

8 April 2022

Mr Christopher Hui Ching-yu, JP
Secretary for Financial Services & the Treasury
Financial Services and the Treasury Bureau
24/F, Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

Dear Mr Hui,

Proposal to Provide Tax Concession for Family-owned Investment Holding Vehicles

The Hong Kong General Chamber of Commerce welcomes the opportunity to comment on the proposals as set out in the subject consultation.

Although the provision of tax concession, in this case exemption from paying tax by qualifying entities, is a welcomed measure, we believe that attention should also be given to non-taxation issues if Hong Kong aspired to become a preferred destination for family offices.

We hope you will find our comments useful.

Yours sincerely,



George Leung
CEO

Encl.

**Consultation Paper on
Proposal to Provide Tax Concession for Family-owned Investment Holding Vehicles
Response by the Hong Kong General Chamber of Commerce (HKGCC)**

1. The HKGCC welcomes the opportunity to respond to the consultation paper (CP) on “Proposal to Provide Tax Concession for Family-owned Investment Holding Vehicles (FIHVs).” We believe that this is a positive and welcome measure that is conducive to further consolidating Hong Kong’s position as a premier international financial centre. Our comments comprise two parts, namely, our reactions to the proposals as set out in the CP and related but material issues that go beyond the CP’s purview.

Response to CP Proposals

Requirements for setting up an FIHV

2. The CP proposes that the central management and control (CMC) of FIHVs must be exercised in Hong Kong as a criterion to satisfy substance requirements. This could have the unintended effect of undermining the proposed tax regime as it may not be practical for non-Hong Kong based wealthy families to exercise the CMC of FIHVs in the SAR. **We note that there are other substance requirements that have been proposed in the CP and would suggest that these are already adequate in preventing harmful tax practices. As such, the CMC requirement should be eliminated.**

Management of assets by SFO

3. The CP proposes that FIHVs be exclusively and beneficially owned by one or more individuals who are “connected persons” of the same family (Single Family) either directly or indirectly and the Single Family Office (SFO) can only provide investment management services to the FIHVs owned by the Single Family. However, it is not uncommon for the SFO to look after other aspects of the Single Family (such as philanthropy, children’s education, family governance, etc) as well as managing investments co-owned with close acquaintances. Given the range of activities that a family office may wish to undertake in Hong Kong, it is neither realistic nor pragmatic for a newly established family office to be fully operational within a short space of time. This is because putting together a capable and competent management team requires local and regional knowledge, as well as access to talent. The nature of family offices requires such qualities as careful management and discreet execution. Many of the core and ancillary functions are more appropriately executed by professional family office (multi-family office) platforms that have in-house expertise on asset management (liquid, private equity, venture capital, private credit, etc), portfolio construction, mid/back-office reporting, philanthropy, family governance, and family office network. It would therefore be highly improbable nor feasible for overseas-based family offices to come to Hong Kong and hire two locals, who are equipped with the appropriate skills and expertise to undertake all these functions. **We suggest that some flexibility be incorporated into the legislative proposals to take into account such situations to render the regime more relevant and practical.**

Minimum asset threshold

4. The CP proposes that the aggregate average value of Schedule 16C specified assets managed by each family-owned structure to be at least HK\$240 million. While gains from Hong Kong real properties would not be exempted under the proposed tax regime, it is very common for UHNWIs to invest in Hong Kong real estate. **We suggest that the government consider raising the minimum asset threshold to also include assets acquired from non-qualifying**

transactions (such as properties in Hong Kong) or private investments (private equity, venture capital and private credit – which are all core investment strategies for family offices), as currently defined under the CP, to enhance the regime’s attractiveness. In the case of investments in Hong Kong real estate, we propose that a cap (which could be 50% of the Minimum Asset Threshold) be imposed. FIHVs would enjoy the benefit of diversifying their investments while also preventing a concentration of such in Hong Kong real estate, which could push up prices.

