For information

Legislative Council Panel on Financial Affairs

**Inland Revenue Ordinance (Cap. 112) –
Exemption from Profits Tax
(People's Bank of China Debt Instrument) Order**

PURPOSE

This paper briefs Members on the Exemption from Profits Tax (People's Bank of China Debt Instrument) Order ("the Exemption Order") made under the Inland Revenue Ordinance (Cap. 112) ("IRO").

THE EXEMPTION ORDER

2. On 18 December 2018, the Chief Executive in Council ("CE-in-C") made the Exemption Order pursuant to section 87 of the IRO to exempt a person from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, and profits on the sale or other disposal or on the redemption on maturity or presentment of, debt instruments issued in Hong Kong by the People's Bank of China ("PBoC"). The Exemption Order will apply to the year of assessment commencing on 1 April 2018 and for all subsequent years of assessment.

3. The profits tax exemption provided in the Exemption Order is intended to accord debt instruments issued in Hong Kong by the PBoC the same profits tax exemption as in the case of sovereign bonds issued in Hong Kong. This will help ensure that Hong Kong continues to be the premier platform facilitating the internationalisation of Renminbi ("RMB") and the Mainland to "go global".

4. The Exemption Order was gazetted on 21 December 2018 and a Legislative Council ("LegCo") Brief, at **Annex**, was issued on the same

day. The Exemption Order is a piece of subsidiary legislation and will be tabled at LegCo for negative vetting on 9 January 2019.

BACKGROUND

5. On 31 October 2018, the PBoC announced that it would issue RMB debt instruments totalling RMB20 billion, half in three-month tenor and another half one-year, in Hong Kong on 9 November 2018. The debt instruments were tendered on 7 November 2018 and concluded with yields at 3.79% and 4.20% for three-month tenor and one-year tenor respectively. The aim is to enrich the spectrum of RMB financial products, improve the yield curve of RMB bonds, thereby supporting the development of Hong Kong as the global hub for offshore RMB business.

Financial Services and the Treasury Bureau
21 December 2018

<u>Annex</u>

File Reference: MA/2/1/10C(2018)

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance
(Chapter 112)

EXEMPTION FROM PROFITS TAX (PEOPLE'S BANK OF CHINA DEBT INSTRUMENT) ORDER

INTRODUCTION

At the meeting of the Executive Council on 18 December 2018, the Executive Council **ADVISED** and the Acting Chief Executive **ORDERED** to make the Exemption from Profits Tax (People's Bank of China Debt Instrument) Order ("the Exemption Order") at **<u>Appendix</u>** pursuant to section 87 of the Inland Revenue Ordinance (Cap. 112) ("IRO") to exempt a person from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, and profits on the sale or other disposal or on the redemption on maturity or presentment of, debt instruments issued in Hong Kong by the People's Bank of China ("PBoC").

JUSTIFICATIONS

2. Having regard to the justifications set out in paragraphs 3 to 5 below, we consider it appropriate that profits tax exemption available to sovereign bonds issued in Hong Kong should be extended to cover debt instruments issued in Hong Kong by the PBoC.

3. The Exemption from Profits Tax (Renminbi Sovereign Bonds) Order (Cap. 112BH) and the Exemption from Profits Tax (Non-Renminbi

Sovereign Bonds) Order (Cap. 112DA) were made then to promote further issuance of sovereign bonds in Hong Kong by the Central People's Government ("CPG") on an on-going and regular basis with a view to strengthening our role as a testing ground for policy measures for diversification of Renminbi ("RMB") business and upholding our position as an international financial centre. We consider that the extension of profits tax exemption to debt instruments issued in Hong Kong by the PBoC aligns with these policy objectives.

4. The issuance of RMB20 billion PBoC debt instruments in Hong Kong in November 2018 is an important measure to help Hong Kong consolidate its position as a leading international financial centre and the global offshore RMB business hub to promote the internationalisation of RMB. Following the annual sovereign bond issuance by the Ministry of Finance in Hong Kong since 2009, the PBoC debt instruments provide another stable and sound investment option for local and international investors to cater for their strong demand for liquid RMB assets, particularly debt instruments of a shorter tenor, in the offshore market. It also helps establish a benchmark yield curve for the offshore RMB market, especially at the shorter end, which facilitates financial institutions to develop offshore RMB products. This issuance in Hong Kong has marked another milestone in the development of our financial services through increasing the breadth and depth of our RMB debt market and enhancing financial cooperation between the Mainland and Hong Kong.

