9 July 2021

Inland Revenue Department (IRD)
Revenue Tower
5 Gloucester Road
Wan Chai
Hong Kong

Attention:
Ms LEUNG Wing Chi, Wings, Acting Deputy Commissioner (Technical)
Ms CHAN Shun Mei, Michelle, Acting Assistant Commissioner, Unit 1
Mr CHAN Sze Wai, Benjamin, Acting Assistant Commissioner, Unit 3
Ms WONG Ka Yee, Anissa, Chief Assessor (Profit Tax)B
Mr HONG Wai-Kuen, Raymond, Chief Assessor (Stamp Office)

ASIFMA Letter to IRD re 23 Apr 2021 Tax Meeting

Dear Ms Leung and IRD Team

The Asia Securities Industry & Financial Markets Association ("**ASIFMA**[1]") appreciates the opportunity to have a meeting to discuss a range of tax issues with IRD on 23 April 2021. Members found the discussion and insights to be very useful and we thank you and your team for your time. As a follow-up, we thought it might be useful to highlight a few areas where we would like to draw further attention to:

1. Group Loss Relief Framework

We note IRD's explanation during the meeting about its stance on group loss relief. Having said that, ASIFMA continues to be of the view that the benefits of introducing a group loss relief regime far outweigh any "costs" and we respectfully submit that the Government consider introducing this provision. This should be viewed in the existing context where under current rules, tax losses are already permitted to be carried forward indefinitely which means that "revenue loss" should ultimately be a timing issue. Further, the Government could consider introducing the relief only for prospective losses.

[1] ASIFMA is an independent, regional trade association with over 145 member firms comprising a diverse range of leading financial institutions from both the buy and sell side, including banks, asset managers, professional and consulting firms, and market infrastructure service providers. Together, we harness the shared interests of the financial industry to promote the development of liquid, deep and broad capital markets in Asia. ASIFMA advocates stable, innovative, competitive and efficient Asian capital markets that are necessary to support the region's economic growth. We drive consensus, advocate solutions and effect change around key issues through the collective strength and clarity of one industry voice. Our many initiatives include consultations with regulators and exchanges, development of uniform industry standards, advocacy for enhanced markets through policy papers, and lowering the cost of doing business in the region. Through the GFMA alliance with SIFMA in the United States and AFME in Europe, ASIFMA also provides insights on global best practices and standards to benefit the region.

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The impact of group loss relief should not negatively impact Hong Kong's position under Pillar 2. Group loss relief could result in the utilization of losses that may otherwise be trapped, which could result in lower covered taxes in Hong Kong. However, the reduced covered taxes would be matched by the ability to utilize losses under the jurisdictional blending approach adopted by Pillar 2 in any case. In other words, providing for group relief within Hong Kong would allow for the Hong Kong domestic tax position to align with the Pillar 2 position.

If Hong Kong does not provide group relief, losses would be utilized for Pillar 2 purposes, but not for domestic Hong Kong purposes, leading to a mismatch. This would inflate the effective tax rate of the Hong Kong group temporarily and could create excess taxes above the minimum rate. These excess taxes are unlikely to be carried forward indefinitely for Pillar 2 purposes except where an IIR tax credit is created. If the group then utilized the losses at a subsequent point in time its Pillar 2 effective tax rate could be below the minimum which may lead to unavoidable top-up tax (because there may be no benefit from the previous excess taxes). Accordingly, a failure to introduce group relief could negatively impact certain Hong Kong groups, albeit in limited circumstances.

Further, we understand the Government is likely to introduce its own domestic minimum tax in any case, meaning that any top-up tax would be collected by Hong Kong, rather than another jurisdiction. Accordingly, Pillar 2 related revenue collection concerns should not be relevant.

2. ASIFMA's E-Means Report: Simplified Stamp Duty Process for Stock Borrowing and Lending Transactions ("SBL"), E-Payment and E-Signature

With reference to the ASIFMA E-means Report ("Report"), it is suggested that IRD should simplify the registration process with the following suggestions:

- ***Item 21 of Report –*** Stock loan agreement registration: to simplify registration method by removing the requirement of submitting the stock borrowing agreement. The registration to be done by filing a simple registration form OR the registration requirement to be removed entirely.