Qualifying transactions by FIHVs

5. The tax regime as currently proposed only exempts trading receipts derived from qualifying transactions in assets specified in Schedule 16C of the Inland Revenue Ordinance. However, it is not atypical for family offices to invest in asset classes outside the scope of Schedule 16C (these include overseas real estate, collectible items such as art pieces, and digital assets (such as cryptocurrency, NFTs)) which do not meet the definition of qualified transactions or investments under the proposed tax regime. **We suggest that consideration be given to broadening the scope of qualifying assets that a FIHV can invest in, as and when legislative amendments have been made to add new asset categories under Schedule 16C, to render the regime more competitive.**

Substantial activity requirement (Threshold for operating expenditure)

6. The proposed tax regime specifies that trading receipts arising from incidental transactions would be exempted, subject to a 5% threshold. Based on the current practice under the Unified Fund Exemption regime, interest income derived from debt securities is regarded as trading receipts arising from incidental transactions. Since it is not uncommon for family offices to hold a sizable portfolio of debt securities through which interest derived constitutes a major source of income during the holding period, the 5% threshold could easily be exceeded. **We suggest that interest income arising from qualifying transactions be exempted as well to make it the proposed regime more relevant and attractive.**
7. Under the proposed regime, FIHVs can only serve as an investment vehicle for holding and administering assets and are prohibited from engaging directly in activities of a general commercial or industrial nature. However, it should be noted that FIHVs may be involved from time to time in the sale and purchase of listed securities as part of their asset management activities. Given such ambiguity, **we suggest that clarification be provided on the definition of permitted activities to avoid jeopardising FIHV’s tax exemption status. Alternatively, clear guidance should be provided on the meaning of “activities for general commercial or industrial purposes.”**
8. One of the proposed substance requirements on FIHV involves the employment of at least two full-time qualified staff. As it is not unusual for an SFO to simultaneously manage a number of FIHVs (which could be up to 50) especially in the case of a large family, it is neither pragmatic nor viable for the SFO to have a large payroll. At the same time, FIHV-related activities often do not require day-to-day management. As such, the number of FIHVs does not provide a meaningful or accurate gauge of the size of the workforce required to manage such investments. Given the foregoing, **we suggest reviewing the requirement on the “number of employees” to enable this to be applied on a “group basis” instead of an “entity basis.” We would also invite clarification on the permissibility for an SFO to employ an adequate number of workers (with a minimum of two) in cases where core income generating activities have been outsourced to the same SFO.**

Administration of the regime

9. In the paragraph 18 of the CP, it is proposed that “(t)o ensure the fulfilment of the eligibility criteria, the FIHV and SFO have to file tax returns to the IRD annually...” To the extent that a FIHV fulfills the scheme and qualifies for profits tax exemption, **we suggest to instead adopt a simplified certification or self-declaration process to be made annually by FIHVs that derive income only from qualifying transactions and incidental transactions for that year of assessment.**

Issues of significance not in the CP

Talent

10. As pointed out in our submission¹ of 26 November 2021 to the Secretary for Financial Services and the Treasury, FIHVs are no different from any legitimate businesses when considering where to locate their operations. Issues such as the availability of talent and a business-friendly environment are some of the determining factors that family offices take into account when making such assessments.
11. In that connection, **we would like to reiterate our call for the government to direct resources and policy support for the purpose of attracting, retaining and developing talent.** This is especially important given the CP’s proposal requiring FIHVs to have a minimum of 2 qualified full-time employees, which could be quite challenging amidst intense competition for talent within the financial services sector and a dwindling labour pool. Given the unique and complex nature of managing family offices and the associated demands for talent (as explained in Paragraph 3 above), **policies to facilitate residency status in Hong Kong could be considered to attract international talent.**

Residency

12. **We would also urge the government to give serious consideration to granting permanent residence status to qualifying FIHV principals.** As mentioned in our previous submission, we believe that Hong Kong has much to offer as a regional base given our international character. This is especially the case for ultra-high net worth individuals (UHNWIs) from the Mainland given such intrinsic advantages as a shared culture and geographical proximity.

BEPS 2.0

13. Given the likelihood that underlying investments held by the FIHVs may be subject to the OECD’s Pillar Two Model Rules, there should be **proactive measures taken by the government to ensure that such private investment structures do not get caught under the Model Rules. At the same time, it is important that the government to consult with and provide stakeholders with timely updates on developments in this regard.**

¹ https://www.chamber.org.hk/en/advocacy/policy_comments.aspx?ID=534

Cross-sectoral support

14. The work of Singapore’s Economic Development Board (EDB) in promoting a family office-friendly environment provides a useful and instructive model for Hong Kong to draw upon. As a key driver in developing tax incentives and administering the Global Investor Programme – a scheme to promote Singapore as a base for qualified individuals, EDB also works closely with providers of professional services such as accounting and law firms to build an ecosystem that supports family offices. **To enhance Hong Kong's attractiveness as a family office hub, coordination among the government, regulators and the industry is required to support and address the needs of family offices.**

HKGCC Secretariat
April 2022