

Inland Revenue (Amendment) (No. 2) Ordinance 2016

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HONG KONG SPECIAL ADMINISTRATIVE REGION

ORDINANCE NO. 12 OF 2016



C. Y. LEUNG
Chief Executive
2 June 2016

An Ordinance to amend the Inland Revenue Ordinance to give profits tax concession to qualifying corporate treasury centres, to make provisions for profits tax purposes regarding interests on money borrowed from or lent to associated corporations, and to treat regulatory capital securities as debt securities; and to amend the Stamp Duty Ordinance to give stamp duty relief in relation to regulatory capital securities; and to make consequential amendments.

[3 June 2016]

Enacted by the Legislative Council.

Part 1

Preliminary

1. Short title

This Ordinance may be cited as the Inland Revenue (Amendment) (No. 2) Ordinance 2016.

2. Enactments amended

- (1) The Inland Revenue Ordinance (Cap. 112) is amended as set out in Part 2.

- (2) The Inland Revenue Rules (Cap. 112 sub. leg. A) are amended as set out in Division 1 of Part 3.
 - (3) The Stamp Duty Ordinance (Cap. 117) is amended as set out in Division 2 of Part 3.
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Part 2

Amendments to Inland Revenue Ordinance

Division 1—Profits Tax Concession for Qualifying Corporate Treasury Centres

3. Sections 14C to 14F added

After section 14B—

Add

“14C. **Qualifying corporate treasury centre: interpretation**

(1) In this section and sections 14D, 14E and 14F—

associated corporation (相聯法團), in relation to a corporation, means—

- (a) another corporation over which the corporation has control;
- (b) another corporation that has control over the corporation; or
- (c) another corporation that is under the control of the same person as is the corporation;

corporate treasury activity (企業財資活動) means—

- (a) carrying on an intra-group financing business;
- (b) providing a corporate treasury service; or
- (c) entering into a corporate treasury transaction;

corporate treasury asset (企業財資資產), in relation to a corporation, means an asset of the corporation used by it to carry out a corporate treasury activity;

corporate treasury profits (企業財資利潤), in relation to a corporation, means any profits of the corporation that are derived from a corporate treasury activity;

corporate treasury service (企業財資服務)—see section 1 of Schedule 17B;

corporate treasury transaction (企業財資交易)—see section 2 of Schedule 17B;

intra-group financing business (集團內部融資業務), in relation to a corporation, means the business of the borrowing of money from and lending of money to its associated corporations;

non-Hong Kong associated corporation (非香港相聯法團) means an associated corporation that does not carry on any trade, profession or business in Hong Kong;

prescribed asset percentage (訂明資產百分率)—see section 4 of Schedule 17B;

prescribed profits percentage (訂明利潤百分率)—see section 3 of Schedule 17B;

qualifying corporate treasury centre (合資格企業財資中心)—see section 14D(2) and (9);

qualifying corporate treasury service (合資格企業財資服務)—see subsection (3);

qualifying corporate treasury transaction (合資格企業財資交易)—see subsection (4);

qualifying lending transaction (合資格貸款交易), in relation to a corporation, means a transaction under which the corporation lends money, in the ordinary course of its intra-group financing business, to a non-Hong Kong associated corporation;

qualifying profits (合資格利潤), in relation to a corporation, means the assessable profits of the corporation that fall within section 14D(1)(a), (b) or (c).

- (2) For the purposes of the definition of ***associated corporation*** in subsection (1), a person has control over a corporation if the person has the power to secure—
- (a) by means of the holding of shares or the possession of voting power in or in relation to that or any other corporation; or
 - (b) by virtue of any powers conferred by the articles of association or other document regulating that or any other corporation,
- that the affairs of the first-mentioned corporation are conducted in accordance with the wishes of that person.
- (3) A corporate treasury service provided by a corporation to an associated corporation is a qualifying corporate treasury service if the associated corporation is a non-Hong Kong associated corporation.
- (4) A corporate treasury transaction entered into by a corporation that is related to the business of an associated corporation is a qualifying corporate treasury transaction if the associated corporation is a non-Hong Kong associated corporation.
- (5) The Secretary for Financial Services and the Treasury may by order published in the Gazette amend Schedule 17B.

14D. Qualifying corporate treasury centre: profits tax concession

- (1) For the purposes of this Part, the assessable profits of a corporation that is a qualifying corporate treasury centre for a year of assessment are, subject to subsections (5) and (8), chargeable to tax under this Part at one-half of the rate specified in Schedule 8 to the extent to which those profits are—
 - (a) assessable profits derived from its qualifying lending transaction;
 - (b) assessable profits derived from its qualifying corporate treasury service; or
 - (c) assessable profits derived from its qualifying corporate treasury transaction.
- (2) A corporation is a qualifying corporate treasury centre for a year of assessment if, for that year of assessment—
 - (a) it satisfies the conditions specified in subsection (3);
 - (b) it satisfies the safe harbour rule under section 14E; or
 - (c) it has obtained the Commissioner's determination under section 14F(1).
- (3) The conditions specified for the purposes of subsection (2)(a) are that, in the basis period for the year of assessment, the corporation—
 - (a) has carried out in Hong Kong one or more corporate treasury activities; and
 - (b) has not carried out in Hong Kong any activity other than a corporate treasury activity.

- (4) For the purposes of subsection (3)(b), in determining whether a corporation has carried out any activity other than a corporate treasury activity, only activities that generate income to the corporation are to be taken into account.
- (5) Subsection (1) applies to a corporation for a year of assessment only if—
 - (a) in that year of assessment—
 - (i) the central management and control of the corporation is exercised in Hong Kong; and
 - (ii) the activities that produce its qualifying profits in that year are—
 - (A) carried out in Hong Kong by the corporation; or
 - (B) arranged by the corporation to be carried out in Hong Kong; and
 - (b) the corporation has elected in writing that subsection (1) applies to it.
- (6) An election under subsection (5)(b), once made, is irrevocable.
- (7) If subsection (1) does not apply to a corporation for a year of assessment (*cessation year*) while it did for the previous year of assessment—
 - (a) the election made by the corporation under subsection (5)(b) ceases to be effective; and
 - (b) despite anything in this section, subsection (1) is not to apply to the corporation for the year of assessment that follows the cessation year.