- ***Item 20 of Report –*** Stock Loan Semi-annual Return (SBUL 1): to remove the requirement of filing Form SBUL 1 semi-annually where there are no failed transactions during the relevant period. In the case where there are any regulatory hurdles in removing the requirement, we would cordially request that (a) the frequency of filing be reduced, and (b) bulk upload option be available for electronic filing of Form SBUL 1 with e-signature.

In addition, we suggested IRD to enable payment of stamp duty to be made via electronic payment methods that are commonly used by our members, ie credit transfer or direct debit. IRD has suggested that we look into use of FPS. We are continuing to look into this and has had further post-meeting engagement on this.

At IRD's request at the meeting, we are also looking at arranging a demonstration of e-signature platforms for the IRD and our members.

With respect to the request to extend deadlines for stamp duty transactions, IRD mentioned that it would involve policy update and the IRD will be seeking comments from the FSTB.

3. Stamp Duty on Bearer HKD-Denominated ("HKDD") Equity Linked Notes ("ELNs") with Physical Settlement

ASIFMA requests IRD to consider the elimination of the stamp duty on bearer HKD-denominated equity linked notes that are physically settled.

Currently, bearer stamp duty liability depends on two broad parameters: (A) features of the instrument; and (B) place of incorporation of the issuer or the place of issuance as follows:

(A) Instrument is:

a. bearer in nature;
b. denominated or repayable **in HKD**; or
c. by delivery of such instrument any stock can be transferred.

(B) Such Instrument is issued:

a. in HK (by any entity regardless of the place of incorporation of the Issuer i.e., HK and non-HK both); or
b. anywhere in the world by a HK-incorporated entity.

Where these conditions above are met, a 3% issuance stamp duty is payable (on value of ELN) before the issuance of ELN.

We submit the following key points in support of the elimination of such stamp duty:

(i) There is a significant appetite for HKD-denominated ELNs as it is often the functional currency of the investors who prefer not to take FX risk if the ELNs are denominated in any other currency (e.g. GBP and USD). From a practical perspective, such bearer stamp creates a cost and pricing hurdle for issuing HKD-denominated ELNs.

(ii) The current stamp duty treatment does not create a level-playing field for HK-incorporated issuers since a foreign entity (i.e., non-HK entity) can issue such ELNs outside of HK and will not be subject to such bearer stamp duty. This hampers issuance of such ELNs by HK entities as it makes them uncompetitive on pricing given the stamp duty cost.

(iii) On physical settlement of the ELN, there is HK transfer stamp duty payable in respect of HK stock underlying the ELN – this continues as usual. Bearer stamp therefore is an additional significant cost for such ELNs.

(iv) It is believed that such HKD-denominated bearer ELNs are not often issued by HK entities (given the economic cost of 3%) and therefore the elimination of such 3% bearer stamp should not result in any material revenue loss to the HK Government.

(v) Since the enactment of the stamp law in 1981, there has been no review of bearer stamp duty. Given the development in financial market and products since then, bearer stamp duty on HKD ELNs appears as a fit candidate for elimination of stamp duty.

From an operational perspective, ELNs are issued in bearer form by various recognized clearing systems such as Euroclear, Clearstream, etc. for settlement and clearing purposes. Anti-money laundering and know your customer infrastructure with respect to the investors holding the ELNs are well established.

The Government is focused on developing HK as a private wealth management center and promoting the use of HK product. If a non-HK issuer can issue the same product outside of HK without the stamp duty cost while a HK issuer issuing in HK would attract additional cost, that seems to go against the concept of active promotion of more HK product to promote/support Hong Kong's wealth management industry.

4. Potential Tax Treaty Partners for HK

Following the discussion with IRD during the meeting regarding the potential tax treaty partners, ASIFMA understands that IRD will check with FSTB on the progress of tax treaty negotiations with African nations and if any have been stalled to let us know so that we may mobilize some of our members to provide assistance on the ground. Please kindly let us know.

ASIFMA would welcome an opportunity to discuss this with IRD further, or to receive any feedback on the matters set out above. If you have any follow up comments or questions, please feel free to contact Patrick Pang at ppang@asifma.org or +852-25316520.

Yours sincerely,

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