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HK FINANCIAL SERVICES DEVELOPMENT COUNCIL 香港金融發展局

Asset and Wealth Management in Hong Kong Tax Recommendations towards Further Development

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Contents

Executive Summary

Hong Kong's asset and wealth management (AWM) industry has prospered over the past years thanks to the city's unparalleled advantages as an international financial centre, and the collective efforts of the industry and the HKSAR Government. However, the economic and geopolitical changes that have taken place reminds us that Hong Kong should not rest on its laurels. Improvements to the existing tax laws and policies are needed for Hong Kong to retain its competitiveness and cement its position as a leading international AWM hub.

The FSDC has formed a dedicated Working Group comprising of tax experts to review the existing tax laws and identify potential measures that can bolster the AWM ecosystem and industry in Hong Kong, and support the organic growth of asset classes, asset owners, and service providers alike.

This paper mainly focuses on the following areas, which are considered as (i) the most pressing issues hindering Hong Kong's further development in AWM, and (ii) the areas which can be addressed quickly, simply, and easily with the largest beneficial effect. To this end, the FSDC has identified the following three key areas where tax can play a pivotal role to bring Hong Kong's AWM industry to greater heights.

- Promoting asset classes that are currently underdeveloped in Hong Kong by providing incentives, clarity and operational efficiency.

- Attracting institutional investors by providing a level playing field in terms of tax to each type of asset owners.

- Addressing other deficiencies in the unified profits tax exemption for funds (UTE) and the open-ended fund company (OFC) regime.

Introduction and overview

Hong Kong has long been regarded as a leading asset and wealth management centre in Asia and internationally, managing a combined AUM of USD4.5 trillion at the end of 2020.[1] The success it has seen can be attributed in part to its strategically unique geographic position. Hong Kong is a port city and a gateway to Mainland China – consistently having been the largest source of foreign direct investment into and the largest destination for outward direct investment out of Mainland China.[2]

Recognising the strength of the industry, over the past few years, the Hong Kong SAR Government has launched several initiatives either specifically aimed at or related to the asset and wealth management (AWM) sector and its market players. The number of tax law developments are indicative of the commitment by the Government to strengthen the industry.[3]

Nonetheless, the FSDC believes more can be done. Uncertainties in the geopolitical landscape, major markets and economies, and more recently the international tax environment, are making businesses and industry players more cautious in their decision making. This will continue to impact Hong Kong and its position as an AWM hub. The FSDC calls for coordinated action from the HKSAR Government, regulators, and the industry to ensure Hong Kong remains internationally competitive as an AWM centre.

The FSDC believes that an effective way of doing this is to review the existing tax laws and policies and look for areas of improvement. In doing so, any tax policies or measures introduced should cater to the entire AWM ecosystem and develop the industry as a whole. This means they should apply to and benefit asset classes, asset owners, and service providers alike.

This paper mainly focuses on the following areas, which are considered as (i) the most pressing issues hindering Hong Kong's further development in AWM, and (ii) the areas which can be addressed quickly, simply, and easily with the largest beneficial effect.

I. Promoting asset classes that are currently underdeveloped in Hong Kong.

II. Attracting asset owner classes that are important institutional investors to invest in or through Hong Kong to which the taxation regime should apply on a fair and equitable basis, thus offering a level playing field to each class of asset owners.

III. Addressing other deficiencies in the unified profits tax exemption for funds (UTE)[4] and the open-ended fund company regime (OFC).

The FSDC notes that in May 2021, the law to introduce a tax concession for carried interest derived from private equity funds operating in Hong Kong was enacted with retrospective effect from 1 April 2020.[5] The FSDC understands that since then, the HKSAR Government has been liaising closely with the industry to look for a practical approach to ensure the successful implementation of the regime, for example, extending the Hong Kong Monetary Authority (HKMA)'s certification application deadline. In view of the progress already taking place, this paper does not include the discussion of the tax concession for carried interest.

[1] Securities and Futures Commission, Hong Kong's asset and wealth management business reached HKD34,931 billion in 2020, July 2021, https://www.sfc.hk/-/media/EN/files/COM/Reports-and-surveys/AWMAS2020_e.pdf, accessed 18 January 2022.
[2] The Government of The Hong Kong Special Administrative Region, Speech by SFST at European Financial Forum in Dublin, https://www.info.gov.hk/gia/general/201902/14/P2019021400255.htm, accessed 28 October 2019.
[3] Please refer to Appendix 1 for the key Hong Kong legislative developments relating to the asset and wealth management industry in recent years.
[4] Inland Revenue (Profits Tax Exemption for Funds) (Amendment) Ordinance 2019.
[5] The Inland Revenue (Amendment) (Tax Concessions for Carried Interest) Ordinance 2021.

I. Promoting asset classes that are currently underdeveloped in Hong Kong

Debt capital market

Hong Kong's thriving and strong equity capital market has long been recognised globally as one of its fortes. The Stock Exchange of Hong Kong (SEHK) is Asia's fourth largest stock exchange in terms of market capitalisation and seventh largest in the world.[6] While this is already down compared with prior periods, in comparison, Hong Kong's debt capital market (both public debt and private debt) has developed at a much slower pace. This trend is also true when compared to other leading global (and regional) financial centre counterparts. According to data from the Bank of International Settlements, Hong Kong's outstanding international debt instruments totalled USD 564 billion, which represents only 8% of the UK and 1% of the US' figures.[7] Whether viewed in terms of local issuances by government and corporates, or in terms of volumes traded locally (regardless of issuer), Hong Kong's role in debt markets does not compare to its role in equity markets. And yet the debt markets, along with the accompanying currency markets, are much larger globally.

The stunted growth of Hong Kong's debt market can be attributed to various factors. Some of them relate to features of the public debt markets in Asia that have been well documented, as well as the policies of those jurisdictions such as Hong Kong seeking to grow their status as a global financial centre.[8] In fact, the HKSAR Government has already taken some steps to boost the growth of the debt market, initially geared towards public debt, and more recently, towards bonds and marketable debt instruments. In 2009, it established the Government Bond Programme to "promote further and sustainable development of the local bond market", to "complement the equity and the banking sector as an effective channel of financial intermediation."[9] In the 2016-17 Budget Speech, Hong Kong's Financial Secretary said that the Government Bond Programme "has successfully attracted local and overseas investors and issuers to participate in Hong Kong's bond market." The Financial Secretary has time and again acknowledged the importance of the bond market as a key component of the capital market. In the 2018-19 Budget Speech, the Financial Secretary stressed again that the Government is committed to improving various facets of the financial services industry, in particular, developing the bond market and green finance to enhance Hong Kong's competitiveness and to "[attract] corporate bond issuance, [facilitate] investors participation and [broaden] investment platform." In his 2022-23 Budget Speech, the Financial Secretary expressed that "developing the bond market in Hong Kong has been one of our key objectives in recent years."[10] The Steering Committee on Bond Market Development in Hong Kong set up under the Financial Secretary's purview, has reviewed the current bond market situation and has put forward recommendations and look to implement these. While the initiatives and efforts to date to support and promote Hong Kong's debt market are good steps in the right direction, the FSDC believes that more can be done to further stimulate its growth.

[6] As at end September 2021. See: https://www.sfc.hk/-/media/EN/files/SOM/MarketStatistics/a01.pdf, accessed 18 January 2022.
[7] Q2 2021, Bank for International Settlements, Statistics, https://stats.bis.org/statx/srs/table/c1?f=pdf, accessed 18 January 2022.
[8] Bank credit has dominated Asia markets for a long time, though the public bond market has grown considerably. See: https://www.mckinsey.com/~/media/McKinsey/Industries/Financial%20Services/Our%20Insights/Deepening%20capital%20markets%20in %20emerging%20economies/Deepening-capital-markets-in-emerging-economies.ashx, accessed 9 July 2020.
[9] Government of the Hong Kong Special Administrative Region of the People's Republic of China, Government Bond Programme (n.d, Hong Kong), https://www.hkgb.gov.hk/en/overview/introduction.html, accessed 12 August 2019.
[10] The 2022-23 Budget Speech (23 February 2022, Hong Kong), https://www.budget.gov.hk/2022/eng/budget23.htmlhttps://www.budget.gov.hk/2019/eng/budget13.html, accessed 23 February 2022.

Thus, in order to advance as a financial centre, Hong Kong's development need is in the area of debt, which is one of the components of fixed income, currencies and commodities (FICC)[11]. A number of major institutions in Hong Kong recognise this and are working to advance it, prominently the HKMA[12] and Hong Kong Exchanges and Clearing Limited (HKEX).[13] This means developing all the tools and functions to offer a fully capable platform for trading in bonds and other debt instruments, as well as the institutional arrangements, including legal and regulatory certainty, for a healthy participation in debt markets.[14] In this context, Hong Kong should be promoting policies that enable it as a fully capable financial centre with respect to non-equity instruments such that it is on par with equities. Naturally this means a high degree of certainty required from the tax and legal systems in their treatment of these instruments. This is especially important given the return characteristics of these instruments in contrast to those of equities. **The FSDC takes a deeper look into the tax issues associated with debt as an asset class, and offers recommendations below.**

The FSDC acknowledges that some initiatives have followed the above assertions. In May 2018, the HKMA introduced the Government's Pilot Bond Grant Scheme – a three-year scheme to attract bond issuers to Hong Kong, providing first time bond issuers with a grant to cover half its eligible expenses, subject to meeting specified criteria upon application.[15] On public debt, in June 2019, the Government also amended the qualifying debt instrument (QDI) scheme to expand the tax exemption available and increased the types of qualifying instruments by including debt securities listed on the SEHK. The intention behind these changes was for Hong Kong investors to enjoy a tax concession for interest income and trading profits derived.

Raising awareness of current tax concessions and facilitating international debt capital flow

The profits tax exemption for QDI was expanded to any interest income and trading profits derived from bonds listed on the Hong Kong Stock Exchange on or after 1 April 2018, regardless of its tenor. However, the awareness of such concessions among the public is relatively low, particularly amongst corporates in the financial sector of the current tax concessions relating to QDIs.

In order to raise the awareness of current tax relating to QDIs, the FSDC recommends that Hong Kong' tax concessions on QDIs should be more widely publicised.

