HK FINANCIAL SERVICES DEVELOPMENT COUNCIL 香港金融發展局

FSDC Paper No. 18

A Paper on the Tax Issues on Open-ended Fund Companies and Profits Tax Exemption for Offshore Private Equity Funds

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A) Executive Summary

1. The Financial Services Development Council (FSDC) published proposals on 18 November 2013 including: (i) Proposals on Legal and Regulatory Framework for Open-ended Investment Companies in Hong Kong and (ii) Synopsis Paper Proposing Tax Exemptions and Anti-avoidance Measures on Private Equity Funds in the 2013-14 Budget. This Paper sets out the FSDC's recommendations on two topics, both of which are consistent with the FSDC's proposals published on 18 November 2013.

   (a) The open-ended fund companies (OFCs) tax framework in Hong Kong; and
   (b) The profits tax exemption for offshore private equity (PE) funds enacted on 17 July 2015[1]

The OFCs tax framework in Hong Kong

2. The FSDC recommends that:

   (a) There should not be any restriction or stipulation on the residency of directors on the board of any private OFC thus allowing a private OFC to be centrally managed and controlled in Hong Kong to be eligible for the profits tax exemption if the relevant exemption conditions are satisfied.

   (b) Both public and private OFCs should be exempt from stamp duty.

3. The above two recommendations are consistent with the tax framework proposals set out in the FSDC's Proposals on Legal and Regulatory Framework for Open-ended Investment Companies in Hong Kong issued on 18 November 2013 and are important for Hong Kong's OFC tax framework. The OFC tax framework should create competitive conditions for setting up the OFCs in Hong Kong compared to other global investment fund centres. To achieve this, the OFC tax framework should be tax neutral, maintain a level playing field with other types of investment vehicle commonly used by fund managers particularly unit trusts, and at all times – to put the interest of investors first and to facilitate good corporate governance.

The profits tax exemption for offshore PE funds

4. The FSDC makes two recommendations.

   First Recommendation: In determining whether or not a PE fund is "bona fide widely held", the criteria should be relaxed. A PE fund will be regarded as "bona fide widely held" if one of the two conditions below is satisfied:

[1] As the Inland Revenue (Amendment) (No. 2) Ordinance 2015.

a. no person holds a participation interest of 20% or more in the non-resident fund; or
b. there are no five or fewer persons with a combined participation interest of at least 50% in the non-resident fund.

5. These recommended conditions are largely in line with the latest practices of comparable jurisdictions that have investment manager exemptions or regimes.

6. Second Recommendation: The "bona fide widely held" concession should be extended to the following specified types of entities which are genuinely widely held entities:

   (a) sovereign wealth funds
   (b) pension funds that comply with the requirements / regulations of certain stipulated jurisdictions
   (c) central banks
   (d) government agencies; and
   (e) the special purpose vehicles for investments set up and controlled by (a) to (d) above.

7. The revised Departmental and Interpretation Practice Note No. 43 (DIPN 43) to be issued by the Inland Revenue Department (IRD) should include a non-tainting rule and clarify that in certain situations, the profits derived by a profits tax exempt fund from disposals of investments in excepted private companies (EPCs) (as defined) (either through a special purpose vehicle or disposal of the EPC itself) will continue to be eligible for the profits tax exemption, despite its investment(s) in a private company, which is not an EPC. The assessability of the profits from the investment in the private company, which is not an EPC would be subject to the ordinary assessing provisions of the Inland Revenue Ordinance.

8. The FSDC also sets out in this Paper other issues to be addressed and/or clarified by the IRD.

B) Tax Issues on Open-ended Fund Companies

9. This section of the paper summarises the FSDC's recommendations for the OFCs tax framework in Hong Kong with reference to the FSDC's Proposals on Legal and Regulatory Framework for Open-ended Investment Companies in Hong Kong issued on 18 November 2013, and the Financial Services and the Treasury Bureau (FSTB) of the Hong Kong Government's public consultation paper on OFCs issued in March 2014.