- (8) In computing the qualifying profits of a corporation for the purposes of subsection (1), if any sum payable to the corporation by a person in respect of the transaction or service mentioned in subsection (1)(a), (b) or (c) is deductible under this Part, the amount of the qualifying profits attributable to that transaction or service is to be deducted by reference to the amount of that sum.
- (9) Despite subsection (2), a financial institution is not eligible to be a qualifying corporate treasury centre.

14E. Qualifying corporate treasury centre: safe harbour rule

- (1) For the purposes of section 14D(2)(b), a corporation satisfies the safe harbour rule for a year of assessment (*subject year*) if the corporation falls within—
 - (a) the 1-year safe harbour under subsection (2); or
 - (b) the multiple-year safe harbour under subsection (3).
- (2) A corporation falls within the 1-year safe harbour if, for the subject year—
 - (a) its CTP percentage is not lower than the prescribed profits percentage; and
 - (b) its CTA percentage is not lower than the prescribed asset percentage.
- (3) A corporation falls within the multiple-year safe harbour if, for the specified years—
 - (a) its average CTP percentage is not lower than the prescribed profits percentage; and
 - (b) its average CTA percentage is not lower than the prescribed asset percentage.

- (4) In subsections (3), (7) and (8), the *specified years* (指明年度) for a corporation means—
- (a) if the corporation has carried on a trade, profession or business in Hong Kong for less than 2 consecutive years of assessment immediately before the subject year—the subject year and the preceding year of assessment (*the 2 years*); or
 - (b) if the corporation has carried on a trade, profession or business in Hong Kong for 2 or more consecutive years of assessment immediately before the subject year—the subject year and the preceding 2 years of assessment (*the 3 years*).
- (5) The *CTP percentage* (企業財資利潤總額百分率) of a corporation for a year of assessment is calculated in accordance with the following formula—

$$\frac{\text{CTP}}{\text{P}}$$

where: CTP means the aggregate amount of the corporate treasury profits of the corporation in the basis period for the year of assessment; and

P means the aggregate amount of profits accruing to the corporation from all sources, whether in Hong Kong or not, in the basis period for the year of assessment.

- (6) The *CTA percentage* (企業財資資產總值百分率) of a corporation for a year of assessment is calculated in accordance with the following formula—

CTA
A

where: CTA means the aggregate value of the corporate treasury assets of the corporation as at the end of the basis period for the year of assessment; and

A means the aggregate value of all assets, whether in Hong Kong or not, of the corporation as at the end of the basis period for the year of assessment.

- (7) The ***average CTP percentage*** (企業財資利潤總額平均百分率) of a corporation for the specified years means the percentage arrived at by—
- (a) if subsection (4)(a) applies—dividing the sum of the CTP percentages of the corporation for the 2 years by 2; or
 - (b) if subsection (4)(b) applies—dividing the sum of the CTP percentages of the corporation for the 3 years by 3.
- (8) The ***average CTA percentage*** (企業財資資產總值平均百分率) of a corporation for the specified years means the percentage arrived at by—
- (a) if subsection (4)(a) applies—dividing the sum of the CTA percentages of the corporation for the 2 years by 2; or
 - (b) if subsection (4)(b) applies—dividing the sum of the CTA percentages of the corporation for the 3 years by 3.

- (9) For the purposes of subsection (6), in computing the aggregate value of the corporate treasury assets of a corporation, if a corporate treasury asset is used partly to carry out a corporate treasury activity and partly for another purpose, only the part of the value of the asset that is proportionate to the extent to which the asset is used to carry out a corporate treasury activity is to be taken into account.

14F. Qualifying corporate treasury centre: Commissioner's determination

- (1) For the purposes of section 14D(2)(c), the Commissioner may, on application by a corporation, determine that the corporation is a qualifying corporate treasury centre for a year of assessment.
- (2) A corporation may apply for the Commissioner's determination under subsection (1) only if—
- (a) it is not a financial institution; and
 - (b) for the year of assessment, it satisfies neither of the following—
 - (i) the conditions specified in section 14D(3);
 - (ii) the safe harbour rule under section 14E.
- (3) The Commissioner may make a determination under subsection (1) only if the Commissioner is of the opinion that the conditions specified in section 14D(3), or the safe harbour rule under section 14E, would, in the ordinary course of business of the corporation, have been satisfied for the year of assessment.”.

4. Section 19CA amended (treatment of losses: concessionary trading receipts)

(1) Section 19CA(4)—

Repeal

“or 14B”

Substitute

“, 14B or 14D”.

(2) Section 19CA(5), definition of *chargeable concessionary trading receipts*, after paragraph (b)—

Add

“(c) where the concessionary trading receipts are of a kind in respect of which assessable profits of a corporation are chargeable to tax at the rate specified in section 14D, the amount of such concessionary trading receipts as—

(i) reduced by the aggregate of—

(A) the amount of any outgoings and expenses deductible under this Part to the extent to which they are incurred during the basis period for that year of assessment by the corporation in the production of the concessionary trading receipts; and

(B) the amount of any allowances made under Part 6 for that year of assessment to the corporation to the extent to which the relevant assets are used during the basis period for that year of assessment in the production of the concessionary trading receipts; and

(ii) increased by the amount of any balancing charge directed to be made on that corporation under Part 6 for that year of assessment to the extent to which the relevant assets are used in the production of the concessionary trading receipts;”.

- (3) Section 19CA(5), definition of *concessionary trading receipts*—

Repeal

“or 14B”

Substitute

“, 14B or 14D”.

- (4) Section 19CA(5), Chinese text, definition of 關於獲特惠的營業收入的未吸納虧損, paragraph (b)—

Repeal the full stop

Substitute a semicolon.

- (5) Section 19CA(5), definition of *unabsorbed loss in respect of the concessionary trading receipts*, after paragraph (b)—

Add

“(c) where the concessionary trading receipts are of a kind in respect of which assessable profits of a corporation are chargeable to tax at the rate specified in section 14D, the loss ascertained by—

- (i) adding to the amount of the concessionary trading receipts the amount of any balancing charge directed to be made on that corporation under Part 6 for that year of assessment to the extent to which the relevant assets are used in the production of the concessionary trading receipts; and

- (ii) reducing from the resulting amount the aggregate of—
 - (A) the amount of any outgoings and expenses deductible under this Part to the extent to which they are incurred during the basis period for that year of assessment by the corporation in the production of the concessionary trading receipts; and
 - (B) the amount of any allowances made under Part 6 for that year of assessment to the corporation to the extent to which the relevant assets are used during the basis period for that year of assessment in the production of the concessionary trading receipts;”.