On a broader level, the platform on which the market operates should be attractive and allow a certain level of flexibility for debt instrument issuers. **The Hong Kong Government should explore ways to facilitate the flow of international debt capital by attracting appropriate candidates, and encouraging a variety of investors with a view to diversifying the market (in terms of investors' geographical location (i.e. cross-border listings) and issuer types).**

[11] Currencies and commodities traded on exchanges and their derivatives are within the Schedule 16 classes of assets and thus tax-exempt specified transactions for the purposes of Section 20AN of the Inland Revenue Ordinance.
[12] Hong Kong Monetary Authority, https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/bond-market-development/ and https://www.hkma.gov.hk/media/eng/publication-and-research/quarterly-bulletin/qb202003/fa1.pdf, accessed 9 July 2020.
[13] Hong Kong Exchanges and Clearing Limited, https://www.hkexgroup.com/-/media/HKEX-Group-Site/Ir/IR-Pack/2019-Annual/20200309_HKEX-IR-deck,-d-,w,-d-,new.pdf, accessed 9 July 2020.
[14] McKinsey&Company, https://www.mckinsey.com/~/media/McKinsey/Industries/Financial%20Services/Our%20Insights/Deepening%20capital%20markets%20in%20emerging%20economies/Deepening-capital-markets-in-emerging-economies.ashx, accessed 9 July 2020.
[15] The Pilot Bond Grant Scheme and the Green Bond Grant Scheme consoidated into a Green and Sustainable Finance Grant Scheme, which commenced on 10 May 2021 and lasts for three years, see: https://www.hkma.gov.hk/media/eng/doc/key-information/press-release/2021/20210504e4a1.pdf.

Reviewing the tax regime for the debt capital market

Fixed income (including funds that invest in bonds, marketable fixed income and other debt instruments)

With the introduction of economic substance requirements in the Cayman Islands, the inclusion of the Cayman Islands in the European Union's blacklist in February 2020 and subsequent removal in October 2020, investor preferences are changing to a preference for onshore structures and vehicles, which could bring benefits to Hong Kong. Hong Kong's existing tax regime, as compared to that of Singapore, lacks in support and certainty for ordinary participation in the international bond market, and various forms of credit funds (whether focused on secondary or primary market opportunities). Thus, it is not in an optimal position to capitalise on the potential business opportunities. According to Alternative Credit Council's Financing the Economy publication, private credit managers face unique regulatory barriers and, in some markets, such barriers continue to be the single biggest detriment of growth of private credit in those jurisdictions. In fact, 58% of managers surveyed see the ability to structure a fund effectively – tax and fund structuring specifically – as their biggest regulatory challenge.[16] It is clear that Hong Kong needs policy changes to address this issue imminently.

While the FSDC acknowledges that the slow development of the debt market is not an isolated issue specific to Hong Kong, what is specific to Hong Kong is the tax regime which is not fully conducive to the development of the fixed income market. While recognising that "the Government has introduced a host of measures to promote the development of Hong Kong's bond market.",[17] the FSDC recommends that the Government consider revamping its current tax policies to support and encourage the development of the private funds that invest in bonds and other securities consisting of fixed income debt securities in Hong Kong. Most significantly, consideration should be given to the immediate need for the inclusion of interest income on bonds and other fixed income and other marketable debt securities in the categories of specifically exempted income under the UTE. The Hong Kong Government can explore a variety of ways of doing this – whether by removing the current constraints legislatively, or relaxing or clarifying (favourably) its view in its interpretation of the law. Such a change to the taxation regime can act as a catalyst to promote Hong Kong's bond / fixed income market more generally. The key need, as explained below, is for a regime of certainty.

Under the UTE (and the "non-resident, non-funds" tax exemption),[18] there is an inherent disadvantage to investment managers wanting to manage private fixed income funds in Hong Kong, owing to the fact that a significant portion of the total income derived by such a fund is 'interest income'. The IRD's interpretation of the UTE is that interest income is 'income from incidental transactions' as opposed to 'income from specified transactions'. In contrast, an investment fund qualifying for UTE that invests in listed/public or/and private equities deriving dividend income will not have to worry about the Hong Kong profits tax treatment of dividends because dividend income from Hong Kong companies is statutorily tax exempt, and dividend income from overseas companies is treated as non-taxable offshore income. This puts the fixed income fund in a disadvantageous position because the interest income derived by a private fund does not enjoy exemption unless the interest income is less than 5% of the total trading receipts of the fund – which is difficult to achieve by a private fund adopting a buy and hold strategy.

[16] See https://acc.aima.org/research/financing-the-economy.html and https://www.dechert.com/knowledge/publication/2019/11/financing-the-economy--the-future-of-private-credit.html, accessed 14 February 2022.
[17] The 2019-20 Budget Speech (27 February 2019, Hong Kong), https://www.budget.gov.hk/2019/eng/budget13.html, accessed 12 August 2019.
[18] See Inland Revenue (Profits Tax Exemption for Funds) (Amendment) Ordinance 2019, Inland Revenue (Amendment) (No.2) Ordinance 2015, Revenue (Profits Tax Exemption for Offshore Funds) Ordinance 2006.

The current fund exemption provisions provide an exemption from tax for assessable profits from qualifying transactions, comprising transactions in assets of a class specified in Schedule 16C. Whilst it is accepted that gains from purchasing and selling debt securities is a qualifying transaction, interest received on debt securities is not regarded by the IRD as arising from a qualifying transaction. Technically the qualifying transaction to which the interest relates should be considered as the purchase of the bond / debt instrument, since the acquisition of the bond / debt instrument allows for the receipt of interest (being the assessable profit).

The result of the IRD's position means that funds investing (but not trading) in bonds and other marketable debt instruments will not be able to avail of the exemption, and are therefore at an adverse tax position as compared to funds that invest in equities. This is not a new issue and has been raised on several occasions over the past ten years by asset and wealth management market players and the broader financial services industry. The FSDC considers a policy change in this regard, especially in the current economic climate, is of high priority.

Over the past five years, investors have shifted their investments towards fixed income instruments and this category of investments has now become more popular than stocks and equities.[19] In view of the growth in private credit, and given that such funds increasingly form part of the broader investment platform of traditional private equity groups, it is not clear what mischief the IRD is seeking to address by adopting this position. The current tax policy and law reflect an "old-world" investment landscape and does not work to serve the modern market. Singapore on the other hand has amended its fund exemption provisions to specifically cater for private funds to provide a specific exemption for interest income. This has resulted in many of those fund groups establishing their Asian investment platforms in Singapore instead of Hong Kong in the past decade.

One way of mitigating the Hong Kong tax exposure is to invest in overseas bonds. However, this discourages the growth of Hong Kong's debt / bond market. Rather, **the FSDC recommends that the legislation should be amended to clarify that interest income on debt investments constitutes a qualifying transaction**. Therefore, provided all the other requisite conditions of the exemption regime are met, private credit strategies that consist primarily of fixed instruments including bonds, debts, loans and the like, can too make use of the exemption. Potential legitimate areas of abuse could be dealt with directly through a targeted anti-abuse provision. For example, to disallow any Hong Kong interest expense deduction for borrowers that receive debt funding from tax exempt private funds. The FSDC also stresses that debt should not be seen as a widely practiced form of tax avoidance. On the contrary, the use of debt is a commercially used funding mechanism by businesses, big and small, to fund working capital, and to invest with a view of growth and expansion. Related party debt should be priced on commercial terms, i.e. at arm's length.

Bond issuers also often face uncertain tax positions. There are currently no specific rules, tax incentives or concessions to attract corporates to issue bonds which have hybrid or quasi-equity features e.g. perpetual bonds, which are becoming more popular in the debt market. Therefore, the profits tax implications to issuers are determined based on the general Hong Kong tax principles. The introduction of the new law to grant tax deductions to financial institutions for distributions on regulatory capital securities (RCS) and stamp duty relief for transfers of RCSs was welcomed by the banking industry as it clarified the tax treatment and enhances treasury operations within financial institutions.

To this end, the FSDC recommends that issuers which are not financial institutions would need similar certainty and/or flexibility in this respect to increase the number of bond issuances in Hong Kong.

[19] According to the Natixis Global Survey of Institutional Investors (interviewed 500 investors who collectively manage more than USD15 trillion in assets for Pensions, Insurers, SWFs, Foundations and Endowments around the world). In 2015, bonds / fixed income accounted for 28.0% and stocks / equities accounted for 42.0% as compared to the 2020 projection figures where bonds / fixed income was 38.7% and stocks / equities was 35.8%. See https://www.im.natixis.com/us/resources/2020-institutional-outlook-executive-overview, accessed 24 July 2020.

Private credit, distressed debts and NPLs

Hong Kong had taken efforts to change its tax policies to facilitate private funds to invest in non-Hong Kong private equities,[20] and later to allow private funds to invest in Hong Kong private equities.[21] However, the current tax policies do not offer strong support to private credit. Private credit has brought value to investors for many years – even during the pandemic, private credit has "continued to effectively deploy capital … and was a vital provider of capital support to businesses during this period."[22] The Government should take more steps to level the playing field for private credit especially in light of the current market environment and economic landscape. In Hong Kong and the Asia Pacific, private credit has become an increasingly popular alternative asset class in the current low interest environment and will likely remain so after the global economy starts its recovery. "Larger companies with access to various financing options are increasingly choosing the private route to capital, prizing the tailored and efficient financing solutions that private credit can offer."[23] Naturally, it is expected that the growth of private equity would significantly widen the origination channels for potential credit opportunities. "Following the 2008-09 global financial crisis, private credit has been transformed into a major global institutional asset class: the global volume of private credit AUM grew ~3.2 times between 2008 and 2018."[24] In 2020, private credit managers deployed almost USD 200 billion.[25] There is also a significant uptick expected in institutional investment in the private credit asset class in the coming years, especially in Asia – with 88% of pension funds, 80% of insurers, and 67% of sovereign wealth funds surveyed in 2019 expecting more investment into private credit strategies from their investors.[26]

Investing in distressed debts or portfolios of NPLs[27] is a rapidly growing sector of the private investment universe, having first emerged at scale in the region following the Asian financial crisis of 1997 and then globally, as a result of the global financial crisis, just over a decade ago. The sector is focused on investment opportunities where the value of the underlying asset is severely depressed for a reason particular to the issuer; and where there is a clear path to realise a return, through an action or special event. In general, NPLs or distressed assets are not income generating, meaning the return generally can be realised via capital appreciation (or via identifying opportunities which can be acquired at a discount to their recoverable value).

[20] See Inland Revenue (Amendment) (No.2) Ordinance 2015, Revenue (Profits Tax Exemption for Offshore Funds) Ordinance 2006.