10. In coming up with these recommendations, the FSDC has paid due consideration to the criteria:

    - the OFC tax framework should create competitive conditions for setting up the OFCs in Hong Kong compared to other global investment fund centres;
    - the OFC tax framework should be tax neutral
    - the desire to maintain a level playing field with other types of investment vehicle commonly used by fund managers, in particular unit trusts;
    - at all times to put the interest of investors first; and
    - at all times to facilitate good corporate governance.

11. This paper sets out two recommendations[2] summarised below, both of which will be addressed in turn:

    - There should not be any restriction or stipulation on the residency of directors on the board of any private OFC thus allowing a private OFC to be centrally managed and controlled in Hong Kong to be eligible for the profits tax exemption if the relevant exemption conditions are satisfied.
    - Both public and private OFCs should be exempt from stamp duty.

Board of directors / Central management and control

12. The OFC framework provides an alternative for fund managers to set up Hong Kong (or "onshore") domiciled funds. To be on par with the other common types of offshore investment vehicles currently used by fund managers (e.g. offshore companies and unit trusts), it is essential for the OFC to be tax neutral, and to do so, private OFCs should

[2] Both of these recommendations are consistent with the tax framework proposals set out in the FSDC's Proposals on Legal and Regulatory Framework for Open-ended Investment Companies in Hong Kong issued on 18 November 2013.

benefit from the profits tax exemption currently available to offshore domiciled funds and on the same conditions.

13. However, unlike offshore domiciled funds, the FSDC recommends that the central management and control of Hong Kong domiciled private OFCs can take place in Hong Kong, and in doing so, the private OFC can have any number or proportion of Hong Kong resident directors (including 100% Hong Kong resident directors) as opposed to a requirement of a majority non-Hong Kong resident directors. The Inland Revenue Department (IRD) and the rules / guidelines should not stipulate that the OFC must have non-Hong Kong resident directors on its board. Doing so would seriously impede the use of the OFC as a **Hong Kong domiciled** investment fund vehicle *[note: emphasis added]* and would go against the objective and spirit of the government policy to attract and retain talent of relevant competency in Hong Kong. It would represent a step back in developing Hong Kong as an international investment fund hub.

14. While the IRD acknowledges in its Departmental Interpretation and Practice Notes No. 43 (Revised) (**DIPN 43**) that the location of "central management and control" is wholly a question of fact, and that the residence of individual directors is generally not relevant in determining the locality of a company's central management and control, the onus is still on the offshore domiciled funds to prove that no one in Hong Kong manages and controls the fund by himself/herself/themselves. Thus in practice, many offshore domiciled funds that enjoy the current offshore funds tax exemption under the Revenue (Profits Tax Exemption for Offshore Funds) Ordinance 2006 would have entirely or majority non-Hong Kong resident directors. However, it would not be reasonable to expect a Hong Kong domiciled fund vehicle to be centrally managed and controlled offshore and, as such, this should not be a prerequisite for private OFCs.

15. Having the private OFC centrally managed and controlled in Hong Kong would be conducive to and advance the development of corporate governance in Hong Kong as it would be much easier for the regulators to contact directors based in Hong Kong than directors resident offshore, translating to better supervision. It would also allow regulators to have better investigatory and enforcement powers in addition to their supervisory powers, thereby reinforcing the robust regulatory regime and investor protection aspects for Hong Kong and OFCs.

16. Similarly, having Hong Kong based directors who are responsible for the central management and control of OFCs would provide a heightened sense of accountability and responsibility to the Hong Kong investing public / professional investors.

Anti-tax avoidance

17. To avoid any potential abuse of the current offshore funds exemption regime, section 20AE of the Inland Revenue Ordinance already provides sufficient and effective

safeguards (as set out in the "deeming provisions"). The Inland Revenue (Amendment) (No. 2) Ordinance 2015 has refined, expanded, and/or added to the definitions of certain terms like "associates", "associated partnerships", "control", "principal officer", etc. By doing so, the Hong Kong legislature has not only recognised the inherent complexities of fund structures, but has tightened the applicability of the "deeming provisions" to mitigate tax avoidance. The deeming provisions, together with the general anti-avoidance provisions in the Inland Revenue Ordinance (section 61A) as extended to cover private OFCs, should be adequate to address the IRD's concerns over tax avoidance.