5. Schedule 8 amended (rate of profits tax in respect of a corporation)

Schedule 8, after “14B(1)”—

Add

“, 14D(1)”.

6. Schedule 17B added

After Schedule 17A—

Add

“Schedule 17B

[s. 14C]

Qualifying Corporate Treasury Centre: Corporate Treasury Services, Corporate Treasury Transactions and Prescribed Percentages

Part 1

Corporate Treasury Services

1. Meaning of *corporate treasury service*

(1) For the purposes of sections 14C, 14D and 14E—

corporate treasury service (企業財資服務), in relation to a corporation, means any of the following services that is provided by the corporation to an associated corporation—

- (a) managing the cash and liquidity position, including cash forecasting or pooling, of the associated corporation and providing related advice;
- (b) processing payments to the vendors or suppliers of the associated corporation;
- (c) managing the associated corporation’s relationships with financial institutions;
- (d) providing corporate finance advisory service, including—
 - (i) activities supporting the raising of capital, such as by way of debt or equity, by the associated corporation; and

- (ii) capital budgeting for the associated corporation;
- (e) advising on the management of the investment of the funds of the associated corporation;
- (f) managing investor relations regarding the investors in the debt or equity instruments issued by the associated corporation;
- (g) providing service in relation to—
 - (i) the provision of guarantees, performance bonds, standby letters of credit or other credit risk instruments to or on behalf of the associated corporation; or
 - (ii) remittances to or on behalf of the associated corporation;
- (h) providing advice or service in relation to the management of interest rate risk, foreign exchange risk, liquidity risk, credit risk, commodity risk or any other financial risk of the associated corporation;
- (i) providing assistance in the merger or acquisition of a business by the associated corporation;
- (j) providing advice or service in relation to the associated corporation's compliance with—
 - (i) accounting standards;
 - (ii) internal treasury policies; or
 - (iii) regulatory requirements in relation to treasury management;
- (k) providing advice or service in relation to the operations of the treasury management system of the associated corporation;

- (l) providing business planning and co-ordination, including economic or investment research and analysis, for the associated corporation in connection with any of the activities specified in paragraphs (a) to (k).
- (2) In this section—
associated corporation (相聯法團) has the meaning given by section 14C(1).

Part 2

Corporate Treasury Transactions

2. Meaning of *corporate treasury transaction*

- (1) For the purposes of sections 14C, 14D and 14E—
corporate treasury transaction (企業財資交易), in relation to a corporation, means any of the following transactions that is entered into by the corporation on its own account and related to the business of an associated corporation—
 - (a) a transaction in relation to the provision of guarantees, performance bonds, standby letters of credit or other credit risk instruments in respect of the borrowing of money by the associated corporation;
 - (b) a transaction investing the funds of the corporation or the associated corporation in any of the following financial instruments for managing the cash and liquidity position of the corporation or the associated corporation—
 - (i) deposits;

- (ii) certificates of deposit;
 - (iii) bonds;
 - (iv) notes;
 - (v) debentures;
 - (vi) money-market funds;
 - (vii) other financial instruments (except securities issued by a private company as defined by section 20ACA(2));
 - (c) a transaction in respect of any of the following contracts that are entered into for the purpose of hedging interest rate risk, foreign exchange risk, liquidity risk, credit risk, commodity risk or any other financial risk of the associated corporation—
 - (i) contracts for difference;
 - (ii) foreign exchange contracts;
 - (iii) forward or futures contracts;
 - (iv) swap contracts;
 - (v) options contracts;
 - (d) a factoring or forfaiting transaction.
- (2) In this section—
- associated corporation*** (相聯法團) has the meaning given by section 14C(1).

Part 3

Prescribed Percentages for Safe Harbour Rule

3. Prescribed profits percentage

For the purposes of section 14E, the prescribed profits percentage is 75%.

4. Prescribed asset percentage

For the purposes of section 14E, the prescribed asset percentage is 75%.”.

Division 2—Interest in respect of Borrowing and Lending of Money with Associated Corporations

7. Section 15 amended (certain amounts deemed trading receipts)

(1) After section 15(1)(i)—

Add

“(ia) sums, not otherwise chargeable to tax under this Part, received by or accrued to a corporation (other than a financial institution), by way of interest that arises through or from the carrying on in Hong Kong by the corporation of its intra-group financing business within the meaning of section 16(3), even if the moneys in respect of which the interest is received or accrues are made available outside Hong Kong;”.

(2) Section 15(1)(l)(ii)—

Repeal

“and”.

(3) After section 15(1)(l)—

Add

- “(la) sums, not otherwise chargeable to tax under this Part, received by or accrued to a corporation (other than a financial institution), by way of gains or profits arising through or from the carrying on in Hong Kong by the corporation of its intra-group financing business within the meaning of section 16(3), from the sale or other disposal or on the redemption, on maturity or presentment or otherwise, of a certificate of deposit, bill of exchange or regulatory capital security, even if—
- (i) the moneys laid out for the acquisition of the certificate, bill or security were made available outside Hong Kong; or
 - (ii) the sale, disposal or redemption is effected outside Hong Kong; and”.

8. Section 16 amended (ascertainment of chargeable profits)

- (1) Section 16(1)(a)—

Repeal

“and (2C)”

Substitute

“, (2C), (2CA) and (2CC)”.

- (2) Section 16(1)(c)—

Repeal

“(j), (k) or (l)”

Substitute

“(ia), (j), (k), (l) or (la)”.

- (3) Section 16(2)(e)(iv)—

Repeal

“; or”

Substitute a semicolon.

- (4) Section 16(2)(f)(iii)—

Repeal the full stop

Substitute

“; or”.

- (5) After section 16(2)(f)—

Add

- “(g) the borrower is a corporation carrying on in Hong Kong an intra-group financing business and—
- (i) the deduction claimed is in respect of interest payable by it on money borrowed from a non-Hong Kong associated corporation (*lender*) in the ordinary course of that business;
 - (ii) the lender is, in respect of the interest, subject to a similar tax in a territory outside Hong Kong at a rate that is not lower than the reference rate; and
 - (iii) the lender’s right to use and enjoy that interest is not constrained by a contractual or legal obligation to pass that interest to any other person, unless the obligation arises as a result of a transaction between the lender and a person other than the borrower dealing with each other at arm’s length.

