
 - (a) the activities carried on for the enterprise through the place consist solely of any combination of the activities mentioned in subsection (3)(a)(i), (ii), (iii), (iv) and (v); and
 - (b) the overall activity of the place resulting from the combination of the activities is of a preparatory or auxiliary character.

6. Section 5(2) of this Schedule does not apply if certain activities constitute complementary functions

Section 5(2) of this Schedule does not apply to an enterprise (*subject enterprise*) with a fixed place of business (*place A*) in Hong Kong if—

- (a) either or both of the following apply—
 - (i) business activities at place A are carried on by a closely related enterprise of the subject enterprise;
 - (ii) business activities are carried on at another place (*place B*) in Hong Kong by the subject enterprise or its closely related enterprise;
- (b) the business activities carried on at place A by the subject enterprise and those referred to in paragraph (a) constitute complementary functions that are part of a cohesive business operation; and
- (c) any one or more of the following apply—

- (i) place A would have constituted a permanent establishment for the subject enterprise but for section 5(2) of this Schedule;
- (ii) place A constitutes a permanent establishment for the closely related enterprise;
- (iii) place B constitutes a permanent establishment for the subject enterprise or the closely related enterprise;
- (iv) the overall activity resulting from the combination of the following is not of a preparatory or auxiliary character—
 - (A) the business activities carried on at place A by the subject enterprise;
 - (B) business activities referred to in paragraph (a).

7. Permanent establishment constituted by agent's activities

- (1) Despite section 4(1) of this Schedule, an enterprise (*the enterprise*) that is a non-DTA territory resident person is taken to have a permanent establishment in Hong Kong in respect of any activities (*the activities*) that a person (*the person*) undertakes for the enterprise if—
 - (a) the person is acting in Hong Kong on behalf of the enterprise and in doing so—
 - (i) habitually concludes contracts; or
 - (ii) habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise; and
 - (b) the contracts are—
 - (i) in the name of the enterprise;

- (ii) for the transfer of the ownership of, or for the granting of the right to use, property owned by the enterprise or that the enterprise has the right to use; or
 - (iii) for the provision of services by the enterprise.
- (2) Subsection (1) does not apply if the activities of the person are limited to activities that, if exercised through a fixed place of business, would not make the fixed place of business a permanent establishment under section 4(1) of this Schedule, having regard to sections 5 and 6 of this Schedule.
- (3) Subsection (1) does not apply if the person—
 - (a) carries on business in Hong Kong as an independent agent; and
 - (b) acts for the enterprise in the ordinary course of that business.
- (4) A person is not an independent agent for the purposes of subsection (3) if the person acts exclusively, or almost exclusively, on behalf of one or more enterprises that are closely related to the person.

8. Company not constituted permanent establishment of another company

- (1) Even if—
 - (a) a company (*company A*) controls or is controlled by another company (*company B*);
 - (b) company A is resident for tax purposes in a non-DTA territory;
 - (c) company B—
 - (i) is resident for tax purposes in Hong Kong; or

- (ii) carries on business in Hong Kong (whether through a permanent establishment or otherwise),
- these matters do not of themselves constitute either company a permanent establishment of the other.
- (2) This section does not affect the operation of the other provisions of this Schedule.

Schedule 17H

[ss. 50AAP, 50AAV & 80
& Sch. 42]

Advance Pricing Arrangement

1. Interpretation

- (1) An expression used in this Schedule, and defined or otherwise explained in Part 8AA, has the same meaning as in that Part.
- (2) In this Schedule—
- (a) *application* (申請) means an application for an advance pricing arrangement made under section 50AAP(1); and
- (b) *applicant* (申請人) means a person who makes an application.

2. Contents of application

An application must include—

- (a) the details of the applicant and associated persons of the applicant involved in the transactions in respect of which the advance pricing arrangement is applied for;
- (b) the facts and documents relating to the applicant, the associated persons and the transactions;
- (c) the proposed methodology for determining the income or loss of the applicant;
- (d) the evidence showing that the proposed methodology can produce a result that complies with sections 50AAF and 50AAK (as applicable);
- (e) the period in respect of which an advance pricing arrangement is applied for; and
- (f) a draft advance pricing arrangement.

3. Information to be provided for purposes of application

The applicant must provide further information in respect of an application if required by the Commissioner by notice.

4. Commissioner may appoint independent expert

The Commissioner may appoint an independent expert to inquire into and report on any matters in relation to an application.

5. Withdrawal of application

An applicant may withdraw an application by written notice to the Commissioner.

6. Reasons to be given for refusal

If the Commissioner refuses to make an advance pricing arrangement, the Commissioner must give the applicant a

written notice stating the decision and the reasons for the refusal.

7. Fees

- (1) The fees specified in subsection (9) and incurred in respect of an application are payable by the applicant.
- (2) The Commissioner may require that an applicant must pay a deposit of an amount determined by the Commissioner before the application is entertained.
- (3) When the application is determined, the Commissioner, on ascertaining the total amount of the fees payable, must apply the deposit already paid to settle the fees and—
 - (a) if the amount of the deposit is less than the amount of the fees payable—the applicant must pay the balance; or
 - (b) if the amount of the deposit exceeds the amount of the fees payable—the Commissioner must refund the surplus to the applicant.
- (4) Subject to subsections (5), (6) and (8), subsection (1) applies even if the application is refused or withdrawn.
- (5) If an application is withdrawn, the applicant is liable to pay all the fees specified in subsection (9) and incurred in respect of the application before the Commissioner receives notice of withdrawal given under section 5 of this Schedule.
- (6) In exceptional circumstances, the Commissioner may, at the Commissioner's discretion, waive all or part of any fees payable in respect of an application.
- (7) Any fees due and payable in respect of an application are recoverable as a civil debt due to the Government.

- (8) In exceptional circumstances, the Commissioner may, at the Commissioner's discretion, direct that all or part of any fees paid in respect of an application be refunded to the applicant if the Commissioner does not make an advance pricing arrangement.
- (9) The fees payable in respect of an application are—
 - (a) a service charge calculated on the basis of each hour (or any part of an hour) spent by—
 - (i) a Deputy Commissioner \$2,650
 - (ii) an Assistant Commissioner \$2,240
 - (iii) a Chief Assessor \$1,960
 - (iv) any other person appointed under this Ordinance; and \$1,730
 - (b) payment or reimbursement of—
 - (i) any fees paid by the Commissioner to any independent expert appointed under section 4 of this Schedule; and
 - (ii) any costs and reasonable expenses incurred by the Commissioner in relation to the application.”.

Division 3—Amendments Relating to Transfer Pricing: Other Provisions Relating to New Part 8AA

11. Section 7D added

Part 2, after section 7C—

Add

“7D. Part 8AA applies

Part 8AA applies for the purposes of calculation of property tax.”.

12. Section 13A added

Part 3, after section 13—

Add

“13A. Part 8AA applies

Part 8AA applies for the purposes of calculation of salaries tax.”.

13. Section 15BA added

Before section 15C—

Add

“15BA. Changes in trading stock

(1) In this section—

trading stock (營業存貨), in relation to a trade—

- (a) means anything (whether movable property or immovable property) that—
 - (i) is sold in the ordinary course of trade; or
 - (ii) would be so sold if it were mature or its manufacture, preparation or construction were complete; but
- (b) does not include—
 - (i) materials used in the manufacture, preparation or construction of any such thing;
 - (ii) any services performed in the ordinary course of the trade; or

(iii) any article produced, or any material used, in the performance of any such services.

- (2) If trading stock of a person’s trade is appropriated by the person for non-trade purpose, then in calculating the profits of the trade—
 - (a) the amount that the trading stock appropriated would have realized if sold in the open market at the time of the appropriation is brought into account as a receipt;
 - (b) the value of anything in fact received from the appropriation of the trading stock is left out of account; and
 - (c) the receipt referred to in paragraph (a) is treated as arising on the date of the appropriation.
- (3) If something that belongs to a person carrying on a trade, but that is not trading stock of the trade, becomes trading stock of the trade, then in calculating the profits of the trade—
 - (a) the cost of the stock is taken to be the amount that it would have realized if sold in the open market at the time it became trading stock of the trade;
 - (b) the value of anything in fact given for it becoming trading stock of the trade is left out of account; and
 - (c) the cost referred to in paragraph (a) is treated as being incurred on the date it became trading stock of the trade.
- (4) If trading stock of a trade is disposed of otherwise than in the course of trade and subsection (2) does not apply, then in calculating the profits of the trade—
 - (a) the amount that the trading stock disposed of would have realized if sold in the open market at the time

- of the disposal is brought into account as the receipt;
- (b) any consideration obtained for the disposal of the trading stock is left out of account; and
 - (c) the receipt referred to in paragraph (a) is treated as arising on the date of the disposal.
- (5) If trading stock of a trade has been acquired otherwise than in the course of trade and subsection (3) does not apply, then in calculating the profits of the trade—
- (a) the cost of the stock is taken to be the amount that it would have realized if sold in the open market at the time of the acquisition;
 - (b) the value of anything in fact given for the acquisition of the trading stock is left out of account; and
 - (c) the cost referred to in paragraph (a) is treated as being incurred on the date of the acquisition.”.

14. Section 15F added

After section 15E—

Add

“15F. Sums derived from intellectual property by non-Hong Kong resident associates

- (1) For the purposes of this section, a person makes value creation contributions in relation to any intellectual property if the person has made contributions in relation to the intellectual property through—
- (a) performing the functions of and assuming risks relating to the development, enhancement,

- maintenance, protection or exploitation of the intellectual property; or
- (b) providing assets in and assuming risks relating to the development, enhancement, maintenance, protection or exploitation of the intellectual property.
- (2) This section applies if—
- (a) a person has made value creation contributions in Hong Kong in relation to any intellectual property;
 - (b) a sum (*relevant sum*) accrues to an associate of the person, or is received by or for the benefit of the associate, in respect of—
 - (i) the exhibition or use of, or a right to exhibit or use, (whether in or outside Hong Kong) the intellectual property; or
 - (ii) the imparting or undertaking to impart knowledge directly or indirectly connected with the use (whether in or outside Hong Kong) of the intellectual property; and
 - (c) the associate is a non-Hong Kong resident person.
- (3) 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 the 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.
- (4) The associate is not to be chargeable to profits tax in respect of the attributable amount.
- (5) In this section—

associate (相聯者) has the meaning given by section 20AC(6);

intellectual property (知識產權) means—

- (a) cinematograph or television film or tape, any sound recording, any advertising material connected with such film, tape or recording; or
- (b) patent, design, trade mark, copyright material, secret process or formula or other property of a similar nature;

non-Hong Kong resident person (非香港居民人士) has the meaning given by section 50AAC(1).”.

15. Section 26AC added

At the end of Part 4—

Add

“26AC. Part 8AA applies

Part 8AA applies for the purposes of calculation of profits tax.”.

Division 4—Amendments Relating to Transfer Pricing: Addition of New Part 9A and Schedule 17I

16. Part 9A added

After Part 9—

Add

“Part 9A

Transfer Pricing Documentation Including Country-by-Country Reporting

Note (with no legislative effect) providing an overview of Part 9A—

1. Division 1 provides for interpretation.
2. Division 2 requires a Hong Kong entity of a group in the extended sense to prepare, for each accounting period, a master file and a local file and to retain the files for 7 years.
3. Division 3 gives effect to the country-by-country reporting requirements of the Organisation for Economic Co-operation and Development.

Division 1—Interpretation

58B. Interpretation of Part 9A

- (1) Except for *permanent establishment*, an expression used in this Part, and defined or otherwise explained in Part 8AA, has the same meaning as in that Part.

