

# Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Bill 2022

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# A BILL

## To

Amend the Inland Revenue Ordinance to provide that certain foreign-sourced income is to be regarded as arising in or derived from Hong Kong; to provide for relief against double taxation in respect of certain foreign-sourced income; and to provide for related and transitional matters.

Enacted by the Legislative Council.

**1. Short title and commencement**

- (1) This Ordinance may be cited as the Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Ordinance 2022.
- (2) This Ordinance comes into operation on 1 January 2023.

**2. Inland Revenue Ordinance amended**

The Inland Revenue Ordinance (Cap. 112) is amended as set out in sections 3 to 17.

**3. Part 4, Division 3A added**

Part 4, after Division 3—

**Add**

## “Division 3A—Specified Foreign-sourced Income

### Subdivision 1—Preliminary

#### 15H. Interpretation of Division 3A of Part 4

(1) In this Division—

*consolidated financial statements* (綜合財務報表) means—

- (a) subject to paragraphs (b) and (c), the financial statements prepared by an entity under applicable accounting principles, in which the assets, liabilities, income, expenses and cash flows of the entity and the entities in which it has a controlling interest are presented as those of a single economic unit;
- (b) in relation to a stand-alone MNE entity—the financial statements of the entity prepared under applicable accounting principles; or
- (c) in relation to an ultimate parent entity that does not prepare any financial statements described in paragraph (a) or (b)—the financial statements that would have been prepared if the entity had been required to prepare financial statements under applicable accounting principles;

*controlling interest* (控制權益), in relation to an entity, means an equity interest in the entity such that—

- (a) the interest holder is required to consolidate the assets, liabilities, income, expenses and cash flows of the entity on a line-by-line basis under applicable accounting principles; or

- (b) the interest holder would have been required to consolidate the assets, liabilities, income, expenses and cash flows of the entity on a line-by-line basis under applicable accounting principles if the interest holder had prepared consolidated financial statements;

**disposal gain** (處置收益) means any gain or profit derived from the sale of equity interests (other than partnership interests) in an entity;

**entity** (實體) means—

- (a) a legal person (other than a natural person); or
- (b) an arrangement that prepares separate financial accounts, such as a partnership and a trust;

**equity interest** (股權權益), in relation to an entity, means an interest that carries rights to the profits, capital or reserves of the entity and is accounted for as equity under applicable accounting principles;

**excluded entity** (豁除實體)—see section 15I;

**group** (集團) means—

- (a) a collection of entities that are related through ownership or control such that the assets, liabilities, income, expenses and cash flows of those entities—
  - (i) are required under applicable accounting principles to be included in the consolidated financial statements of the ultimate parent entity of the collection; or
  - (ii) are excluded from the consolidated financial statements of the ultimate parent entity solely on size or materiality grounds

or on the grounds that the entities are held for sale; or

(b) a stand-alone MNE entity;

***Hong Kong resident person*** (香港居民人士) has the meaning given by section 50AAC(1);

***intellectual property*** (知識產權) includes—

(a) cinematograph film, film or tape used for radio or television broadcasting, sound recording, and advertising material connected with such film, tape or recording; and

(b) patent, design, model, plan, trade mark, copyright material, layout-design (topography) of an integrated circuit, performer's right, plant variety right, secret process or formula, know-how, information concerning industrial, commercial or scientific experience, and other property or right of a similar nature;

***IP income*** (知識產權收入) means income derived from intellectual property in respect of—

(a) the exhibition or use of, or a right to exhibit or use, (whether in or outside Hong Kong) the property; or

(b) the imparting of, or undertaking to impart, knowledge directly or indirectly connected with the use (whether in or outside Hong Kong) of the property;

***MNE entity*** (跨國企業實體), subject to subsection (4), means a person that—

(a) is, or acts for, an MNE group or an entity included in an MNE group; and

(b) is not an excluded entity;



***MNE group*** (跨國企業集團) means a group that includes at least one entity or permanent establishment that is not located or established in the jurisdiction of the ultimate parent entity of the group;

***partnership interest*** (合夥權益) means an equity interest in a partnership that is not a legal person;

***permanent establishment*** (常設機構)—see subsection (3);

***regulated financial entity*** (受規管財務實體) means—

- (a) an insurer (as defined by section 2(1) of the Insurance Ordinance (Cap. 41)) authorized under that Ordinance, Lloyd’s or an approved association of underwriters;
- (b) an authorized institution as defined by section 2(1) of the Banking Ordinance (Cap. 155); or
- (c) an entity licensed under Part V of the Securities and Futures Ordinance (Cap. 571) to carry on a business in any regulated activity as defined by Part 1 of Schedule 5 to that Ordinance;

***sale*** (出售), in relation to equity interests, means a transfer of the interests (other than a transfer effected by extinguishing the interests) for valuable consideration;

***specified foreign-sourced income*** (指明外地收入) means any interest, dividend, disposal gain or IP income arising in or derived from a territory outside Hong Kong, but does not include any interest, dividend or disposal gain derived by a regulated financial entity from the carrying on of a business as such a regulated financial entity;

***stand-alone MNE entity*** (獨立跨國企業實體) means an entity that—

- (a) is located in one jurisdiction and has one or more permanent establishments in other jurisdictions; and
- (b) is not part of a collection of entities described in paragraph (a) of the definition of ***group***;

***ultimate parent entity*** (最終母實體) means—

- (a) an entity that—
    - (i) owns directly or indirectly a controlling interest in any other entity; and
    - (ii) is not owned, with a controlling interest, directly or indirectly by another entity; or
  - (b) a stand-alone MNE entity.
- (2) For the purposes of this Division—
- (a) if an entity is a tax resident in a jurisdiction based on its place of management, place of creation or similar criteria—the entity is to be regarded as located in that jurisdiction; or
  - (b) in any other case—the entity is to be regarded as located in the jurisdiction in which it was created.
- (3) For the purposes of this Division, an entity has a permanent establishment in a jurisdiction if—
- (a) where the jurisdiction is Hong Kong—the entity has a permanent establishment in Hong Kong under Schedule 17G; or
  - (b) where the jurisdiction is not Hong Kong—the entity is to be regarded as having a permanent establishment in the jurisdiction under the laws

of the jurisdiction or under a bilateral or multilateral tax convention to which the jurisdiction is a party,

and a reference to a permanent establishment in a jurisdiction is to be read accordingly.

- (4) For the purposes of this Division, if an MNE entity is a Hong Kong resident person, any permanent establishment of the entity outside Hong Kong is to be regarded as a separate MNE entity carrying on a trade, profession or business in the territory in which the permanent establishment is established.
- (5) For the purposes of this Division, without limiting the meaning of “received in Hong Kong”, a sum is to be regarded as received in Hong Kong if—
  - (a) the sum is remitted to, or is transmitted or brought into, Hong Kong;
  - (b) the sum is used to satisfy any debt incurred in respect of a trade, profession or business carried on in Hong Kong; or
  - (c) the sum is used to buy movable property, and the property is brought into Hong Kong.
- (6) For the purposes of subsection (5)(c), the sum is to be regarded as being received at the time when the movable property is brought into Hong Kong.
- (7) Subsection (5) applies regardless of whether or not the source from which the sum is derived has ceased.

**15I. Meaning of *excluded entity***

- (1) Each of the following is an excluded entity—
  - (a) a governmental entity;
  - (b) an international organization;

- (c) a non-profit organization;
  - (d) a pension fund;
  - (e) an investment fund that is an ultimate parent entity;
  - (f) a real estate investment vehicle that is an ultimate parent entity;
  - (g) an insurance investment entity;
  - (h) an entity the assessable profits of which are chargeable to tax at the rate specified in a concession provision (as defined by section 19CA) other than section 14A(1);
  - (i) an entity that has any exempt sums (as defined by section 23B(12)) excluded under section 23B(4AA) from the amount of relevant sums (as defined by section 23B(12)) earned by or accrued to the entity.
- (2) In this section—
- governmental entity** (政府實體) means an entity in relation to which all of the following criteria are met—
- (a) the entity is part of, or is wholly owned by—
    - (i) a government; or
    - (ii) any political subdivision or local authority of a government;
  - (b) the entity has the principal purpose of—
    - (i) fulfilling a government function; or
    - (ii) managing or investing the specified assets through the making and holding of investments, asset management and investment activities related to the specified assets;

- (c) the entity does not carry on a trade or business, other than an investment business described in paragraph (b)(ii);
- (d) the entity is accountable to the government on its overall performance;
- (e) the entity provides annual information reporting to the government;
- (f) the entity's assets vest in the government on dissolution;
- (g) to the extent the entity distributes net earnings, the earnings are distributed solely to the government with no portion of the earnings inuring to the benefit of any private person;