Note—

See subsection (2I) for elaboration on how a person is regarded as subject to a tax at a certain rate and the meanings of *similar tax* and *reference rate*.”.

- (6) Section 16(2A)—

Repeal

“and (2C)”

Substitute

“, (2C) and (2CA)”.

- (7) Section 16(2B)—

Repeal

“and (2C)” (wherever appearing)

Substitute

“, (2C) and (2CA)”.

- (8) Section 16(2C)—

Repeal

“and (2B)” (wherever appearing)

Substitute

“, (2B) and (2CA)”.

- (9) After section 16(2C)—

Add

“(2CA) Where the condition for the application of subsection (1)(a) is satisfied under subsection (2)(g), the application of subsection (1)(a) is nevertheless qualified by subsection (2CB) if—

- (a) at any time during the basis period of the borrower for the year of assessment concerned, arrangements are in place, whether between the borrower and the lender or otherwise, by which

- any sum payable by way of interest on the money borrowed or on any part of the money borrowed is payable, whether directly or through any interposed person, to a related person; and
- (b) the related person is, in respect of the sum—
- (i) neither subject to profits tax in Hong Kong, nor subject to a similar tax in any territory outside Hong Kong; or
 - (ii) subject to profits tax in Hong Kong, or subject to a similar tax in a territory outside Hong Kong, but no rate at which the person is subject to such tax is equal to or higher than the reference rate.

Note—

See subsection (2I) for elaboration on how a person is regarded as subject to a tax at a certain rate and the meanings of *similar tax*, *reference rate* and *related person*.

- (2CB) For the purposes of subsection (2CA), the amount of the deduction that, but for subsections (2A), (2B), (2C) and (2CA), would have been allowed under subsection (1)(a) for the year of assessment concerned in respect of sums payable by the borrower by way of interest on the money borrowed or on the relevant part of the money borrowed, as the case may be, is to be reduced by an amount calculated in accordance with the following formula—

$$\frac{A}{B} \times C$$

where: A means the total number of days during the basis period of the borrower for the year of assessment concerned, at the end of each of which the principal in respect of the money borrowed or in respect of the relevant part of the money borrowed, as the case may be, is outstanding and the arrangements mentioned in subsection (2CA)(a) are in place;

B means the total number of days during the basis period of the borrower for the year of assessment concerned, at the end of each of which the principal in respect of the money borrowed or in respect of the relevant part of the money borrowed, as the case may be, is outstanding; and

C means the total amount of sums payable by the borrower by way of interest on the money borrowed or on the relevant part of the money borrowed, as the case may be, that, but for subsections (2A), (2B), (2C) and (2CA), would have been deductible under subsection (1)(a) for the year of assessment concerned.

(2CC) Where a deduction under subsection (1)(a) is claimed, by virtue of subsection (2)(g), for a year of assessment in respect of interest payable on money

borrowed by a corporation, no deduction is to be allowed in respect of the interest if the Commissioner is satisfied that the main purpose, or one of the main purposes, of the borrowing of the money is to utilize a loss to avoid, postpone or reduce any liability, whether of the corporation or another person, to profits tax under this Ordinance.

(2CD) In subsection (2CC)—

loss (虧損)—

(a) means a loss sustained by a related person within the meaning of subsection (2I)(d)(ii) or (iii) in a trade, profession or business, whether in Hong Kong or elsewhere; and

(b) includes any balance of such loss.”.

(10) Section 16(2E)—

Repeal

“subsection (2B)”

Substitute

“subsections (2B) and (2CA)”.

(11) Section 16(2E)(a)—

Repeal

“that subsection”

Substitute

“those subsections”.

(12) After section 16(2H)—

Add

“(2I) For the purposes of this subsection and subsections (2)(g) and (2CA)—

- (a) a person is, in respect of an interest or a sum, subject to a tax at a certain rate in a territory if the Commissioner is satisfied that—
 - (i) for a similar tax in a territory outside Hong Kong as mentioned in subsections (2)(g)(ii) and (2CA)(b)(i) and (ii)—tax of that nature has been paid or will be paid, whether by deduction or otherwise, at that rate by that person in respect of the interest or sum concerned in that territory as required by the laws of that territory; or
 - (ii) for profits tax in Hong Kong as mentioned in subsection (2CA)(b)(i) and (ii)—profits tax under this Ordinance has been paid or will be paid at that rate by that person in respect of the sum concerned in Hong Kong;
- (b) **similar tax** (類似稅項) means a tax that is of substantially the same nature as profits tax under this Ordinance;
- (c) **reference rate** (參考稅率) means—
 - (i) the rate specified in Schedule 8 for the year of assessment concerned; or
 - (ii) if section 14D(1) applies in respect of the borrower for the year of assessment concerned, the rate applicable under that section; and
- (d) **related person** (有關連人士) means—
 - (i) the borrower;
 - (ii) a person (other than the lender) who is connected with the borrower; or

- (iii) a person (other than the borrower) who is connected with the lender.”.

(13) Section 16(3)—

Add in alphabetical order

“*intra-group financing business* (集團內部融資業務), in relation to a corporation, means the business of the borrowing of money from and lending of money to its associated corporations;

non-Hong Kong associated corporation (非香港相聯法團) means an associated corporation that does not carry on any trade, profession or business in Hong Kong;”.

(14) Section 16(3B), English text—

Repeal

“shall be”

Substitute

“is”.

(15) Section 16(3B)(a), after “borrower;”—

Add

“or”.

(16) After section 16(3B)—

Add

“(3C) In this section, a person is regarded as being connected with a lender if the person is—

- (a) an associated corporation of the lender; or
- (b) a person (other than a corporation)—
 - (i) who controls the lender;
 - (ii) who is controlled by the lender; or

(iii) who is under the control of the same person as is the lender.”.

(17) After section 16(6)—

Add

“(7) The Secretary for Financial Services and the Treasury may by order published in the Gazette amend the definition of *reference rate* in subsection (2I)(c).”.

9. Schedule 8 amended (rate of profits tax in respect of a corporation)

Schedule 8, before “19CA(4)”—

Add

“16(2I),”.

