香港特別行政區政府
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INNOVATION AND
TECHNOLOGY BUREAU
THE GOVERNMENT OF THE HONG KONG
SPECIAL ADMINISTRATIVE REGION
20/F, West Wing, Central Government Offices,
2 Tim Mei Avenue, Tamar, Hong Kong

By email

11 May 2018

Mr Desmond LAM
Clerk to Panel on Commerce and Industry
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

Dear Mr LAM,

Panel on Commerce and Industry
Meeting on 16 January 2018

Proposal for enhanced tax deduction
for research and development expenses

At the meeting of the Panel on Commerce and Industry on 16 January 2018, the Administration was requested to provide a comparison of its proposal for enhanced tax deduction for research and development expenses with similar tax deduction arrangements in countries such as Singapore and Israel. The relevant information is enclosed herewith for Members' reference.

Yours sincerely,

(Ricky CHONG)
for Secretary for Innovation and Technology

c.c. Innovation and Technology Commission (Attn.: Mr WONG Wang Wah)

Panel on Commerce and Industry
Meeting on 16 January 2018

Proposal for enhanced tax deduction for research and development ("R&D") expenses

The proposed enhanced tax deduction for R&D expenses

Under the Administration's proposed enhanced tax deduction arrangement, the deduction will be 300% for the first $2 million of the aggregate amount of payments made to "designated local research institutions" for "qualifying R&D activities" (i.e. out-sourced qualifying R&D") and "qualifying expenditures" incurred by the enterprises (i.e. in-house qualifying R&D), and 200% for the balance. There is no cap on the amount of enhanced tax deduction. A qualifying R&D activity should be wholly undertaken and carried out in Hong Kong.

2. The expenditure related to other R&D activities that do not fit into the definition of "qualifying R&D activities", for example, expenditure incurred on market, business and management research; and non-qualifying R&D expenditure incurred by the enterprises on qualifying R&D activities (e.g. director's remuneration, fees paid for leasing or maintenance of plant or machinery, etc.), may still be eligible for 100% basic deduction.

Comparison with similar tax deduction arrangement in overseas countries

Singapore

3. Under the existing Productivity and Innovation Credit ("PIC") Scheme of Singapore, a "PIC deduction" of 250% of qualifying expenditure would be provided on top of the basic 100% deduction of expenditure on R&D and 50% additional deduction of qualifying expenditure for R&D activities carried out in Singapore. For R&D activities carried out outside Singapore, a "PIC deduction" of 300% of qualifying expenditure would be provided on top of the basic 100% deduction of expenditure on R&D.

4. However, whether it is R&D activities carried out locally or overseas, the qualifying expenditure (i.e. staff costs or consumables) is subject to a cap ranging from S$400,000 to S$600,000, depending on the scale of the enterprise. The balance of expenditure on R&D in excess of the cap would be entitled to 100% or 150% tax deduction as appropriate. In addition, there is an option to convert qualifying expenditure up to S$100,000 at a conversion rate of 40% into non-taxable cash payout.

5. As regards out-sourced R&D activities, the relevant expenses could be paid to any R&D organisations. However, the enhanced deduction is generally limited to 60% of the fee paid for the out-sourced R&D activities.

6. The PIC Scheme mentioned above is an existing scheme in Singapore which will expire in the year of assessment ("YA") 2018. As proposed in the Singapore 2018 Budget Speech, with effect from YA2019 to YA2025, the deduction rate for R&D activities carried out in Singapore will be increased from 150% to 250%. The deduction rate for overseas R&D activities will be 100%.

7. On the whole, in respect of local R&D activities, the rate we propose for enhanced tax deduction is different, but more or less comparable, with that under the existing PIC Scheme or the new proposal to be effective in YA2019 in Singapore. However, as we do not impose a cap on qualifying R&D, expenditures, our proposal is competitive in this regard. In respect of overseas R&D activities, the deduction rate under the PIC Scheme is more generous as compared to our proposal. However, the deduction rate in Singapore will be lowered to the same level of 100% as ours starting from YA2019.

Israel

8. While Israel provides preferential tax regimes for high technology companies operating in specified locations, it does not provide enhanced deductions for R&D expenditures.

Innovation and Technology Bureau
Innovation and Technology Commission
May 2018