***insurance investment entity*** (保險投資實體) means an entity in relation to which all of the following criteria are met—

- (a) the entity—
  - (i) is not an investment fund, but would be an investment fund if it were designed to pool assets (whether financial or non-financial) from a number of investors, at least some of which were not connected (within the meaning of subsection (3)); or
  - (ii) is not a real estate investment vehicle, but would be a real estate investment vehicle if it held predominantly immovable property and were itself widely held;
- (b) the entity is established in relation to liabilities under an insurance or annuity contract;

- (c) the entity is wholly owned by an entity (*latter*) that is subject to regulation in the latter's location as an insurance company;

***international organization*** (國際組織) means any intergovernmental organization (including a supranational organization), or its wholly owned agency or instrumentality, in relation to which all of the following criteria are met—

- (a) the organization, agency or instrumentality (*subject entity*) is comprised primarily of governments;
- (b) the subject entity has, with the jurisdiction in which it is established, in effect—
  - (i) a headquarters agreement;
  - (ii) arrangements that entitle its offices or establishments in the jurisdiction (including a subdivision, a local office or a regional office) to privileges and immunities; or
  - (iii) any other agreement substantially similar to a headquarters agreement;
- (c) the subject entity's income is prevented, by law or by its governing documents, from inuring to the benefit of any private person;

***investment fund*** (投資基金) means any of the following entities—

- (a) an entity that is exempt from tax under section 20AC, 20ACA, 20AN or 20AO;
- (b) an entity that is a mutual fund, unit trust or similar investment scheme that—

- (i) is authorized as a collective investment scheme under section 104 of the Securities and Futures Ordinance (Cap. 571); or
  - (ii) is, in the Commissioner's opinion, a bona fide widely held investment scheme that complies with the requirements of a supervisory authority within an acceptable regulatory regime;
- (c) an entity in relation to which all of the following criteria are met—
- (i) the entity is designed to pool assets (whether financial or non-financial) from a number of investors, at least some of which are not connected (within the meaning of subsection (3));
  - (ii) subject to subsection (4), the entity invests in accordance with a defined investment policy;
  - (iii) the entity allows investors—
    - (A) to reduce transaction, research and analytical costs; or
    - (B) to spread risk collectively;
  - (iv) the entity is solely designed to generate—
    - (A) investment income or gains; or
    - (B) protection against a particular or general event or outcome;
  - (v) the investors of the entity have, based on the contributions they make, a right to return from its assets or income earned on those assets;

- (vi) the entity or its management is subject to a regulatory regime in the jurisdiction in which it is established or managed (including appropriate anti-money laundering and investor protection regulations);
- (vii) the entity is managed by investment fund management professionals on behalf of its investors;

***non-profit entity*** (非牟利實體) means—

- (a) a professional organization;
- (b) a business league;
- (c) a chamber of commerce;
- (d) a labour organization;
- (e) an agricultural or horticultural organization;
- (f) a civic league; or
- (g) an organization operated exclusively for the promotion of social welfare;

***non-profit organization*** (非牟利組織) means an entity in relation to which all of the following criteria are met—

- (a) the entity is established and operated in its jurisdiction of residence—
  - (i) exclusively for a non-profit purpose; or
  - (ii) as a non-profit entity;
- (b) substantially all of the entity's income from the following activities is exempt from income tax in its jurisdiction of residence—



- (i) if the entity is established and operated in its jurisdiction of residence exclusively for a non-profit purpose—activities carried out for that non-profit purpose; or
  - (ii) if the entity is established and operated in its jurisdiction of residence as a non-profit entity—activities carried out as such a non-profit entity;
- (c) the entity has no shareholders or members who have a proprietary or beneficial interest in its income or assets;
- (d) the entity's income or assets may not be distributed to, or applied for the benefit of, a private person or non-charitable entity other than—
  - (i) pursuant to the conduct of its charitable activities;
  - (ii) as payment of reasonable compensation for services rendered or for the use of property or capital; or
  - (iii) as payment representing the fair market value of property that it has purchased;
- (e) on termination, liquidation or dissolution of the entity, all of the entity's assets are to be distributed, or revert, to—
  - (i) a non-profit organization; or
  - (ii) the government of its jurisdiction of residence (including any political subdivision of the government and any governmental entity),

but does not include any entity carrying on a trade or business that is not directly related to the purposes for which it was established;

***non-profit purpose*** (非牟利目的) means—

- (a) a religious, charitable, scientific, artistic, cultural, athletic or educational purpose; or
- (b) any other similar purpose;

***pension fund*** (退休基金) means—

- (a) a pension fund entity; or
- (b) a pension services entity;

***pension fund entity*** (退休基金實體) means an entity in relation to which both of the following criteria are met—

- (a) the entity is an entity established and operated in a jurisdiction exclusively or almost exclusively to administer, or provide to individuals, retirement benefits and ancillary or incidental benefits;
- (b) either—
  - (i) the entity is regulated as such an entity by that jurisdiction or one of its political subdivisions or local authorities; or
  - (ii) those benefits—
    - (A) are secured or otherwise protected by that jurisdiction's regulations; and
    - (B) are funded by a pool of assets held through a fiduciary arrangement or trust to secure the fulfilment of the corresponding pension obligations against a case of insolvency of the

group of which the entity is a member;

***pension services entity*** (退休金服務實體) means an entity (***former***) that is established and operated exclusively or almost exclusively—

- (a) to invest funds for the benefit of a pension fund entity; or
- (b) to carry out activities that are ancillary to the regulated activities carried out by a pension fund entity that is a member of the group of which the former is a member;

***real estate investment vehicle*** (房地產投資工具) means—

- (a) a collective investment scheme in relation to which all of the following criteria are met—
  - (i) the scheme does not engage in active trading of real estate;
  - (ii) the scheme invests predominantly in real estate for generating recurrent rental income;
  - (iii) the majority of income of the scheme derives from rentals of real estate;
  - (iv) the scheme distributes a significant portion of its income to holders in the form of regular dividends or other distributions (however described); or
- (b) an entity—
  - (i) that holds predominantly immovable property and is itself widely held; and
  - (ii) the taxation in relation to which achieves a single level of taxation either in its hands

or in the hands of its interest holders (with at most one year of deferral);

**specified assets** (指明資產), in relation to a governmental entity, means—

- (a) the assets of the government, political subdivision or local authority—
    - (i) of which the entity is part; or
    - (ii) by which the entity is wholly owned; or
  - (b) the assets of the jurisdiction to which the government, political subdivision or local authority relates.
- (3) For the purposes of paragraph (a)(i) of the definition of **insurance investment entity** and paragraph (c)(i) of the definition of **investment fund** in subsection (2), 2 investors are connected if—
- (a) they are closely related (within the meaning of section 2 of Schedule 17G); or
  - (b) they are relatives (within the meaning of section 20AN(6)).
- (4) For the purposes of paragraph (c)(ii) of the definition of **investment fund** in subsection (2), the following factors are relevant in determining whether an investment policy is a defined one—
- (a) whether the investment policy is determined and fixed, at the latest by the time that investors' commitments to the fund concerned become binding on them;
  - (b) whether the investment policy is set out in a document that becomes part of, or is referenced in, the rules, or instruments of incorporation, of the fund;

- (c) whether the fund or legal person managing the fund has an obligation (however arising) to investors, which is legally enforceable by them, to follow the investment policy, including all changes to it;
- (d) whether the investment policy specifies any investment guidelines, such as requiring the fund—
  - (i) to invest in certain categories of assets or conform to certain restrictions on asset allocation;
  - (ii) to pursue certain strategies;
  - (iii) to invest in particular geographical regions;
  - (iv) to conform to restrictions on leverage;
  - (v) to conform to minimum holding periods;  
or
  - (vi) to conform to other restrictions designed to provide risk diversification.

### **Subdivision 2—Treatment of Specified Foreign-sourced Income for Charging Profits Tax**

#### **15J. Specified foreign-sourced income regarded as arising in or derived from Hong Kong**

- (1) For charging profits tax, specified foreign-sourced income to which this subsection applies—
  - (a) is to be regarded as a receipt arising in or derived from Hong Kong for the basis period of the year of assessment during which the income is received in Hong Kong; and

- (b) is to be regarded as not arising from the sale of capital assets even if it so arises.
- (2) Subsection (1) is subject to Subdivision 3.
- (3) Subsection (1) applies to specified foreign-sourced income that—
  - (a) is received in Hong Kong by an MNE entity carrying on a trade, profession or business in Hong Kong; and
  - (b) is not otherwise chargeable to profits tax under this Part.
- (4) Despite subsection (3), if a sum is both—
  - (a) a sum to which section 15 or 15F applies; and
  - (b) but for this subsection, income to which subsection (1) would have applied,subsection (1) does not apply to the sum.
- (5) To avoid doubt, if—
  - (a) any specified foreign-sourced income is received in Hong Kong by an MNE entity after the entity ceases to carry on a trade, profession or business in Hong Kong; and
  - (b) had the income been received before the cessation, it would have been chargeable to profits tax because of subsection (1),section 15D applies in relation to the income.

