Statement
Statement by Representative of HKICPA at the Bills Committee on the Inland Revenue (Amendment) (No. 6) Bill 2017
(English Only)
Tuesday 13 February 2018

Good afternoon. Thank you for inviting the Hong Kong Institute of Certified Public Accountants to address the committee. While the Institute supports in principle and appreciates the efforts of the Government in codifying the transfer pricing rules in the Hong Kong tax legislation, so as to meet the relevant OECD requirements, certain aspects of the Bill go beyond what the Institute would have expected to see in this legislation.

1. Firstly, the extension of transfer pricing rules to salaries tax and property tax seems to exceed what is needed to meet the BEPS minimum requirements. This proposed extension of scope is of concern to the profession.

2. The proposed amendment to section 8(1A)(c) in relation to salaries tax, again does not relate directly to the BEPS requirements. It could lead to double taxation for certain taxpayers who hold Hong Kong employment, but are required to work substantially outside Hong Kong on a recurring basis and hence cannot meet the residency requirement under the tax treaty. Therefore, we do not support the proposed amendment.

3. Likewise, we question the amendment to section 16(1)(c). The amendment may result in some financial institutions with substantial operations in Hong Kong in the form of branches being unable to claim foreign taxes paid as deductible expenses. Hence, we do not support this proposed amendment.

4. The new transfer pricing rule 1 could bring uncertainty to the Hong Kong's territorial source principle of taxation. It authorizes the IRD to make transfer pricing adjustments on taxpayers. However, it is not clear if the IRD can impose tax on taxpayers if the adjustments are made to attribute offshore profit to incidental or antecedent activities in Hong Kong. It is worth noting that if the interface between the source principle and the transfer pricing rules is not made clear, this could cast significant uncertainty to the Hong Kong tax system. To this end, we consider that further amendments should be made to the bill to spell out more clearly that the IRD will not impose tax on the transfer pricing adjustments made in relation to offshore profits.

5. In addition, we also note that transfer pricing rule 1 will apply to both domestic and cross-border related party transactions. Likewise, where certain business size and transaction thresholds are exceeded, transfer pricing documentation requirement will apply. It is worth noting that the primary purpose of

implementing BEPS action 13 is to prevent enterprises from exploiting tax rate differentials to obtain tax benefits in cross border related party transactions. In relation to related party transactions between domestic entities, in the vast majority of cases, it is unlikely that any Hong Kong tax advantage can be gained. Therefore, we have reservations about applying the transfer pricing rule to domestic related party transactions, and we do not support the inclusion of domestic related party transactions for the transfer pricing documentation requirement, which could be onerous and yet unproductive.

6. We also note that the threshold for preparation of the "master file" and "local file" is set at the same level. In other jurisdictions, it is common for different thresholds to apply. We suggest raising the threshold for preparing a master file so as to reduce the administrative burden on all relevant parties. In addition, we suggest taxpayers be given more time for preparing the file.

7. With the introduction of transfer pricing rule 1, we question the need for the proposed new section 15F, which deals with certain activities carried out in Hong Kong in relation to intellectual property rights. We consider transfer pricing rule 1 would give the IRD sufficient power to make tax adjustments. Therefore, section 15F could create uncertainty.

Given the time constraint, I would like to stop here. More details of the Institute's views on the Bill can be found in our written submission.

Thank you!

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