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tricolor

Business, Corporate and Investor Services
商務、企業、投資者服務

Tricolor Services Limited
卓佳專業商務有限公司

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Hong Kong Offshore Funds Tax Exemption

The Revenue (Profits Tax Exemption for Offshore Funds) Bill 2005 ("the Bill") which exempts offshore funds from profits tax was passed by the Legislative Council on 1 March 2006.

Prior to enactment of the Bill, the Inland Revenue Ordinance provided that any person deriving trading profits from securities transactions carried out in Hong Kong was liable to pay profits tax regardless of his/her residence. The financial services industry has been expressing the view that due to keen international competition, it is vital for Hong Kong to provide tax exemption to offshore funds as with other major financial centres, otherwise some of the offshore funds may relocate away from Hong Kong.

The Secretary for Financial Services and the Treasury, Mr Frederick Ma, when moving the resumption of the Second Reading of the Bill on 1 March 2006, stressed that the proposed bill is vital to reinforcing Hong Kong's status as an international financial centre and enhancing our competitiveness among other international financial centres such as New York and London, which all exempt offshore funds from tax.

This TechNews contains a summary of the key features of the legislation.



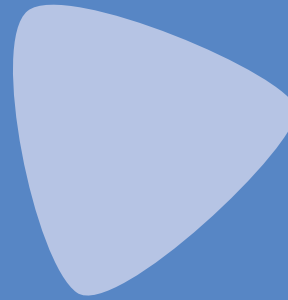
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THE BILL & MAJOR PROVISIONS

The major provisions of the Bill are summarised as follows:

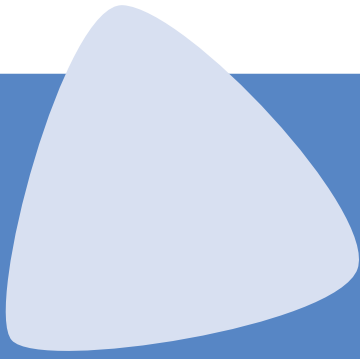
Section	Summary
Section 20AB(2) and (3)	Resident Person <p>This section deals with the determination of the residence of individuals, corporations, partnerships and trustees.</p> <p>The following persons are to be regarded as resident persons in relation to any year of assessment:</p> <ul style="list-style-type: none">(i) a natural person (who is not a trustee of a trust), who:<ul style="list-style-type: none">(a) ordinarily resides in Hong Kong in that year of assessment,(b) stays in Hong Kong for more than 180 days during that year of assessment, or(c) stays in Hong Kong for more than 300 days in 2 consecutive years of assessment, one of which is that year of assessment;(ii) a corporation or a partnership (that is not a trustee of a trust), the central management and control of which is exercised in Hong Kong in that year of assessment;(iii) a trustee of a trust, the central management and control of which is exercised in Hong Kong in that year of assessment.
Section 20AC(1)	Exemption <p>A non-resident person is exempt from profits tax in respect of his/her profits ("exempt person") from 2 kinds of specified transactions.</p>
Section 20AC(2), (3) and (4)	Qualifying Transactions for Exemption <p>The following criteria should be met in order to qualify for exemption:</p> <ul style="list-style-type: none">(i) The person's profits must come from specified transactions which are within the definitions in Part 2 of Schedule 5 to the Securities and Futures Ordinance, such as:<ul style="list-style-type: none">(a) dealing in securities;(b) dealing in futures contracts;(c) leveraged foreign exchange trading.



Section	Summary
Section 20AC(2), (3) and (4) (Cont')	<p>(ii) The above transactions must be carried out through specified persons, such as:</p> <ul style="list-style-type: none">(a) licensed corporations; and(b) authorised financial institutions. <p>The exemption applies in relation to a year of assessment commencing on or after 1 April 1996.</p> <p>Incidental Transactions for Exemption</p> <p>Transactions that are incidental to the carrying out of the qualifying transactions have also exempt.</p>
Section 20AC(5)	<p>Exclusions to Exemptions</p> <p>A non-resident person will lose the entire exemption in a year of assessment if he/she carries on in Hong Kong in that year of assessment any business that involves any transaction other than the specified transactions.</p>
Section 20AC(6)	<p>If a non-resident person's trading receipts from the incidental transactions in a year of assessment exceed 5% of the total trading receipts from all specified transactions in that year of assessment, the exemption in respect of the profits from incidental transactions will be lost.</p>
Section 20AD	<p>No Offset</p> <p>In certain circumstances, a loss arising from the specified transactions in a year of assessment cannot be used to set off assessable profits.</p>