### **15K. Notification**

If an MNE entity is chargeable to profits tax in respect of any specified foreign-sourced income under this Part because of section 15J(1), the entity must notify the Commissioner in writing that the entity is so chargeable

within 4 months after the end of the basis period of the year of assessment during which the income is received in Hong Kong, unless the entity has already been required to furnish a return under section 51(1).

### **Subdivision 3—Exceptions from Section 15J(1)**

#### **15L. Exception 1: interest, dividend or disposal gain subject to economic substance requirement being met**

- (1) Section 15J(1) does not operate in relation to specified foreign-sourced income received in Hong Kong by an MNE entity if—
  - (a) the income is interest, a dividend or a disposal gain; and
  - (b) the economic substance requirement specified in subsection (2) is met.
- (2) The economic substance requirement is that during the basis period of the year of assessment in which the income accrues to the MNE entity—
  - (a) if the entity is a pure equity-holding entity—
    - (i) the entity complies with every applicable registration and filing requirement under the following Ordinances—
      - (A) the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32);
      - (B) the Limited Partnerships Ordinance (Cap. 37);
      - (C) the Business Registration Ordinance (Cap. 310);
      - (D) the Companies Ordinance (Cap. 622);

- (ii) specified economic activities are—
    - (A) carried out in Hong Kong by the entity; or
    - (B) arranged by the entity to be carried out in Hong Kong; and
  - (iii) in the Commissioner’s opinion, the entity has adequate human resources and premises for carrying out the specified economic activities; or
- (b) if the entity is not a pure equity-holding entity—
- (i) specified economic activities are—
    - (A) carried out in Hong Kong by the entity; or
    - (B) arranged by the entity to be carried out in Hong Kong;
  - (ii) the number of employees in Hong Kong who—
    - (A) carry out the specified economic activities; and
    - (B) have the qualifications necessary for doing so,is adequate in the Commissioner’s opinion; and
  - (iii) the total amount of operating expenditure incurred in Hong Kong for carrying out the specified economic activities is adequate in the Commissioner’s opinion.



(3) In this section—

*pure equity-holding entity* (純股權持有實體) means an entity that—

- (a) only holds equity interests in other entities; and
- (b) only earns—
  - (i) dividends;
  - (ii) disposal gains; and
  - (iii) income incidental to the acquisition, holding or sale of such equity interests;

*specified economic activities* (指明經濟活動) means—

- (a) in relation to an MNE entity that is a pure equity-holding entity—holding and managing its equity participations in other entities; or
- (b) in relation to an MNE entity that is not a pure equity-holding entity—
  - (i) making necessary strategic decisions in respect of any assets the entity acquires, holds or disposes of; and
  - (ii) managing and bearing principal risks in respect of such assets.

**15M. Exception 2: excepted portion of qualifying IP income ascertained in accordance with nexus requirement**

- (1) If any specified foreign-sourced income received in Hong Kong by an MNE entity is qualifying IP income, section 15J(1) does not operate in relation to the excepted portion of the income ascertained under Part 2 of Schedule 17FC.
- (2) Part 3 of Schedule 17FC applies in relation to the qualifying IP income.

- (3) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend Schedule 17FC.
- (4) In this section—  
*excepted portion* (例外部分)—see section 3 of Schedule 17FC;  
*qualifying IP income* (合資格知識產權收入) has the meaning given by section 1(2) of Schedule 17FC.

**15N. Exception 3: dividend or disposal gain subject to participation requirement being met**

- (1) Subject to section 15O, section 15J(1) does not operate in relation to specified foreign-sourced income received in Hong Kong by an MNE entity if—
  - (a) the entity is—
    - (i) a Hong Kong resident person; or
    - (ii) a non-Hong Kong resident person who has a permanent establishment in Hong Kong;
  - (b) the income is—
    - (i) if the entity is a Hong Kong resident person—a dividend or disposal gain; or
    - (ii) if the entity is a non-Hong Kong resident person—a dividend or disposal gain attributable to the entity's permanent establishment in Hong Kong under section 50AAK; and
  - (c) the participation requirement specified in subsection (2) is met.

(2) The participation requirement is that the MNE entity has continuously held not less than 5% of equity interests in the investee entity for a period of not less than 12 months immediately before the specified foreign-sourced income accrues to the MNE entity.

(3) In this section—

*investee entity* (獲投資實體) means—

- (a) in relation to an MNE entity that receives a dividend—the entity that distributes the dividend; or
- (b) in relation to an MNE entity that receives a disposal gain—the entity the equity interests in which are sold;

*non-Hong Kong resident person* (非香港居民人士) has the meaning given by section 50AAC(1).

### **150. When does section 15N not apply**

(1) This section applies to specified foreign-sourced income in relation to which section 15J(1), but for this section, would not have operated because of section 15N.

(2) Section 15N only applies if the Commissioner is satisfied that—

- (a) where the specified foreign-sourced income is a dividend (whether or not the underlying profits of the income consist of any dividend)—
  - (i) the income is subject to a qualifying similar tax in a territory outside Hong Kong; or

- (ii) the underlying profits of the income are subject to a qualifying similar tax in a territory outside Hong Kong, and the amount of the profits is equal to or larger than that of the income;
  - (b) where the specified foreign-sourced income (*subject income*) is a dividend, and the underlying profits of the subject income consist wholly or partly of dividends—
    - (i) one or more items of the related downstream income of the profits are subject to a qualifying similar tax in a territory outside Hong Kong; and
    - (ii) the aggregate amount of all such items of income is equal to or larger than the amount of the subject income; or
  - (c) where the specified foreign-sourced income is a disposal gain—the income is subject to a qualifying similar tax in a territory outside Hong Kong.
- (3) Where—
  - (a) the specified foreign-sourced income is a dividend; and
  - (b) tax is charged on the underlying profits of the income in a territory outside Hong Kong,section 15N does not apply if, and to the extent that, the income is allowable for deduction when computing the amount of the tax.

- (4) Section 15N also does not apply if—
  - (a) the MNE entity receiving the specified foreign-sourced income entered into an arrangement in respect of the income; and
  - (b) the Commissioner is satisfied that the main purpose, or one of the main purposes, of the entity in entering into the arrangement was to obtain a tax benefit, whether for the entity or another person, under that section for the income.
- (5) To avoid doubt and without limiting sections 50, 50AAA and 50AAAB (*those sections*), if section 15N does not apply because of this section, any similar tax payable in the source territory—
  - (a) in respect of the specified foreign-sourced income; and
  - (b) if the income is a dividend—in respect of the underlying profits and in respect of any related downstream income of the profits,may, in accordance with those sections, be allowed as a credit against any tax payable in respect of the specified foreign-sourced income in Hong Kong.
- (6) For the purposes of subsection (2), a sum is subject to a qualifying similar tax in a territory outside Hong Kong if—
  - (a) the sum is subject to a similar tax in that territory; and
  - (b) the applicable rate, or (if there is more than one applicable rate) the highest applicable rate, of that tax is equal to or higher than the reference rate.

- (7) For the purposes of subsection (6)(b), the reference rate is 15%.
- (8) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend the reference rate in subsection (7).
- (9) In this section—

***applicable rate*** (適用稅率), in relation to a similar tax to which a sum is subject, means—

- (a) if the tax is chargeable at the time the sum accrues—the rate of the tax applicable to the sum at that time; or
- (b) if the tax is chargeable for the taxable period during which the sum accrues—the rate of the tax applicable to the sum for that taxable period;

***direct investee entity*** (直接獲投資實體)—see section 15P(1);

***indirect investee entity*** (間接獲投資實體)—see section 15P(2);

***investee entity*** (獲投資實體), in relation to an entity, means a direct investee entity, or an indirect investee entity, of the entity;

***qualifying similar tax*** (合資格類似稅項)—see subsection (6);

***related downstream income*** (有關下游收入), in relation to a subject investee entity's underlying profits that consist wholly or partly of dividends (***underlying dividends***), means—

- (a) the underlying dividends;
- (b) if the underlying dividends—

- (i) are paid out of the profits of a direct investee entity of the subject investee entity; or
  - (ii) are derived from the profits of an indirect investee entity of the subject investee entity through another investee entity of the subject investee entity,  
those profits (*downstream profits*); or
  - (c) if the downstream profits consist wholly or partly of dividends—those dividends;
- similar tax** (類似稅項) has the meaning given by section 16(2I)(b);
- source territory** (來源地區) means—
- (a) in relation to specified foreign-sourced income—the territory in which the income accrues;
  - (b) in relation to underlying profits—the territory in which the profits accrue; or
  - (c) in relation to related downstream income—the territory in which the income accrues;
- subject investee entity** (標的獲投資實體), in relation to an MNE entity that receives a dividend, means the entity that distributes the dividend;
- tax benefit** (稅務利益) means an avoidance, postponement or reduction of a liability to pay tax;
- underlying profits** (基礎利潤), in relation to a dividend distributed by a subject investee entity, means the profits of the entity out of which the dividend is paid.