- (2) In this Part—

accounting period (會計期), in relation to Division 3 and a multinational enterprise group, means a period with respect to which the ultimate parent entity of the group prepares its financial statements;

CbCR documents (國別標準文件) means the following documents published by the Organisation for Economic Co-operation and Development—

- (a) the consolidated report, entitled Transfer Pricing Documentation and Country-by-Country Reporting, on Action 13 of the OECD/ G20 Action

Plan on Base Erosion and Profit Shifting published in 2015;

- (b) the document entitled Guidance on the Implementation of Country-by-Country Reporting – BEPS Action 13 published in 2017; and
- (c) the document entitled Country-by-Country Reporting: Handbook on Effective Implementation published in 2017;

consolidated financial statements (綜合財務報表), in relation to a group in the usual sense, means the financial statements of the group in which the assets, liabilities, income, expenses and cash flows of the ultimate parent entity and the constituent entities are presented as those of a single economic entity;

constituent entity (成員實體)—

- (a) in relation to a group in the usual sense, means—
 - (i) any separate business unit of the group that is included in the consolidated financial statements of the group for financial reporting purposes, or would be so included if equity interests in the business unit were traded on a public securities exchange;
 - (ii) any such business unit that is excluded from the consolidated financial statements of the group solely on size or materiality grounds; or
 - (iii) any permanent establishment of any separate business unit of the group included in subparagraph (i) or (ii) if the business unit prepares a separate financial statement for the permanent establishment for financial

reporting, regulatory, tax reporting, or internal management control purposes; or

- (b) in relation to a group in the extended sense that falls within paragraph (b) of the definition of *group in the extended sense* in this section, means—
 - (i) the single enterprise referred to in paragraph (b) of that definition; or
 - (ii) any permanent establishment of the enterprise if the enterprise prepares a separate financial statement for the permanent establishment for financial reporting, regulatory, tax reporting, or internal management control purposes;

country-by-country report (國別報告) means a country-by-country report—

- (a) to be filed annually in respect of a multinational enterprise group by a constituent entity of the group in accordance with the laws or regulations of the constituent entity's jurisdiction of tax residence; and
- (b) covering the items of information, and reflecting the format, set out in the CbCR documents;

country-by-country return (國別申報表), in relation to a multinational enterprise group, means a return for an accounting period of the group if the requirements of section 58K are met in respect of the return;

entity (實體) means a body of persons (corporate or unincorporate) or a legal arrangement, and includes—

- (a) a corporation;
- (b) a partnership;
- (c) a trust; and

(d) a permanent establishment;

file (提交), in relation to a country-by-country return, means file with the Commissioner;

filing deadline (提交期限), in relation to a country-by-country return, means the earlier of the following times—

- (a) the expiry of 12 months after the end of the accounting period to which the return relates;
- (b) the date specified in a notice given under section 58G;

group in the extended sense (廣義集團) means—

- (a) a group in the usual sense; or
- (b) a single enterprise if it is resident for tax purposes in one jurisdiction and is subject to tax in another jurisdiction with respect to the business carried out through a permanent establishment in that other jurisdiction;

group in the usual sense (常義集團) means a collection of enterprises related through ownership or control such that—

- (a) it is required to prepare consolidated financial statements for financial reporting purposes under applicable accounting principles; or
- (b) it would be so required if equity interests in any of the enterprises were traded on a public securities exchange;

HK ultimate parent entity (香港最終母實體), in relation to a multinational enterprise group, means the group's ultimate parent entity if the entity is resident for tax purposes in Hong Kong;

Hong Kong entity (香港實體) means a constituent entity that—

- (a) is resident for tax purposes in Hong Kong; or
- (b) is a permanent establishment in Hong Kong;

jurisdiction of tax residence (稅務居留地管轄區) is to be read in accordance with the meaning of *resident for tax purposes*;

multinational enterprise group (跨國企業集團) means a group in the usual sense that includes—

- (a) 2 or more enterprises the tax residence of which is in different jurisdictions; or
- (b) an enterprise that is resident for tax purposes in one jurisdiction and is subject to tax in another jurisdiction with respect to the business carried out through a permanent establishment in that other jurisdiction;

period P (指定期) and *period P-1* (對上期) have the same meanings as in section 58D(2);

permanent establishment (常設機構) has the meaning given by subsection (3);

reportable group (須申報集團) has the meaning given by section 58D(2);

reporting entity (申報實體) has the meaning given by section 58J;

service provider (服務提供者) means a service provider engaged to carry out the obligations of a reporting entity as referred to in section 58M(1);

surrogate parent entity (代母實體), in relation to a reportable group, means a constituent entity of the group appointed

as the group's surrogate parent entity as mentioned in section 58I(3) or (4);

tax residence (稅務居留地) is to be read in accordance with the meaning of *resident for tax purposes*;

ultimate parent entity (最終母實體), in relation to a group in the usual sense, means a constituent entity (*constituent entity 1*) of the group that meets the following conditions—

- (a) it owns directly or indirectly a sufficient interest in one or more other constituent entities of the group such that it is required to prepare consolidated financial statements under accounting principles generally applied in its jurisdiction of tax residence, or would be so required if its equity interests were traded on a public securities exchange in its jurisdiction of tax residence; and
 - (b) there is no other constituent entity of the group that owns directly or indirectly an interest described in paragraph (a) in constituent entity 1.
- (3) For the purposes of this Part—
- (a) a business unit of a multinational enterprise group, or an enterprise, has a permanent establishment in a jurisdiction if—
 - (i) in the case where the jurisdiction is Hong Kong—the business unit or enterprise has a permanent establishment in Hong Kong under Schedule 17G; or
 - (ii) in the case where the jurisdiction is not Hong Kong—the business unit or enterprise is regarded as having a permanent establishment in the jurisdiction under the laws of the

jurisdiction or under a bilateral or multilateral tax convention to which the jurisdiction is a party; and

- (b) a reference to a permanent establishment in a jurisdiction, in relation to a business unit of a multinational enterprise group or to an enterprise, is to be read accordingly.
- (4) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend the definition of *CbCR documents* in subsection (2).

Division 2—Master File and Local File

58C. Master file and local file to be retained

- (1) This section applies to a Hong Kong entity of a group in the extended sense, except for an accounting period of the entity in respect of which any 2 of the following conditions are satisfied—
 - (a) the total amount of the entity's revenue for the accounting period, as reflected in the entity's financial statement for the accounting period, does not exceed the amount specified in section 3(a) of Schedule 17I;
 - (b) the total value of the entity's assets at the end of the accounting period, as reflected in the entity's financial statement for the accounting period, does not exceed the amount specified in section 3(b) of Schedule 17I;
 - (c) the average number of the entity's employees during the accounting period does not exceed the number specified in section 3(c) of Schedule 17I.
- (2) The Hong Kong entity must—

- (a) prepare, within 6 months after the end of each accounting period of the entity, a file in respect of the accounting period (*local file*) and a file in respect of the corresponding accounting period of the group (*master file*); and
 - (b) retain the files for a period of not less than 7 years after the end of the accounting period of the entity.
- (3) The local file and master file must—
- (a) be in the English or Chinese language; and
 - (b) cover the items of information, and reflect the format (including terminology and order of presentation), set out in Divisions 1 and 2 of Part 3 of Schedule 17I.
- (4) Despite subsection (2)—
- (a) a local file of the Hong Kong entity in respect of an accounting period of the entity is not required to cover a type of controlled transactions specified in section 4 of Schedule 17I if the total amount of that type of controlled transaction undertaken by the entity for the accounting period does not exceed the amount specified in relation to the type in section 4 of Schedule 17I; and
 - (b) if, because of paragraph (a), all types of controlled transaction specified in section 4 of Schedule 17I undertaken by the Hong Kong entity for the accounting period are not required to be covered in the local file of the entity in respect of an accounting period, neither of the following is required to be prepared or retained by the entity—
 - (i) the local file for the accounting period;

- (ii) the master file for the corresponding accounting period of the group.
- (5) In this section, the following expressions have the meanings given by section 2 of Schedule 17I—
- accounting period* (會計期);
- controlled transaction* (受管交易);
- corresponding accounting period* (相應會計期).
- (6) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend Schedule 17I.

Division 3—Country-by-Country Reporting

Note (with no legislative effect) providing an overview of Division 3—

1. Division 3 gives effect to the country-by-country reporting requirements of the Organisation for Economic Co-operation and Development. Under those requirements, a country-by-country report (*CbC report*) must be filed in respect of a group (*reportable group*) whose annual consolidated group revenue reaches the specified threshold amount to provide, annually and for each tax jurisdiction in which the group does business, information such as the amount of revenue, profit before tax, tax paid and accrued, capital and assets.
2. Under section 58D, the requirements for filing a country-by-country return (*CbC return*) (which must include a CbC report) only apply to a reportable group.
3. A reportable group's ultimate parent entity (*UPE*) is required to file a CbC return with the Commissioner for each accounting period beginning on or after 1 January 2018 if the UPE is resident for tax purposes in Hong Kong (section 58E(1)).
4. A Hong Kong entity of a reportable group whose UPE is not resident for tax purposes in Hong Kong is required to file a

CbC return with the Commissioner if any of the following conditions is met—

- (a) the UPE is not required to file a CbC report in its jurisdiction of tax residence (*jurisdiction U*);
- (b) jurisdiction U has a current international agreement with Hong Kong providing for the automatic exchange of tax information but, by the deadline for filing the CbC return, there are no exchange arrangements in place between jurisdiction U and Hong Kong for CbC reports;
- (c) there has been a systemic failure to exchange CbC reports by jurisdiction U, which has been notified to the Hong Kong entity by the Commissioner (sections 58F(1) and 58I(1)).

5. Even if one of the conditions mentioned in item 4 of this Note is met, the Hong Kong entity is not required to file a CbC return if—

- (a) a CbC return for the relevant period is filed by another Hong Kong entity of the reportable group; or
- (b) a CbC report is filed by the reportable group's surrogate parent entity resident in another jurisdiction (*jurisdiction S*) and exchange mechanisms are in place between jurisdiction S and Hong Kong.

This and the concept of *surrogate parent entity* are dealt with in sections 58F(2) and 58I(2) to (7).

6. Also, a reportable group's UPE resident for tax purposes in Hong Kong may voluntarily file a CbC return for an accounting period beginning on or after 1 January 2016 but before 1 January 2018 (section 58E(2)).

58D. Consistency with CbCR documents and application to reportable group

- (1) This Division is to be read in the way that best secures its consistency with the requirements and guidance in the CbCR documents.

- (2) The provisions of this Division about filing a country-by-country return and notices in respect of an accounting period (*period P*) apply in relation to a multinational enterprise group that meets the threshold requirement in the immediately preceding accounting period (*period P-1*). (The group is referred to as a *reportable group* for period P.)
- (3) A multinational enterprise group meets the threshold requirement for the purposes of subsection (2) if—
 - (a) it has a total consolidated group revenue (as shown in its consolidated financial statements for period P-1) of at least the specified threshold amount; or
 - (b) it has a total consolidated group revenue (as would have been shown in its consolidated financial statements for period P-1 had the group been required to produce them by reason of the trading of equity interests in any of the enterprises in the group on a public securities exchange) of at least the specified threshold amount.
- (4) However, if—
 - (a) a multinational enterprise group's ultimate parent entity is resident for tax purposes in a jurisdiction other than Hong Kong (*jurisdiction U*);
 - (b) the group draws up its consolidated financial statements in respect of period P-1 in a currency of jurisdiction U (*currency U*) or would have drawn them up in currency U if the group had been required to produce them; and
 - (c) jurisdiction U requires the filing of a country-by-country report in respect of period P by a multinational enterprise group that has a total

consolidated group revenue for period P-1 of at least jurisdiction U's threshold amount,

the reference to specified threshold amount in subsection (3) has effect as if it were jurisdiction U's threshold amount.