18. Also, given that the FSTB has already pledged to support the Common Reporting Standard for Automatic Exchange of Financial Account Information in Tax Matters (**CRS**) in the future, the IRD should be able to better track the investors of OFCs in case they wish to investigate the tax residency of an investor. This should address any further potential tax avoidance concerns.

19. In order to provide additional comfort to the IRD in relation to anti-tax avoidance, the FSDC would like to highlight that any private OFC seeking profits tax exemption treatment can be subject to the requirement that the relevant OFC is managed by a SFC licensed corporation or registered institution.

20. This recommendation not only helps promote good corporate governance in Hong Kong, but also helps stimulate a "brain gain" by promoting Hong Kong as a talent pool for asset managers and competent directors in the industry[3].

21. Other than our recommendation that the central management and control (CMC) can be in Hong Kong, the framework of the profits tax exemption regime for private OFCs should, to an extent and where relevant, mirror the profits tax exemption under sections 20AC and 20ACA of the Inland Revenue Ordinance (the current offshore fund tax exemption). That is:
    (a) the OFC carries out specified transactions;
    (b) such specified and incidental transactions are arranged by or carried out through a specified person;
    (c) the income from incidental transactions is less than 5% of total trading receipts of the OFC; and
    (d) the OFC has no other business in Hong Kong.

22. The FSDC recommends that the tax exempt investments for private OFCs could follow the scope of "specified transactions" under the current offshore funds tax exemption. Likewise, the definition of "specified person" should also follow the definition under the current offshore funds tax exemption.

[3] By way of example, the available pool of experienced responsible officers and executive officers for SFC licensed corporations and registered institutions is not currently very deep.

Stamp duty

23. To position the OFC regime to be competitive with other jurisdictions[4] and attractive to fund managers, as noted above it is imperative for the OFC to be tax neutral. Not only should the OFC be exempt from Hong Kong profits tax, there should also be a stamp duty exemption for both public and private OFCs on the sale, purchase or transfer of shares in both public and private OFCs, similar to the current stamp duty exemption granted to exchange traded funds (**ETFs**).

24. For unit trusts, the current remission regime provides a stamp duty exemption on the sale or purchase of a unit in a unit trust scheme, which involves a redemption by way of extinguishing the unit; or if the manager of a unit trust scheme sells to a new unit-holder a unit which arises from a transfer of a unit to the manager within the preceding two months or the unit sold is a new unit. Given shares in OFCs and units in unit trusts are quite similar, we agree that they should be treated the same way for stamp duty purposes. However, going a step further, we suggest the abolishment of stamp duty on a transfer of shares in an OFC to provide the necessary impetus and platform for growth as this would allow secondary transactions in the OFC providing greater flexibility, and appeal, for investors.

25. Levying stamp duty on the transfer of shares in OFCs would make the OFC an unattractive investment fund vehicle. It could discourage the setup of funds in Hong Kong, which would go against the spirit of the OFC regime. In respect of using an OFC as a means to avoid paying stamp duty for the transfer of the underlying investments, the FSDC views that the risk of this is practically remote. Establishing an OFC for purposes of avoiding stamp duty is quite burdensome in comparison to other alternatives, such as simply setting up an intermediate offshore company, given the amount of regulatory and legal efforts involved in the OFC regime.

[4] Transfers in other jurisdictions are not subject to stamp duty and therefore in order for the OFC regime to be attractive, it is necessary for the OFC to be exempt from stamp duty on allotment, redemption, transfers, and surrenders, for both public and private OFCs.

Other matters for consideration – Central management and control criteria under current offshore fund tax exemption

26. Separately, with an overarching intention to make Hong Kong into an even more competitive platform for fund managers to thrive and to provide sufficient incentives for talent of relevant competency to stay in Hong Kong, the FSDC considers that the CMC criteria under the current offshore fund tax exemption could be relaxed and be aligned with the recommendations for Hong Kong domiciled private OFCs as set out in paragraphs 5 to 8 above.

