Hong Kong Institute of
Certified Public Accountants
香港會計師公會

**By email (noeltsang@fstb.gov.hk/andrewngan@fstb.gov.hk) and by hand**

27 September 2019

Our Ref.: C/TXG, BH46462

Financial Services Branch Financial Services
and the Treasury Bureau
Central Government Offices
2 Tim Mei Avenue, Tamar, Hong Kong

Attention: Ms Noel Tsang/Mr Andrew Ngan

Dear Sirs,

**PROPOSED PROFITS TAX CONCESSIONS FOR THE INSURANCE SECTOR**

Thank you for inviting the views of the Hong Kong Institute of Certified Public Accountants ("the Institute") on the proposed tax concessions for the insurance sector. The Taxation Faculty ("TF") of the Institute has reviewed the paper and our views and concerns are summarized below.

## 1. ***Background***

The Chief Executive of Hong Kong mentioned in her 2018 policy address that "*The B&R Initiative facilitates the development of infrastructure and trade in countries along the routes. It also generates demand for insurance and risk management services for large-scale infrastructure and investment projects. With a mature insurance market and a robust regulatory regime, Hong Kong is well positioned to provide quality services for these projects. Meanwhile, the development of the Greater Bay Area spurs the flow of production factors, consolidates Hong Kong's advantages in the financial market and supports the growth of real economy in the region, giving a fresh impetus to our insurance sector. After having consulted the Financial Leaders Forum, the Government will adopt various measures, including tax reliefs to promote the development of marine insurance and underwriting of specialty risks in Hong Kong so as to strengthen Hong Kong's status as an international insurance hub*."

The Financial Secretary of Hong Kong also mentioned in his 2019/2020 budget speech that "*the Government will propose legislative amendments to provide tax concessions for marine insurance and the underwriting of specialty risks, and allow for the formation of special purpose vehicle companies specifically for issuing insurance-linked securities. We will continue to look into measures that are conducive to the development of the industry."*

The proposed profits tax concessions under review echo the above statements made by the Chief Executive and the Financial Secretary.

## 2. ***Highlights of the concessions***

I. Specified insurers engaged in general insurance and reinsurance businesses would enjoy a tax concession at 50% of the profits tax rate in respect of their assessable profits derived from their general and long term reinsurance business under Section 14B of the Inland Revenue Ordinance

37th Floor, Wu Chung House,
213 Queen's Road East, Wanchai, Hong Kong
香港灣仔皇后大道東213號胡忠大廈37樓
Tel電話: (852) 2287 7228
Fax傳真: (852) 2865 6776
(852) 2865 6603
Website網址: www.hkicpa.org.hk
Email電郵: hkicpa@hkicpa.org.hk

("IRO"). However, five lines of business of the specified insurers including health risk; mortgage guarantee risk; motor vehicle damage and liability; employees' compensation liability; and owners' corporation third party liability will be excluded from the tax concessionary treatments.

II. Specified insurers are:
   a. A company authorized by the Insurance Authority ("IA") under Section 8 of the Insurance Ordinance ("IO"), except a professional reinsurer and an authorized captive insurer;
   b. Lloyd's as defined under Section 2(1) of the IO; and
   c. An association of underwriters approved by the IA under Section 6(1)(c) of the IO.

III. The tax concession at 50% of profits tax rate would also apply to licensed insurance broker companies in respect of their assessable profits derived from the business of placing: (a) general and long term reinsurance contracts with professional reinsurers; (b) general reinsurance contracts with specified insurers; and (c) certain general insurance contracts with specified insurers, the proposed scope of which is the same as that in point (I) above.

IV. A main purpose test provision will be introduced to counteract potential abuse of the preferential tax regime by artificial insurance exchange arrangements with other reinsurers or specified insurers engaged in reinsurance businesses.

### 3. ***Our comments***

The TF has the following comments on the proposals.

As the insurance categorization detailed in Schedule 1 of the IO does not include specific categories for marine insurance, we note that the proposed scope of the amendments are wider than the categories highlighted for development by the Chief Executive and the Financial Secretary. The TF also appreciates that the proposals exclude five categories of general insurance business which are less relevant to both marine insurance and the Belt and Road Initiative to make the proposals more in line with the policy intention.

Despite the above, the TF suggests that the government should consider expanding the tax concessionary treatment to specified insurers which provide qualified deferred annuity products and retirement scheme management services, classified as long term business in Schedule 1 of the IO. This extension should also cover licensed insurance broker companies on their business placing with specified insurers on these products and services. Such an extension could encourage Hong Kong taxpayers to save for retirement on the assumption that the reduced profits tax liabilities of specified insurers and licensed insurance broker companies would be used to lower management and administrative expenses charged to their clients. Therefore, should the scope be expanded as per suggested, there should be a sound and effective system to monitor how the specified insurers and licensed insurance broker companies use their tax savings. This suggested change is in line with the policy intention of the Inland Revenue and MPF Schemes Legislation (Tax Deductions for Annuity Premiums and MPF Voluntary Contributions) (Amendment) Ordinance 2019 ("the amendment ordinance").

The policy intention of the amendment ordinance is to encourage taxpayers to save for their retirement. As a result of the introduction of the amendment ordinance, new provisions were introduced to the IRO to allow taxpayers claiming tax deductions under salaries tax or personal assessment, subject to a deduction cap, on the premiums they paid for purchasing qualified deferred annuity plans and contributions they made to tax deductible mandatory provident schemes.

The proposed introduction of a specific anti-avoidance provision should in theory be more effective as compared to the general anti-avoidance provision in the IRO in counteracting abuse of tax concession on certain targeted arrangements.

The TF would also like to highlight that developments of the Base Erosion and Profit Shifting ("BEPS") 2.0 proposals by the Organization for Economic Cooperation and Development and further reform to the international taxation environment will have impacts on the proposed concessionary tax rates and other preferential tax regimes in Hong Kong. In short, the BEPS 2.0 proposals have two pillars. Pillar 1 is the revised nexus and profit allocation rules, and pillar 2 is the global anti-base erosion proposal in which it lays out additional measures for protecting tax bases.

Our concerns centre on the latter and whether the concessionary tax rate would still be meaningful if the proposed global minimum tax ("GloBE") and a tax on base-eroding payments under pillar 2 are implemented, which could come as early as 2020. Implementation of BEPS 2.0 proposals in the forms currently proposed could undermine the ability of tax systems to minimize the distortionary effects of corporate income taxes either through appropriate treatment of business investments or through low statutory rates. If the GloBE proposal is implemented then the proposed preferential concessionary tax rate may be below the GloBE rate. Should that be the case, the proposed preferential tax treatment and other preferential tax regimes in Hong Kong would likely become ineffective and will need revisiting by the government.

In all, the TF welcomes the proposals. However, with the anticipated implementation of the BEPS 2.0 initiatives, the TF considers that the government should conduct a comprehensive review of the effectiveness of all preferential tax regimes and, preferably, a holistic review of the entire Hong Kong tax system.

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Should you have any questions on this submission, please contact the undersigned at 2287-7075 or ericchiang@hkicpa.org.hk.

Yours faithfully,

Eric Chiang
Deputy Director,
Advocacy & Practice Development

EKC/pk