**15P. Supplementary provision to section 15O: meaning of *direct investee entity* and *indirect investee entity***

- (1) An entity (***entity B***) is a direct investee entity of another entity (***entity A***) if—
  - (a) entity A has any direct beneficial interest in, or in relation to, entity B; or
  - (b) entity A is directly entitled to exercise, or control the exercise of, any voting rights in, or in relation to, entity B.
- (2) An entity (***entity C***) is an indirect investee entity of entity A if—
  - (a) entity A has any indirect beneficial interest in, or in relation to, entity C through another entity or a series of 2 or 3 entities; or
  - (b) entity A is indirectly entitled to exercise, or control the exercise of, any voting rights in, or in relation to, entity C through another entity or a series of 2 or 3 entities.
- (3) To avoid doubt, an entity (***entity D***) is not an indirect investee entity of entity A if none of the conditions in subsection (2) is satisfied in relation to them, even when—
  - (a) entity A has any indirect beneficial interest in, or in relation to, entity D through a series of 4 or more entities; or
  - (b) entity A is indirectly entitled to exercise, or control the exercise of, any voting rights in, or in relation to, entity D through a series of 4 or more entities.
- (4) In applying subsection (1)(b), (2)(b) or (3)(b), the voting rights attributed to entity A include all the



voting rights of persons other than entity A so far as they are required, or may be required, to be exercised in one or more of the following ways—

- (a) on behalf of entity A;
  - (b) under the direction of entity A;
  - (c) for the benefit of entity A.
- (5) For the purposes of this section, if—
- (a) a reference is made to the exercise of the voting rights in an entity; and
  - (b) the entity is a corporation,  
the reference is to be read as a reference to the exercise of the voting rights at general meetings of the entity.

#### **Subdivision 4—Supplementary Provisions**

##### **15Q. Setting off loss sustained from sale of equity interests outside Hong Kong**

- (1) This section applies if—
- (a) an MNE entity sustains a loss from a sale in a territory outside Hong Kong of its equity interests (other than partnership interests) in another entity;
  - (b) the proceeds of the sale are received in Hong Kong by the MNE entity during the basis period of a year of assessment; and
  - (c) had a gain been derived from the sale and received in Hong Kong by the MNE entity, the gain would have been chargeable to profits tax because of section 15J(1).

- (2) Subject to subsection (3)—
  - (a) the loss may be set off against the MNE entity's assessable profits for that year of assessment; and
  - (b) any amount of the loss not so set off may be carried forward and set off, in accordance with section 19C, against the MNE entity's assessable profits for subsequent years of assessment.
- (3) The loss may only be set off to the extent that the assessable profits concerned are derived from specified foreign-sourced income that is chargeable to profits tax because of section 15J(1).

**15R. Outgoing or expense incurred in production of specified foreign-sourced income may be deducted**

Without limiting Division 4, if—

- (a) an outgoing or expense (however called) is incurred in the production of specified foreign-sourced income; and
- (b) the income is chargeable to profits tax for a year of assessment (*that year of assessment*) because of section 15J(1),

that outgoing or expense may be deducted in accordance with Division 4, to the extent that it has not been deducted for any year of assessment, for that year of assessment as if it were incurred during the basis period of that year of assessment.

**15S. Balancing charge or allowance relating to production of specified foreign-sourced income may be taken into account**

Without limiting sections 18F and 19E and Part 6, if—

- (a) any balancing charge directed to be made on, or any allowance made to, an MNE entity under Part 6 for a year of assessment (or any part of such a charge or allowance) is not taken into account under section 18F or 19E when calculating the amount of the entity's assessable profits or loss for that year of assessment because—
  - (i) that charge or allowance, or that part of the charge or allowance, relates to the production of specified foreign-sourced income; and
  - (ii) the income—
    - (A) is not received in Hong Kong during the basis period of that year of assessment; and
    - (B) is not chargeable to profits tax for that year of assessment; and
- (b) the income—
  - (i) is received in Hong Kong during the basis period of a subsequent year of assessment; and
  - (ii) is chargeable to profits tax for that subsequent year of assessment because of section 15J(1),

that charge or allowance, or that part of the charge or allowance, is to be taken into account under section 18F or 19E (as the case requires) when calculating the amount of the entity's assessable profits or loss for that subsequent year of assessment as if that charge or allowance, or that part of the charge or allowance, were directed to be made

on, or made to, the entity under Part 6 for that subsequent year of assessment.

**15T. Records to be kept**

- (1) Section 51C applies, with the modifications specified in subsection (2), to an MNE entity that receives in Hong Kong specified foreign-sourced income to which section 15J(1) applies.
- (2) The MNE entity must retain records of transactions, acts or operations relating to the specified foreign-sourced income under section 51C at least until the later of the following—
  - (a) the expiry of 7 years after the completion of those transactions, acts or operations; or
  - (b) the expiry of 7 years after the income is received, or to be regarded as received, in Hong Kong.
- (3) Section 80 applies to a failure to comply with section 51C as modified by subsection (2) in the same way section 80 applies to a failure to comply with section 51C.”.

**4. Section 16 amended (ascertainment of chargeable profits)**

Section 16(2J)—

**Repeal**

everything after “in a”

**Substitute**

“territory outside Hong Kong by a person in respect of the profits referred to in that subsection if, under section 50, the tax is to be allowed as a credit against tax payable in Hong Kong by the person in respect of the profits.”.

**5. Section 50 amended (tax credits)**

- (1) Section 50, heading, after “**credits**”—

**Add**

“**under double taxation arrangements**”.

- (2) Section 50(7)—

**Repeal**

“Where—”

**Substitute**

“Subject to subsections (7A) and (7B), where—”.

- (3) After section 50(7)—

**Add**

“(7A) Subsection (7B) applies if the arrangements provide that where—

- (a) the income concerned is a dividend received by a Hong Kong resident person (*subject person*) from a company that is a DTA territory resident person (*investee company*); and
- (b) the dividend is paid out of the investee company’s profits,

the tax payable in respect of the profits in the DTA territory concerned (*underlying tax*) is, subject to the satisfaction of any conditions or provisions stated in the arrangements, to be taken into account in determining the amount of credit and (if any) deduction to be allowed to the subject person in respect of the dividend.

(7B) In determining the amount of credit and (if any) deduction to be allowed to the subject person in respect of the dividend, the underlying tax is to be taken into account in accordance with the arrangements.”.

**6. Sections 50AAA, 50AAAB and 50AAAC added**

After section 50—

**Add**

**“50AAA. Unilateral tax credits—no double taxation arrangements or specified DT arrangements made**

- (1) This section applies if—
  - (a) no double taxation arrangements have been made with the government of a territory outside Hong Kong (*subject territory*); or
  - (b) double taxation arrangements have been made with the government of the subject territory, but the arrangements do not incorporate any of the following articles and rules—
    - (i) the exemption article;
    - (ii) the credit article;
    - (iii) any rules in the same or equivalent terms as those articles.
- (2) Section 50 applies in relation to any similar tax payable in the subject territory in respect of income specified in Part 2 of Schedule 54 (*specified income*) if the condition specified in that Part for the income is satisfied.

- (3) For the purposes of subsection (2), section 50 is to apply, with the modifications specified in Part 2 of Schedule 54 (if any) for applying that section in relation to the similar tax, as if—
  - (a) where no double taxation arrangements have been made with the government of the subject territory—
    - (i) double taxation arrangements containing the provisions specified in Part 2 of Schedule 54 for the similar tax (*specified provisions*) were made with the government of the subject territory; and
    - (ii) the subject territory were a DTA territory; and
  - (b) where double taxation arrangements have been made with the government of the subject territory, but the arrangements do not incorporate any of the articles and rules mentioned in subsection (1)(b)—further double taxation arrangements containing the specified provisions were made with the government of the subject territory.
- (4) The transitional arrangement specified in Part 2 of Schedule 54 for the specification of the specified income has effect.
- (5) Section 50AAAB applies in relation to any profits tax payable in Hong Kong in respect of any specified income that is a dividend as if—
  - (a) specified DT arrangements (as defined by subsection (10) of that section) containing the specified provisions were made with the government of the subject territory; and

- (b) where the subject territory is not already a DTA territory—the territory were a DTA territory.
- (6) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend—
  - (a) the definitions of the following expressions in subsection (7)—
    - (i) *Convention* (《協定》);
    - (ii) *credit article* (抵免條文);
    - (iii) *exemption article* (豁免條文); and
  - (b) Schedule 54.

(7) In this section—

*Convention* (《協定》) means the Model Tax Convention on Income and on Capital as approved by the Organisation for Economic Co-operation and Development on 21 November 2017;

*credit article* (抵免條文) means the rules contained in Article 23B of the Convention;

*exemption article* (豁免條文) means the rules contained in Article 23A of the Convention;

*similar tax* (類似稅項), in relation to specified income, means a tax that is of substantially the same nature as the tax specified in Part 2 of Schedule 54 for the income.

