

# 立法會 *Legislative Council*

LC Paper No. LS26/18-19

## **Paper for the Bills Committee on Inland Revenue (Amendment) (No. 7) Bill 2018**

### **Purpose**

At the meeting of the Bills Committee held on 30 November 2018, a member requested a short note to explain how the Inland Revenue (Amendment) (No. 7) Bill 2018 ("the Bill") proposed to address the decision of the Court of Final Appeal ("CFA") in *Nice Cheer Investment Ltd v. Commissioner of Inland Revenue* (2013) 16 HKCFAR 813 ("*Nice Cheer*"). This paper summarizes the relevant issues.

### **The *Nice Cheer* decision**

2. In *Nice Cheer*, CFA held that "profits" connoted actual or realized (not potential or anticipated) profits, and that on a proper construction of the existing provisions of the Inland Revenue Ordinance (Cap. 112), unrealized revaluation gains (i.e. increases in the value of a company's trading stock of marketable securities) were *not* assessable to tax under Cap. 112. As a result, profits on financial instruments ("FIs") computed on a *fair value basis* accounting for both realized and unrealized profits in accordance with Hong Kong and international financial reporting standards cannot be used for tax reporting, and must be recomputed on a *realization basis*.

3. In view of *Nice Cheer*, clause 3 of the Bill seeks to add an alternative basis for reporting and assessing profits on FIs under Cap. 112. Under the proposed amendments:

- (a) a taxpayer may continue to report profit, gain, loss, income or expense on the realization basis, so that any unrealized revaluation gains on FIs would not be assessable to tax in accordance with CFA's decision; or
- (b) a taxpayer who prepares financial statements in accordance with the Hong Kong or International Financial Reporting Standard 9 (Financial Instruments) would be able to *elect* the fair value basis for tax reporting purposes such that a change in fair value (albeit unrealized) of FIs would also be assessable to profits tax under Cap. 112 (as amended by the Bill).

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