10. Schedule 17A amended (specified alternative bond scheme and its tax treatment)

Schedule 17A, section 21(4)—

Repeal

“and (l)”

Substitute

“, (l) and (la)”.

Division 3—Tax Treatment of Regulatory Capital Security

11. Section 2 amended (interpretation)

(1) Section 2(1)—

Repeal the definition of *debenture*

Substitute

“*debenture* (債權證), in relation to a corporation, includes debenture stock, bond and any other debt security of the corporation, whether or not constituting a charge on the assets of the corporation;”.

(2) Section 2(1)—

Add in alphabetical order

“*regulatory capital security* (監管資本證券) has the meaning given by section 17A;”.

12. Section 15 amended (certain amounts deemed trading receipts)

(1) Section 15(1)(j) and (k)—

Repeal

“on maturity or presentment of a certificate of deposit or bill of exchange”

Substitute

“, on maturity or presentment or otherwise, of a certificate of deposit, bill of exchange or regulatory capital security”.

(2) Section 15(1)(l)—

(a) **Repeal**

“on maturity or presentment of a certificate of deposit or bill of exchange notwithstanding that”

Substitute

“, on maturity or presentment or otherwise, of a certificate of deposit, bill of exchange or regulatory capital security even if”;

- (b) Subparagraph (i)—

Repeal

“certificate or bill”

Substitute

“certificate, bill or security”.

- (3) Before section 15(2)—

Add

“(1C) Subsection (1)(f), (g), (i), (ia), (j), (k), (l) and (la) applies, subject to sections 17B, 17C, 17D, 17E, 17F and 17G, in relation to a regulatory capital security.”.

13. Section 16 amended (ascertainment of chargeable profits)

Before section 16(2A)—

Add

“(2AA) Subsections (1)(a) and (2)(a) apply, subject to sections 17B, 17C, 17D, 17E, 17F and 17G, in relation to a sum payable by a financial institution in respect of a regulatory capital security issued by the financial institution.”.

14. Sections 17A to 17G added

After section 17—

Add

“17A. Financial institution: interpretation

- (1) In this section and sections 17B, 17C, 17D, 17E, 17F and 17G—

Additional Tier 1 capital instrument (額外一級資本票據) means a capital instrument that qualifies as Additional Tier 1 capital under Schedule 4B to the Banking (Capital) Rules (Cap. 155 sub. leg. L), or under the equivalent laws or regulatory requirements of another member jurisdiction of the Basel Committee;

associate (相聯者) has the meaning given by section 16(3);

associated corporation (相聯法團) has the meaning given by section 16(3);

Basel Committee (巴塞爾委員會) has the meaning given by section 2(1) of the Banking Ordinance (Cap. 155);

Common Equity Tier 1 capital instrument (普通股權一級資本票據) means a capital instrument that qualifies as Common Equity Tier 1 capital under Schedule 4A to the Banking (Capital) Rules (Cap. 155 sub. leg. L), or under the equivalent laws or regulatory requirements of another member jurisdiction of the Basel Committee;

debt instrument (債務票據) means an instrument specified in Part 1 of Schedule 6 that is in respect of a debt issue;

fair value (公平價值)—

- (a) in relation to a person's asset, means the amount that, at the time as at which the value of the asset is to be determined, the person would obtain from a knowledgeable and willing person dealing at arm's length for the sale of the asset;

- (b) in relation to a person's liability, means the amount that, at the time as at which the value of the liability is to be determined, the person would have to pay to a knowledgeable and willing person dealing at arm's length for the transfer or release of the liability;

fair value accounting (公平價值會計) means a basis of accounting under which assets and liabilities are shown in a balance sheet at their fair value;

paid-up amount (已付數額), in relation to a regulatory capital security or debenture or debt instrument, means the sum paid to the issuer for the issue of the security or debenture or instrument;

regulatory capital security (監管資本證券) means a security—

- (a) that qualifies or has qualified as an Additional Tier 1 capital instrument, and that forms or formed a component of Additional Tier 1 capital, for the purposes of the Banking (Capital) Rules (Cap. 155 sub. leg. L) or of the equivalent laws or regulatory requirements of another member jurisdiction of the Basel Committee; or
- (b) that qualifies or has qualified as a Tier 2 capital instrument, and that forms or formed a component of Tier 2 capital, for the purposes of the Banking (Capital) Rules (Cap. 155 sub. leg. L) or of the equivalent laws or regulatory requirements of another member jurisdiction of the Basel Committee;

Tier 2 capital instrument (二級資本票據) means a capital instrument that qualifies as Tier 2 capital under Schedule 4C to the Banking (Capital) Rules (Cap. 155 sub. leg. L), or under the equivalent laws or regulatory requirements of another member jurisdiction of the Basel Committee.

(2) For the purposes of the definition ***regulatory capital security*** in subsection (1)—

security (證券) does not include—

- (a) a share;
 - (b) any debt instrument the terms and conditions of which provide for the issuer of the instrument converting, or having an option to convert, the instrument into a Common Equity Tier 1 capital instrument of the issuer or any other corporation after a certain period of time; or
 - (c) subject to subsection (3), any debt instrument—
 - (i) that carries a contractual right to any distribution or redemption payment that depends to any extent on the results of the business of the issuer of the instrument or of any part of that business; or
 - (ii) that provides discretion to the issuer of the instrument to make any distribution or redemption payment that depends to any extent on the results of the business of that issuer or of any part of that business.
- (3) A debt instrument does not fall within paragraph (c) of the definition of ***security*** in subsection (2) by reason only that the terms and conditions of the instrument provide for the reduction in distribution

or redemption payment if the results of the business of the issuer of the instrument, or of any part of that business, worsen.

17B. Financial institution: regulatory capital security treated as debt security

- (1) For the purposes of this Part—
 - (a) a regulatory capital security is to be treated as a debt security; and
 - (b) any sum payable in respect of a regulatory capital security by its issuer, other than a repayment of the paid-up amount of the security, is to be treated as interest payable on money borrowed by the issuer of an amount equal to the paid-up amount of the security.
- (2) Subsection (1) has effect subject to sections 17C, 17D, 17E, 17F and 17G.

17C. Financial institution: general provisions on issuer of regulatory capital security

- (1) This section applies in ascertaining profits in respect of which the issuer of a regulatory capital security is chargeable to tax under this Part for a year of assessment.
- (2) Profits of the issuer are to be determined as if fair value accounting were not generally accepted accounting practice in relation to the security or part of the security.

