

立法會
Legislative Council

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**Paper for the House Committee Meeting
on 13 April 2018**

**Legal Service Division Report on
Inland Revenue (Amendment) (No. 2) Bill 2018**

I. SUMMARY

- 1. The Bill**

The Bill seeks to amend the Inland Revenue Ordinance (Cap. 112) to:

 - (a) expand the scope of profits tax deduction for capital expenditure incurred for the purchase of intellectual property rights ("IPRs") to cover performer's economic rights, protected layout-design (topography) rights and protected plant variety rights;
 - (b) allow deduction of expenses for the grant of plant variety rights;
 - (c) deem certain sums to be trading receipts chargeable to tax; and
 - (d) provide for related matters.

- 2. Public Consultation**

According to the Legislative Council Brief, the Administration has kept key stakeholders including the Hong Kong Bar Association, the Law Society of Hong Kong and the Joint Liaison Committee on Taxation informed during the formulation of the proposal and they have not raised objection.

- 3. Consultation with LegCo Panel**

As advised by the Clerk to the Panel on Commerce and Industry, the Panel was briefed on 15 November 2016 on the proposal to implement the 2016-17 Budget initiative in respect of the expansion of the scope of tax deduction for capital expenditure incurred for the purchase of IPRs from the existing five categories to eight. The Panel supported the proposal in principle and expressed views and concerns on a number of issues.

- 4. Conclusion**

The Legal Service Division is scrutinizing the legal and drafting aspects of the Bill. Members may wish to consider whether a Bills Committee should be formed to study the Bill in detail.

II. REPORT

The date of First Reading of the Bill is 11 April 2018. Members may refer to the Legislative Council ("LegCo") Brief (File Ref.: CITB CR 81/45/2) issued by the Commerce, Industry and Tourism Branch of the Commerce and Economic Development Bureau on 21 March 2018 for further details.

Object of the Bill

2. The Bill seeks to amend the Inland Revenue Ordinance (Cap. 112) to:
 - (a) expand the scope of profits tax deduction for capital expenditure incurred for the purchase of intellectual property rights ("IPRs") to cover performer's economic rights, protected layout-design (topography) rights and protected plant variety rights;
 - (b) allow deduction of expenses for the grant of plant variety rights;
 - (c) deem certain sums to be trading receipts chargeable to tax; and
 - (d) provide for related matters.

Background

3. At present, capital expenditure incurred for the purchase of five categories of IPRs, namely, patent rights, rights to any know-how (i.e. industrial information or techniques likely to assist in the manufacture or processing of goods or materials), copyrights, registered designs and registered trade marks ("existing IPRs") used in the production of profits chargeable to tax in Hong Kong are deductible under sections 16E and 16EA of Cap. 112 when computing profits tax. Further, expenditure relating to the registration of a trade mark or design, or the registration or grant of a patent that is used for producing taxable profits is deductible under section 16(1)(g) of Cap. 112.

4. To encourage enterprises to engage in the development of related intellectual property ("IP") trading business, and to promote Hong Kong as an IP trading hub in the region, the Financial Secretary ("FS") proposed in the 2016-17 Budget that the Government would expand the scope of tax deduction for capital expenditure incurred for the purchase of IPRs from the existing five categories to eight i.e. to cover three additional rights in layout-design (topography) of integrated circuits, plant varieties and performances.

Provisions of the Bill

5. The Bill seeks to implement FS's proposal in the 2016-17 Budget mentioned in paragraph 4 above. The key provisions are summarized below.

Expanding the scope of the existing profits tax deduction regime for intellectual property rights

6. Clause 5 of the Bill seeks to amend section 16EA of Cap. 112 to allow tax deductions for capital expenditure incurred for the purchase of three additional IPRs, namely, performer's economic rights, protected layout-design (topography) rights and protected plant variety rights ("three additional types of IPRs") during any year of assessment beginning on or after 1 April 2018 if certain conditions are met.

7. For the purpose of the proposed tax deductions, the definitions of the three additional types of IPRs are proposed to be added to section 16EA(11) of Cap. 112 (clause 5(9)) as follows:

- (a) "Performer's economic right" means a right mentioned in section 215(1)(a), (b), (c) or (d) of the Copyright Ordinance (Cap. 528) and conferred by Part III of Cap. 528 on a performer. These rights refer to those in respect of reproduction, distribution and making available to the public copies of a fixation of their performances and the right for renting to the public copies of a sound recording of their performances¹ or its corresponding rights subsisting under the law of a place outside Hong Kong.
- (b) "Protected layout-design (topography) right" means a right in a layout-design (topography) that is protected under section 3 of the Layout-design (Topography) of Integrated Circuits Ordinance (Cap. 445) or its corresponding rights subsisting under the law of a place outside Hong Kong. Under Cap. 445, for layout-design (topography) of integrated circuits to be protected, it must be original, and recorded in documentary form or incorporated into an integrated circuit. A qualified owner has the right to reproduce or commercially exploit his protected layout-design (topography).
- (c) "Protected plant variety right" means a right granted under Part III of the Plant Varieties Protection Ordinance (Cap. 490) or its corresponding rights subsisting under the law of a place outside Hong Kong. Under Cap. 490, plant variety rights are rights granted to owners of plant