5. Given that the Mainland's capital account is not fully open yet, the offshore issuance of PBoC debt instruments in Hong Kong could serve as a channel through means such as roadshows to showcase the Mainland's latest development on various fronts and instill confidence in international investors, which will in turn help accelerate the internationalisation of RMB. Being the global offshore RMB business hub, it is important that Hong Kong continues to play a key role in this strategic development and remains as the premier platform facilitating the Mainland to "go global".

THE EXEMPTION ORDER

6. Section 87 of the IRO provides that the Chief Executive in Council ("CE-in-C") may by order exempt any person, office or institution from payment of the whole or any portion of any tax chargeable under the IRO. The Exemption Order exempts a person from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, and profits on the sale or other disposal or on the redemption on maturity or presentment of debt instruments issued in Hong Kong by the PBoC, so that the relevant tax arrangement is on par with that applicable to the sovereign bonds issued in Hong Kong by the CPG.

7. The Exemption Order covers debt instruments issued in Hong Kong by the PBoC. As the PBoC issued debt instruments in Hong Kong on 9 November 2018 (i.e. falling within the year of assessment 2018/19), the Exemption Order shall apply to the year of assessment commencing on 1 April 2018 and for all subsequent years of assessment.

LEGISLATIVE TIMETABLE

8. The legislative timetable is as follows –

Publication in the Gazette	21 December 2018
Tabling at Legislative Council ("LegCo")	9 January 2019
Commencement date	1 March 2019

IMPLICATIONS OF THE PROPOSAL

9. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. It will not affect the binding effect of the existing provisions of the IRO. There are no productivity, environmental, family, gender and civil service implications. Apart from the economic implications in paragraph 10 below, there are no other

sustainability implications.

10. On economic implications, the Exemption Order will facilitate the PBoC's issuance of debt instruments in Hong Kong and is conducive to the further development of our offshore RMB business and debt market. It will also help strengthen financial cooperation between Hong Kong and the Mainland, thereby strengthening our position as an international financial centre.

11. On financial implications, on the basis that the coupon rates for the RMB10 billion 3-month debt instruments and RMB10 billion 1-year debt instruments are 3.79% and 4.20% respectively, the estimated amount of tax foregone following the implementation of the Exemption Order would be around HK$95.7 million. The above estimation only includes profits arising from interest payment. No revenue foregone could be estimated for profits on the sale, other disposal, and redemption on maturity or presentation of the bonds as there is no basis to make this projection.

PUBLIC CONSULTATION

12. In the Government's press release on 31 October 2018 welcoming the PBoC's issuance of debt instruments in Hong Kong, we mentioned that we would study extending the scope of the profits tax exemption to cover debt instruments issued in Hong Kong by the PBoC. We also issued an information note to the LegCo Panel on Financial Affairs on 21 December 2018.

PUBLICITY

13. We shall arrange a spokesperson to deal with press enquiries on the Exemption Order.

BACKGROUND

14. On 31 October 2018, the PBoC announced that it would issue RMB debt instruments totalling RMB20 billion, half in three-month tenor and another half one-year, in Hong Kong on 9 November 2018. The debt instruments were tendered on 7 November 2018 and concluded with yields at 3.79% and 4.20% for three-month tenor and one-year tenor respectively. The aim is to enrich the spectrum of RMB financial products, improve the yield curve of RMB bonds, thereby supporting the development of Hong Kong as the global hub for offshore RMB business.

ENQUIRIES

15. Enquiries on this brief may be directed to Ms Estrella Cheung, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services), at 2810 2150.

Financial Services and the Treasury Bureau
21 December 2018

Exemption from Profits Tax (People's Bank of China Debt Instrument) Order

(Made by the Chief Executive in Council under section 87 of the Inland Revenue Ordinance (Cap. 112))

1. Commencement

This Order comes into operation on 1 March 2019.

2. Interpretation

In this Order—

PBoC debt instrument (**中國人民銀行債務票據**) means a debt instrument issued in Hong Kong by the People's Bank of China.

3. Exemption

(1) A person is exempt from the payment of profits tax chargeable under Part 4 of the Ordinance in respect of sums received by, or accrued to, the person as—

(a) interest paid or payable on a PBoC debt instrument;

(b) profits on the sale, or other disposal, of a PBoC debt instrument; or

(c) profits on the redemption, on maturity or presentment, of a PBoC debt instrument.

(2) This section applies in relation to profits tax chargeable for the year of assessment commencing on 1 April 2018 and for all subsequent years of assessment.

Appendix

Clerk to the Executive Council

COUNCIL CHAMBER

2018

Explanatory Note

This Order exempts a person from the payment of profits tax chargeable under Part 4 of the Inland Revenue Ordinance (Cap. 112) in respect of sums received by, or accrued to, the person as interest or profits arising from a debt instrument issued in Hong Kong by the People's Bank of China.