(5) In this section—

jurisdiction U's threshold amount (終區門檻款額) means an amount, in currency U, that is equivalent to EUR 750 million as at January 2015;

specified threshold amount (指明門檻款額) means \$6.8 billion.

(6) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend the definitions in subsection (5).

58E. HK ultimate parent entity required to file country-by-country returns

- (1) A HK ultimate parent entity of a reportable group must file a country-by-country return in respect of period P by the filing deadline if period P begins on or after 1 January 2018.
- (2) A HK ultimate parent entity of a reportable group may file a country-by-country return in respect of period P by the filing deadline if period P begins on or after 1 January 2016 but before 1 January 2018.

58F. Other Hong Kong entities required to file country-by-country returns

- (1) A Hong Kong entity of a reportable group that is not the group's ultimate parent entity must file a country-by-country return in respect of period P by the filing deadline if, in relation to the group, a condition

precedent for Hong Kong to require a Hong Kong entity of the group that is not the ultimate parent entity to file a country-by-country report is met within the meaning of section 58I(1).

(2) Subsection (1) does not apply if—

- (a) the SPE-filing-elsewhere exception or SPE-filing-in-HK exception applies within the meaning of section 58I(2); or
- (b) by the filing deadline, another Hong Kong entity of the group has filed a country-by-country return in accordance with this section in respect of period P.

58G. Assessor's notice to entity

- (1) An assessor may give a written notice to an entity requiring it to file a country-by-country return for an accounting period specified in the notice (*specified accounting period*) by a date specified in the notice.
- (2) An entity to whom an assessor has given a notice under subsection (1) is not required to comply with the notice if the entity satisfies the assessor—
 - (a) that the entity is not a Hong Kong entity of a reportable group in respect of the specified accounting period; or
 - (b) where the entity is a Hong Kong entity of a reportable group, any of the following—
 - (i) both—
 - (A) the entity is not the group's HK ultimate parent entity; and
 - (B) in relation to the group, no condition precedent for Hong Kong to require a Hong Kong entity of the group that is

- not the ultimate parent entity to file a country-by-country report is met within the meaning of section 58I(1);
- (ii) by the filing deadline, another Hong Kong entity of the group has filed a country-by-country return in accordance with section 58E or 58F in respect of the specified accounting period;
- (iii) the SPE-filing-elsewhere exception or SPE-filing-in-HK exception applies within the meaning of section 58I(2) in respect of the specified accounting period.

58H. Notice by Hong Kong entities

- (1) Subject to subsection (3), each Hong Kong entity of a reportable group must file a written notice with the Commissioner, informing the Commissioner of the following in respect of period P—
 - (a) the name, address and business registration number of each of the group's Hong Kong entities, identifying among them (as applicable)—
 - (i) the HK ultimate parent entity;
 - (ii) the surrogate parent entity that is resident for tax purposes in Hong Kong; or
 - (iii) a Hong Kong entity (not falling within subparagraph (i) or (ii)) that is to file a country-by-country return in accordance with section 58F;
 - (b) if the group's ultimate parent entity is resident for tax purposes in a jurisdiction other than Hong Kong—

- (i) the jurisdiction of tax residence of the ultimate parent entity (*jurisdiction U*);
 - (ii) the name, address and business registration number (or equivalent particulars) of the ultimate parent entity;
 - (iii) whether, in relation to the group, a condition precedent for Hong Kong to require a Hong Kong entity of the group that is not the ultimate parent entity to file a country-by-country report is met within the meaning of section 58I(1); and
 - (iv) the date on which the ultimate parent entity has notified the tax authority of jurisdiction U in accordance with the laws or regulations of jurisdiction U that it is the ultimate parent entity (if the laws or regulations of jurisdiction U require the notification);
- (c) if the SPE-filing-elsewhere exception is to apply within the meaning of section 58I(2)(a)—
 - (i) the jurisdiction of tax residence of the surrogate parent entity (*jurisdiction S*);
 - (ii) the name, address and business registration number (or equivalent particulars) of the surrogate parent entity; and
 - (iii) the date on which the surrogate parent entity has notified the tax authority of jurisdiction S in accordance with the laws or regulations of jurisdiction S that it is the surrogate parent entity (if the laws or regulations of jurisdiction S require the notification); and

- (d) any other information relevant for determining a Hong Kong entity's obligation to file a country-by-country return under this Division.
- (2) The notice required by subsection (1) must be filed within 3 months after the end of period P (*notification deadline*).
- (3) A Hong Kong entity of a reportable group is not required to comply with subsection (1) if—
 - (a) it is none of the following—
 - (i) the HK ultimate parent entity of the group;
 - (ii) the group's surrogate parent entity resident for tax purposes in Hong Kong;
 - (iii) a Hong Kong entity of the group (not falling within subparagraph (i) or (ii)) that is to file a country-by-country return in accordance with section 58F in respect of period P; and
 - (b) by the notification deadline, another Hong Kong entity of the group (*notifying entity*) has filed a notice in accordance with subsection (1) which—
 - (i) identifies the notifying entity as an entity referred to in paragraph (a)(i), (ii) or (iii);
 - (ii) states that, in relation to the group, no condition precedent for Hong Kong to require a Hong Kong entity of the group that is not the ultimate parent entity to file a country-by-country report is met within the meaning of section 58I(1); or
 - (iii) states that the SPE-filing-elsewhere exception is to apply within the meaning of section 58I(2)(a).

58I. Condition precedent for requiring local filing; SPE-filing exceptions

- (1) For the purposes of this Division, a condition precedent for a jurisdiction (*jurisdiction R*) to require a jurisdiction R entity of a reportable group that is not the ultimate parent entity to file a country-by-country report is met in relation to the group only if—
 - (a) the ultimate parent entity is not required to file a country-by-country report in the jurisdiction in which it is resident for tax purposes (*jurisdiction U*);
 - (b) jurisdiction U has entered into an international agreement but has no exchange arrangements in effect with jurisdiction R by the time by which the report is due to be filed in jurisdiction R; or
 - (c) jurisdiction U has exchange arrangements in effect with jurisdiction R but the tax authority of jurisdiction R has notified the jurisdiction R entity that jurisdiction U—
 - (i) has suspended automatic exchange of country-by-country reports (for reasons other than those that are in accordance with the terms of those arrangements); or
 - (ii) has otherwise persistently failed to automatically provide to jurisdiction R country-by-country reports, in jurisdiction U's possession, of reportable groups that have constituent entities in jurisdiction R.
- (2) In relation to a requirement under section 58F or 58G for a Hong Kong entity (*subject entity*) of a reportable group (*group*) to file a country-by-country return in respect of period P—

- (a) the SPE-filing-elsewhere exception applies if—
 - (i) the surrogate parent entity is appointed as mentioned in subsection (3);
 - (ii) filing is effected after notification within the meaning of subsection (5); and
 - (iii) exchange mechanisms are in place within the meaning of subsection (7); and
- (b) the SPE-filing-in-HK exception applies if—
 - (i) the surrogate parent entity is appointed as mentioned in subsection (4); and
 - (ii) filing is effected after notification within the meaning of subsection (6).
- (3) A constituent entity is appointed as the surrogate parent entity of the group concerned if—
 - (a) it is resident for tax purposes in a jurisdiction other than Hong Kong (*jurisdiction S*); and
 - (b) it is appointed by the group as the sole substitute for the ultimate parent entity to file the country-by-country report in respect of period P in jurisdiction S, on behalf of the group, when a condition precedent for jurisdiction S to require a jurisdiction S entity of a reportable group that is not the ultimate parent entity to file a country-by-country report is met within the meaning of subsection (1).
- (4) A constituent entity is appointed as the surrogate parent entity of the group concerned if—
 - (a) it is resident for tax purposes in Hong Kong; and
 - (b) it is appointed by the group as the sole substitute for the ultimate parent entity to file the country-by-country return in respect of period P in Hong Kong

- on behalf of the group, when a condition precedent for Hong Kong to require a Hong Kong entity of a reportable group that is not the ultimate parent entity to file a country-by-country report is met within the meaning of subsection (1).
- (5) Filing is effected after notification if—
 - (a) a surrogate parent entity appointed under subsection (3) notifies the tax authority of jurisdiction S, in accordance with the laws or regulations of jurisdiction S, that it is the surrogate parent entity (if the laws or regulations of jurisdiction S require the notification);
 - (b) the surrogate parent entity's name, address and business registration number (or equivalent particulars) are notified to the Commissioner in accordance with section 58H; and
 - (c) by the filing deadline of the country-by-country return in respect of period P, the surrogate parent entity has filed, in jurisdiction S and in accordance with the laws or regulations of jurisdiction S, a country-by-country report in respect of period P.
- (6) Filing is also effected after notification if—
 - (a) a surrogate parent entity appointed under subsection (4) has filed a notice with the Commissioner in accordance with section 58H; and
 - (b) by the filing deadline for the country-by-country return in respect of period P, the surrogate parent entity has filed a country-by-country return in accordance with section 58F in respect of period P.
- (7) For subsection (2)(a)(iii), exchange mechanisms are in place if—

- (a) jurisdiction S has entered into an international agreement;
 - (b) by the filing deadline of the country-by-country return in respect of period P, jurisdiction S has exchange arrangements in effect with Hong Kong; and
 - (c) the Commissioner has not notified the subject entity that jurisdiction S—
 - (i) has suspended automatic exchange of country-by-country reports (for reasons other than those that are in accordance with the terms of those arrangements); or
 - (ii) has otherwise persistently failed to automatically provide to Hong Kong country-by-country reports, in jurisdiction S's possession, of reportable groups that have Hong Kong entities.
- (8) In this section—
- competent authority* (主管當局) has the meaning given by the international agreement concerned;
- exchange arrangements* (交換安排), means arrangements that—
- (a) are between the authorized representatives or competent authorities of those jurisdictions to which an international agreement applies; and
 - (b) require the automatic exchange of the country-by-country reports between the jurisdictions;
- international agreement* (國際協議) means—
- (a) unless paragraph (b) applies—

- (i) the Convention for Mutual Administrative Assistance in Tax Matters; or
 - (ii) any other arrangement or arrangements that—
 - (A) has or have effect under section 49(1) or (1A); and
 - (B) by its or their terms, provides or provide legal authority for the exchange of tax information between Hong Kong and the other territory or territories to which the arrangement or arrangements applies or apply, including automatic exchange of the information; or
 - (b) for the purposes of subsection (1) where jurisdiction R is not Hong Kong—
 - (i) the Convention for Mutual Administrative Assistance in Tax Matters; or
 - (ii) any bilateral or multilateral tax convention or any tax information exchange agreement—
 - (A) to which jurisdiction R is a party; and
 - (B) that by its terms provides legal authority for the exchange of tax information between jurisdictions, including automatic exchange of the information;
- jurisdiction R entity* (申報管轄區實體) means a constituent entity that—
- (a) is resident for tax purposes in jurisdiction R; or
 - (b) is a permanent establishment in jurisdiction R;
- jurisdiction S entity* (代母管轄區實體) means a constituent entity that—
- (a) is resident for tax purposes in jurisdiction S; or

- (b) is a permanent establishment in jurisdiction S.