**50AAAB. Unilateral tax credits—no relief for underlying profits etc. under specified DT arrangements made**

(1) This section applies if—



- (a) a Hong Kong resident person (*subject person*) receives a dividend (*subject dividend*) from a company that is a DTA territory resident person (*subject company*);
  - (b) the subject dividend is paid out of the subject company's profits (*underlying profits*);
  - (c) when the subject dividend is distributed, the subject person has an adequate interest in the subject company; and
  - (d) specified DT arrangements are made with the government of the DTA territory concerned.
- (2) Subsection (3) applies if, under the specified DT arrangements, no provision is made for a similar tax payable in the DTA territory in respect of the underlying profits (*first-tier UP tax*) to be allowed as a credit against profits tax payable in Hong Kong.
- (3) Subject to subsection (9), the first-tier UP tax is to be allowed under section 50(7B) as a credit against profits tax payable in Hong Kong by the subject person in respect of the subject dividend as if—
- (a) the specified DT arrangements contained a provision to that effect; and
  - (b) in section 50(7B)—
    - (i) the reference to “dividend” were a reference to the subject dividend;
    - (ii) the reference to “underlying tax” were a reference to the first-tier UP tax; and
    - (iii) the reference to “arrangements” were a reference to the specified DT arrangements.

- (4) Subsection (5) applies if—
  - (a) the underlying profits consist wholly or partly of dividends (*underlying dividends*);
  - (b) a similar tax (*first-tier D tax*) is payable in a territory outside Hong Kong in respect of the underlying dividends;
  - (c) when the underlying dividends are distributed, the subject person has an adequate interest in the subject company; and
  - (d) under the specified DT arrangements, no provision is made for the first-tier D tax to be allowed as a credit against profits tax payable in Hong Kong.
- (5) Subject to subsection (9), the first-tier D tax is to be allowed under section 50(7B) as a credit against profits tax payable in Hong Kong by the subject person in respect of the subject dividend as if—
  - (a) the specified DT arrangements contained a provision to that effect; and
  - (b) in section 50(7B)—
    - (i) the reference to “dividend” were a reference to the subject dividend;
    - (ii) the reference to “underlying tax” were a reference to the first-tier D tax; and
    - (iii) the reference to “arrangements” were a reference to the specified DT arrangements.
- (6) Subsections (7) and (8) apply if—
  - (a) the underlying dividends—
    - (i) are paid out of the profits of a direct investee entity of the subject company; or

- (ii) are derived from the profits of an indirect investee entity of the subject company through another investee entity of the subject company; and
  - (b) the subject person has an adequate interest in—
    - (i) in the case of paragraph (a)(i)—that direct investee entity; or
    - (ii) in the case of paragraph (a)(ii)—that indirect investee entity.
- (7) If—
- (a) a similar tax (*downstream UP tax*) is payable in a territory outside Hong Kong in respect of the profits mentioned in subsection (6)(a)(i) or (ii) (as the case requires); and
  - (b) under the specified DT arrangements, no provision is made for the downstream UP tax to be allowed as a credit against profits tax payable in Hong Kong,
- subsection (3) applies to the downstream UP tax as if the references to the first-tier UP tax in subsection (3) were references to the downstream UP tax.
- (8) If—
- (a) the profits mentioned in subsection (6)(a)(i) or (ii) (as the case requires) consist wholly or partly of dividends (*downstream dividends*);
  - (b) a similar tax (*downstream D tax*) is payable in a territory outside Hong Kong in respect of the downstream dividends; and

- (c) under the specified DT arrangements, no provision is made for the downstream D tax to be allowed as a credit against profits tax payable in Hong Kong,

subsection (5) applies to the downstream D tax as if the references to the first-tier D tax in subsection (5) were references to the downstream D tax.

- (9) Any credit allowed under section 50 because of subsection (3) or (5) must represent the extent of—

(a) the direct or indirect beneficial interest the subject person has in, or in relation to, the subject company or investee entity concerned (as the case requires); or

(b) the voting rights the subject person is (whether directly or indirectly) entitled to exercise, or control the exercise of, in or in relation to the subject company or investee entity concerned (as the case requires),

as ascertained when determining whether the subject person has an adequate interest in that company or investee entity.

- (10) In this section—

**adequate interest** (足夠權益)—see section 50AAAC;

**direct investee entity** (直接獲投資實體)—see section 15P(1);

**entity** (實體) has the meaning given by section 15H(1);

**indirect investee entity** (間接獲投資實體)—see section 15P(2);

**investee entity** (獲投資實體), in relation to an entity, means a direct investee entity, or an indirect investee entity, of the entity;

*similar tax* (類似稅項) has the meaning given by section 16(2I)(b);

*specified DT arrangements* (指明雙重課稅安排) means double taxation arrangements that incorporate—

- (a) the credit article or exemption article as defined by section 50AAA(7); or
- (b) any rules in the same or equivalent terms as those articles.

**50AAAC. Supplementary provision to section 50AAAB: determining whether interest is adequate**

- (1) A person (*person A*) has an adequate interest in another person (*person B*) if—
  - (a) person A has at least 10% of direct or indirect beneficial interest in, or in relation to, person B; or
  - (b) person A is, directly or indirectly, entitled to exercise, or control the exercise of, at least 10% of the voting rights in, or in relation to, person B.
- (2) In applying subsection (1), if person A has a direct beneficial interest in person B, the extent of the beneficial interest of person A in person B is—
  - (a) if person B is a corporation that is not a trustee of a trust estate—the percentage of the issued share capital (however described) of the corporation held by person A;
  - (b) if person B is a partnership that is not a trustee of a trust estate—the percentage of the income of the partnership to which person A is entitled;

- (c) if person B is a trustee of a trust estate—the percentage in value of the trust estate in which person A is interested; or
  - (d) if person B is an entity that does not fall within any of paragraphs (a), (b) and (c)—the percentage of person A's ownership interest in the entity.
- (3) In applying subsection (1), if person A has an indirect beneficial interest in, or is indirectly entitled to exercise or control the exercise of voting rights in, person B through another person (*interposed person*), the extent of the beneficial interest or voting rights of person A in person B is—
- (a) if there is only one interposed person—the percentage arrived at by multiplying the percentage representing the extent of the beneficial interest or voting rights of person A in the interposed person by the percentage representing the extent of the beneficial interest or voting rights of the interposed person in person B; or
  - (b) if there is a series of 2, 3 or 4 interposed persons—the percentage arrived at by multiplying the percentage representing the extent of the beneficial interest or voting rights of person A in the first interposed person in the series by—
    - (i) the percentage representing the extent of the beneficial interest or voting rights of each interposed person (other than the last interposed person) in the series in the next interposed person in the series; and

- (ii) the percentage representing the extent of the beneficial interest or voting rights of the last interposed person in the series in person B.
- (4) In applying subsection (1)—
  - (a) any indirect beneficial interest person A has in, or in relation to, person B through a series of 5 or more persons; and
  - (b) any voting rights person A is indirectly entitled to exercise, or control the exercise of, in or in relation to person B through a series of 5 or more persons,are not to be taken into account.
- (5) For the purposes of subsection (3)—
  - (a) subsection (2) applies in determining the extent of the beneficial interest of person A in an interposed person as if the references to person B in subsection (2) were references to an interposed person;
  - (b) subsection (2) applies in determining the extent of the beneficial interest of an interposed person in person B as if the references to person A in subsection (2) were references to an interposed person; and
  - (c) subsection (2) applies in determining the extent of the beneficial interest of an interposed person (*interposed person X*) in another interposed person (*interposed person Y*) as if—
    - (i) the references to person A in subsection (2) were references to interposed person X; and

- (ii) the references to person B in subsection (2) were references to interposed person Y.
- (6) In applying subsection (1)(b), the voting rights attributed to person A include all the voting rights of persons other than person A so far as they are required, or may be required, to be exercised in one or more of the following ways—
  - (a) on behalf of person A;
  - (b) under the direction of person A;
  - (c) for the benefit of person A.
- (7) For the purposes of this section, if—
  - (a) a reference is made to the exercise of the voting rights in a person; and
  - (b) the person is a corporation,  
the reference is to be read as a reference to the exercise of the voting rights at general meetings of the person.”.

**7. Section 51C amended (business records to be kept)**

- (1) Before section 51C(5)(a)—

**Add**

“(aa) section 15T (records to be kept);”.

- (2) Section 51C(5)(b)—

**Repeal the full stop**

**Substitute a semicolon.**

- (3) After section 51C(5)(b)—

**Add**



“(c) section 9 of Schedule 17FC (qualifying IP income: nexus requirement for ascertaining excepted portion etc.).”.

**8. Section 63C amended (amount of provisional salaries tax)**

(1) Section 63C(1), after “subsections”—

**Add**

“(1B),”.

(2) Before section 63C(2)—

**Add**

“(1B) In computing the amount of provisional salaries tax for a year of assessment, any credit or deduction allowed under section 50 for the preceding year of assessment is to be taken into account.”.

