



Inland Revenue Department
The Government of the Hong Kong Special Administrative Region
of the People's Republic of China

DEPARTMENTAL INTERPRETATION AND PRACTICE NOTES

NO. 26 (REVISED)

PROFITS TAX

**SPECIFIED SECURITIES FOR THE PURPOSES
OF SECTION 15E OF THE
INLAND REVENUE ORDINANCE**

These notes are issued for the information of taxpayers and their tax representatives. They contain the Department's interpretation and practices in relation to the law as it stood at the date of publication. Taxpayers are reminded that their right of objection against the assessment and their right of appeal to the Commissioner, the Board of Review or the Court are not affected by the application of these notes.

These notes replace those issued in August 1996.

LAU MAK Yee-ming, Alice
Commissioner of Inland Revenue

June 2009

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INTRODUCTION

Section 15E of the Inland Revenue Ordinance was enacted in 1994 to provide for the Profits Tax treatment of certain stock borrowing and lending transactions in respect of Hong Kong stock subject to the rules and practices of the Stock Exchange of Hong Kong. Inland Revenue (Amendment) (No. 4) Ordinance 1996, which was assented to on 18 July 1996, extended the application of the relevant provisions to “specified securities”.

DEFINITION

2. For the purposes of section 15E, the expression “specified securities” is defined in the following terms -

“specified securities” means any of the following, not being Hong Kong stock the sale and purchase of which in Hong Kong are subject to the rules and practices of a recognized stock market -

- (a) any shares, stocks, debentures, loan stocks, funds, bonds or notes of or issued by any body, whether corporate or unincorporate, or any government or local government authority, or any other similar investment of any description;
- (b) any units under a unit trust scheme;
- (c) any right, option or interest in or in respect of any security referred to in paragraph (a) or (b),

which the Commissioner may specify in writing, either generally or in any particular case, for the purposes of this section.

SPECIFIED SECURITIES

3. Pursuant to the authority provided under the definition of “specified securities”, the Commissioner has specified for the purposes of section 15E the categories of securities detailed on the schedule(s) attached to these Practice Notes.

SCHEDULE

Inland Revenue Ordinance (Chapter 112)

SPECIFIED SECURITIES FOR THE PURPOSES OF SECTION 15E

I, WONG Ho-sang, the Commissioner of Inland Revenue, pursuant to section 15E of the Inland Revenue Ordinance as amended by the Inland Revenue (Amendment) (No. 4) Ordinance 1996, hereby specify that where associated parties are not involved (see paragraph 2 below), securities falling into the following categories are specified securities for the purposes of section 15E -

- (i) any debt or equity security listed on a stock exchange in Hong Kong or any other stock exchange or over-the-counter market recognized for the purposes of this paragraph by the Commissioner;
- (ii) any unlisted debt issued to third parties or guaranteed to third parties by listed companies (including affiliates owned 50% or more by listed companies);
- (iii) any unlisted sovereign debt (including, for this purpose, government agency debt, multilateral agency debt and debt guaranteed by multilateral agencies or sovereign governments); and
- (iv) any unlisted debt or equity securities issued pursuant to a private placement authorized by the Hong Kong Securities and Futures Commission or a similar supervisory body in another jurisdiction.

2. Subject to paragraph 4, associated parties are considered to be involved if under what would otherwise be a stock borrowing and lending agreement the borrower is an associate of the lender or it is intended by any of the parties concerned that, either directly or indirectly, any or all of the securities borrowed under the agreement are to be on-lent to an associate of the lender. For the purpose of ascertaining whether a person is an associate of the lender, regard will be had to the definition of "associate", and related definitions, in section 21A of the Ordinance.

3. If the lender or borrower under the agreement, or any subsequent borrower (i.e. if the securities are to be on-lent) is a trustee of a trust estate or a corporation controlled by such a trustee, the definition of “associate” will be applied on the basis that the lender or borrower, as the case may be, is each of the trustee, the corporation and the beneficiary under the trust (as defined in section 21A).

4. For the purposes of this Schedule, associated parties are deemed not to be involved where it would otherwise be the case if the parties to a stock borrowing and lending agreement are securities dealing and underwriting firms, which are regulated by the Hong Kong Securities and Futures Commission or a similar supervisory body in another jurisdiction, or affiliates owned 50% or more, directly or indirectly, by such firms. It should be noted in relation to any such case that section 15E only applies where the parties concerned deal with each other on an arm’s length basis and the lender does not enter into the stock borrowing and lending agreement with the purpose, or main purpose, of avoiding or deferring tax (see section 15E(1)(d) and (e)).

5. For agreements involving associated parties, application may be made on a “particular case” basis to the Commissioner to have the subject securities declared to be “specified securities”. In such a case, it will be necessary to establish to the satisfaction of the Commissioner that the agreement is in essence a bona fide stock borrowing and lending agreement entered into on an arm’s length basis and not having as a main purpose the obtaining of a tax benefit.

(WONG Ho-sang)
Commissioner of Inland Revenue
30 August 1996