- (3) A sum representing—
- (a) the paid-up amount of the security being written down on a permanent or temporary basis in accordance with any laws or regulatory requirements or the terms and conditions of the security; or
 - (b) the paid-up amount of the security being converted to a Common Equity Tier 1 capital instrument in accordance with any laws or regulatory requirements or the terms and conditions of the security,
- is not to be treated as a receipt arising in or derived from Hong Kong by the issuer from a trade, profession or business carried on in Hong Kong.
- (4) No deduction is to be allowed to the issuer under section 16(1) for any sum representing the paid-up amount of the security being written up in accordance with any laws or regulatory requirements or the terms and conditions of the security, following a write-down of the paid-up amount on a temporary basis in accordance with those laws or requirements or those terms and conditions.

17D. Financial institution: general provisions on regulatory capital security held by, or for benefit of, issuer's specified connected person

- (1) This section applies in ascertaining profits in respect of which a specified connected person of the issuer of a regulatory capital security is chargeable to tax under this Part for a year of assessment if, during the basis period for the year of assessment, the security is held by or for the benefit of the specified connected person.

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- (2) Profits of the specified connected person are to be determined as if fair value accounting were not generally accepted accounting practice in relation to the security or part of the security.
- (3) No deduction is to be allowed to the specified connected person under section 16(1) for any sum representing—
- (a) the paid-up amount of the security being written down on a permanent or temporary basis in accordance with any laws or regulatory requirements or the terms and conditions of the security; or
 - (b) the paid-up amount of the security being converted to a Common Equity Tier 1 capital instrument in accordance with any laws or regulatory requirements or the terms and conditions of the security.
- (4) A sum representing the paid-up amount of the security being written up in accordance with any laws or regulatory requirements or the terms and conditions of the security, following a write-down of the paid-up amount on a temporary basis in accordance with those laws or requirements or those terms and conditions, is not to be treated as a receipt arising in or derived from Hong Kong by the specified connected person from a trade, profession or business carried on in Hong Kong.
- (5) In this section—
- connected person*** (有關連者), in relation to the issuer of a regulatory capital security, means—
- (a) an associated corporation of the issuer; or
 - (b) a person (other than a corporation) who—

- (i) controls the issuer;
- (ii) is controlled by the issuer; or
- (iii) is under the control of the same person as is the issuer;

market maker (市場莊家) means a person who—

- (a) is licensed or registered for dealing in securities under the Securities and Futures Ordinance (Cap. 571) or is authorized to do so by a regulatory authority in a major financial centre outside Hong Kong recognized by the Commissioner for the purposes of this section;
- (b) in the ordinary course of conduct of the person's trade, profession or business in respect of market making, holds oneself out as being willing to buy and sell securities for the person's own account and on a regular basis; and
- (c) is actively involved in market making in securities issued by a wide range of unrelated institutions;

specified connected person (指明有關連者), in relation to the issuer of a regulatory capital security, means a connected person of the issuer who is not excepted within the meaning of subsection (6).

- (6) In this section, a connected person of the issuer of a regulatory capital security is excepted if the connected person—
 - (a) is chargeable to tax under this Part in respect of a sum payable in respect of the security;
 - (b) is entitled to a sum payable in respect of the security in the capacity of—

- (i) a person acting as a trustee of a trust estate, or holding property belonging to others pursuant to the terms of a contract, where the person is not beneficially entitled to the sum;
 - (ii) a beneficiary of a unit trust to which section 26A(1A)(a)(i) or (ii) applies, where the sum is payable to a trustee of the unit trust in respect of a specified investment scheme referred to in section 26A(1A)(b); or
 - (iii) a member of a retirement scheme that is either a recognized retirement scheme or a substantially similar retirement scheme established outside Hong Kong, where the Commissioner is satisfied that the latter scheme complies with the requirements of a supervisory authority within an acceptable regulatory regime;
- (c) is a market maker who, in the ordinary course of conduct of the market maker's trade, profession or business in respect of market making, holds the security for the purpose of providing liquidity for the security;
- (d) is a public body; or
- (e) is a body corporate, where the Government owns beneficially more than half of the issued share capital of that body corporate for the time being.

17E. Financial institution: profits adjusted if associates deal not at arm's length in connection with regulatory capital security

- (1) This section applies if—
 - (a) conditions are made or imposed between a financial institution and a person who is an associate of the financial institution, in their commercial or financial relations in connection with a regulatory capital security; and
 - (b) the conditions differ from those that would be made if the person were not such an associate.
- (2) Any profits that, but for the conditions referred to in subsection (1)(a), would have accrued to the financial institution or the person and, by reason of those conditions, have not so accrued, are to be included in the profits of the financial institution or the person and taxed in accordance with this Part.

17F. Financial institution: issuer's deduction if regulatory capital security is issued to, held by or issued or held for benefit of specified connected person

- (1) No deduction is to be allowed to the issuer of a regulatory capital security (*specified issuer*) under section 16(1) for any sum payable in respect of the security if it is issued to, held by or issued or held for the benefit of a specified connected person of the specified issuer.
- (2) Subsection (1) does not apply to a sum payable in respect of a regulatory capital security issued to or for the benefit of a specified connected person of the specified issuer if both of the following conditions are met—

- (a) the money paid by or on behalf of the specified connected person for the issue of the security has been entirely funded, either directly or indirectly, by the proceeds of an external issue of a regulatory capital security or debenture or debt instrument by the specified connected person or an associated corporation of the specified issuer;
 - (b) the externally issued regulatory capital security or debenture or debt instrument is not, at any time during the basis period of the specified issuer for the year of assessment concerned, held by or for the benefit of a specified connected person of the specified issuer.
- (3) The amount of any deduction allowable under subsection (2) is not to exceed the sum payable by the specified connected person or associated corporation (as the case requires) in respect of the externally issued regulatory capital security or debenture or debt instrument (other than the repayment of the paid-up amount).
- (4) Subsection (5) applies to a deduction allowable under subsection (2) if the externally issued regulatory capital security or debenture or debt instrument is held by or for the benefit of an associate (other than a specified connected person) of the specified issuer.
- (5) The amount of the deduction that, but for this subsection, would have been allowed under section 16(1) is to be reduced by any amount by which the sum payable to, or for the benefit of, that associate exceeds a reasonable commercial return on money borrowed of an amount equal to the paid-up amount

for the externally issued regulatory capital security or debenture or debt instrument.