**9. Section 63H amended (amount of provisional profits tax)**

(1) Section 63H(1), after “subsections”—

**Add**

“(1E),”.

(2) After section 63H(1D)—

**Add**

“(1E) In computing the amount of provisional profits tax for a year of assessment, any credit or deduction allowed under section 50 for the preceding year of assessment is to be taken into account.”.

**10. Section 63M amended (amount of provisional property tax)**

(1) Section 63M(1)—

**Repeal**

“Provisional”

**Substitute**

“Subject to subsection (1A), provisional”.

- (2) After section 63M(1)—

**Add**

“(1A) In computing the amount of provisional property tax for a year of assessment, any credit or deduction allowed under section 50 for the preceding year of assessment is to be taken into account.”.

**11. Section 80 amended (penalties for failure to make returns, making incorrect returns, etc.)**

- (1) After section 80(2V)—

**Add**

“(2W) A person who, without reasonable excuse, fails to comply with section 15K commits an offence and is liable on conviction to—

- (a) a fine at level 3; and
- (b) a further fine of treble the undercharged amount.

(2X) A person who, without reasonable excuse, fails to comply with section 8(2) of Schedule 17FC commits an offence and is liable on conviction to—

- (a) a fine at level 3; and
- (b) a further fine of treble the undercharged amount.”.

- (2) Before section 80(6)(a)—

**Add**

“(aa) section 15T (records to be kept);”.

- (3) Section 80(6)(b)—

**Repeal the full stop**

**Substitute a semicolon.**

- (4) After section 80(6)(b)—

**Add**

“(c) section 9 of Schedule 17FC (qualifying IP income: nexus requirement for ascertaining excepted portion etc.).”.

**12. Section 82A amended (additional tax in certain cases)**

- (1) After section 82A(1H)—

**Add**

“(1I) If—

- (a) a person, without reasonable excuse, fails to comply with section 15K; and
- (b) no prosecution for an offence under section 80 has been instituted in respect of the same facts, the person is liable to be assessed under this section to additional tax of an amount not exceeding treble the undercharged amount.

(1J) If—

- (a) a person, without reasonable excuse, fails to comply with section 8(2) of Schedule 17FC; and
- (b) no prosecution for an offence under section 80 has been instituted in respect of the same facts,

the person is liable to be assessed under this section to additional tax of an amount not exceeding treble the undercharged amount.”.

(2) After section 82A(4)(a)(i)(E)—

**Add**

“(F) for additional tax to be assessed under subsection (1I)—the alleged failure to comply with section 15K;

(G) for additional tax to be assessed under subsection (1J)—the alleged failure to comply with section 8(2) of Schedule 17FC;”.

**13. Section 89 amended (transitional provisions)**

After section 89(28)—

**Add**

“(29) Schedule 55 sets out transitional provisions that have effect for the purposes of the amendments to this Ordinance made by the Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Ordinance 2022 ( of 2022).”.

**14. Schedule 17FC added**

After Schedule 17FB—

**Add**

## “Schedule 17FC

[ss. 15M, 51C, 80 &  
82A & Sch. 55]

### Qualifying IP Income: Nexus Requirement for Ascertaining Excepted Portion etc.

#### Part 1

#### Preliminary

##### 1. Interpretation of Schedule 17FC

(1) An expression used in this Schedule, and defined or otherwise explained in Division 3A of Part 4, has the same meaning as in that Division.

(2) In this Schedule—

*excepted portion* (例外部分)—see section 3 of this Schedule;

*non-Hong Kong resident person* (非香港居民人士) has the meaning given by section 50AAC(1);

*non-qualifying expenditure* (不合資格開支)—see section 6 of this Schedule;

*qualifying intellectual property* (合資格知識產權) means—

(a) a patent granted under the Patents Ordinance (Cap. 514) (*Cap. 514*) or under the law of any place outside Hong Kong;

(b) a patent application made under Cap. 514 or under the law of any place outside Hong Kong;  
or

- (c) a copyright subsisting in software under the Copyright Ordinance (Cap. 528) or under the law of any place outside Hong Kong;

**qualifying IP income** (合資格知識產權收入) means income derived from qualifying intellectual property in respect of—

- (a) the exhibition or use of, or a right to exhibit or use, (whether in or outside Hong Kong) the property; or
- (b) the imparting of, or undertaking to impart, knowledge directly or indirectly connected with the use (whether in or outside Hong Kong) of the property;

**qualifying R&D expenditure** (合資格研發開支)—see section 5 of this Schedule;

**R&D activity** (研發活動) has the meaning given by section 2 of Schedule 45;

**R&D fraction** (研發分數)—see section 4 of this Schedule;

**specified period** (指明期間), in relation to an MNE entity to which any qualifying IP income accrues, means the period—

- (a) beginning on 1 January 2023 or on an earlier date elected by the entity; and
  - (b) ending on the last day of the entity's basis period of the year of assessment during which the income accrues.
- (3) For the purposes of this Schedule—
- (a) a person is to be regarded as associated with another person if, as between them, the participation condition is met under section 50AAG; and

(b) a reference to associated person is to be read accordingly.

**2. Consistency with OECD 2015 Report**

(1) This Schedule is to be read in the way that best secures consistency with the requirements and guidance in Chapter 4 of the OECD 2015 Report.

(2) In this section—

**OECD 2015 Report** (《經合組織 2015 年報告》) means the Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report published by the Organisation for Economic Co-operation and Development in 2015.

## Part 2

### Excepted Portion of Qualifying IP Income

**3. Ascertaining excepted portion**

The excepted portion of qualifying IP income received by an MNE entity is to be ascertained in accordance with the following formula—

$$P = I \times F$$

where: P means the excepted portion;

I means the qualifying IP income; and

F means the R&D fraction applicable to the qualifying IP income.

#### 4. Ascertaining R&D fraction

- (1) The R&D fraction applicable to qualifying IP income received by an MNE entity is to be ascertained in accordance with the following formula—

$$F = \frac{QE \times 130\%}{QE + NE}$$

where: F means the R&D fraction;

QE means the qualifying R&D expenditure incurred in respect of the qualifying intellectual property to which the qualifying IP income relates (*subject intellectual property*); and

NE means the non-qualifying expenditure incurred in respect of the subject intellectual property.

- (2) However, an R&D fraction is to be regarded as 100% if the percentage ascertained in accordance with subsection (1) is more than 100%.

#### 5. Meaning of QE: qualifying R&D expenditure

- (1) This section explains the meaning of *qualifying R&D expenditure* in relation to qualifying IP income received by an MNE entity.
- (2) Any expenditure (including capital expenditure) incurred by the MNE entity during the specified period for an R&D activity that—
- (a) is connected to the qualifying intellectual property to which the qualifying IP income relates (*subject intellectual property*); and



- (b) is carried out—
  - (i) by the MNE entity;
  - (ii) on behalf of the MNE entity by a person that is not associated with the MNE entity; or
  - (iii) in Hong Kong on behalf of the MNE entity by an associated person of the MNE entity that is a Hong Kong resident person,is, subject to subsections (3), (4), (5) and (6), a qualifying R&D expenditure incurred in respect of the subject intellectual property.
- (3) The following expenditures are not to be regarded as qualifying R&D expenditures—
  - (a) interest payments;
  - (b) payments for any land or building, or for any alteration, addition or extension to any building;
  - (c) any expenditure (including capital expenditure) incurred by the MNE entity for obtaining from another person (whether by acquisition, licensing, amalgamating with another company or otherwise) the subject intellectual property.
- (4) Subsection (5) applies if—
  - (a) the subject intellectual property is or was owned by another company that is a Hong Kong resident person (*original owner*);
  - (b) the MNE entity—
    - (i) obtained the property by amalgamating with the original owner; or

- (ii) acquired all equity interests in the original owner and subsequently acquired, or obtained a licence for, the property from the original owner; and
  - (c) the original owner has sufficient records of the expenditures it incurred in respect of the property, so that the MNE entity would still be able to comply with section 51C (as modified by section 9(2) and (3) of this Schedule) in respect of the expenditures even if—
    - (i) the references to the MNE entity in subsections (2) and (3)(c) were regarded as including the original owner; and
    - (ii) as a result, the expenditures became qualifying R&D expenditures.
- (5) Subsections (2) and (3)(c) apply as if the references to the MNE entity in those subsections included the original owner.
- (6) If, in addition to the subject intellectual property, a qualifying R&D expenditure is also connected to other items of intellectual property (including other qualifying intellectual property), the expenditure is to be apportioned between the subject intellectual property and those other items on a just and reasonable basis.
- (7) For the purposes of subsection (6), an expenditure is apportioned between the subject intellectual property and other items on a just and reasonable basis if the amount apportioned to the subject intellectual property represents the extent to which the expenditure was incurred in respect of the property.