[21] See Inland Revenue (Profits Tax Exemption for Funds) (Amendment) Ordinance 2019.

[22] Alternative Credit Council, Financing the Economy, 2021. See: https://acc.aima.org/research/financing-the-economy-2021.html, accessed 26 January 2022. AIMA (or The Alternative Investment Management Association) set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 200 members that manage USD 450bn of private credit assets globally. The ACC is an affiliate of AIMA and is governed by its own board which ultimately reports to the AIMA Council. ACC members provide an important source of funding to the economy. They provide finance to mid-market corporates, SMEs, commercial and residential real estate developments, infrastructure as well the trade and receivables business. The ACC's core objectives are to provide guidance on policy and regulatory matters, support wider advocacy and educational efforts and generate industry research with the view to strengthening the sector's sustainability and wider economic and financial benefits. Alternative credit, private debt or direct lending funds have grown substantially in recent years and are becoming a key segment of the asset management industry. The ACC seeks to explain the value of private credit by highlighting the sector's wider economic and financial stability benefits.

[23] Ibid.

[24] Global AUM of private credit grew from US$237.9bn to US$767.5bn from 2008 to 2018. See: Alternative Credit Council, Financing the Economy, November 2019, https://acc.aima.org/research/financing-the-economy.html, accessed 18 January 2022

[25] Alternative Credit Council, Financing the Economy, 2021. See: https://acc.aima.org/research/financing-the-economy-2021.html, accessed 26 January 2022.

[26] Alternative Credit Council, Financing the Economy, 2019. See: https://www.aima.org/article/press-release-acc-publishes-financing-the-economy.html, accessed 24 July 2020.

[27] The Hong Kong Monetary Authority adopts a loan classification framework. Its guidelines classify three grades (substandard of below) as NPLs. However, the definition may be different for banks when they classify credit-impaired loans under the current IFRS 9 / HKFRS 9 accounting definition. See: https://www.hkma.gov.hk/media/eng/doc/key-functions/banking-stability/banking-policy-and-supervision/regulatory-framework/ma(bs)2aci(app2)_e.pdf, accessed 4 August 2020.

Over the last few years, the NPL and distressed asset investment market has been deepest in Europe, but a shift towards Asia had begun long-before the COVID-19 pandemic hit the region in early 2020 – with global distressed funds building out teams and deploying capital across, in particular, Mainland China, India and Australia. The FSDC expects the pandemic to only further interest in this asset class in Asia - as companies struggle to serve their existing debt; more regular opportunities for private investors to either buy individual distressed loans (at a discount) or pools of NPLs from lenders, should emerge.

A deep distressed investment market with a variety of investor categories focused on distressed debt resolution, can benefit emerging market economies: whilst NPLs are an inevitable by-product of lending, at elevated levels, NPLs can lead to reduced lending and limited credit to productive sectors and individuals, slowing down the economy and negatively acting as a drag on economic output.

In a survey for credit fund managers,[28] 60% of respondents said that they would or would be more likely to establish or expand their business operations in Hong Kong if the Hong Kong tax regime became more attractive, for example, by way of tax concessions. In a 2021 survey,[29] where all respondents had offices in Hong Kong and investment management or advisory personnel as well as non-investment staff in Hong Kong, a significant majority indicated that over 2% of their total expenditure were incurred in Hong Kong. An increase in total expenditure spent in Hong Kong will likely result in a higher demand for professionals working in the fund management industry as well as other ancillary sectors. In this way, Hong Kong's capital market on the whole will become more vibrant with more investment management and advisory staff attracted to and based in Hong Kong.

In addition, the majority of respondents considered Hong Kong's tax treatment of credit funds weaker than other jurisdictions. However, most of them indicated they would each increase their AUMs managed in Hong Kong by approximately USD 1-2 billion if Hong Kong improves its tax regime. Respondents said that, if appropriate changes were made, they would increase their operations in Hong Kong and launch a credit fund domiciled in Hong Kong.[30] As such, Hong Kong needs to evolve further and respond to market demands and changes in order to retain and consolidate its position as an international financial centre and leading AWM centre.

On this, the FSDC recommends extending the tax exemption to privately offered funds investing in distressed debts, NPLs and credit strategies. This also alludes to the FSDC's earlier recommendation for the Hong Kong Government to take appropriate steps to remove the current obstacles to ensure that privately offered funds investing in distressed debts, NPLs, and credit strategies are on equal footing as their hedge and private equity fund counterparts by being able to clearly enjoy the same tax exemptions. That is, by way of expanding the scope of the UTE. Although it would be preferable for legislative amendments to be enacted to provide high levels of certainty, the FSDC notes that in fact these changes could be enacted through the issue of administrative guidance notes.

Referring to the legislation, the Money Lending Ordinance provides a definition of a "loan" and "money lender" and therefore, the scope of money lending activities. The FSDC would like to recommend that where a fund invests in private credit, but its activities do not fall within such defined parameters, the fund should not be regarded as a money lender and its activities should not be regarded as money lending.

[28] A flash survey conducted by Alternative Credit Council, where 88% of the respondents run credit strategies.

[29] A survey of AIMA / ACC members to understand the factors influencing the Hong Kong private credit market with the benefit of data on their business in Hong Kong and other financial centres in the APAC region.

[30] In the survey conducted in 2021, the vast majority of the respondents had less than 10% aggregate capital commitments from Hong Kong financial investors. Additionally, only a handful of the respondents reportedly had private credit investments in Hong Kong companies. As such, the risk of potential tax leakage of granting tax exemption to private credit funds is insignificant given the low involvement of Hong Kong financial investors.

The Securities and Futures Ordinance (SFO) provides definitions for the term “securities”, which includes debentures and notes.[31] The SFO then goes on to define “debentures” but not the term “note”. Fund managers face uncertainty on whether or not a “loan note” is a security. To facilitate the growth of private credit in Hong Kong, as long as the borrower is disallowed from claiming a Hong Kong tax deduction on the interest expense, then private credit should be an allowable investment under the UTE, be it in the form of notes or direct lending.

The FSDC understands the Government’s tax avoidance concerns and therefore has suggested previously in the section in relation to tax regime review for fixed income, to disallow any Hong Kong interest expense deduction for borrowers that receive debt funding from tax exempt private funds.

Infrastructure funds

Currently under the UTE, if a fund invests in a private company that directly or indirectly holds more than 10% of its assets in immovable property, the fund will be taxed on the profits arising from such an investment. For this purpose, immovable property does not include infrastructure,[32] which is defined as “any publicly or privately owned facility providing or distributing services for the benefit of the public, and includes any water, sewage, energy, fuel, transportation or communication facility.”[33] In some ways, the intention of this carve-out or distinction from real estate has widened the type of assets a fund can invest in, while making use of the UTE. However, in practice, the separation between infrastructure and real estate is imperfect and blurred. More generally, where does real estate end and infrastructure start? The challenges and difficulties in making a clear segregation between the two affects infrastructure investments, and to an extent, hinders the growth of infrastructure funds in Hong Kong.

According to the Global Competitiveness Report 2019 of the World Economic Forum, Hong Kong’s infrastructure is ranked third in the world. There are currently and will be potentially many infrastructure projects in and involving Hong Kong due to its role in the Greater Bay Area to ensure closer and easier connectivity between Hong Kong and the Mainland. This includes more projects to develop cross-boundary transportation networks and facilities to support the increased and increasing demand and traffic. In 2018, over 235 million passenger trips crossed the border via land crossings, which include Lo Wu, Lok Ma Chau Spur Line, Hung Hom, Shenzhen Bay Port, Lok Ma Chau (Huanggang), Sha Tau Kok, Man Kam To, West Kowloon Station and Hong Kong-Zhuhai-Macao Bridge Hong Kong Port, with a daily average of over 640,000 passenger trips.[34]

[31] See Section 1, Part 1 of Schedule 1 to the Securities and Future Ordinance. The definition of “securities” includes "shares, stocks, debentures, loan stocks, funds, bonds or notes of, or issued by, a body, whether incorporated or unincorporated, or a government or municipal government authority" and "interests in any collective investment scheme" , but excludes (among others) "any debenture that specifically provides that it is not negotiable or transferable".

[32] Investments in infrastructure are permissible under the exemption provided that the fund itself does not directly engage in the construction or direct acquisition of infrastructure (sections 20AM(6) and (7)(f)). However, section 20AP(2)(a) prevents the exemption from applying where the value of immovable property in Hong Kong held by an investee company exceeds 10% of the value of its assets. Given that the infrastructure to which section 20AP(4) refers will generally require acquisition of land rights and construction of immovable property on the land, the effect of section 20AP(2)(a) is that Hong Kong infrastructure projects would not fall within the exemption if the value of the immovable property in Hong Kong held by an investee company exceeds 10% of the value of its assets.

[33] Section 20AP(4) of the Inland Revenue Ordinance.

[34] Greater Bay Area, Connectivity, https://www.bayarea.gov.hk/en/connectivity/key.html, accessed 9 July 2020.

The FSDC understands the policy intention for having the 10% threshold on immovable property investments in place. However, improvements can be made such that the restriction does not come at the expense of the burgeoning infrastructure landscape of Hong Kong. In view of the above, a distinction should be drawn between infrastructure and real estate for the purpose of recommending tax concessions or other incentives to promote infrastructure development in Hong Kong. The FSDC acknowledges that, as with any concession or incentive, any tax concessions or incentives introduced for infrastructure needs to be sustainable and robust.[35]

Infrastructure may be defined in a number of different ways. The World Bank takes a public policy-based perspective when defining infrastructure, the OECD uses a simple and general definition as a system of public works in a country, state or region, including roads, utility lines and public buildings, whereas other definitions look at classifying certain investments as infrastructure.

The FSDC has considered how various companies or organisations have defined infrastructure (see Appendix 2) and suggest revising the scope similar to the one as follows: *infrastructure is considered as the facilities, structures, networks, systems, plant, property, equipment, or physical assets that enable the services necessary to sustain or enhance the economy and society of Hong Kong. Infrastructure assets differ from real estate assets in that they are operating businesses which require a high level of expertise – both to manage the actual physical asset as well as to work with regulators and their local communities – to be successful.*

The FSDC would also like to reference and reiterate the recommendations made by the Hong Kong Green Finance Association (HKGFA) to review and revise certain tax policies and incentives in Hong Kong to cater for the various scopes of infrastructure, and to encourage investments in such projects. These recommendations were summarised below for ease of reference.[36]

- Expand the definition of “infrastructure” to include certain additional assets classes (e.g. data infrastructure), and those that are widely recognised by other jurisdictions (e.g. “new infrastructure”, non-Hong Kong “housing” properties, warehouses, logistic centres, etc.), and to include “incidental” components of an infrastructure project or asset (e.g. offices, employee dormitories, parking areas attached to the infrastructure).