¹ Under section 200(2) of Cap. 528, a performance means a dramatic performance (which includes dance and mime), a musical performance, a reading or recitation of a literary work, a performance of an artistic work, an expression of folklore, or a performance of a variety act or any similar presentation.

varieties over cultivated plant varieties they have bred or discovered and developed. Except Inedible Algae and Inedible Fungi, varieties of all types of plants are eligible for protection provided that they are new, distinct, stable and homogeneous. A grantee of plant variety right has the exclusive right to produce for sale, offer for sale, sell and import/export reproductive material of the protected variety; to propagate the variety for commercial production of fruit or flowers; and to license others to carry out any of the above activities.

Conditions for the proposed tax deduction

8. Under the Bill, the proposed tax deduction for the three additional types of IPRs would be subject to certain conditions that are the same as those applicable to copyright, registered designs and registered trade marks provided under section 16EA of Cap. 112. These conditions include (a) the taxpayer possesses the legal and the economic ownership² of the relevant IPR; and (b) the IPR has been used by the taxpayer for the production of profits chargeable to tax in Hong Kong. As to the other condition that IPR should subsist (in the case of copyright) or the registration of IPR be in force (in the case of registered design and registered trade mark) during the basis period of the year of assessment under the tax deduction regime provided in section 16EA(6), clause 5(2) proposes to amend section 16EA(6) to provide that the deduction would only be allowed if the performer's economic right has not expired, the protection of the layout-design (topography) has not ceased or the grant of the protected plant variety right is in force.

Deduction of expenses for the grant of plant variety rights

9. Clause 4 seeks to amend section 16(1)(g) of Cap. 112 to allow profits tax deduction for expenditure for the grant of plant variety rights, in addition to the existing deduction for expenditure relating to the registration of a trade mark or design, or the registration or grant of a patent, with effect from a year of assessment beginning on or after 1 April 2018.

Anti-avoidance provisions

10. Clause 6 seeks to amend section 16EC(8) of Cap. 112 to provide that the existing anti-avoidance measures (in relation to tax deduction for capital expenditure for the purchase of the existing IPRs) under section 16EC would apply to the three additional types of IPRs to the effect that tax deduction would not be allowed under certain circumstances.

² Under section 16EA(13) of Cap. 112, any expenditure incurred on the acquisition of a licence (as defined by section 16EC(8)) of any specified intellectual property right is not deductible under section 16EA.

Deemed trading receipts to cover sums received in relation to the three additional types of intellectual property rights

11. Clause 3 seeks to amend section 15 of Cap. 112 to expand the scope of gains deemed as taxable receipts arising in or derived from a trade, profession or business carried on in Hong Kong to cover (a) sums received by or accrued to a person for the use, or the right to the use, of the three additional types of IPRs in Hong Kong or outside Hong Kong; and (b) sums received by or accrued to a performer or an organizer for an assignment of, or an agreement to assign, a performer's right in relation to a performance given by the performer in Hong Kong.

Other amendments

12. The Bill contains related amendments including providing for recovery of tax from a person in Hong Kong who paid or credited to a non-resident person the sums in relation to a performance given in Hong Kong (as stated in paragraph 11(b) above) under section 20B of Cap. 112 (clause 7) and other minor amendments.

Commencement

13. The Bill, if passed, would come into operation on the day on which it is published in the Gazette as an Ordinance.

Public Consultation

14. According to paragraph 18 of the LegCo Brief, the Administration has kept key stakeholders including the Hong Kong Bar Association, the Law Society of Hong Kong and the Joint Liaison Committee on Taxation informed during the formulation of the proposal and they have not raised objection.

Consultation with LegCo Panel

15. According to the Clerk to the Panel on Commerce and Industry, the Panel was briefed at its meeting on 15 November 2016 on the legislative proposal to implement the measure announced in the 2016-17 Budget relating to the expansion of the scope of tax deduction for capital expenditure incurred for the purchase of IPRs from the existing five categories to eight. While supporting the legislative proposal, members urged the Administration to put in place other necessary policy measures to facilitate the development of various industries and boost Hong Kong's economy. Members raised concern on whether there would be any contradiction in respect of the treatment of new varieties of plants deriving from genetic modifications in the legislative proposal and other relevant local legislation, such as the Food Safety

Ordinance (Cap. 612). Members also urged the Administration to step up publicity on the proposed tax deduction measures upon the passage of the legislative proposal so that the concerned enterprises could be fully aware of the relevant arrangements.

Conclusion

16. The Legal Service Division is scrutinizing the legal and drafting aspects of the Bill. Members may wish to consider whether a Bills Committee should be formed to study the Bill in detail.

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