58J. Reporting entities

For the purposes of this Division, each of the following entities is a reporting entity—

- (a) a HK ultimate parent entity required to file a country-by-country return and provide a notice by sections 58E(1) and 58H;
- (b) a HK ultimate parent entity that files a country-by-country return under section 58E(2);
- (c) a Hong Kong entity (not being a HK ultimate parent entity) required to file a country-by-country return by section 58F or to provide a notice by section 58H;
- (d) an entity required to file a country-by-country return by a notice given under section 58G.

58K. Further requirements concerning country-by-country return and notice

- (1) A country-by-country return filed for the purposes of this Division for a reportable group must contain—
 - (a) a country-by-country report for the group; and
 - (b) any other information specified by the Board of Inland Revenue.
- (2) A country-by-country return filed for the purposes of this Division for a reportable group—
 - (a) must be filed in the form of an electronic record that—
 - (i) is sent by using a system designated by the Commissioner; and

- (ii) contains the required information arranged in a form specified by the Commissioner; and
- (b) if the return is filed because of a notice given under section 58G—must be filed in the way specified in the notice.
- (3) A notice filed for the purposes of section 58H for a reportable group must be filed—
 - (a) in the form of an electronic record that is sent by using a system designated by the Commissioner; and
 - (b) in the way that the Commissioner specifies.
- (4) The Commissioner may designate a system for communication with the Commissioner for the purposes of subsections (2) and (3).
- (5) The Commissioner may, by notice published in the Gazette, specify requirements as to—
 - (a) the way of generating or sending an electronic record for the purposes of this section or any attachment required to be given with such an electronic record;
 - (b) how a digital signature is to be affixed to a country-by-country return filed under this Division or to a notice filed under section 58H; and
 - (c) the software and communication in relation to any attachment required to be given with an electronic record.
- (6) The Commissioner may, either generally or in a particular case, accept a country-by-country return for the purpose of this Division, despite a requirement under subsection (2) or (5) not being complied with in respect of the return.

- (7) The Commissioner may, either generally or in a particular case, accept a notice for the purposes of section 58H, despite a requirement under subsection (3) or (5) not being complied with in respect of the notice.
- (8) The Commissioner may, by a means that, the Commissioner considers appropriate, specify the circumstances or conditions in or under which a return or notice is to be accepted under subsection (6) or (7).
- (9) Any notice or other thing that specifies any matter for the purposes of this section is not subsidiary legislation.

58L. Record keeping and other obligations

- (1) If a reporting entity has changed its address, it must give notice of the change to the Commissioner within 1 month after the change of the address.
- (2) A reporting entity must—
 - (a) keep sufficient records to enable the accuracy and completeness of the country-by-country return filed under this Division to be readily ascertained; and
 - (b) retain the records for a period of 6 years beginning on the date on which the return is filed.
- (3) The Commissioner may give a notice to a reporting entity requiring it to provide information for the purposes of determining whether the information in a country-by-country return filed by the entity is accurate and complete.
- (4) A person who is required to provide information by a notice under subsection (3) must do so—
 - (a) within a period specified in the notice; and
 - (b) at a time, by a means and in a form (if any), specified in the notice.

58M. Engagement of service provider

- (1) A service provider may be engaged for or on behalf of a reporting entity—
 - (a) to comply with any requirement under—
 - (i) section 58E(1) or 58F;
 - (ii) section 58H; and
 - (iii) section 58L(1); or
 - (b) to file a country-by-country return under section 58E(2).
- (2) To avoid doubt, even if a service provider has been engaged under subsection (1) to comply with any requirement under a provision referred to in the subsection, the reporting entity is not relieved from its obligations under the provision.

Division 4—Provisions Applicable to this Part
Generally**58N. Application of obligations to non-corporate reporting entities**

- (1) In relation to a Hong Kong entity that is not a corporation, this Part applies to a person who acts for the entity or is responsible for the management of the entity as if the obligations under this Part were imposed on that person.
- (2) In relation to a Hong Kong entity that is a permanent establishment of an enterprise, this Part also applies to the enterprise as if the obligations under this Part were also imposed on that enterprise.

58O. Anti-avoidance of obligations under this Part

If—

- (a) a person enters into any arrangements; and
- (b) the main purpose, or one of the main purposes, of the person in entering into the arrangements is to avoid any obligation under this Part,

this Part has effect as if the arrangements had not been entered into.”.

17. Schedule 17I added

Before Schedule 18—

Add

“Schedule 17I

[s. 58C & Sch. 42]

**Master File and Local File: Thresholds and
Prescribed Information**

Part 1

Interpretation

1. Except for *accounting period* and *permanent establishment*, an expression used in this Schedule, and defined or otherwise explained in Part 8AA or 9A, has the same meaning as in that Part.
2. In this Schedule—

accounting period (會計期)—

- (a) in relation to a Hong Kong entity that is an enterprise—means the period with respect to which the enterprise’s financial statements are prepared; and
- (b) in relation to a Hong Kong entity that is a permanent establishment—means the period with respect to which the permanent establishment’s financial statements are prepared;

advance pricing agreements and arrangements (預先定價協議及安排) means—

- (a) any advance pricing arrangements made under section 50AAP; and
- (b) any agreements, and any arrangements, that determine, in advance of controlled transactions, an appropriate set of criteria, such as method, comparables and appropriate adjustments thereto, critical assumptions as to future events, for the determination of the transfer pricing for those transactions over a fixed period of time;

associated entity (有聯繫實體), in relation to an entity (*subject entity*) of a group in the extended sense, means—

- (a) if the subject entity is an enterprise—
 - (i) another constituent entity of the group;
 - (ii) an associated person of the subject entity; or
 - (iii) a permanent establishment of an associated enterprise of the subject entity; or
- (b) if the subject entity forms part of an enterprise (*subject enterprise*)—

- (i) another constituent entity of the group;
- (ii) an associated person of the subject enterprise;
or
- (iii) a permanent establishment of an associated enterprise of the subject enterprise;

controlled transaction (受管交易), in relation to a Hong Kong entity of a group in the extended sense, means a transaction between the entity and its associated entity;

corresponding accounting period (相應會計期), in relation to an accounting period of a Hong Kong entity of a group in the extended sense, means a period that meets the following 2 conditions—

- (a) either—
 - (i) if the group is also a group in the usual sense—the period is one in respect of which the consolidated financial statements of the group are prepared; or
 - (ii) if the group falls within paragraph (b) of the definition of **group in the extended sense** in section 58B(2)—the period is one in respect of which the financial statements of the single enterprise referred to in that paragraph are prepared;
- (b) either—
 - (i) the period coincides with the accounting period of the entity; or
 - (ii) the period ends within the accounting period of the entity;

financial asset (財務資產) has the meaning given by section 50A(1);

intangible (無形物) means something—

- (a) that is not a physical asset or a financial asset;
- (b) that is capable of being owned or controlled for use in commercial activities; and
- (c) whose use or transfer would have been compensated had it occurred in a transaction between independent persons in comparable circumstances;

permanent establishment (常設機構) has the meaning given by section 58B(3);

uncontrolled transaction (非受管交易), in relation to a Hong Kong entity of a group in the extended sense, means a transaction that is not a controlled transaction.

Part 2

Thresholds for Purposes of Section 58C

3. The thresholds specified for the purposes of section 58C(1) are—

(a) total amount of revenue	\$200 million
(b) total value of assets	\$200 million
(c) average number of employees	100
4. The amounts of controlled transactions specified for the purposes of section 58C(4) are—

(a) transfers of properties (whether movable or immovable but excluding financial assets and intangibles)	\$220 million
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- | | |
|---|---------------|
| (b) transactions in respect of financial assets | \$110 million |
| (c) transfers of intangibles | \$110 million |
| (d) other transactions | \$44 million |

Part 3

Prescribed Information

Division 1—Local File

5. A local file prepared and retained by a Hong Kong entity (*subject entity*) of a group in the extended sense in respect of an accounting period of the subject entity (*subject accounting period*) must include the following information—
- (a) in relation to the subject entity—
 - (i) a description of the management structure of the subject entity, an organization chart of the subject entity, and a description of the individuals to whom the subject entity's management reports and the territory or territories in which the individuals maintain their principal offices;
 - (ii) a detailed description of the business and business strategy pursued by the subject entity including an indication whether the subject entity has been involved in or affected by business restructurings or intangibles transfers in the subject accounting period of the subject entity or the subject entity's accounting period immediately before it and

- an explanation of those aspects of such transactions affecting the subject entity; and
- (iii) a list of key competitors;
- (b) in relation to controlled transactions, the following information for each material category of controlled transactions—
 - (i) a description of the material controlled transactions and the context in which the transactions took place;
 - (ii) the amount of payments and receipts among the subject entity and its associated entities for each category of controlled transactions broken down by tax jurisdictions of the payers or recipients;
 - (iii) an identification of the subject entity's associated entities involved in each category of controlled transactions, and the relationship among them;
 - (iv) copies of all material agreements concluded by the subject entity with any of its associated entities;
 - (v) a detailed comparability and functional analysis of the subject entity and the relevant associated entities with respect to each documented category of controlled transactions, including any changes compared to the accounting periods before the subject accounting period;
 - (vi) an indication of the most appropriate transfer pricing method with regard to the category of

- transaction and the reasons for selecting that method;
- (vii) an indication of which associated entity is selected as the tested party, if applicable, and an explanation of the reasons for this selection;
- (viii) a summary of the important assumptions made in applying the transfer pricing methodology;
- (ix) if applicable, an explanation of the reasons for performing a multi-year analysis;
- (x) a list and description of the selected comparable uncontrolled transactions (internal or external), if any, and information on the financial indicators that are relied on in the transfer pricing analysis, including a description of the comparable search methodology and the source of such information;
- (xi) a description of any comparability adjustments performed, and an indication of whether adjustments have been made to the results of the tested party, the comparable uncontrolled transactions, or both;
- (xii) a description of the reasons for concluding that the controlled transactions were priced on an arm's length basis based on the application of the selected transfer pricing method;
- (xiii) a summary of financial information used in applying the transfer pricing methodology; and

- (xiv) a copy of existing unilateral, bilateral and multilateral advance pricing agreements and arrangements and other tax rulings that are related to the controlled transactions;
- (c) in relation to financial information—
 - (i) the subject entity's audited financial statements for the subject accounting period or, if no audited financial statements exist, the subject entity's existing unaudited statements for the subject accounting period;
 - (ii) information and allocation schedules showing how the financial data used in applying the transfer pricing method may be tied to the financial statements; and
 - (iii) summary schedules of the financial data relating to the comparables used in the analysis and the sources from which that data was obtained.