- To cater for offshore (i.e. non-Hong Kong) infrastructure projects held directly by the fund, to revise the definition of “business undertaking for general commercial or industrial business purposes” in Section 20AM of the IRO and update paragraph 59 of the Departmental Interpretation and Practice Notes No. 61 to allow an infrastructure fund to engage directly in the construction or acquisition of infrastructure projects / assets, to the extent they satisfy the definition of “infrastructure”.

[35] In 2007, Spain implemented a series of concessions and investment incentives to drive foreign investment in renewable energy infrastructure. Following the Global Financial Crisis and the greater than expected uptake of the programme, Spain retracted some of its concessions in 2010, resulting in over 40 investor arbitrations commenced against Spain.

There have been approximately four ISDS decisions so far arising out of these disputes against Spain. Generally, the disputes focus around Fair and Equitable Treatment of the investor and investor’s Legitimate Expectations through the underlying treaty, the Energy Charter Treaty, which created opportunities between member states. The concessions and incentives proposed for Hong Kong should also consider any risks or liability if the concession or incentives are retracted after investors have already committed.

See also: https://www.iisd.org/itn/2019/06/27/spains-renewable-energy-saga-lessons-for-international-investment-law-and-sustainable-development-isabella-reynoso/, accessed 9 July 2020.

[36] See: https://www.hkgreenfinance.org/wp-content/uploads/2022/02/HKGFA-Green-InfrastructureInvestment-Report.pdf, accessed 4 February 2022.

- While this paper does not discuss the carried interest tax concession regime, before the implementation details are finalised, the FSDC agrees with the HKGFA that the regime should be extended to cover carried interest arising from such "qualifying assets"[37] should the scope of "qualifying assets" be expanded to cover private debt financing.

The above recommendations come at a particularly important time given Hong Kong's insufficient land supply and its impact on social and economic wellbeing. Putting aside the issue of insufficient space needed for new facilities and services, new infrastructure projects (be it standalone or more likely, mixed with real estate projects), should continue to be developed and pursued to support the future growth of Hong Kong.

The FSDC recommends amending the relevant section of the law to allow that infrastructure assets be excluded from the requirement in that section. Clarification should also be provided as to what assets comprise infrastructure and how non-infrastructure assets are to be identified and separated. To do this, the FSDC recommends the Government to develop a whitelist of socially important infrastructure projects that should make use of a tax concession or incentive. If designed, defined, and implemented well, this would provide more certainty to taxpayers, while still allowing some sort of restriction in lieu of a blanket exemption.

[37] As specified in Section 4(2)© and Section 4(2)(d) of Schedule 16D to the Inland Revenue Ordinance.

II. Attracting institutional investors by providing a level playing field in terms of taxation to each type of asset owners

Offering a level playing field to each class of asset owners is considered essential to bolster the asset and wealth management industry to new heights. It cultivates a fair and equitable environment to attract asset owner classes that are important institutional investors to invest in or through Hong Kong. **As such, the FSDC recommends that a taxation regime should be applied on a fair and equitable basis for each type of asset owners.** This section lays out the relevant tax regime recommendation details for asset owners including pension funds, endowment funds, family office investment vehicles, insurance companies, employee investment vehicles, and co-investment vehicles.

Pension funds

Over recent years, sovereign wealth and pension funds have emerged as an important investor class, with USD 56 trillion of retirement assets as at the end of 2020.[38] Pension funds hold the bulk of assets among institutional investors, accounting for approximately 57% of the market in 2020.[39] Private and public pension funds are the top two largest investors in private equity. According to the 2019 Preqin Global Private Equity & Venture Capital Report, pension funds continue to play a key role, with CPP Investment Board holding the largest allocation (USD 61.3 billion) to private equity of any investor globally. This is not surprising, as globally, pension fund assets are growing rapidly due to an increasing working population. Also, pension funds are breaking with tradition and looking to spread their investments across a much broader spectrum of investments and geographies, more so than ever before. Similar to other institutional investors like life insurance companies (see above) and sovereign wealth funds, pension funds have long investment horizons too. It is therefore important for Hong Kong's tax regime to be competitive and attractive to overseas pension funds, or at least place pension funds on equal footing as other institutional investors.

In reality, there is room for improvement in this regard. Under the UTE, where the pension fund of a company is managed or operated by its employees and/or beneficiaries who are also the "participating persons" of the fund, there is no certainty that the pension fund would be considered as a "fund". In other words, overseas pension funds that have set up wholly owned subsidiaries to be their own fund manager may not qualify as a fund, and therefore would not be entitled to the beneficial treatment otherwise provided under the UTE. This is problematic as it incentivises such pension funds to establish themselves, hold assets and potentially conduct value added activity elsewhere.

The FSDC recommends changes to the tax law to encourage pension funds to set up offices in Hong Kong for their in-house fund management arm. It considers one of the simplest ways of doing this is to extend the definition of a "fund" or create a definition of "qualified institutional investor" under the UTE to include (genuine) pension funds. More comprehensive work needs to be done to determine an appropriate definition for a genuine pension fund.[40] Likewise, further work should be done to ensure fund-of-one structures are covered under the definition of "fund" or "qualified institutional investor".[41]

[38] OECD, Pension fund assets rise despite the shock of COVID-19, 2021, https://www.oecd.org/pensions/globalpensionstatistics.htm, accessed 19 January 2022.

[39] OECD, Pension markets in focus 2021, November 2021, https://www.oecd.org/daf/fin/private-pensions/Pension-Markets-in-Focus-2021.pdf, accessed 21 January 2021.
BCG, The $100 Trillion Machine, July 2021, https://www.bcg.com/publications/2021/global-asset-management-industry-report, accessed 21 January 2022.

[40] Please refer to Appendix 3 for various definitions of "pension fund".

[41] Funds of one are commonly formed by large institutional investors (e.g. pension funds, insurance companies, endowment funds, and sovereign wealth funds). They are also used for practical reasons (e.g. client onboarding, or when limited partners invest through an alternative investment vehicle). If the IRD upholds its view in Departmental Interpretation and Practice Notes No. 61 issued on 30 June 2020 that "an arrangement intended to have one single investor only is unlikely an arrangement under which the capital contributions and profits or income are pooled and would not qualify as a fund", and effectively denies funds of one as a fund, it would be Hong Kong in a disadvantaged position in the region (as compared to Singapore), and internationally.

Endowment funds (and foundations, institutional investors that invest to advance their missions)

An endowment fund is typically an investment fund established by a not-for-profit organisation to invest capital that it has received in the form of donations to generate returns that can be used to support the organisation's ongoing operation.[42] Common examples of endowment funds include those established by prestigious universities in the United States (the Harvard endowment fund has approximately USD 53.2 billion of assets under management in the fiscal year of 2021), but are also used by certain religious organisations or charities. Notably, several of the largest endowment funds such as Harvard and Yale are managed by in-house professional fund management units.

It remains unclear whether endowment funds would qualify for the UTE in its current form due to the source of their capital and the way in which they are established; however, they carry out the type of activity that the UTE is seeking to attract to Hong Kong. **Therefore, the FSDC recommends that a specific provision should be included to treat endowment funds as a fund or a "qualifying institutional investor" under the UTE.**

Family office investment vehicles

"A family office is, in its simplest form, the private office for a family of significant wealth."[43] The estimated total AUM of USD 5.9 trillion attributable to family offices is equivalent to almost 8% of the total AUM for the world's asset management businesses as at the end of 2018.[44]

Asia Pacific is the largest owner of wealth in the world and home to the fastest billionaire population growth.[45] Hong Kong ranked third in terms of density of ultra-wealthy individuals – higher than jurisdictions such as Switzerland, Luxembourg and Singapore.[46] While this is the case, the family office concept is still relatively new in Asia as compared to the West. As the families look to have more control and management of their wealth, Hong Kong has the chance to make use of its position and seize the present opportunities to become a leading global and regional family office hub. In fact, estimates predict that assuming Hong Kong can attract 30% of new family offices that are set up in Asia every year, this will bring an additional AUM of USD 48.7 billion and generate additional spending of as much as USD 600 million (equivalent to 0.2% of GDP), which will compound over time.[47]

As mentioned, Hong Kong's position as an international financial centre and asset and wealth management hub, and as the gateway to Mainland China, already work to Hong Kong's advantage, distinguishing it from its closest competitors. Hong Kong's role in the Belt and Road and Greater Bay Area initiatives also makes it a distinctive location, and the FSDC is optimistic that there would only be more opportunities for Hong Kong to grow. Developing an environment that is conducive and business-friendly to family office operations for Hong Kong and Mainland Chinese families, as well as family office of other Asian and Western families would help enrich Hong Kong's current asset and wealth management ecosystem.

[42] Please refer to Appendix 4 for various definitions of "endowment fund".
[43] The Global Family Office Report, UBS 2019, https://www.ubs.com/global/en/wealth-management/uhnw/global-family-office-report/global-family-office-report-2019.html, accessed 9 July 2020.
[44] BCG estimates that the total AUM in the world is worth USD 74.3 trillion. See https://www.bcg.com/publications/2019/global-asset-management-will-these-20s-roar.aspx, accessed 9 July 2020.
[45] Billionaires report 2020, UBS, https://www.ubs.com/content/dam/static/noindex/wealth-management/ubs-billionaires-report-2020-spread.pdf, accessed 19 January 2022.
[46] Wealth-X, Ultra Wealthy Analysis: The World Ultra Wealth Report 2021, https://go.wealthx.com/world-ultra-wealth-report-2021, accessed 19 January 2022.
[47] The Global Family Office Report, UBS 2019, https://www.ubs.com/global/en/wealth-management/uhnw/global-family-office-report/global-family-office-report-2019.html, accessed 9 July 2020.