**6. Meaning of NE: non-qualifying expenditure**

- (1) This section explains the meaning of *non-qualifying expenditure* in relation to qualifying IP income received by an MNE entity.
- (2) Each of the following expenditures is, subject to subsections (3), (4), (5), (6) and (7), a non-qualifying expenditure incurred in respect of the qualifying intellectual property to which the qualifying IP income relates (*subject intellectual property*)—
  - (a) any expenditure (including capital expenditure) incurred by the MNE entity during the specified period for obtaining from another person (whether by acquisition, licensing, amalgamating with another company or otherwise) the subject intellectual property;
  - (b) any expenditure (including capital expenditure) incurred by the MNE entity during the specified period for an R&D activity that—
    - (i) is connected to the subject intellectual property; and
    - (ii) is carried out—
      - (A) on behalf of the MNE entity by an associated person of the MNE entity that is a non-Hong Kong resident person; or
      - (B) outside Hong Kong on behalf of the MNE entity by an associated person of the MNE entity that is a Hong Kong resident person.

- (3) The following expenditures are not to be regarded as non-qualifying expenditures—
  - (a) interest payments;
  - (b) payments for any land or building, or for any alteration, addition or extension to any building.
- (4) Subsections (5) and (6) apply if—
  - (a) the subject intellectual property is or was owned by another company that is a Hong Kong resident person (*original owner*);
  - (b) the MNE entity—
    - (i) obtained the property by amalgamating with the original owner; or
    - (ii) acquired all equity interests in the original owner and subsequently acquired, or obtained a licence for, the property from the original owner; and
  - (c) the original owner has sufficient records of the expenditures it incurred in respect of the property, so that the MNE entity would still be able to comply with section 51C (as modified by section 9(2) and (3) of this Schedule) in respect of the expenditures even if—
    - (i) the references to the MNE entity in subsection (2) were regarded as including the original owner; and
    - (ii) as a result, the expenditures became non-qualifying expenditures.
- (5) Subsection (2) applies as if the references to the MNE entity in that subsection included the original owner.

- (6) In calculating the total amount of non-qualifying expenditures, the expenditure incurred by the MNE entity during the specified period for obtaining the subject intellectual property from the original owner is to be deducted.
- (7) If, in addition to the subject intellectual property, a non-qualifying expenditure is also connected to other items of intellectual property (including other qualifying intellectual property), the expenditure is to be apportioned between the subject intellectual property and those other items on a just and reasonable basis.
- (8) For the purposes of subsection (7), an expenditure is apportioned between the subject intellectual property and other items on a just and reasonable basis if the amount apportioned to the subject intellectual property represents the extent to which the expenditure was incurred in respect of the property.

### **Part 3**

## **Supplementary Provisions for Qualifying IP Income**

- 7. Setting off loss sustained in respect of qualifying intellectual property**
  - (1) This section applies if—
    - (a) any qualifying IP income received by an MNE entity is chargeable to profits tax for a year of assessment because of section 15J(1); and

- (b) during the basis period of that year of assessment, a loss is sustained in respect of the qualifying intellectual property to which the income relates.
- (2) The qualifying portion of the loss may be set off against the MNE entity's assessable profits for that year of assessment.
- (3) Any amount of the qualifying portion of the loss not so set off may be carried forward and set off, in accordance with section 19C, against the MNE entity's assessable profits for subsequent years of assessment.
- (4) The qualifying portion of a loss sustained in respect of qualifying intellectual property is to be ascertained in accordance with the following formula—

$$QP = L \times (1 - F)$$

- where: QP means the qualifying portion;  
L means the loss; and  
F means the R&D fraction applicable to the qualifying IP income to which the qualifying intellectual property relates.

- (5) To avoid doubt, the non-qualifying portion of a loss sustained in respect of qualifying intellectual property must not be set off against any assessable profits of the MNE entity.
- (6) The non-qualifying portion of a loss sustained in respect of qualifying intellectual property is to be ascertained in accordance with the following formula—

$$NP = L \times F$$

where: NP means the non-qualifying portion;  
L means the loss; and  
F means the R&D fraction applicable to the qualifying IP income to which the qualifying intellectual property relates.

**8. Effect of withdrawal, abandonment and refusal of patent application**

- (1) This section applies if—
  - (a) because of section 15M, section 15J(1) does not operate in relation to the excepted portion of qualifying IP income received by an MNE entity in a year of assessment;
  - (b) the income is derived from a patent application made under the Patents Ordinance (Cap. 514) or under the law of any place outside Hong Kong; and
  - (c) the application is withdrawn, abandoned or refused in a subsequent year of assessment.
- (2) The MNE entity must notify the Commissioner in writing of the withdrawal, abandonment or refusal within 4 months after the end of the basis period of that subsequent year of assessment, unless the entity has already been required to furnish a return under section 51(1).
- (3) Section 15J(1) applies to the excepted portion of the qualifying IP income as if it were specified foreign-sourced income received in Hong Kong during the basis period of that subsequent year of assessment.

**9. Records to be kept**

- (1) Without limiting section 15T, section 51C applies, with the modifications specified in subsections (2) and (3), to an MNE entity that relies on section 15M to claim that section 15J(1) does not operate in relation to the excepted portion of qualifying IP income it receives.
- (2) The MNE entity must retain records of transactions, acts or operations relating to the qualifying IP income under section 51C at least until the later of the following—
  - (a) the expiry of 7 years after the completion of those transactions, acts or operations; or
  - (b) the expiry of 7 years after making the claim mentioned in subsection (1).
- (3) The MNE entity must keep records of the following, in addition to records within the meaning of section 51C(3) and (4)—
  - (a) information sufficient to establish that the income concerned is qualifying IP income;
  - (b) details of all corresponding expenditures incurred;
  - (c) details of the qualifying intellectual property to which the income relates;
  - (d) if an apportionment is made under section 5(6) or 6(7) of this Schedule—information sufficient to establish that the apportionment is made on a just and reasonable basis;
  - (e) if a loss is set off under section 7 of this Schedule—details of the loss.



- (4) To avoid doubt, the records mentioned in subsection (3) are records of transactions, acts or operations relating to the qualifying IP income.
- (5) Section 80 applies to a failure to comply with section 51C as modified by subsections (2) and (3) in the same way section 80 applies to a failure to comply with section 51C.
- (6) In this section—  
*corresponding expenditures* (相應開支), in relation to qualifying IP income, means all of the following expenditures—
  - (a) qualifying R&D expenditures incurred in respect of the qualifying intellectual property to which the income relates;
  - (b) non-qualifying expenditures incurred in respect of the qualifying intellectual property to which the income relates;
  - (c) any other expenditures incurred in producing the income.

**10. Transitional arrangement for MNE entity with insufficient records**

- (1) This section applies if—
  - (a) qualifying IP income accrues to an MNE entity during the period—
    - (i) beginning on 1 January 2023; and
    - (ii) ending on the last day of the entity's basis period of the year of assessment beginning on 1 April 2024; and

- (b) the entity is unable to ascertain the R&D fraction applicable to the income under Part 2 of this Schedule because there are insufficient records.
- (2) For ascertaining the R&D fraction and keeping records, the MNE entity may elect that sections 5, 6 and 9 of this Schedule apply on the following basis—
  - (a) the references to “specified period” in sections 5(2) and 6(2)(a) and (b) of this Schedule are to be regarded as references to the period of 3 years ending on the last day of the entity’s basis period of the year of assessment during which the qualifying IP income accrues;
  - (b) the references to “the subject intellectual property” in sections 5(3)(c) and 6(2)(a) of this Schedule are to be regarded as references to any intellectual property;
  - (c) the following provisions of this Schedule are to be omitted—
    - (i) section 5(2)(a), (4), (5), (6) and (7);
    - (ii) section 6(2)(b)(i), (4), (5), (6), (7) and (8);
    - (iii) section 9(3)(d).”.

**15. Schedule 17G amended (meaning of *permanent establishment* in Hong Kong)**

Schedule 17G, after “[ss.]—

**Add**

“15H, 15I.”.

**16. Schedule 45 amended (deduction of R&D expenditures)**

Schedule 45—

**Repeal**

“Sch.”

**Substitute**

“Schs. 17FC &”.

**17. Schedules 54 and 55 added**

After Schedule 53—

**Add**

**“Schedule 54**

[s. 50AAA]

**Specifications for Section 50AAA in relation to  
Unilateral Tax Credits**

**Part 1**

**Preliminary**

**1. Interpretation of Schedule 54**

In this Schedule—

*adequate interest* (足夠權益)—see section 50AAAC;

*Hong Kong resident person* (香港居民人士) has the meaning given by section 50AAC(1);

*resident for tax purposes* (稅務居民) has the meaning given by section 50AAC(1);

*similar tax* (類似稅項) has the meaning given by section 50AAA(7);

*specified foreign-sourced income* (指明外地收入) has the meaning given by section 15H(1).