Division 2—Master File

6. A master file to be prepared and retained, by a Hong Kong entity (*subject entity*) of a group in the extended sense (together with a local file in respect of an accounting period of the subject entity) must include the following information—
 - (a) in relation to organizational structure—a chart illustrating—
 - (i) the group's legal and ownership structure; and
 - (ii) (if the group is a multinational enterprise group) geographical location of constituent entities of the group;

- (b) in relation to description of group's business—a general written description of the group's business including—
 - (i) important drivers of business profits;
 - (ii) a description of the supply chain for the group's 5 largest products or service offerings by turnover and for any other products or services amounting to more than 5% of group turnover;
 - (iii) a list and brief description of important service arrangements (other than those relating to research and development services) between constituent entities of the group, including a description of the capabilities of the principal locations providing the services and transfer pricing policies for allocating services costs and determining prices to be paid for the services;
 - (iv) a description of the main geographic markets for the group's products and services that are referred to in subparagraph (ii);
 - (v) a brief written functional analysis describing the principal contributions to value creation (including key functions performed, important risks assumed, and important assets used) by individual constituent entities within the group; and
 - (vi) a description of important business restructuring transactions, acquisitions and divestitures occurring during the corresponding accounting period of the group;

- (c) in relation to the group's intangibles—
 - (i) a general description of the group's overall strategy for the development, ownership and exploitation of intangibles, including location of principal research and development facilities and location of research and development management;
 - (ii) a list of intangibles or categories of intangibles of the group that are important for transfer pricing purposes, identifying which constituent entities of the group legally own or effectively control the intangibles;
 - (iii) a list of important agreements among the group's constituent entities related to intangibles, including cost contribution arrangements, principal research service agreements and licence agreements;
 - (iv) a general description of the group's transfer pricing policies related to research and development and intangibles; and
 - (v) a general description of any important transfers of interests in or control of intangibles among the group's constituent entities during the group's corresponding accounting period, including the constituent entities, territories, and compensation involved;
- (d) in relation to the financial activities between constituent entities of the group—
 - (i) a general description of how the group is financed, including important financing arrangements with unrelated lenders;

- (ii) the identification of any constituent entity (*financing entity*) of the group that provides a central financing function for the group, including the territory under whose laws the financing entity is organized and the place of effective management of the financing entity; and
- (iii) a general description of the group's general transfer pricing policies related to financing arrangements among the group's constituent entities; and
- (e) in relation to the group's financial and tax positions—
 - (i) the group's consolidated financial statements for the corresponding accounting period; and
 - (ii) a list and brief description of the group's existing unilateral advance pricing agreements and arrangements and other tax rulings relating to the allocation of income among territories.”.

Division 5—Amendment Relating to Transfer Pricing: Other Amendments Relating to New Part 9A

18. Section 2 amended (interpretation)

Section 2(1)—

Repeal the definition of *service provider*

Substitute

“*service provider* (服務提供者)—

- (a) except in relation to a provision of Part 9A, has the meaning given by section 50A(1);

- (b) in relation to a provision of Part 9A, has the meaning given by section 58B(2);”.

Division 6—Amendments Relating to Penalties and Offences

19. Section 80 amended (penalties for failure to make returns, making incorrect returns, etc.)

- (1) Section 80(2)—

Repeal

everything after “treble”

Substitute

“the undercharged amount.”.

- (2) After section 80(2F)—

Add

“(2G) A person commits an offence—

- (a) if the person, without reasonable excuse, fails to comply with section 50AA(5);
- (b) if the person, without reasonable excuse, fails to comply with a requirement of a notice given to the person under section 50AAB(2); or
- (c) if—
 - (i) the person, without reasonable excuse—
 - (A) makes an incorrect statement, or provides incorrect information, in connection with any mutual agreement procedure or arbitration referred to in section 50AAB; or
 - (B) omits anything from a statement or information made or provided in

- connection with the procedure or arbitration; and
- (ii) the statement or information referred to in subparagraph (i)(A), or the thing referred to in subparagraph (i)(B), is material to the case or issue to which the procedure or arbitration relates.
- (2H) A person who commits an offence under subsection (2G)(a) is liable on conviction to—
- (a) a fine at level 3; and
- (b) a further fine of the undercharged amount.
- (2I) A person who commits an offence under subsection (2G)(b) is liable on conviction to a fine at level 3, and the court may order the person to comply, within a time specified in the order, with the requirements of the notice given to the person under section 50AAB(2).
- (2J) If a person fails to comply with an order of the court under subsection (2I), the person commits an offence and is liable on conviction to a fine at level 4.
- (2K) A person who commits an offence under subsection (2G)(c) is liable on conviction to—
- (a) a fine at level 3; and
- (b) a further fine of treble the undercharged amount.
- (2L) A person commits an offence—
- (a) if the person, without reasonable excuse, fails to comply with a requirement under section 50AAM(11), 50AAN(3) or 50AAO(3);
- (b) if—
- (i) the person, without reasonable excuse, makes an incorrect statement or provides incorrect

- information in connection with the following claim or application, or omits anything from a statement made or information provided in connection with the following claim or application—
- (A) the person's claim for relief under section 50AAM, 50AAN or 50AAO; or
- (B) the person's application for an advance pricing arrangement under section 50AAP(1); and
- (ii) the statement or information that is incorrect, or thing that is omitted, is material to the claim or application;
- (c) if the person, without reasonable excuse, fails to comply with a requirement under section 50AAS;
- (d) if—
- (i) the person either—
- (A) without reasonable excuse and in purported compliance with a requirement under section 50AAS, provides incorrect information in relation to an advance pricing arrangement; or
- (B) without reasonable excuse, omits anything from information provided, in relation to an advance pricing arrangement, in purported compliance with the requirement; and
- (ii) the information referred to in subparagraph (i)(A), or the thing referred to in

- subparagraph (i)(B), is material to the arrangement;
- (e) if the person, without reasonable excuse, fails to comply with a requirement of section 50AAT; or
 - (f) if the person, without reasonable excuse, fails to comply with the requirement of a notice given to the person under section 3 of Schedule 17H.
- (2M) A person who commits an offence under subsection (2L)(a), (b), (c) or (d) is liable on conviction to—
- (a) a fine at level 3; and
 - (b) a further fine of the undercharged amount.
- (2N) A person who commits an offence under subsection (2L)(e) is liable on conviction to a fine at level 5, and the court may order the person to do, within a time specified in the order, the act that the person has failed to do.
- (2O) If a person fails to comply with an order of the court under subsection (2N), the person commits an offence and is liable on conviction to a fine at level 6.
- (2P) A person who commits an offence under subsection (2L)(f) is liable on conviction to a fine at level 3.
- (2Q) A person commits an offence if the person, without reasonable excuse, fails to comply with a requirement of section 58C.
- (2R) A person who commits an offence under subsection (2Q) is liable on conviction to a fine at level 5, and the court may order the person to do, within a time specified in the order, the act that the person has failed to do.
- (2S) If a person fails to comply with an order of the court under subsection (2R), the person commits an offence and is liable on conviction to a fine at level 6.”

- (3) After section 80(6)—

Add

- “(7) In this section—

undercharged amount (少徵稅款)—

- (a) for an offence that relates to any incorrect return, statement or information or an omission from any statement or information—means the amount of tax that—
 - (i) has been undercharged as a result of the incorrect return, statement or information or omission; or
 - (ii) would have been so undercharged if the return, statement or information had been accepted as correct or the omission had not been detected;
- (b) for an offence that relates to a failure to comply with a provision of this Ordinance or with a notice under the provision—means the amount of tax that has been undercharged as a result of the failure, or would have been so undercharged if the failure had not been detected; or
- (c) for any other offence—means the amount of tax that has been undercharged as a result of the offence, or would have been so undercharged had the offence not been detected.”.

20. Sections 80G to 80J added

After section 80F—

Add

“80G. Offences of reporting entities in relation to country-by-country reporting

- (1) A reporting entity commits an offence if the entity, without reasonable excuse—
 - (a) fails to comply with a requirement under—
 - (i) section 58E(1) or 58F;
 - (ii) section 58H;
 - (iii) section 58L(1); or
 - (iv) section 58L(2); or
 - (b) fails to comply with a requirement of a notice given to it under section 58L(3).
- (2) For subsection (1)(a)(i), (ii) and (iii), engaging a service provider does not in itself constitute a reasonable excuse.
- (3) A reporting entity that commits an offence under subsection (1) is liable on conviction to a fine at level 5, and the court may order the entity to do, within the time specified in the order, the act that the entity has failed to do.
- (4) In case of an offence under subsection (1)(a)(i) and (ii), the reporting entity is liable to a further fine of \$500 for every day or part of a day during which the offence continues after conviction.
- (5) If a reporting entity fails to comply with an order of the court under subsection (3), the entity commits an offence and is liable on conviction to a fine at level 6.
- (6) A reporting entity commits an offence if—
 - (a) the entity—
 - (i) files, or causes or allows to be filed on its behalf, a specified document for a specified purpose and the document is misleading, false

- or inaccurate in a material particular, whether or not because any information is omitted from the document; or
- (ii) in purported compliance with a requirement of a notice given to the entity under section 58L(3), provides any information that is misleading, false or inaccurate in a material particular, whether or not because anything is omitted from the information; and
- (b) the entity—
 - (i) knows the document referred to in paragraph (a)(i), or the information referred to in paragraph (a)(ii), is misleading, false or inaccurate in a material particular;
 - (ii) is reckless as to whether the document or information is misleading, false or inaccurate in a material particular; or
 - (iii) has no reasonable ground to believe that the document or information is true or accurate.
- (7) A reporting entity commits an offence if the entity—
 - (a) discovers that—
 - (i) a specified document that the entity has filed, or has caused or allowed to be filed on its behalf, for a specified purpose is misleading, false or inaccurate in a material particular, whether or not because any information is omitted from the document; or
 - (ii) any information provided, in purported compliance with a requirement of a notice given to the entity under section 58L(3), is misleading, false or inaccurate in a material

- particular, whether or not because anything is omitted from the information; and
- (b) without reasonable excuse, fails to notify the Commissioner of the discovery within a reasonable time.
- (8) A reporting entity that commits an offence under subsection (6) or (7) is liable on conviction to a fine at level 5.
- (9) A reporting entity commits an offence if the entity—
- (a) with intent to defraud, files or causes or allows to be filed on its behalf, a specified document for a specified purpose and the document is misleading, false or inaccurate in a material particular, whether or not because any information is omitted from the document; or
- (b) with intent to defraud and in purported compliance with a requirement of a notice given to the entity under section 58L(3), provides any information that is misleading, false or inaccurate in a material particular, whether or not because anything is omitted from the information.
- (10) A reporting entity that commits an offence under subsection (9) is liable—
- (a) on summary conviction to—
- (i) a fine at level 3; and
- (ii) imprisonment for 6 months; or
- (b) on conviction on indictment to—
- (i) a fine at level 5; and
- (ii) imprisonment for 3 years.

- (11) In relation to a reporting entity that is not a corporation, this section applies to a person who acts for the entity or is responsible for the management of the entity as if references to a reporting entity were references to that person.
- (12) In relation to a reporting entity that is a permanent establishment of an enterprise, this section also applies to the enterprise as if references to a reporting entity were references to that enterprise.
- (13) In this section—
- (a) *specified document* (指明文件) means a return or notice; and
- (b) a reference to filing a specified document for a specified purpose means—
- (i) filing a return in purported compliance with section 58E(1) or 58F;
- (ii) filing a return under section 58E(2); or
- (iii) filing a notice in purported compliance with section 58H.

80H. Offences of service provider in relation to country-by-country reporting

- (1) A person who is a service provider engaged by a reporting entity to carry out the entity's obligations commits an offence if—
- (a) where the engagement relates to obligations under section 58E(1) or 58F—the person, without reasonable excuse, fails to cause a country-by-country return to be filed as required under section 58E(1) or 58F; or

- (b) where the engagement relates to obligations under section 58H—the person, without reasonable excuse, fails to cause a notice to be filed as required under section 58H.
- (2) A person who is a service provider engaged by a reporting entity commits an offence if—
 - (a) the person files on behalf of the entity, or causes or allows the entity to file, a specified document for a specified purpose and the document is misleading, false or inaccurate in a material particular, whether or not because any information is omitted from the document; and
 - (b) the person—
 - (i) knows the document is misleading, false or inaccurate in a material particular;
 - (ii) is reckless as to whether the document is misleading, false or inaccurate in a material particular; or
 - (iii) has no reasonable ground to believe that the document is true or accurate.
- (3) A person who is a service provider engaged by a reporting entity commits an offence if the person—
 - (a) discovers that a specified document that the person has filed on behalf of the entity, or has caused or allowed the entity to file, for a specified purpose is misleading, false or inaccurate in a material particular, whether or not because any information is omitted from the document; and
 - (b) without reasonable excuse, fails to notify the Commissioner of the discovery within a reasonable time.