The FSDC has already highlighted the importance and need of a family office hub in Hong Kong in its paper, "Family Wisdom: A Family Office Hub in Hong Kong".[48] In this paper, the FSDC provided recommendations for development in the areas of regulatory requirements, tax considerations, talent development and setting up a one-stop liaison and service centre. The FSDC also understands that the HKSAR Government has recognised this weakness in Hong Kong's AWM ecosystem and has since been consulting with the industry and is seeking feedback on proposals for an attractive, effective, and easily implementable family office tax incentive framework. This was confirmed in the 2022-23 Budget Speech, during which the Financial Secretary proposed to provide tax concessions for eligible family investment management entities managed by single family offices. Subject to legislative process, he expects the relevant tax concessions to come into effect in the 2022/23 year of assessment. This proposal, together with the continued focus by the industry and FSDC on family offices and private wealth management, would all serve to enhance Hong Kong's attractiveness as a family office hub.

It is encouraging to see that the Government has taken steps to improve the related Hong Kong tax regime. Compared to Singapore, Hong Kong's current tax regime lacks attractiveness to family offices in certain aspects, as it does not have any specific regime that caters to the intricacies of a family office structure, nor does it include family offices explicitly as a specific or distinctive class of asset owners.[49] These should be addressed to optimise the operating environment for family offices in Hong Kong.

Looking more closely at the issue, under the prevailing tax law, a family office's investment vehicle would not typically qualify as a fund (as defined) under the UTE. Therefore, a genuine family office looking to set up operations in Hong Kong would not be able to make use of the tax exemption.

Further, the inherent deeming provisions[50] in the UTE are not family office friendly and would give rise to adverse tax implications to the family office members in Hong Kong. Typically, a family office would establish its own professional investment management arm to manage the family's investments. In such case, under the current tax laws, the Hong Kong based investment manager would be considered as an associate of the family members, who are stakeholders in the family office investment vehicle(s), invoking the deeming provision and giving rise to unintended adverse tax implications.

[48] See: https://www.fsdc.org.hk/en/insights/family-wisdom-a-family-office-hub-in-hong-kong. Accessed 27 January 2022.

[49] Singapore offers an extensive number of exemptions and incentives that could apply to a family office. Specifically, the following tax exemptions in Singapore are helpful to the family office structure:

- Capital gains safe harbour exemption (Section 13Z): gains upon disposal of an equity investment are not treated as trading income subject to the guidelines.
- Enhanced Tier Fund Scheme (Section 13X): reduces tax rate to 10% (from 20%) subject to the guidelines being met (at least SGD50 million (approximately HKD300 million) in assets, must incur at least SGD200,000 in annual business spending, fund is managed or advised by a fund management company in Singapore, fund employs at least 3 investment professionals in Singapore).
- Qualifying Foreign Trust Exemption (Section 13G): These trusts and their underlying holding companies are exempt from Singapore tax on certain income (interest, dividends, etc.) and distributions to beneficiaries of QFTs are exempted from Singapore taxes.

[50] The deeming provisions were aimed to prevent Hong Kong residents from abusing the profits tax exemption. Under the deeming provisions, if a Hong Kong resident investor holds a 30% or more beneficial ownership in the fund or is considered as an "associate" of the fund (as defined). In such cases, the Hong Kong resident investor would be required to report its/his/her percentage share of the Hong Kong sourced profits of a trading nature generated by the fund as taxable income in its/his/her own tax return.

The FSDC recommends a tax incentive or extending the tax exemption to include family office investment vehicles.

a) This can be achieved in the form of expanding the current scope of the UTE or introducing a specific tax exemption regime to attract family offices to Hong Kong. On the former, the FSDC recommends that the current UTE be extended to cover family-owned investment vehicles managed by genuine family offices. One way of doing this is to extend the definition of a "fund" or create a definition of "qualified institutional investor" to include a definition of family-owned investment vehicles managed by family offices.[51] It is important to keep the definition broad enough to include all genuine family offices' investment vehicles. The FSDC recognises that there is no simple or easy fix as there are many intricacies and complexities to consider. However, the potential solution should look to offer market players more tax certainty.

b) The FSDC recommends a complete removal of the current deeming provisions and sets out the rationale and recommendation for this in paragraphs under *section III - Addressing other deficiencies in the current UTE and OFC regimes* below.

c) The FSDC reiterates the policy recommendations on tax considerations in the FSDC paper, "Family Wisdom: A Family Office Hub in Hong Kong". In particular, the recommendations to introduce a more competitive tax treatment for family offices to retain and attract ultra-high net-worth (UHNW) families to set up and run their operations in Hong Kong. More specifically, the recommendations to (i) expand the current tax exemption regimes (e.g. UTE) to single family offices, and (ii) to align the tax treatment for local and overseas family offices.

Once a family office is set up in one jurisdiction, it would be very difficult to entice it to relocate to Hong Kong. As such, urgent action is needed for Hong Kong to stay competitive and capture the opportunities from new generations of wealth. However, the FSDC acknowledges that tax is just one of the many considerations a family office would take into account before setting up its operations in any jurisdiction. The FSDC notes that the ease and cost of compliance with the regulatory framework is another key factor.[52,53]

Insurance companies

The FSDC published a paper in March 2020, "Insuring Hong Kong's future – tax recommendations to enhance and grow Hong Kong's insurance industry", particularly those that work to help insurance companies as a class of asset owners. As mentioned in that paper, insurance companies are large employers, significant consumers of professional services, and are very large investors in a diverse range of assets.

[51] Please refer to Appendix 5 for the legal definition of "family office" in various jurisdictions.

[52] Hong Kong's licensing regime is activity-based and so there is no specific licensing regime for family offices. In January 2020, the Securities and Futures Commission (SFC) issued guidance on the licensing obligations of family offices conducting business in Hong Kong. Broadly, while the potential implications depend on how a family office operates, if the services provided by a family office do not constitute any regulated activity or they fall within any of the available carve-outs, it is not required to be licensed. In the Circular, the SFC acknowledges the unique operations of a single family office and provides that "where a family appoints a trustee to hold its assets of a family trust, and the trustee operates a family office as an internal unit to manage the trust assets, the family office will not need a licence because it will not be providing asset management services to a third party." Even if the single family office provides asset management services, given it is solely to related entities, the single family office is not required to be licensed. The FSDC is pleased to see the SFC make this clarification.

[53] Also see: FSDC, "Family Wisdom: A Family Office Hub in Hong Kong", 2020, https://www.fsdc.org.hk/sites/default/files/FSDC_Paper_No_45_-Family_Wisdom_A_Family_Office_Hub_in_Hong_Kong_Paper_Eng.pdf, accessed 4 August 2020.

The FSDC recommended a tax exemption on (a) the investment income of Hong Kong insurers if their insurance funds' assets are managed in Hong Kong. The context behind this was that the majority of insurance funds' assets are managed by non-Hong Kong based investment managers. This means that the investment income derived from such assets would not have been subject to tax in Hong Kong regardless. The FSDC emphasises that the proposed tax exemption should not lead to a significant loss of tax revenue in Hong Kong because a significant portion of the investment income of Hong Kong insurance companies should already be non-taxable. Yet, the proposed change may bring more investment management activities to Hong Kong, and support other industries, such as professional services, which would generate additional tax revenue and economic growth for Hong Kong as a whole. Indicatively, based on the experience of neighbouring markets, the FSDC expects that each asset management company of an insurance group could bring 5-10 investment professionals and another 5-10 non-investment positions. Again, this touches on the deeming provisions and the FSDC's recommendation to remove them in their entirety (see paragraphs under section III on removing the existing deeming provisions below).

The FSDC would also like to re-emphasise a second recommendation from the same paper, also on insurance companies. That is, (b) to address the tax issues faced by insurance groups with Hong Kong resident parent companies or regional holding companies / headquarters if they manage the assets of their overseas insurance group entities in Hong Kong. The current potential double taxation exposure (i.e. investment income of overseas subsidiaries taxed both in their respective jurisdictions and Hong Kong)[54] would adversely impact the insurance groups concerned and reduce Hong Kong's attractiveness as a regional insurance headquarter.

The FSDC recommends revisiting the applicability of the tax exemption to insurance companies. The proposed changes should help ensure the continued growth of the insurance sector, driving economic development and have overall benefits to Hong Kong.

[54] Under the current tax regime, when insurance groups with Hong Kong resident parent companies or regional holding companies / headquarters engage Hong Kong investment managers to manage the assets of and invest the cash arising from their overseas insurance subsidiaries, the relevant investment income would potentially be subject to double taxation.

Employee investment vehicles

Employee investment or co-investment plans have been for many years, a means for fund management companies to allow their key people to invest in the funds they create. Under the UTE, an employee investment vehicle is excluded from the definition of "fund" where the management team of a genuine fund consists of employees of the fund management group or a subsidiary, the employee investment vehicle does not qualify for the UTE under its definition.

For example, if a multinational fund management group (MNC) appoints its investment manager subsidiary company in Hong Kong to manage the group's employee investment vehicle, the MNC would not be confident that the UTE would apply to its circumstances if one or certain employees of the Hong Kong subsidiary is/are also investor in the group's employee investment vehicle. Considering this uncertainty and the potential tax exposure, the MNC may choose to appoint another investment manager subsidiary company outside of Hong Kong instead for managing not only the group's employee investment vehicle, but the main investment fund(s) too.[55]

The FSDC recommends extending the tax exemption to include employee investment vehicles. The Government should address this uncertainty to ensure that employee investment vehicles are treated on par with other investor classes. Specifically, tax policy and legislative changes should be made to Section 20 AM such that employee investment vehicles are explicitly included. Hong Kong should go a step further and consider measures to attract MNCs to come to Hong Kong to manage their employee investment vehicles and this change would be a positive first step in achieving this.

Co-investment vehicles

Co-investment vehicles are entities that invest alongside another (main) investor and as such, they are usually minority investments. They are commonly seen in private equity structures. Co-investment vehicles (whether these be in the form of a legal entity, contract or arrangement) should also be accorded the same tax treatment as the main fund it invests alongside. Otherwise, whilst the (main) fund can invest in Hong Kong private equities and enjoy UTE, a co-investment vehicle has no certainty that it could accord the same tax exemption. Further, a co-investor which itself is not an investment fund could face the disadvantageous "tainting" consequences. It would thus be extremely difficult for a Hong Kong fund manager to service the main fund if its investments would be co-invested by other investors, as the latter would also look for the same favourable tax treatments as the main fund, resulting in the attractiveness of using a Hong Kong fund manager for managing the main fund being impaired.

The FSDC recommends extending the tax exemption to include co-investment vehicles. If the main fund is tax exempt under the UTE, the co-investment vehicle should likewise be tax exempt.