- (6) For the purposes of subsection (5), a reasonable commercial return means a return that, at the time the security or debenture or instrument was issued, would be regarded in the prevailing market conditions as a reasonable commercial return between persons dealing with each other at arm's length in the open market.
- (7) In this section, a regulatory capital security or debenture or debt instrument is externally issued if the security or debenture or instrument is not issued to, or for the benefit of, a specified connected person of the specified issuer.
- (8) Subject to subsections (9) and (10), section 17D(5) and (6) applies to this section.
- (9) The definition of *market maker* in section 17D(5) applies as if a reference to “this section” in paragraph (a) of that definition were a reference to this section.
- (10) Section 17D(6) applies for the purposes of construing a reference to specified connected person appearing in subsection (2)(b), (4) or (7) as if—
 - (a) the reference to “the issuer of a regulatory capital security” in section 17D(6) were a reference to the specified issuer; and
 - (b) each reference to “the security” in section 17D(6)(a), (b) or (c) were a reference to the externally issued regulatory capital security or debenture or debt instrument referred to in subsection (2)(b), (4) or (7) (as the case requires).

17G. Financial institution: non-resident financial institution's Hong Kong branch treated as separate enterprise

- (1) This section applies in ascertaining profits in respect of which a non-resident financial institution with capital raised through the issue of a regulatory capital security is chargeable to tax under this Part in relation to its Hong Kong branch.
- (2) The profits of the Hong Kong branch of the non-resident financial institution are those that the Hong Kong branch would have made if it were a distinct and separate enterprise that—
 - (a) engaged in the same or similar activities under the same or similar conditions; and
 - (b) dealt wholly independently of the non-resident financial institution.
- (3) In applying subsection (2), account is to be taken of the functions performed, assets used and risks assumed by the non-resident financial institution—
 - (a) through the Hong Kong branch; and
 - (b) through the other parts of the non-resident financial institution.
- (4) In applying subsection (2), it is to be assumed that the Hong Kong branch—
 - (a) has the same credit rating as the non-resident financial institution; and
 - (b) has such equity and loan capital as it could reasonably be expected to have if it were a distinct and separate enterprise as described in that subsection.
- (5) In accordance with subsection (2), transactions in connection with a regulatory capital security between

the Hong Kong branch and any other part of the non-resident financial institution are treated as taking place on such terms and conditions as would have been agreed between parties dealing at arm's length.

- (6) No deduction is to be allowed for costs and expenses in excess of those that would have been incurred on the assumptions in subsection (4).
- (7) In this section—
 - (a) ***non-resident financial institution*** (境外財務機構) means any financial institution whose head office is situated outside Hong Kong;
 - (b) ***Hong Kong branch*** (香港分行) means any business carried on in Hong Kong by a non-resident financial institution.”.

15. Schedule 6 amended

- (1) Schedule 6—

Repeal

“[ss. 14A(4) & 26A(2) & (3) & Schs. 17A & 29]”

Substitute

“[ss. 14A(4), 17A(1) & 26A(2) & (3) & Schs. 17A, 29 & 36]”.

- (2) Schedule 6, Part 1, item 3, after “any other instrument”—

Add

“(other than a regulatory capital security)”.

16. Schedule 16 amended (specified transactions)

- (1) Schedule 16—

Repeal

“& 29]”

Substitute

“, 29 & 36]”.

- (2) Schedule 16, Part 2, after section 2—

Add

- “3. For the purposes of paragraphs (a), (b) and (c) of the definition of *securities* in section 1 of this Part, a regulatory capital security is treated as a bond.”.

Division 4—Transitional Provisions

17. Section 89 amended (transitional provisions)

At the end of section 89—

Add

- “(16) Schedule 36 sets out transitional provisions that have effect for the purposes of amendments to this Ordinance made by the Inland Revenue (Amendment) (No. 2) Ordinance 2016 (12 of 2016).”.

18. Schedule 36 added

At the end of the Ordinance—

Add

“Schedule 36

[s. 89(16)]

Transitional Provisions for Inland Revenue (Amendment) (No. 2) Ordinance 2016

1. In this Schedule—
 - (a) **2016 Amendment Ordinance** (《2016年修訂條例》) means the Inland Revenue (Amendment) (No. 2) Ordinance 2016 (12 of 2016);
 - (b) **commencement date** (生效日期) means the day on which the 2016 Amendment Ordinance comes into operation;
 - (c) **qualifying profits** (合資格利潤) has the meaning given by section 14C(1); and
 - (d) in relation to a person, a year of assessment is the **transitional year of assessment** (過渡課稅年度) if the commencement date falls within the basis period of the person for the year of assessment.
2. For the purposes of section 14D(1), in computing the qualifying profits of a corporation, sums received by or accrued to the corporation before 1 April 2016 are not to be taken into account.
3. For the purposes of section 14E(5), in computing the corporate treasury profits of a corporation, sums received by or accrued to the corporation before 1 April 2016 are not to be taken into account.

4. Section 15(1)(ia) and (la) does not apply to sums received or accrued before the commencement date.
5. The following provisions apply only to sums payable on or after 1 April 2016—
 - (a) the amendments made to section 16(1), (2), (2A), (2B), (2C), (2E), (3) and (3B) by section 8 of the 2016 Amendment Ordinance;
 - (b) section 16(2)(g), (2CA), (2CB), (2CC), (2CD), (2I) and (3C).
6. Subject to section 7 of this Schedule, the following provisions apply only in ascertaining the profits in respect of which a person is chargeable to tax under Part 4 for the transitional year of assessment or any subsequent year of assessment—
 - (a) the amendments made to sections 2, 15 and 16 and Schedules 6 and 16 by Division 3 of Part 2 of the 2016 Amendment Ordinance;
 - (b) sections 15(1C), 16(2AA), 17A, 17B, 17C, 17D, 17E and 17F.
7. For a regulatory capital security issued before the commencement date—
 - (a) the following provisions apply only to sums received or accrued, in respect of the security, on or after the commencement date—
 - (i) the amendments made to section 15 and Schedule 6 by Division 3 of Part 2 of the 2016 Amendment Ordinance;