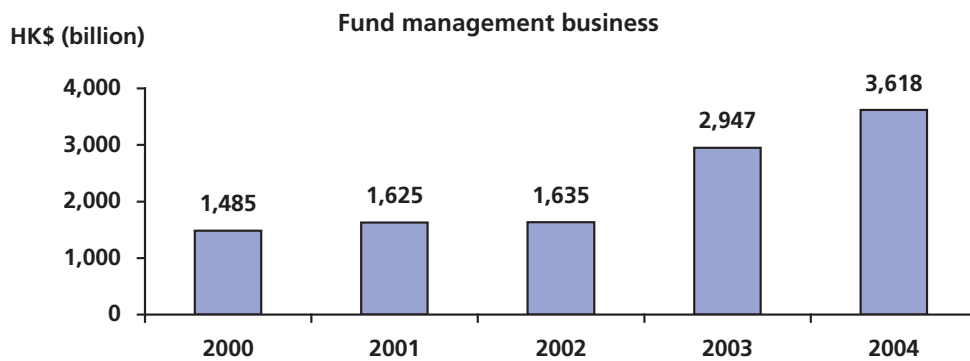
Section	Summary
Section 20AE(1) and (3)	<p data-bbox="544 909 788 931">The Deeming Provisions</p> <p data-bbox="544 976 1366 1061">In certain circumstances, the assessable profits of an exempt person are to be regarded as the assessable profits of a resident person. It applies in relation to the year of assessment 2006/2007.</p> <p data-bbox="544 1106 1107 1128">The provisions will be invoked in the following circumstances:</p> <ul data-bbox="544 1173 1366 1285" style="list-style-type: none"><li data-bbox="544 1173 1366 1218">(i) where a resident person has a direct or indirect beneficial interest in an exempt person and the interest reaches a specified threshold; and<li data-bbox="544 1229 1366 1285">(ii) where a resident person has a direct or indirect beneficial interest in an exempt person and the exempt person is the resident person's associate. <p data-bbox="544 1330 879 1352">The specified threshold is as follows:</p> <ul data-bbox="544 1397 1366 1541" style="list-style-type: none"><li data-bbox="544 1397 1366 1442">(i) if the exempt person is a corporation, an interest in not less than 30% of its issued share capital,<li data-bbox="544 1453 1366 1487">(ii) if the exempt person is a partnership, an interest in not less than 30% of its profits, or<li data-bbox="544 1487 1366 1541">(iii) if the exempt person is a trustee, an interest in not less than 30% in value of the relevant trust estate.
Section 20AE(8)	The deeming provisions do not apply in relation to a resident person if the Commissioner of Inland Revenue is satisfied that beneficial interests in the relevant exempt person are <i>bona fide</i> widely held.
Section 70AB	This provides for the revision of an assessment necessitated by the commencement of the exemption provisions.
Schedule 15	<p data-bbox="544 1906 628 1928">Formula</p> <p data-bbox="544 1962 1350 2020">It contains a formula for ascertaining the amount regarded as the assessable profits of a resident person under the deeming provisions.</p>



To allow adequate time for the financial services industry to change its systems to facilitate provision of information to resident investors for tax return purposes, the deeming provisions will apply from the year of assessment 2006/07.

SUSTAINED GROWTH IN FUND MANAGEMENT INDUSTRY

The new legislation will have impact on the fund management industry. According to the 2004 fund management activities survey conducted by the Securities and Futures Commission, the fund management business for the year ended December 2004 reported by licensed corporations increased by 22.8% to HK\$3,618 billion from HK\$2,947 billion in 2003, and jumped by 80.2% from HK\$1,635 billion in 2002. A bar chart showing the growth of the fund management business for the years 2000 to 2004, as reported by licensed corporations is shown below:



SUMMARY

The new legislation will further strengthen Hong Kong's position as an international financial centre by removing the uncertainty concerning the Hong Kong profits tax position on offshore funds, thus stimulating growth for the investment management industry.

Should you need further information or clarification regarding this TechNews, please do not hesitate to approach your usual Tricor contact.

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Tricor has built its reputation and professional expertise through the acquisition of certain practices from major international accounting firms in Hong Kong, Mainland China, Singapore, Thailand and the BVI.

Our mission is to be The Business Enabler of choice.

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