[55] Section 20AM of the UTE contains further conditions to the definition of 'fund'. In particular, section 20AM(2)(b) provides that the participating persons must not have day-to-day control over the management of the property; and section 20AM(5)(c) prevents participating persons from being employees or former employees of a corporation in the same group of companies as the operator of the arrangement. The effect of these provisions, even if unintended, is to potentially prevent the exemption from applying to feeder funds or investment vehicles in which employees or specific types of investors may wish to invest. As such, this constraint creates a disincentive to types of funds and investors who may otherwise find Hong Kong to be an attractive place to organise and operate collective investing activities.

III. Addressing other deficiencies in the current UTE and OFC regimes

Creating streamlined and friendly UTE and OFC regimes

The scope of Hong Kong's exemption for privately offered funds regime has worked well since it was first introduced in 2006. The funds industry has welcomed subsequent amendments to the provisions, which have greatly expanded the scope of the exemption regime to include both offshore and onshore funds, as well as a broader category of eligible investments and asset classes.

However, the UTE does have some deficiencies. The way in which the UTE provisions have been drafted, and their interpretation by the IRD, has resulted in uncertainty at the fund and SPE level as well as for the industry as to their application to specific investor groups, such as pension funds, family offices and other investment vehicles.

These issues can be readily addressed as outlined below and maintain Hong Kong as the preferred jurisdiction in Asia for funds to establish their operations.

Expanding the scope of funds that can fall within the exemption

The scope of what constitutes a 'fund' as defined under the UTE (in section 20AM(2)) is on the face of it very broad, as it comprises an arrangement in respect of any property whereby the property is managed by or on behalf of the person operating the arrangement. This starting point is largely consistent with the definition of a collective investment scheme in Schedule 1 to the Securities and Futures and Ordinance.

However, the particular wording in the subsections of the definition creates uncertainty as to whether some common investment structures would qualify as a fund. Such wording also limits the ability of investing groups such as family offices, pension funds, employee investment schemes and separate investment arms within corporate groups from qualification for the exemption (as covered earlier).

Specifically, section 20AM(2)(a)(ii) refers to contributions made by persons ("participating persons" – i.e., investors) in the arrangement. As the reference to persons is in the plural, it is uncertain whether the definition allows for single investor funds, or to put it another way, a "fund-of-one". In DIPN 61, it notes that an arrangement should include different types of bona fide funds, regardless of the structure. However, that guidance also states that under very special circumstances, an arrangement may be accepted or may continue to be accepted as a fund even if it has only one investor at a certain point in time within a tax year. However, an arrangement intended to have only a single investor may not satisfy the pooling of capital requirement. This suggests that a single investor fund may not be regarded by the IRD to qualify as fund for the purposes of the UTE. This implies that the fund-of-one structure (which is commonly used by pension funds, insurance companies, endowments and sovereign wealth funds for engaging external fund managers for ring-fencing purposes) is denied under the exemption regime.[56] Additionally, fund-of-one structures are used for practical reasons (as client onboarding, accounting purposes or when investors invest outside a fund through an alternative investment vehicle / side car). There is considerable benefit to Hong Kong in encouraging these kinds of institutional investors to use Hong Kong fund managers. Note that this structural flexibility is well-recognised by other countries, such as Singapore.

[56] According to the Limited Partnership Fund Ordinance (which will come into operation on 31 August 2020), a limited partnership fund (or LPF) can be constituted with one general partner and at least one limited partner. This suggests that under the LPF regime, a "fund-of-one" is a fund, despite the IRD's view under DIPN 61.

Expanding the scope of permitted asset classes (particularly private investments) that can fall within the exemption

The Inland Revenue Ordinance (IRO) Schedule 16C, in its current form restricts the UTE to the category of assets as stipulated in that schedule. The asset classes include 'securities' (Part 1.1) and "shares, stocks, debentures, loan stocks, funds, bonds, or notes of, or issued by, a private company" (Part 1.2). Although the definition of securities is very broadly defined in Part 2 to include 'shares, stocks, debentures, loan stocks, funds, bonds, or notes of, or issued by, a body, whether incorporated or unincorporated….", the definition could still exclude some types of assets including but not limited to equity rights and convertible obligations issued by other commonly used non-corporate investment vehicles.

Such examples could include an 'equity' interest in a Japanese Tokumei Kumiai (TK) and an Australian Managed Investment Trust (MIT). A Japanese TK is a common investment vehicle used for real estate investing in Japan. A TK arrangement is a silent partnership structure and is not a corporate vehicle. An MIT is commonly used for private equity and real estate investing in Australia.

The inclusion of more types of assets to the current exemption scheme could attract more PE funds to be launched onshore. It is anticipated that for every US$100 billion under management, a Hong Kong domiciled fund would need to incur or spend at least 1% of its capital under management on payroll expenses and other service providers, i.e. US$1 billion.[57] With more fund managers basing their operations in Hong Kong, a higher percentage of operational costs would be deployed in Hong Kong, in turn, benefitting the financial services industry in terms of market vibrancy and talent readiness.

The FSDC therefore recommends legislative changes be made to ensure that fund-of-one structures are included in the definition of fund, so that fund-of-one structures can make use of the UTE. In addition, the FSDC recommends that the category of permitted asset classes in Schedule 16C is recommended be expanded to clearly include other types of investments in private entities including but not limited to, trusts and partnerships. This would then ensure that investments made by private equity funds in common private investment structures outside of Hong Kong would be covered by the UTE.

Removing the existing deeming provisions

A number of MNC corporate groups have both historically and more recently established investment arms, generally with a specific focus on investing in a related area. Although often drawing funding from different sources of capital than a typical "fund", these enterprises often operate, invest and control risk in similar ways, and yet would not benefit under the UTE. An MNC corporate group wishing to set up an investment arm in Hong Kong to manage the group's global investments may not qualify for exempt treatment under the UTE because of the likely source of the funding. Further, if the investments were directly or indirectly held by a Hong Kong company within the group, the deeming provisions under the UTE may operate to deem the investment gains as taxable in Hong Kong (see paragraphs under section II on the impact on the insurance sector).

[57] Reference is made to a FSDC paper published in 2015, titled "A Paper on Limited Partnership for Private Equity Funds". While the estimation is not scientifically deduced, it is still valid based on market feedback.

As mentioned previously, the FSDC believes that the existing deeming provisions are on the restrictive side, which makes the regime less attractive than it ought to be in today's international tax environment. The FSDC suggests a review of the existing deeming provisions. Most importantly, the FSDC recommends that the Government review whether the existing deeming provisions serve to promote key multinational institutional investors that are increasingly prominent in today's investment landscape, such as family offices, insurance groups, and other MNCs setting up regional headquarters / treasury centres in Hong Kong, or whether it can be refined and/or relaxed to encourage such investors to be set up in Hong Kong.

The FSDC recommends the complete removal of the deeming provisions. In comparison, the Singapore fund exemption regulations deal with the issue in a different manner. For one exemption (Section 13U, formerly Section 13X), there is no restriction on Singapore investors at all. In particular, the 13U regime has been used as an investment structure by family offices given the lack of restrictions on ownership.

Removing or refining the restriction on 'short-term assets'

For 'short-term assets', the minimum two-year holding period for specified securities in section 20AQ(3) to avail of an automatic exemption from tax is acknowledged and accepted. However, the limit under section 20AQ(3)(b)(ii) in the value of short-term assets held by an investee company where the investee company is held for less than two years unnecessarily complicates the UTE provisions.

Specifically, for both SPEs and parent funds the effect of section 20AQ(3)(b)(ii) is that the exemption will not apply where:

- The specified securities being sold have been held by the fund or SPE for less than 2 years;
- The fund or SPE has control over a portfolio company; and
- If the fund or SPE has control over the investee company, the aggregate value of that company's 'short-term assets' (irrespective of where they are situated) exceeds 50% of the value of the company's total assets.

'Short-term asset' is defined in section 20AP(4) as an asset that is not of a class specified in Schedule 16C, is not immovable property in Hong Kong, and has been held for less than consecutive 3 years before the date of disposal.

The FSDC recommends that either the restriction on 'short term assets' be removed altogether, or be restricted to Hong Kong assets with further clarification be provided on the nature of 'short term assets' which are the subject of the perceived mischief either through legislative amendments or through specific IRD guidance.

Streamlining the procedure for issuing certificates of resident status

The FSDC is pleased to see that currently, any special purpose entities (SPEs) owned by the fund are exempt in the same manner as the fund itself, without additional restrictions on the types of activities carried out by the SPE and restrictions on the types of assets qualifying for exempt treatment. However, an issue remains from only allowing limited activities (e.g. holding and administering investments) to be conducted at the SPE level in obtaining certificates of Hong Kong resident status or tax residence certificates (TRCs) from the Hong Kong IRD. There is currently broad concern throughout the investment management industry about the difficulty and length of time required to obtain TRCs. This difficulty arises for various reasons, but certainly a lower level of substantive activities in the company requesting the TRC, which would otherwise allow for exemption under the UTE, would compound such difficulties. Most investee jurisdictions require a TRC as a minimum to be granted treaty benefits.

As such, the FDSC recommends that a streamlined TRC procedure for SPEs be implemented (including providing guidance as to the level of activities that the IRD would expect to see in the context of a SPE under a fund) so that TRCs may be easily obtained in a matter of weeks rather than months.

Providing an exemption of Hong Kong stamp duty on the transfer of stocks in open ended fund companies (OFC)

An OFC is a limited liability company that operates as an investment vehicle and is managed by an SFC licensed manager. Unlike a limited partnership fund, OFCs are not limited to operate for only a stipulated period of time. OFCs are unique in their flexibility to create and cancel shares for investors' subscriptions and redemptions, which is not an option for conventional private companies. In order to qualify as an OFC, the entity must be a Hong Kong resident, and managed and operated in Hong Kong (i.e. all key decisions are made in Hong Kong). Essentially, OFCs provide another platform to establish an investment fund in Hong Kong and effectively diversifies the investment platform options in Hong Kong. However, since its launch in 2018, the OFC regime is far from being widely adopted. One of the reasons is that the transfer of shares of an OFC is subject to stamp duty. Recently the SFC announced amendments to the OFC Code including the removal of investment restrictions in order to enhance the attraction of OFCs to promoters and investors.