## Part 2

### Specifications for Section 50AAA

#### 2. Specified foreign-sourced income

- (1) For the purposes of section 50AAA(2)—
  - (a) the following income is specified: specified foreign-sourced income; and
  - (b) the following condition is specified for the income: the income is chargeable to profits tax because of section 15J(1).
- (2) For the purposes of section 50AAA(3), the following modification is specified for applying section 50 in relation to the similar tax payable in respect of specified foreign-sourced income: section 50(1A)(a)(ii) and (1B) is to be omitted.
- (3) For the purposes of section 50AAA(3)(a)(i), the following provisions are specified for the similar tax payable in respect of specified foreign-sourced income—
  - (a) the similar tax is to be allowed as a credit (*tax credit*) against the profits tax payable in respect of the income in Hong Kong;

- (b) if—
- (i) the income is a dividend received by a Hong Kong resident person (*subject person*) from a company that is resident for tax purposes in the territory concerned (*investee company*);
  - (ii) the dividend is paid out of the investee company's profits; and
  - (iii) at the time the dividend accrues, the subject person has an adequate interest in the investee company,  
the tax credit allowed to the subject person is, subject to paragraph (c), to include any similar tax payable in respect of the profits in the territory;
- (c) only the portion of the similar tax that represents the extent of—
- (i) the direct or indirect beneficial interest the subject person has in, or in relation to, the investee company; or
  - (ii) the voting rights the subject person is (whether directly or indirectly) entitled to exercise, or control the exercise of, in or in relation to the investee company,  
as ascertained when determining whether the subject person has an adequate interest in the investee company, is to be included in the tax credit.
- (4) For the purposes of section 50AAA(4), the following transitional arrangement is specified for the specification of specified foreign-sourced income

under subsection (1)(a): section 50AAA applies in relation to profits tax payable for a year of assessment beginning on or after 1 April 2022 in respect of income accrued and received on or after 1 January 2023.

- (5) For the purposes of the definition of *similar tax* in section 50AAA(7), the following tax is specified: profits tax.

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## Schedule 55

[s. 89(29)]

### **Transitional Provisions for Inland Revenue (Amendment) (Taxation on Specified Foreign- sourced Income) Ordinance 2022**

#### **1. Interpretation of Schedule 55**

In this Schedule—

*specified foreign-sourced income* (指明外地收入) has the meaning given by section 15H(1).

#### **2. Transitional arrangements**

- (1) Division 3A of Part 4 and Schedule 17FC apply in relation to specified foreign-sourced income accrued and received on or after 1 January 2023.
- (2) Without limiting subsection (1), section 7 of Schedule 17FC and section 15Q apply in relation to losses sustained on or after 1 January 2023.

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- (3) Sections 50(7A) and (7B) and 50AAAB apply in relation to tax payable for a year of assessment beginning on or after 1 April 2022 in respect of income accrued and received on or after 1 January 2023.
  - (4) The amendments made to sections 63C, 63H and 63M by the Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Ordinance 2022 ( of 2022) apply in relation to provisional tax payable for a year of assessment beginning on or after 1 April 2023.”.
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## Explanatory Memorandum

The objects of this Bill are—

- (a) to amend the Inland Revenue Ordinance (Cap. 112) (*principal Ordinance*)—
  - (i) to provide that certain foreign-sourced income is to be regarded as arising in or derived from Hong Kong; and
  - (ii) to provide for relief against double taxation in respect of certain foreign-sourced income; and
- (b) to provide for related and transitional matters.

- 2. The Bill contains 17 clauses.
- 3. Clause 1 sets out the short title and provides for commencement.
- 4. Clause 2 is the standard enactments amended clause included in amending legislation.
- 5. Clause 3 adds a new Division 3A to Part 4 of the principal Ordinance. This new Division contains provisions in relation to foreign-sourced income (new sections 15H to 15T).
- 6. The new sections 15H and 15I contain the definitions for the interpretation of the new Division. In particular, the new section 15H(1) defines *specified foreign-sourced income* to mean any interest, dividend, disposal gain or intellectual property income arising in or derived from a territory outside Hong Kong, not including any interest, dividend or disposal gain derived by a regulated financial entity from the carrying on of a business as such a regulated financial entity.



7. The new section 15J provides that any specified foreign-sourced income that—
  - (a) is received in Hong Kong by a multinational enterprise entity (*MNE entity*) carrying on a trade, profession or business in Hong Kong; and
  - (b) is not otherwise chargeable to profits tax under Part 4 of the principal Ordinance,is to be regarded as a receipt arising in or derived from Hong Kong and is to be regarded as not arising from the sale of capital assets even if it so arises.
8. The new section 15K provides that, if an MNE entity is chargeable to profits tax in respect of any specified foreign-sourced income under Part 4 of the principal Ordinance because of the new section 15J(1), the entity must notify the Commissioner of Inland Revenue of this fact in writing.
9. The new section 15L provides that the new section 15J(1) does not operate in relation to specified foreign-sourced income received in Hong Kong by an MNE entity if—
  - (a) the income is interest, a dividend or a disposal gain; and
  - (b) the entity has economic substance in Hong Kong.
10. The new section 15M, together with the new Schedule 17FC added by clause 14, provides that, if the specified foreign-sourced income is intellectual property income (*qualifying IP income*) derived from a patent, patent application or copyright subsisting in software (*qualifying intellectual property*), the new section 15J(1) does not operate in relation to the excepted portion of the income. The excepted portion is to be ascertained under the new Schedule 17FC. This new Schedule also provides for—

- (a) the setting off of losses sustained in respect of qualifying intellectual property;
  - (b) the effect of withdrawal, abandonment and refusal of patent applications; and
  - (c) the records to be kept for qualifying IP income, including a transitional arrangement for MNE entities with insufficient records.
11. The new section 15N provides that the new section 15J(1) also does not operate if—
- (a) the MNE entity receiving the specified foreign-sourced income concerned is a Hong Kong resident person or has a permanent establishment in Hong Kong;
  - (b) the income is a dividend or disposal gain; and
  - (c) the MNE entity has continuously held not less than 5% of equity interests in the investee entity for a period of not less than 12 months immediately before the specified foreign-sourced income accrues.
12. The new section 15O provides that the new section 15N does not apply in certain circumstances.
13. The new section 15P gives the meaning of *direct investee entity* and *indirect investee entity*.
14. The new section 15Q provides that a loss sustained overseas by an MNE entity may be set off against the entity's assessable profits, but only to the extent that the assessable profits are derived from specified foreign-sourced income that is chargeable to profits tax because of the new section 15J(1).

15. The new section 15R provides that outgoings and expenses incurred in the production of specified foreign-sourced income may be deducted.
16. The new section 15S provides that balancing charges and allowances under Part 6 of the principal Ordinance that relate to specified foreign-sourced income may be taken into account under sections 18F and 19E of the principal Ordinance.
17. The new section 15T requires an MNE entity to retain certain records if it receives in Hong Kong any specified foreign-sourced income to which the new section 15J(1) applies.
18. Clause 4 makes a related amendment to section 16(2J) of the principal Ordinance in view of the amendments made to section 50 of the principal Ordinance and the addition of the new sections 50AAA, 50AAAB and 50AAAC to the principal Ordinance.
19. Clause 5 amends section 50 of the principal Ordinance so that, if any double taxation arrangements contain a provision that foreign tax payable in respect of the underlying profits of a dividend is to be taken into account in determining the amount of credit and (if any) deduction to be allowed in respect of the dividend, the provision is to have effect.
20. Clause 6 adds new sections 50AAA, 50AAAB and 50AAAC to the principal Ordinance. The new section 50AAA sets up a framework for unilateral tax credits to be allowed. Details of unilateral tax credits are provided in the new Schedule 54 added by clause 17.

21. The new section 50AAAB provides that, against profits tax payable in Hong Kong in respect of a dividend (*subject dividend*), unilateral tax credits are to be allowed for any similar tax payable in a territory outside Hong Kong in respect of any underlying profits, underlying dividends, downstream profits and downstream dividends to which the subject dividend relates. Those tax credits are allowed even if the double taxation arrangements made do not contain a provision to that effect. However, for the new section 50AAAB to apply, the person receiving the subject dividend must have an adequate interest in the company distributing the subject dividend.
22. The new section 50AAAC gives the meaning of *adequate interest*.
23. Clause 7 makes related amendments to section 51C of the principal Ordinance.
24. Clauses 8, 9 and 10 respectively amend sections 63C, 63H and 63M of the principal Ordinance so that any tax credit or deduction allowed under the amended section 50 of the principal Ordinance is to be taken into account in computing the amount of provisional salaries tax, provisional profits tax and provisional property tax.
25. Clauses 11 and 12 respectively make related amendments to sections 80 and 82A of the principal Ordinance in view of the addition of the new sections 15K and 15T and the new Schedule 17FC to the principal Ordinance.
26. Clauses 15 and 16 respectively make minor related amendments to Schedules 17G and 45 to the principal Ordinance.

27. Clauses 13 and 17 respectively add a new section 89(29) and new Schedules 54 and 55 to the principal Ordinance. The new section 89(29) and new Schedule 55 provide for transitional arrangements.