- (4) A person who commits an offence under subsection (1), (2) or (3) is liable on conviction to a fine at level 5.
- (5) A person who is a service provider engaged by a reporting entity commits an offence if the person, with intent to defraud, files on behalf of the entity, or causes or allows the entity to file, a specified document for a specified purpose and the document is misleading, false or inaccurate in a material particular, whether or not because any information is omitted from the document.
- (6) A person who commits an offence under subsection (5) is liable—
 - (a) on summary conviction to—
 - (i) a fine at level 3; and
 - (ii) imprisonment for 6 months; or
 - (b) on conviction on indictment to—
 - (i) a fine at level 5; and
 - (ii) imprisonment for 3 years.
- (7) The court may order a service provider who commits an offence under subsection (1) to do, within the time specified in the order, the act that the person has failed to do.
- (8) If a service provider fails to comply with an order of the court under subsection (7), the service provider commits an offence and is liable on conviction to a fine at level 6.
- (9) In this section—
 - (a) *specified document* (指明文件) means a return or notice; and
 - (b) a reference to filing a specified document for a specified purpose, in relation to a service provider engaged by a reporting entity, means—

- (i) if the engagement relates to obligations under section 58E(1) or 58F—filing a return in purported compliance with that section;
- (ii) if the engagement relates to filing a return under section 58E(2)—filing a return under that section; or
- (iii) if the engagement relates to obligations under section 58H—filing a notice in purported compliance with that section.

80I. Offences of directors, etc. of reporting entities and service provider in relation to country-by-country reporting

If—

- (a) any of the following persons is a corporation—
 - (i) a reporting entity that commits an offence under section 80G;
 - (ii) a person who commits an offence under section 80G by virtue of section 80G(11) or (12);
 - (iii) a service provider that commits an offence under section 80H; and
- (b) the offence was committed with the consent or connivance of a director, or other officer concerned in the management, of the corporation, or any person purporting to act as such director or officer (*specified person*),

the director or officer or specified person, as the case requires, also commits the offence and is liable on conviction to the penalty provided for that offence.

80J. Miscellaneous provisions for certain offences relating to country-by-country reporting

- (1) Despite section 26 of the Magistrates Ordinance (Cap. 227), proceedings in respect of an offence under section 80G, 80H or 80I, other than an indictable offence, may be brought within 6 years after the date on which the offence was committed.
- (2) The Commissioner may compound an offence under section 80G, 80H or 80I, and may, before judgment, stay or compound any proceedings instituted for the offence.”.

21. Section 82 amended (penal provisions relating to fraud, etc.)

- (1) After section 82(1)—

Add

“(1AA) A person commits an offence if—

- (a) the person wilfully, with intent to evade tax or to assist any other person to evade tax—
 - (i) makes an incorrect statement, or provides incorrect information, in connection with any mutual agreement procedure or arbitration referred to in section 50AAB; or
 - (ii) omits anything from a statement or information made or provided in connection with the procedure or arbitration; and
- (b) the statement or information referred to in paragraph (a)(i), or the thing referred to in paragraph (a)(ii), is material to the case or issue to which the procedure or arbitration relates.

(1AAB) A person commits an offence if—

- (a) the person wilfully, with intent to evade tax or to assist any other person to evade tax, makes an incorrect statement or provides incorrect information in connection with the following claim or application, or omits anything from a statement made or information provided in connection with the following claim or application—
 - (i) the person's claim for relief under section 50AAM, 50AAN or 50AAO; or
 - (ii) the person's application for an advance pricing arrangement under section 50AAP(1); and
 - (b) the statement or information that is incorrect, or thing that is omitted, is material to the claim or application.
- (1AAC) A person commits an offence if—
- (a) the person either—
 - (i) wilfully, with intent to evade tax or to assist any other person to evade tax and in purported compliance with a requirement under section 50AAS, provides incorrect information in relation to an advance pricing arrangement; or
 - (ii) wilfully, with intent to evade tax or to assist any other person to evade tax, omits anything from the information provided, in relation to an advance pricing arrangement, in purported compliance with the requirement; and
 - (b) the information referred to in paragraph (a)(i), or the thing referred to in paragraph (a)(ii), is material to the arrangement.”.

- (2) Section 82(1A), after “(1)—”
Add
“, (1AA), (1AAB) or (1AAC)”.
 - (3) Section 82(1A)(a)(ii)—
Repeal
everything after “treble”
Substitute
“the undercharged amount; and”.
 - (4) Section 82(1A)(b)(ii)—
Repeal
everything after “treble”
Substitute
“the undercharged amount; and”.
 - (5) After section 82(2)—
Add
“(3) In this section—
undercharged amount (少徵稅款), in relation to an offence, means the amount of tax that has been undercharged as a result of the offence, or would have been so undercharged had the offence not been detected.”.
22. **Section 82A amended (additional tax in certain cases)**
- (1) Section 82A(1)—
Repeal
everything after “treble”
Substitute
“the undercharged amount.”.

(2) After section 82A(1)—

Add

“(1A) If—

- (a) a person, without reasonable excuse, fails to comply with section 50AA(5); and
- (b) no prosecution for an offence under section 80 has been instituted in respect of the same facts,

the person is liable to be assessed under this section to additional tax of an amount not exceeding the undercharged amount.

(1B) If—

- (a) a person, without reasonable excuse—
 - (i) makes an incorrect statement, or provides incorrect information, in connection with any mutual agreement procedure or arbitration referred to in section 50AAB; or
 - (ii) omits anything from a statement or information made or provided in connection with the procedure or arbitration;
- (b) the statement or information referred to in paragraph (a)(i), or the thing referred to in paragraph (a)(ii), is material to the case or issue to which the procedure or arbitration relates; and
- (c) no prosecution for an offence under section 80 or 82 has been instituted in respect of the same facts,

the person is liable to be assessed under this section to additional tax of an amount not exceeding treble the undercharged amount.

(1C) Subsection (1D) applies if—

- (a) an assessment or additional assessment made on a person under section 50AAF(5) or 50AAK(9) has become final and conclusive under section 70 (the assessment or additional assessment is referred to as the *relevant assessment*); and
- (b) the amount of the person's income as assessed under section 50AAF(5) or 50AAK(9) to which the relevant assessment relates (*the person's assessed income*) is larger than the amount of the person's income as stated in the person's tax return.

(1D) The person is liable to be assessed to additional tax under this section of an amount not exceeding the difference between—

- (a) the amount of tax assessed on the basis of the amount of the person's assessed income; and
- (b) the amount of tax that would have been assessed if the amount of the person's income as stated in the person's tax return had been accepted for the purpose of assessment.

(1E) Subsection (1F) applies if—

- (a) an assessment made on a person for a year of assessment (*subject year*) has become final and conclusive under section 70 and the assessment has taken into account the person's loss for an earlier year of assessment (*year of loss*) as computed under section 50AAF(5) or 50AAK(9) (*the person's computed loss*); and
- (b) the amount of the person's computed loss is smaller than the amount of the person's loss as stated in the person's tax return for the year of loss.

- (1F) The person is liable to be assessed to additional tax under this section for the subject year of an amount not exceeding the difference between—
- (a) the amount of tax assessed taking into account the amount of the person's computed loss; and
 - (b) the amount of tax that would have been assessed if the amount of the person's loss as stated in the person's tax return for the year of loss had been accepted for the purpose of assessment.
- (1G) A person is not liable to be assessed to additional tax under subsection (1D) or (1F) if the person proves that the person has made reasonable efforts to determine the arm's length amount under section 50AAF(1) or 50AAK(2).
- (1H) If—
- (a) any of the following applies—
 - (i) a person, without reasonable excuse, fails to comply with a requirement under section 50AAM(11), 50AAN(3) or 50AAO(3);
 - (ii) both—
 - (A) a person, without reasonable excuse, makes an incorrect statement or provides incorrect information in connection with the following claim or application, or omits anything from a statement made or information provided in connection with the following claim or application—
 - (I) the person's claim for relief under section 50AAM, 50AAN or 50AAO; or

- (II) the person's application for an advance pricing arrangement under section 50AAP(1); and
 - (B) the statement or information that is incorrect, or thing that is omitted, is material to the claim or application;
- (iii) a person, without reasonable excuse, fails to comply with a requirement under section 50AAS;
- (iv) both—
- (A) a person either—
 - (I) without reasonable excuse and in purported compliance with a requirement under section 50AAS, provides incorrect information in relation to an advance pricing arrangement; or
 - (II) without reasonable excuse, omits anything from information provided, in relation to an advance pricing arrangement, in purported compliance with the requirement; and
 - (B) the information referred to in sub-subparagraph (A)(I), or the thing referred to in sub-subparagraph (A)(II), is material to the arrangement; and
- (b) no prosecution for an offence under section 80 or 82 has been instituted in respect of the same facts,

the person is liable to be assessed under this section to additional tax of an amount not exceeding the undercharged amount.”.

- (3) Section 82A(3), after “deputy commissioner personally”—

Add

“(each is referred to as the *specified authority*)”.

- (4) Section 82A—

Repeal subsection (4)

Substitute

“(4) Before making an assessment of additional tax, the specified authority must—

- (a) give notice to the person that the specified authority proposes to assess additional tax and the notice must—

- (i) inform the person of the following—

- (A) for additional tax to be assessed under subsection (1)—the alleged incorrect return, incorrect statement or incorrect information or alleged failure to comply with a requirement of the notice given to the person under section 51(1) or (2A) or alleged failure to comply with section 51(2);
- (B) for additional tax to be assessed under subsection (1A)—the alleged failure to comply with section 50AA(5);
- (C) for additional tax to be assessed under subsection (1B)—the alleged incorrect statement, incorrect information or

omission from any statement or information;

- (D) for additional tax to be assessed under subsection (1D) or (1F)—the assessment or additional assessment made or computation of loss issued or revised under section 50AAF(5) or 50AAK(9);
 - (E) for additional tax to be assessed under subsection (1H)—the alleged failure to comply with a requirement under section 50AAM(11), 50AAN(3), 50AAO(3) or 50AAS or the alleged incorrect statement, incorrect information or omission from any statement or information;
- (ii) include a statement that, with regard to the proposed assessment on the person of additional tax, the person has the right—
- (A) to submit written representations to the specified authority; and
 - (B) for additional tax to be assessed under subsection (1D) or (1F)—to submit to the specified authority written representations and evidence for the purposes of subsection (1G); and
- (iii) specify the date, which must not be earlier than 21 days from the date of service of the notice, by which representations and evidence that the person may wish to submit under subparagraph (ii) must be received by the specified authority; and

- (b) consider and take into account any representations and evidence that the specified authority may receive under paragraph (a).”.

(5) Section 82A—

Repeal subsection (4A)

Substitute

- “(4A) Despite subsection (4), if the specified authority is of the opinion that the person the authority proposes to assess to additional tax under this section is about to leave Hong Kong, the authority may assess the person to additional tax under this section without giving the notice otherwise required to be given under subsection (4)(a).”.

(6) Section 82A(7)—

Repeal

everything after “additional tax”

Substitute

“under this section is not liable to be charged on the same facts with an offence under section 80 or 82.”.