Given that a stamp duty exemption is available to the trading of shares in Exchange Traded Funds (ETFs), and the transfer of interest in a limited partnership fund set up under the newly enacted Limited Partnership Fund regime is also exempted from stamp duty, it would be logical to apply the same exemption to shares in OFCs. By nature, these shares and equity interest in an investment vehicle are similar and should enjoy equal tax exemptions. It would be punitive to not allow a stamp duty exemption to OFCs. The FSDC recommends that an exemption from Hong Kong stamp duty should apply on the transfer of OFC shares. Allowing OFCs to qualify for stamp duty exemption will enhance the attraction of OFC as a viable investment vehicle for investments in securities and other asset classes. This will further enhance Hong Kong's position as a place to establish funds and would encourage more capital into Hong Kong, thereby bolstering Hong Kong's position internationally as an asset management hub.

Conclusion

Hong Kong has historically been regarded as, and is still very much so, a premier global asset and wealth management centre and various steps have been taken to strengthen its position. In the past few years, the asset and wealth management industry has undergone many changes and there are already important and unique facets to the Hong Kong tax regime that should be retained.

However, with the hurried introduction of new international tax rules, a changing market, and fierce regional competition, the pace and scope of Hong Kong's development is coming under the spotlight. **The FSDC believes that further changes are needed to ensure Hong Kong retains and widens its leading position for future growth. In this paper, the FSDC have identified areas of priority or, quick fixes to be addressed first and are instrumental for Hong Kong to build a better asset and wealth management ecosystem.**

The FSDC is aware of the Government's concerns over the potential loss of tax revenue from the introduction of the above recommendations, especially those that propose to extend the UTE to a wider investor group and asset class. However, the FSDC would like to point out that asset and wealth management covers a diverse and broad spectrum of market players who have extensive choices in the arrangement of their business (including tax) affairs, and they will invariably have options that do not involve Hong Kong at all. The existing regime, to an extent, is not sufficient for attracting them to conduct their activities and making use of resources in Hong Kong. As such, the above recommendations should not result in exempting profits which are currently taxed in Hong Kong (as such profits are not currently in Hong Kong) and any potential loss of tax revenue would not be significant as a result of implementing the changes the FSDC proposes.

The FSDC acknowledges that the international tax landscape is constantly evolving, which may mean that these proposals need to be tweaked and refined before implementation. The FSDC hopes that that Hong Kong will continue to expand its tax treaty and Automatic Exchange of Financial Account Information (AEOI) network to facilitate growth of asset classes in broader markets. The FSDC has come up with the current proposals to provide an impetus for changes to the tax laws that are applicable to the industry, and ultimately, for the betterment of Hong Kong's economy and people.

Appendix 1 Key Hong Kong legislative developments relating to the asset and wealth management industry in recent years

Legislation	Subject matter	Enactment date
Inland Revenue (Amendment) (No.2) Ordinance 2015	• Extending the profits tax exemption for offshore funds to PE funds	17 July 2015 (gazettal date)
Securities and Futures (Amendment) Ordinance 2016	• Introducing the legal, regulatory and tax framework for an open-ended fund company regime in Hong Kong	10 June 2016 (gazettal date)
Inland Revenue (Amendment) (No. 2) Ordinance 2018	• Extending the profits tax exemption for offshore funds to onshore privately offered open-ended fund companies	29 March 2018 (gazettal date)
Inland Revenue Ordinance (Amendment of Schedule 16) Notice 2018	• Extending the profits tax exemption for offshore funds participating in the Innovation and Technology Venture Fund Corporation Scheme	22 June 2018 (date it came into operation)
Inland Revenue (Profits Tax Exemption for Funds) (Amendment) Ordinance 2019	• Unifying the profits tax exemption for a fund irrespective of whether the central management and control of the fund was exercised in Hong Kong or not • Unifying the profits tax exemption for a fund's investments in Hong Kong and non-Hong Kong private companies • Removing the ring-fencing features identified by the EU in respect of the offshore fund regime and offshore private equity fund regime	1 April 2019
The Limited Partnership Fund Ordinance	• Introduces a new registration regime for limited partnership funds to be established and operational in Hong Kong	31 August 2020
Inland Revenue (Amendment) (Tax Concessions for Carried Interest) Ordinance 2021	• Provides profits tax and salaries tax concessions in relation to eligible carried interest received by, or accrued to, qualifying persons and qualifying employees on or after 1 April 2020 from the provision of investment management services to certified investment funds • Expands the profits tax exemption to eligible classes of assets that may be held and administered by a special purpose entity (SPE) on behalf of a fund that owns the entity	7 May 2021

Legislation	Subject matter	Enactment date
Securities and Futures (Amendment) Ordinance 2021 Limited Partnership Fund and Business Registration Legislation (Amendment) Ordinance 2021	• Enables non-Hong Kong domiciled investment funds to be re-domiciled and registered in Hong Kong as open-ended fund companies (OFCs) or limited partnership funds (LPFs)	1 November 2021

Appendix 2 Various definitions of "infrastructure"[58]

Company / organisation	Definition of "infrastructure"
Global Infrastructure Company Classification Standard	The GICCS has developed a 4-pillar classification system of infrastructure companies for the purposes of including:[59] a. Business Risk Classification – infrastructure must be "used" to have value, this differentiates it other real-assets. The long-term contracts that sit behind the infrastructure determines its usability; b. Industrial Classification – 68 individual industrial subclasses or asset-level categories; c. Geo-economics Classification – global, national, regional and global infrastructure; d. Corporate-Governance Classifications – monitored v unmonitored project companies and corporates.
OECD Definition	Public infrastructure is defined as facilities, structures, networks, systems, plant, property, equipment, or physical assets – and the enterprises that employ them – that provide public goods, or goods that meet a politically mandated, fundamental need that the market is not able to provide on its own. … These services range from the traditional public-sector domains of defence, law enforcement, power generation, water, sanitation and transport to the social infrastructure, such as health care, social security, skills development, knowledge and innovation. The nature of the asset also varies from traditional fixed assets such as bridges and buildings to ICT architecture. In addition, sound public infrastructure is a key driver of enhanced capacity for real economic growth, both in the short and long terms. Infrastructure networks reduce the effect of distance, help integrate markets, and provide the necessary connections to international markets. These networks are also trade enhancing, especially when it comes to exports. Infrastructure services such as energy and water are critical inputs in production chains, the availability and quality of which determine both the quantity and price of outputs.[60]
OECD Glossary of Statistical Terms	The system of public works in a country, state or region, including roads, utility lines and public buildings.[61]
World Bank Definition[62]	1. Collection and Transport- Waste Collection, Waste Transport, and both 2. Treatment/Disposal -Sorting and Recycling, Mechanical and Biological Treatment, Incineration/ Waste to Energy, and Sanitary Landfill 3. electricity - generation, transmission, and distribution 4. natural - gas Transmission and distribution

58 See: https://www.hkgreenfinance.org/wp-content/uploads/2022/02/HKGFA-Green-InfrastructureInvestment-Report.pdf, accessed 4 February 2022.
59 The Infrastructure Company Classification Standard (TICCS) https://edhec.infrastructure.institute/wp-content/uploads/2018/10/TICCS_2018_light.pdf
60 OECD, 'Towards a Framework for the Governance of Infrastructure' https://www.oecd.org/gov/budgeting/Towards-a-Framework-for-the-Governance-of-Infrastructure.pdf
61 The Infrastructure Company Classification Standard (TICCS) https://edhec.infrastructure.institute/wp-content/uploads/2018/10/TICCS_2018_light.pdf
62 Ibid.

Company / organisation	Definition of “infrastructure”
World Bank Definition	5. ICT – ICT backbone like hard infrastructure cable assets (such as fiber optic networks and other types of broadband networks) where the government is involved either through being a contracting authority (i.e. a party to a concession agreement), the owner of the assets, or some other form of government support 6. airports - runway and terminal 7. ports - channel dredging and terminal 8. railways - fixed assets, freight, local passenger/light rail, and regional passenger 9. roads - bridge, highway, and tunnel 10. treatment plant – potable and sewerage treatment plants 11. utilities – water utilities with and without sewerage service, sewer age collection and treatment
IPF Research definition[63]	The definition of what constitutes real estate can be imposed on a top down basis, for example by asset allocation processes or by reference to a set of common characteristics. Type of land and building alone seems insufficient. A better focus would be on the factors that drive risk and return: source of income, exposure to operational risk, legal structure and institutional factors. Infrastructure, for example, includes buildings and other structures on land that create cashflows. Their land and physical structure give these a real estate component but the distinct ‘project risk’ element to infrastructure is frequently seen as a different source of risk from real estate, reflecting the regulatory/policy and operational risks of infrastructure cashflows and the specific characteristics of infrastructure projects.
UBS Asset Management definition	Infrastructure is defined as the permanent facilities and structures that a society requires to facilitate the orderly operation of its economy. Examples include:[64] a. Transportation such as toll roads, airports, ports, bridges, tunnels and rail b. Utility and energy infrastructure such as water and wastewater services, power generation, electricity and gas networks and fuel storage facilities c. Communications infrastructure such as transmission towers and fibre networks d. Social infrastructure such as education, recreation, waste management and healthcare facilities.