- (ii) section 17B (in so far as it relates to a person to whom or for whose benefit a sum is payable in respect of the security);
 - (iii) section 17D(1);
- (b) the following provisions apply only to sums payable, in respect of the security, on or after the commencement date—
 - (i) section 16(2AA);
 - (ii) section 17B (in so far as it relates to the issuer of the security);
 - (iii) sections 17C(1) and 17F;
- (c) in applying section 17C(2) to the issuer of the security who has included any sums as assessable profits or losses when bringing the security into account at a fair value—
 - (i) the liability under the security is taken to have been released and re-assumed at its fair value on the commencement date; and
 - (ii) any change in value between that date and the end of the basis period is to be brought into account for computing the assessable profits for the transitional year of assessment;
- (d) in applying section 17D(2) to a specified connected person of the issuer of the security if the specified connected person has included any sums as assessable profits or losses when bringing the security into account at a fair value—

- (i) the security is taken to have been disposed of and re-acquired at its fair value on the commencement date; and
 - (ii) any change in value between that date and the end of the basis period is to be brought into account for computing the assessable profits for the transitional year of assessment;
 - (e) sections 17C(3) and 17D(3) apply only to a write-down or conversion effected on or after the commencement date;
 - (f) sections 17C(4) and 17D(4) apply only to a write-up effected on or after the commencement date; and
 - (g) the amendment made to Schedule 16 by section 16 of the 2016 Amendment Ordinance applies only to a transaction carried out on or after the commencement date.
8. Section 17G applies only in ascertaining the profits in respect of which a non-resident financial institution with capital raised through the issue of a regulatory capital security (whether before, on or after the commencement date) is chargeable to tax under Part 4—
- (a) for the year of assessment beginning on the first day of April in the calendar year next following the commencement date; or
 - (b) for any subsequent year of assessment.”.
-

Part 3

Consequential and Related Amendments Concerning Regulatory Capital Securities

Division 1—Consequential Amendments to Inland Revenue Rules

19. Cross-heading before rule 3 amended

Cross-heading before rule 3—

Repeal

“BANK WHOSE HEAD OFFICE IS ELSEWHERE THAN IN HONG KONG”

Substitute

“FINANCIAL INSTITUTION WHOSE HEAD OFFICE IS OUTSIDE HONG KONG”.

20. Rule 3 amended (banks; Hong Kong branch offices)

(1) Rule 3, heading—

Repeal

“Banks;”

Substitute

“Financial institution: profits of”.

(2) Before rule 3(1)—

Add

“(1A) This rule has effect to the extent to which it is not inconsistent with sections 17B, 17C, 17D, 17E, 17F and 17G of the Ordinance.”.

(3) Rule 3—

Repeal paragraph (1)

Substitute

“(1) In this rule—

- (a) *non-resident financial institution* (境外財務機構) means any financial institution whose head office is situated outside Hong Kong;
- (b) *Hong Kong branch* (香港分行) means any business carried on in Hong Kong by a non-resident financial institution.”.

(4) Rule 3(2) and (3)—

Repeal

“bank” (wherever appearing)

Substitute

“non-resident financial institution”.

21. Cross-heading before rule 5 amended

Cross-heading before rule 5—

Repeal

“WHOSE HEAD OFFICE IS ELSEWHERE THAN IN HONG KONG”

Substitute

“, OTHER THAN A FINANCIAL INSTITUTION, WHOSE HEAD OFFICE IS OUTSIDE HONG KONG”.

22. Rule 5 amended (profit of Hong Kong branch offices)

(1) Rule 5, heading—

Repeal

“Profit of Hong Kong branch offices”

Substitute

“Profits of Hong Kong branch offices of person other than financial institution”.

(2) Rule 5(2)—

(a) **Repeal**

“a person having”

Substitute

“a person, other than a financial institution, having”;

(b) **Repeal**

“elsewhere than in Hong Kong”

Substitute

“outside Hong Kong”.

23. Rule 7 added

At the end of the Rules—

Add

“7. Transitional provisions

The amendments made to rules 3 and 5 by the Inland Revenue (Amendment) (No. 2) Ordinance 2016 (12 of 2016) apply only in ascertaining the profits in respect of which a person is chargeable to tax under Part 4 of the Ordinance—

- (a) for the year of assessment beginning on the first day of April in the calendar year next following the day on which the amendments come into operation; or
- (b) for any subsequent year of assessment.”.

Division 2—Related Amendments to Stamp Duty Ordinance

24. Section 19 amended (contract notes, etc. in respect of sale and purchase of Hong Kong stock)

Section 19(1DA), after “Schedule 8”—

Add

“or Part 2 of Schedule 9”.

25. Section 63 amended (regulations)

Section 63(c)—

Repeal

“Schedule 8”

Substitute

“Schedules 8 and 9”.

26. First Schedule amended

(1) First Schedule—

Repeal

“Schs. 7 & 8]”

Substitute

“Schs. 7, 8 & 9]”.

(2) First Schedule, head 2(3), Note 4, after “Schedule 8”—

Add

“or Part 3 of Schedule 9”.

(3) First Schedule, head 2(4), Note 2, after “Schedule 8”—

Add

“or Part 4 of Schedule 9”.

27. Schedule 9 added

After Schedule 8—

Add

“Schedule 9

[ss. 19 & 63 & 1st Sch.]

**Transactions and Transfers Relating to
Regulatory Capital Security**

Part 1

Interpretation

1. In this Schedule—

purchase (購買), *sale* (售賣) and *sale or purchase* (售賣或購買) have the meanings given by section 19(16);

regulatory capital security (監管資本證券) has the meaning given by section 17A of the Inland Revenue Ordinance (Cap. 112).

Part 2

**Transactions to which Section 19(1) does not
Apply**

1. A sale or purchase of a regulatory capital security.

2. A transaction that is deemed under section 19(1E)(a) or (12) to be a sale and purchase of Hong Kong stock where the stock involved is a regulatory capital security.

Part 3

Transfers on which Stamp Duty under Head 2(3) in First Schedule is not Payable

1. A transfer executed for a transaction by which the beneficial interest in a regulatory capital security passes otherwise than on sale and purchase.

Part 4

Transfers on which Stamp Duty under Head 2(4) in First Schedule is not Payable

1. A transfer executed for a transaction by which a regulatory capital security is transferred.”.