(7) After section 82A(8)—

Add

“(9) In this section—

undercharged amount (少徵稅款)—

- (a) for additional tax assessed because of any incorrect return, statement or information or an omission from any statement or information—means the amount of tax that—

- (i) has been undercharged as a result of the incorrect return, statement or information or omission; or

- (ii) would have been so undercharged if the return, statement or information had been accepted as correct or the omission had not been detected; or

- (b) for additional tax assessed because of a failure to comply with a provision of this Ordinance or with a notice under the provision—means the amount of tax that has been undercharged as a result of the failure, or would have been so undercharged if the failure had not been detected.”.

Division 7—Amendments Relating to Advance Rulings

23. Schedule 10 amended

- (1) Schedule 10, Part 1—

Repeal section 1

Substitute

- “1. Subject to section 1A and on an application made by a person in accordance with this Part, the Commissioner may make a ruling on how a provision of this Ordinance applies to the applicant or to the arrangement described in the application, whether or not reference is made to that provision in the application.

- 1A. A ruling is not to be made under section 1 on how a provision of this Ordinance applies if the provision relates to—

- (a) the imposition or remission of a penalty;

- (b) the correctness of a return or other information supplied by a person;
 - (c) the prosecution of a person;
 - (d) the recovery of a debt owing by a person; or
 - (e) the computation of income or loss under section 50AAF or 50AAK.”.
- (2) Schedule 10, Part 2, section 1(a)(i)—
Repeal
 “\$30,000”
Substitute
 “\$45,000”.
- (3) Schedule 10, Part 2, section 1(a)(ii)—
Repeal
 “\$10,000”
Substitute
 “\$15,000”.
- (4) Schedule 10, Part 2, section 1(a)(iii)—
Repeal
 “\$10,000”
Substitute
 “\$15,000”.
- (5) Schedule 10, Part 2, section 1(b)(i)—
Repeal
 “\$1,330”
Substitute
 “\$2,650”.

- (6) Schedule 10, Part 2, section 1(b)(ii)—
Repeal
 “\$1,260”
Substitute
 “\$2,240”.
- (7) Schedule 10, Part 2, section 1(b)(iii)—
Repeal
 “\$1,000”
Substitute
 “\$1,730”.

Division 8—Amendments Relating to Profits Tax Concessions for Particular Classes of Person

- 24. **Section 14B amended (qualifying reinsurance business and captive insurance business)**
 - (1) Section 14B(1), after “subsection (2)”—
Add
 “and section 26AB”.
 - (2) Section 14B(1)(a)—
Repeal
 everything after “reinsurance”
Substitute
 “as a professional reinsurer; or”.
 - (3) Section 14B(1)(b)—
Repeal
 everything after “insurance”

Substitute

“as an authorized captive insurer.”.

(4) Section 14B—

Repeal subsection (2)

Substitute

“(2) Subsection (1) applies to a corporation for a year of assessment only if—

(a) in that year of assessment, the activities that produce the corporation’s assessable profits that fall within subsection (1)(a) or (b) in that year are—

(i) carried out in Hong Kong by the corporation;
or

(ii) arranged by the corporation to be carried out in Hong Kong; and

(b) the corporation has elected in writing that subsection (1) applies to it.”.

(5) After section 14B(2)—

Add

“(3) An election under subsection (2)(b), once made, is irrevocable.

(4) In this section—

authorized captive insurer (獲授權專屬自保保險人) means a company that—

(a) is a captive insurer as defined by section 2(7)(a) of the Insurance Ordinance (Cap. 41); and

(b) is authorized under section 8 of that Ordinance to carry on in or from Hong Kong insurance business as such a captive insurer;

professional reinsurer (專業再保險人) means a company authorized under section 8 of the Insurance Ordinance (Cap. 41) to carry on in or from Hong Kong reinsurance business only.”.

25. Section 14C amended (qualifying corporate treasury centre: interpretation)

(1) Section 14C(1)—

(a) definition of *non-Hong Kong associated corporation*;

(b) definition of *qualifying corporate treasury service*;

(c) definition of *qualifying corporate treasury transaction*;

(d) definition of *qualifying lending transaction*—

Repeal the definitions.

(2) Section 14C(1)—

Add in alphabetical order

“*intra-group lending transaction* (集團內部貸款交易), in relation to a corporation, means a transaction under which the corporation lends money, in the ordinary course of its intra-group financing business, to its associated corporation;”.

(3) Section 14C—

Repeal subsections (3) and (4).

26. Section 14D amended (qualifying corporate treasury centre: profits tax concession)

(1) Section 14D(1)—

Repeal

“subsections (5) and (8)”

Substitute

“subsection (5) and section 26AB”.

- (2) Section 14D(1)(a)—

Repeal

“qualifying”

Substitute

“intra-group”.

- (3) Section 14D(1)(b)—

Repeal

“qualifying”.

- (4) Section 14D(1)(c)—

Repeal

“qualifying”.

- (5) Section 14D—

Repeal subsection (8).

27. Section 14H amended (aircraft leasing tax concessions: concession for qualifying aircraft lessor)

Section 14H(1), after “(6)”—

Add

“and section 26AB”.

28. Section 14J amended (aircraft leasing tax concessions: concession for qualifying aircraft leasing manager)

Section 14J(1), after “(7)”—

Add

“and section 26AB”.

29. Section 16 amended (ascertainment of chargeable profits)

- (1) Section 16(1A)(a)—

Repeal

“(as defined by section 14G(1))”.

- (2) Section 16(1A)(c), before “14H(1)”—

Add

“14B(1), 14D(1),”.

- (3) After section 16(1A)—

Add

“(1B) However, subsection (1A) does not apply in relation to a person for a year of assessment if, had the sum mentioned in subsection (1A)(b) not been so payable, it would have been included in the assessable profits of the person chargeable at a reduced rate under section 14B(1), 14D(1), 14H(1) or 14J(1) for the year of assessment.

- (1C) For subsection (1A), a person is a connected person of a corporation if the person is—

(a) an associated corporation of the corporation; or

(b) a person (other than a corporation)—

(i) over whom the corporation has control;

(ii) who has control over the corporation; or

(iii) who is under the control of the same person as is the corporation.

- (1D) For subsection (1A), a person is also a connected person of a corporation in relation to a case where a sum is included in the corporation’s assessable profits chargeable at a reduced rate under section 14H(1) or 14J(1) for a year of assessment if the person is a

partnership in which the corporation or its associate (as defined by section 14G(1)) is a partner.”.

30. Section 23A amended (ascertainment of assessable profits of insurance corporations other than life insurance corporations)

(1) Section 23A—

Repeal subsections (2) and (2A).

(2) Section 23A(3), definition of *premiums from insurance business in Hong Kong*, paragraph (b)—

Repeal the semicolon

Substitute a full stop.

(3) Section 23A(3)—

(a) definition of *additional amount for unexpired risks, claims outstanding, fund and unearned premiums*;

(b) definition of *authorized captive insurer*;

(c) definition of *gains or profits from offshore insurance investments*;

(d) definition of *gains or profits from offshore reinsurance investments*;

(e) definition of *offshore insurance income*;

(f) definition of *offshore reinsurance income*;

(g) definition of *permanent establishment*;

(h) definition of *premiums from insurance of offshore risks*;

(i) definition of *premiums from reinsurance of offshore risks*;

(j) definition of *professional reinsurer*;

(k) definition of *technical reserves*—

Repeal the definitions.

31. Section 23B amended (ascertainment of the assessable profits of a ship-owner carrying on business in Hong Kong)

(1) Section 23B(3)—

Repeal

“and (5)”

Substitute

“, (4AA) and (5) and section 26AB”.

(2) Section 23B(4)—

Repeal

“subsection (5)”

Substitute

“subsections (4AA) and (5) and section 26AB”.

(3) After section 23B(4)—

Add

“(4AA) For the purposes of subsection (3) or (4), in determining the amount of relevant sums earned by or accrued to a person during the basis period for a year of assessment, the exempt sums are to be excluded if, in that period, the activities that produce the exempt sums are—

(a) carried out in Hong Kong by the person; or

(b) arranged by the person to be carried out in Hong Kong.”.

(4) Section 23B(12), definition of *relevant sums*—

Repeal

everything after “river trade”

Substitute

“waters;”.

32. Section 26AB added

Part 4, after section 26A—

Add

“26AB. Threshold requirements for determining whether profits producing activities are carried out in Hong Kong etc.

(1) The Commissioner may, by notice published in the Gazette, prescribe a threshold requirement for determining whether an activity producing—

(a) the assessable profits of a corporation that fall within section 14B(1)(a) or (b), 14D(1)(a), (b) or (c), 14H(1) or 14J(1); or

(b) the exempt sums mentioned in section 23B(4AA), is carried out in Hong Kong by the corporation or the person concerned (*taxpayer*) or is arranged by the taxpayer to be carried out in Hong Kong for a year of assessment or a basis period.

Note (with no legislative effect)—

See sections 14B(2)(a), 14D(5)(a)(ii), 14H(4)(a)(ii), 14J(5)(a)(ii) and 23B(4AA) which set out the condition for activities producing the assessable profits or the exempt sums concerned to be carried out in Hong Kong or arranged to be carried out in Hong Kong.

(2) If a threshold requirement is prescribed for an activity, the activity is not considered to be carried out in Hong Kong by the taxpayer or arranged by the taxpayer to be carried out in Hong Kong for the year of assessment or the basis period unless the threshold requirement is met.

(3) In this section—

threshold requirement (門檻要求), in relation to an activity, means the level of the activity in Hong Kong as measured by various indicators, such as—

(a) the number of full time employees in Hong Kong engaged in the activity; and

(b) the amount of expenditure incurred in Hong Kong for the activity.”.

Division 9—Amendments Relating to Transitional Provisions

33. Section 89 amended (transitional provisions)

Section 89—

Add

“(20) Schedule 42 sets out transitional provisions that have effect for the purposes of amendments to this Ordinance made by the Inland Revenue (Amendment) (No. 6) Ordinance 2017 (of 2017).”.

34. Schedule 42 added

The Ordinance—

Add

“Schedule 42

[s. 89(20)]

Transitional Provisions for Inland Revenue (Amendment) (No. 6) Ordinance 2017

1. Interpretation

In this Schedule—

Amendment Ordinance (《修訂條例》) means the Inland Revenue (Amendment) (No. 6) Ordinance 2017 (of 2017);

commencement date (生效日期) means the day on which the Amendment Ordinance comes into operation.

2. Provisions relating to tax credit

The amendments made to sections 8, 16 and 50 by the Amendment Ordinance, and section 50AA, apply in relation to tax payable for a year of assessment beginning on or after 1 April 2018.

3. Provisions relating to mutual agreement procedure and arbitration

Section 50AAB applies in relation to—

- (a) any case presented for mutual agreement procedure on or after the commencement date, regardless of whether the case relates to a year of assessment that began before the date; and
- (b) any issue if the request for referring the issue for arbitration is made on or after the commencement date, regardless of whether the issue relates to a year of assessment that began before the date.