[63] IPF Research Programme, What Constitutes Property for Investment Purposes? A Review of Alternative Real Estate Assets, https://www.ipf.org.uk/resourceLibrary/what-constitutes-property-for-investment-purposes--a-review-of-alternative-real-estate-assets--february-2015-.html

[64] UBS Asset Management, 'All you need to know: About Infrastructure', https://www.ubs.com/global/en/asset-management/insights/asset-class-research/real-assets/2018/2018-09-pfi-extract-infrastructure/_jcr_content/mainpar/toplevelgrid/col1/teaser/linklist/actionbutton.1742416867.file/bGluay9wYXRoPS9jb250ZW50L2RhbS9hc3NldHMvYW0vZ2xvYmFsL2luc2lnaHRzL2Fzc2V0LWNsYXNzLXJlc2VhcmNoL3JlYWwtYXNzZXRzL3JlYWwtZXN0YXRlLWdsb2JhbC9kb2MvcGZpLWV4dHJhY3QtaW5mcmFzdHJ1Y3R1cmUucGRm/pfi-extract-infrastructure.pdf

Company / organisation	Definition of “infrastructure”
Callan Definition[65]	In general, infrastructure facilitates the movement of people, goods, and ideas, and it is essential for the economic productivity of a society. Infrastructure assets commonly have many of the following characteristics: a. Long and useful lives; b. Monopoly market position or high barriers to entry; c. Operation in a regulated environment or other resistance to economic cycles; d. Stable cash flows, often linked to inflation; e. Difficult to replicate due to high construction costs or scarcity of resources (i.e., land, equipment, or planning restrictions). Infrastructure assets differ from real estate assets in that they are operating businesses which require a high level of expertise—to manage the actual physical asset as well as to work with regulators and their local communities—to be successful. Similar to real estate, though, investors are interested in the predictable stream of distributions from operations over a long horizon of asset ownership.
Kempen definition[66]	Infrastructure typically involves heterogeneous, tangible assets that are essential to the functioning of the economy and/or society. Furthermore, infrastructure assets often occupy a natural monopoly or oligopoly position due to the high entry barriers (such as high initial capital requirements and location), which leads to lower competition (or the threat of it). Infrastructure typically involves long-term contracts with reliable counterparties who use the assets in question. Moreover, infrastructure assets often have a long life. Combined with long-term contracts, this creates greater predictability and/or certainty about future cashflows. Kempen infrastructure classification "In order for something to be classed as infrastructure, it must involve physical assets that fulfil an essential role in (enabling) the functioning of the economy or society. For instance, we do not consider telecom companies to be infrastructure. These are commercial companies that aim to maximise their profits: they experience a great deal of competition and are highly sensitive to the economic cycle. Yet telecom companies use essential infrastructure networks, such as masts, which we do class as infrastructure. To give another example: we count airports as infrastructure (regulated, partial monopolies, reasonably stable incomes), but not airlines (unregulated, cyclical income, risky). Other examples are ski lifts or football stadiums. We do not include these assets in the infrastructure asset class."

[65] Callan Institute, 'Infrastructure—No Longer a Niche Option' https://www.callan.com/wp-content/uploads/2018/07/Callan-Infrastructure-Paper.pdf
[66] Kempen, 'Infrastructure White Paper' https://www.kempen.com/-/media/News-and-Knowledge/Whitepapers-en-Artikelen/White-paper-infra-vEN-DEF.pdf

Company / organisation	Definition of “infrastructure”
Morgan Stanley[67]	Infrastructure is the tangible assets (i.e. land and structures) that provide essential services to society and help the economy to function and grow. It is the essential, “mission critical” nature of these assets which makes infrastructure such an attractive investment—as a result of their essentiality, as well as the capital intensity of the assets (infrastructure assets typically require large amounts of upfront capital to build and maintain), infrastructure project companies typically operate in an environment with little demand elasticity over a business cycle, as well as with little competition. As an example, utility services such as providing drinking water or electricity will always be needed regardless of underlying economic demand. Due to the potentially exorbitant cost of re-creating/duplicating a utility-scale network throughout a large urban area, not to mention the political and popular resistance to zoning and siting duplicative water pipes, transmission lines, transformer stations, etc., such infrastructure assets tend to operate in a monopoly market position in the jurisdictions in which they provide services. The common attributes of infrastructure investments are: essential to society or the economy; long, useful lives; monopoly/quasi-monop-oly market position or high barriers to entry; operate in regulated environment and/or resistance to business cyclicality; can produce more stable, predictable cash flows, often linked to inflation; are difficult to replicate due to high construction costs and scarcity of resources.
Infrastructure South Australia[68]	Defined as: "Infrastructure is the physical assets and structures that enable the services necessary to sustain or enhance the economy and liveability of South Australia." This includes road, rail and ports, health, cultural, sports, tourism and education facilities, and water and waste utilities. Increasingly, it includes digital connectivity infrastructure and other physical assets that can act as enablers for industry and other sectors of the economy. Both public and privately-owned infrastructure are in scope.

[67] Morgan Stanley, 'The Case for a Strategic Allocation to Global Listed Infrastructure Securities' https://www.morganstanley.com/im/publication/insights/in-vestment-insights/ii_globallistedinfrastructure_en.pdf

[68] Infrastructure South Australia, ‘20-Year State Infrastructure Strategy Discussion Paper’ https://infrastructure.sa.gov.au/our-work/20-year-strategy/-discussion-paper/Discussion-Paper-Text.pdf

Appendix 3 Various definitions of "pension fund"

Jurisdiction	Definition of "pension fund" or equivalent
Australia	(Source: Commonwealth Consolidated Acts) Superannuation fund – a fund that is an indefinitely continuing fund and is a provident, benefit, superannuation or retirement fund or a public sector superannuation scheme.
UK	(Source: Pension Schemes Act 1993) Categories of pension schemes: **Occupational pension scheme** - is any scheme or arrangement which is comprised in one or more instruments or agreements and which has, or is capable of having, effect in relation to one or more descriptions or categories of employments so as to provide benefits, in the form of pensions or otherwise, payable on termination of service, or on death or retirement, to or in respect of earners with qualifying service in an employment of any such description or category. **Personal pension scheme** – is any scheme or arrangement which is comprised in one or more instruments or agreements and which has, or is capable of having, effect so as to provide benefits, in the form of pensions or otherwise, payable on death or retirement to or in respect of employed earners who have made arrangements with the trustees or managers of the scheme for them to become members of it. **Public service pension scheme** – is an occupational pension scheme established by or under an enactment or the Royal prerogative or a Royal charter. *Pension savings are technically "pension schemes" rather than pension funds but the terms are used somewhat interchangeably.
US	(Source: Department of Labor) **Pension plan (retirement plan)** - designed to provide funds to retirees. Defined contribution plan is one in which the employer makes specified contributions but the amount of the retirement benefit is not specified and may be wholly or partially funded by employers. Defined benefit plan is a retirement plan that uses a specific, predetermined formula to calculate the amount of an employee's future benefit. In the private sector, defined benefit plans are typically funded exclusively by employer contributions. In the public sector, defined benefit plans often require employee contributions.

Appendix 4 Various definitions of "endowment fund"

Jurisdiction	Definition of "pension fund" or equivalent
Australia	(Source: Philanthropy Australia) **Charitable endowment funds** - a type of public fund often referred to as an "umbrella" fund. Generally maintained by a trustee company or financial services company, a charitable endowment fund will be able to maintain donor accounts (sometimes referred to as 'sub-funds') which can be maintained in perpetuity and offer a tax deduction to donors. Endowment - a capital fund, usually invested in perpetuity, to provide income for grantmaking purposes.
UK	(Source: Charity Commission for England and Wales Operational Guidance) **Expendable endowment** - a fund that must be invested to produce income. Depending on the conditions attached to the endowment, the trustees will have a legal power to convert all or part of it into an income fund which can then be spent. An expendable endowment differs from an income fund in that there is no actual requirement to spend the principal for the purposes of the charity unless or until the trustees decide to. However, income generated from expendable endowment is no different from income generated from permanent endowment, and should be spent for the purposes of the charity within a reasonable time of receipt. If there is really no evidence, either direct or circumstantial, as to a donor's intention, then a gift should be treated as income. (See also Permanent endowment). **Permanent endowment** - property of the charity (including land, buildings, cash or investments) which the trustees may not spend as if it were income. It must be held permanently, sometimes to be used in furthering the charity's purposes, sometimes to produce an income for the charity. The trustees cannot normally spend permanent endowment without the Charity Commission authority. The terms of the endowment may permit assets within the fund to be sold and reinvested, or may provide that some or all of the assets are retained indefinitely (for example, a particular building).
US	(Source: Clifford Chance US) **Endowment fund** - refers to a pot of funds with permanent duration held by an institution; generally, the corpus is invested and the investment income is expendable by the institution. An endowment can be created by request of a donor or by designation of the board of directors of a corporation. While there are many regulations applying to the management, investment and use of endowment funds, the majority of these are concerned with endowment funds created at the request of a donor and aim at protecting a donor's intentions.

Appendix 5 Legal definition of “family office” in various jurisdictions

Jurisdiction	Definition of “family office”	Definition of “family”
British Virgin Islands	According to Banks and Trust Companies (Amendment) Act, 2018, Section 10 amendments indicate that the Regulatory Code 2009 may be updated to define the nature and scope of family operated businesses and other closely held group business.	Under Regulatory Code 2009 Division 3 - Risk Management, “close family member”, in relation to a person, means the person’s: a) spouse; b) children, including adopted children; c) parents, including step parents; d) brothers or sisters, including step brothers or sisters; or e) grandchildren.
Jersey	The Family Office Council - a membership group for single family offices - defines a single-family office as a private organisation that manages the investments for a single wealthy family. The assets are the family’s own wealth, often accumulated over many family generations.	Under the Financial Services (Jersey) Law 1998, for the purposes of sale of company in Schedule 2 Part 1: • “close relative” means a person’s spouse or civil partner, children and step-children, parents and step-parents, brothers and sisters and step-brothers and step-sisters Under the Money Laundering (Jersey) Order 2008 under enhanced customer due diligence, an immediate family member of a person mentioned in sub-paragraph (a), including any of the following – i. a spouse, ii. a partner, that is someone considered by his or her national law as equivalent or broadly equivalent to a spouse, iii. children and their spouses or partners as defined in clause (ii), iv. parents, v. grandparents and grandchildren, vi. siblings.
Hong Kong	Not defined	Under the Securities and Futures (Professional Investor) Rules, "associate" in relation to an individual means the spouse or any child of the individual. Under Schedule 1 of the Securities and Futures Ordinance "associate" in relation to a person means, amongst other things, the spouse, or any minor child (natural or adopted) or minor step-child, of the person.

Jurisdiction	Definition of “family office”	Definition of “family”
Singapore	The term "single family office" (SFO) is not defined under the Securities and Futures Act (SFA). An SFO typically refers to a legal entity which manages assets for or on behalf of only one family and is wholly owned or controlled by members of that same family.	The term ‘family’ in the single-family office may refer to individuals who are lineal descendants from a single ancestor, as well as the spouses, ex-spouses, adopted children and stepchildren of these individuals.
Switzerland	The term "family office" has no legal definition in Switzerland. In essence, all legal forms provided by law for commercial purposes are permissible. However, companies limited by shares, in other words public or private limited companies (AG or GmbH) are preferred for the simplicity they offer for the ownership structure of a family office.	

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About the FSDC

The FSDC was established in 2013 by the Hong Kong Special Administrative Region Government as a high-level, cross-sectoral advisory body to engage the industry in formulating proposals to promote the further development of the financial services industry of Hong Kong and to map out the strategic direction for the development.

The FSDC has been incorporated as a company limited by guarantee with effect from September 2018 to allow it to better discharge its functions through research, market promotion and human capital development with more flexibility.

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