4. Provisions relating to transfer pricing rules, relief and advance pricing arrangement

- (1) Subject to this section, the following provisions apply in relation to a year of assessment beginning on or after 1 April 2018—
 - (a) Divisions 2 and 3 of Part 8AA and Schedule 17G;
 - (b) Division 4 of Part 8AA and Schedule 17H;
 - (c) sections 15BA and 15F;
 - (d) the amendments made to rules 3(1A) and 5(1) of the Inland Revenue Rules (Cap. 112 sub. leg. A) by the Amendment Ordinance; and
 - (e) rule 5(1A) of those Rules.
- (2) The provisions referred to in subsection (1)(a), (d) and (e) do not apply in relation to a transaction entered into or effected before the commencement date.
- (3) Subsection (1)(b) does not prevent principles developed in an advance pricing arrangement from being applied, under section 50AAQ(4), in relation to a period which wholly or partly falls before 1 April 2018 if the application for the arrangement is made on or after the commencement date.
- (4) Section 15BA does not apply in relation to a change in trading stock effected before the commencement date.
- (5) A person is not chargeable under section 15F to profits tax in respect of a sum (or any part of it) if the sum accrued to or was received by or for the benefit of an associate of the person before the commencement date.
- (6) A person is chargeable under section 15F to profits tax in respect of a sum (or any part of it) if the sum accrues to or is received by or for the benefit of an associate of

the person on or after the commencement date, regardless of whether the sum arises from a transaction entered into or effected before the commencement date.

5. Provisions relating to master file and local file

Division 2 of Part 9A and Schedule 17I apply in relation to an accounting period of a constituent entity of a group in the extended sense beginning on or after 1 April 2018.

6. Provisions relating to country-by-country reporting

Sections 58F, 58G and 58H apply in relation to an accounting period beginning on or after 1 January 2018.

7. Provisions relating to fees for application for advance ruling

The amendments made to Part 2 of Schedule 10 by the Amendment Ordinance apply in relation to an application for a ruling under section 88A received on or after the commencement date.

8. Provisions relating to profits tax concessions

The amendments made to sections 14B, 14C, 14D, 14H, 14J, 16, 23A and 23B by the Amendment Ordinance, and section 26AB, apply in relation to tax payable for a year of assessment beginning on or after 1 April 2018.”.

Part 3

Amendments to Inland Revenue Rules

35. Rule 3 amended (financial institution: profits of Hong Kong branch offices)

Rule 3(1A)—

Repeal

“17F and 17G”

Substitute

“17F, 17G and 50AAK”.

36. Rule 5 amended (profits of Hong Kong branch offices of person other than financial institution)

(1) Rule 5, before paragraph (1)—

Add

“(1A) This rule has effect to the extent to which it is not inconsistent with section 50AAK of the Ordinance.”.

(2) Rule 5(1)—

Repeal the definition of *permanent establishment*

Substitute

“*permanent establishment* (常設機構) has the meaning given by section 50AAC(4) of the Ordinance;”.

(3) Rule 5(2), Chinese text—

Repeal

“永久”

Substitute

“常設”.

Explanatory Memorandum

The object of this Bill is to amend the Inland Revenue Ordinance (Cap. 112) (*Ordinance*)—

- (a) to codify rules on transfer pricing to require income or loss from provision between associated persons (or between parts of the same enterprise in different territories) to be computed, for tax purposes, on an arm's length basis;
- (b) to provide for an advance pricing arrangement regime under which how the rules apply may be agreed before transactions take place;
- (c) to require documentation relating to transactions;
- (d) to enable effect to be given to mutual agreements made with other jurisdictions under arrangements for relief from double taxation;
- (e) to enhance the current provisions for double taxation relief;
- (f) to adjust fees in respect of an application for advance ruling;
- (g) to revise the requirements relating to profits tax concessions for particular classes of person so as to meet the international standards promulgated by the Organisation for Economic Co-operation and Development (*OECD*); and
- (h) to make related amendments.

Amendments relating to double taxation

2. Clauses 3 to 7 and clause 8 (in so far as it adds a new section 50AA to the Ordinance) make miscellaneous amendments relating to

existing unilateral double taxation relief and to tax credit allowed under double taxation arrangements.

3. Clause 8 (in so far as it adds a new section 50AAB to the Ordinance) enables effect to be given to solutions resulting from the mutual agreement procedure, under double taxation arrangements, resolving disputes arising under the arrangements. The solutions can be agreed between the Commissioner of Inland Revenue (*Commissioner*) and the competent authorities of the territories concerned. The new section also provides for the related powers of the Commissioner in requiring information and in seeking reimbursement for costs and reasonable expenses incurred.

Transfer pricing rules and relief and advance pricing arrangement

4. Clause 9 adds a new Part 8AA to the Ordinance.
5. Apart from defining relevant terms, Division 1 of the new Part 8AA applies the Part to determining property tax, salaries tax and profits tax and requires the Part to be read in a way that best secures consistency between its effect and the effect given to Articles 7 and 9 of the Model Tax Convention on Income and on Capital approved by the OECD. The expression *provision* is broadly equivalent to the expression *condition made or imposed* in Article 9.
6. Division 2 of the new Part 8AA incorporates the international transfer pricing rules to the following effect—
- (a) a person's tax liability under the Ordinance is to be determined on the basis that a provision made or imposed between the person and the person's associated person is made or imposed on an arm's length basis;
 - (b) in other words, a person who would have a Hong Kong tax advantage if taxed on the basis of a non-arm's length provision (*advantaged person*) will have income adjusted upwards or loss adjusted downwards;

- (c) similarly, the income or loss of a non-Hong Kong resident person attributable to the person's permanent establishment in Hong Kong are to be determined as if the permanent establishment were a distinct and separate enterprise.

7. The new Part 8AA is supplemented by the new Schedule 17G (added by clause 10) which contains rules for determining whether a person has a permanent establishment in Hong Kong.
8. Division 3 of the new Part 8AA provides that, after adjustment to tax assessment is made on the advantaged person to reflect the arm's length provision, corresponding relief may be applied for by the disadvantaged person (that is, the person who would suffer a tax disadvantage if taxed on the basis of the non-arm's length provision) to avoid double taxation. Similar relief applies in relation to transactions between parts of the same enterprise in different territories.
9. Under Division 4 of the new Part 8AA, a person and the Commissioner may, by an advance pricing arrangement, agree in advance on a method for resolving pricing issues for the purposes of the above transfer pricing rules. The new Schedule 17H (added by clause 10) supplements that Division 4 by providing for an application for an advance pricing arrangement and fees payable for the application.
10. Clause 13 adds a new section 15BA to the Ordinance to provide for adjustments to taxable profits or allowable losses to reflect any appropriation from or into trading stock or any acquisition or disposal of trading stock other than in the course of trade at market value.
11. Clause 14 adds a new section 15F to the Ordinance. The effect is that a person who has contributed in Hong Kong to the development, enhancement, maintenance, protection or exploitation of intellectual property is to be taxed on such part of the sum

accruing in respect of its exhibition or use or related rights as is attributable to the contribution even if the sum accrues to the person's associate.

Transfer pricing documentation including country-by-country reporting

12. Clauses 16 and 17 add a new Part 9A and a new Schedule 17I to the Ordinance to provide for requirements for transfer pricing documentation.
13. Division 2 of the new Part 9A (that is, the new section 58C) requires a Hong Kong entity of a group in the extended sense to prepare, for each accounting period, a master file and a local file and to retain the files for a period of 7 years. More specifically—
 - (a) the term *group in the extended sense* essentially means a collection of enterprises (whether all or any of them are local enterprises) required to prepare consolidated financial statements for financial reporting purposes under applicable accounting principles but is taken to cover a single enterprise in a territory if the enterprise carries on business through a permanent establishment in another territory;
 - (b) Part 2 of the new Schedule 17I specifies criteria for exemption from the requirement to keep files based on the size of revenue and assets and number of employees of the entity concerned or the value of controlled transactions (as defined in Schedule 17I); and
 - (c) Part 3 of the new Schedule 17I specifies information about the group and the entity itself that must be contained in the master file and local file.
14. Division 3 of the new Part 9A give effect to the OECD's country-by-country reporting requirements—

- (a) under the new section 58D, the requirements for filing a country-by-country return only apply to a *reportable group* (which means a multinational enterprise group whose annual consolidated group revenue reaches the specified threshold amount);
- (b) the new sections 58E and 58F set out requirements for the ultimate parent entity or other entities of a reportable group to file country-by-country returns for each accounting period beginning on or after 1 January 2018 if the ultimate parent entity has or the other entities have a Hong Kong connection (As a transitional measure, the new section 58E(2) provides for voluntary filing of a country-by-country return, by an ultimate parent entity resident for tax purposes in Hong Kong, for an accounting period beginning on or after 1 January 2016 but before 1 January 2018);
- (c) the new section 58G empowers an assessor to require an entity to file a country-by-country return; and
- (d) the new section 58H sets out requirements for filing a notification containing information relevant for determining the obligation for filing a country-by-country return.

Penalties and Offences

- 15. Clauses 19 to 22 amend sections 80, 82 and 82A of the Ordinance and add new sections 80G to 80J to the Ordinance to provide for offences and additional tax for failure to comply with the requirements under new sections 50AA and 50AAB and Parts 8AA and 9A, or for providing misleading, false or inaccurate information or omitting to provide information in connection with those provisions.

Fees for application for advance ruling

- 16. Clause 23 amends the fees for an application for advance ruling under section 88A of the Ordinance.

Requirements relating to profits tax concession for particular classes of person

- 17. Clauses 24 and 30 amend sections 14B and 23A of the Ordinance to extend the profits tax concessions to professional reinsurers and authorized captive insurers in respect of their assessable profits derived from the business of reinsurance and insurance of onshore risks respectively.
- 18. Clauses 25 and 26 amend sections 14C and 14D of the Ordinance to extend the profits tax concessions to corporate treasury centres in respect of their assessable profits derived from carrying on intra-group lending transactions with, providing corporate treasury services to and entering into corporate treasury transactions with, associated corporations that carry on trade, profession or business in Hong Kong.
- 19. Clause 29 amends section 16 of the Ordinance to extend the application of the anti-abuse provisions in that section to situations where profits tax concessions are claimed under section 14B or 14D.
- 20. Clause 32 adds a new section 26AB to the Ordinance to provide that profits tax concessions under sections 14B, 14D, 14H, 14J and 23B are available only if the threshold requirement is met. The Commissioner is empowered to prescribe the threshold requirement by a notice published in the Gazette.

Transitionals and consequential amendments

- 21. Clauses 33 and 34 incorporate a new Schedule 42 to the Ordinance which contains transitional provisions.

22. Clauses 35 and 36 make consequential amendments to the Inland Revenue Rules (Cap. 112 sub. leg. A).

**Economic, Financial and Civil Service
Implications of the Proposal**

Economic Implications

In terms of economic implications, the proposal will demonstrate Hong Kong's commitment to combating cross-border tax evasion. This is particularly crucial for Hong Kong to preserve our competitiveness and reputation as an international financial and business centre, and to avoid being listed as a "non-cooperative" tax jurisdiction.

2. The proposal will incur additional compliance costs on enterprises. Nevertheless, since we are going along with international standards, Hong Kong enterprises should not be any worse off than those in other tax jurisdictions. Since we will implement the minimum standards of the Base Erosion and Profit Shifting ("BEPS") package only and provide exemptions where appropriate, we have made our best efforts to reduce enterprises' compliance burdens. On balance, we consider that implementation of the BEPS package is in line with the overall interest of Hong Kong.

Financial and Civil Service Implications

3. Additional resources have been earmarked for the Financial Services and the Treasury Bureau and the Inland Revenue Department in 2017-18 and beyond to cope with treaty negotiations, stakeholders' engagement, legislative exercises and implementation work arising from international tax cooperation.

4. As regards the proposed amendments to certain preferential tax regimes, the tax revenue forgone arising from the extension of tax concessions to profits derived from domestic transactions is expected to be insignificant. The proposed measures may encourage investment in the relevant sectors and generate more revenue for the Government.