C) **Tax Issues on Profits Tax Exemption for Offshore Private Equity Funds**

The definition of "bona fide widely held"

<u>Background</u>

27. As far as profits tax exemption for offshore funds is concerned, the term "bona fide widely held" is used in sections 20AE(8) and 20AF(7) of the Inland Revenue Ordinance (IRO). Under these two sections, if the Commissioner is satisfied that the beneficial interests in an offshore fund qualifying for profits tax exemption are bona fide widely held, the deeming provisions in sections 20AE and 20AF will not apply in relation to the resident person who has a direct or indirect beneficial interest in the fund.

28. The term "bona fide widely held" is not defined in the IRO. In the Departmental Interpretation and Practice Notes (DIPN) No. 20 and 43, the IRD has indicated that the term will be interpreted as follows:

    (a) during the year of assessment in question, at no time did fewer than 50 persons hold (or have the right to become the holders of) all of the participating units, shares or interests in the non-resident fund; and

    (b) at no time during the year did fewer than 21 persons hold (or have the right to become the holders of) participating units, shares or interests that entitled the holders, directly or indirectly, to 75%, or more, of the income or property of the non-resident fund.

<u>Recommendations</u>

1. Recommendations on the "bona fide widely held test"

29. We consider that in the context of private equity (PE) funds, the requirements in (a) and (b) above should be relaxed. PE funds are typically not held by a large group of investors, therefore it will be difficult for PE funds to meet the benchmarks in (a) and (b) above. If the requirements in (a) and (b) are not relaxed, it is likely that the deeming provisions in section 20AE or 20AF will apply in relation to a resident person who has a direct or indirect beneficial interest in a tax exempt offshore PE fund if he fails the "30% beneficial interest test" or "associate test" despite there being no intention for tax abuse.

30. We therefore recommend that in the context of PE funds, the following options be considered and one of them be selected as the appropriate test (instead of the criteria in (a) and (b) above) for determining whether a PE fund is "bona fide widely held":

    <u>Option 1:</u>

A PE fund will be regarded as "bona fide widely held" if both of the following two conditions are satisfied:

(i) during the year of assessment in question, at no time did fewer than 10 persons hold (or have the right to become the holders of) all of the participating units, shares or interests in the non-resident fund; and

(ii) at no time during the year did fewer than 5 persons hold (or have the right to become the holders of) participating units, shares or interests that entitled the holders, directly or indirectly, to 75%, or more, of the income or property of the non-resident fund.

Option 2:

A PE fund will be regarded as "bona fide widely held" if one of the two conditions below is satisfied:

(i) no person holds a participation interest of 20% or more in the non-resident fund; or

(ii) there are no five or fewer persons with a combined participation interest of at least 50% in the non-resident fund.

31. The recommended options are largely in line with the latest practices of countries that also have investment manager exemptions or regimes.

32. For example, in the UK, the fund will be regarded as "widely held" if either no majority interest in the fund is ultimately held by five or fewer persons and persons connected with them, or no interest of more than 20% is held by a single person and persons connected with that person.

33. Similarly, the "widely held test" in the context of the Australian Investment Manager Regime requires that no member of the fund holds a participating interest of 20% or more, or there are no five or fewer members with a combined participation interest of at least 50%.

34. In Singapore, there are no "widely held" or "closely held" tests per se as there are generally no restrictions on the total number of investors of a fund. However, under the Singapore Resident Fund Scheme and the Offshore Fund Tax Exemption Scheme, the fund cannot be 100% owned by "Singapore persons" (basically any Singapore resident individual or entity). In addition, for a fund with fewer than 10 investors, if a Singapore resident non-individual investor (either alone or with certain "associates") owns more than 30% of the issued securities in the fund, that investor will be subject to a tax penalty equal to 17% of its share of the fund's profits per the accounts. For a fund with 10 or

more investors, the above mentioned ownership percentage of the Singapore resident non-individual investor is raised from 30% to 50%.

35. Additionally, although the US also has investment manager exemptions or regimes, there are no "widely held" or "closely held" tests applicable to funds as funds in the US usually take the form of a Delaware limited partnership (LP) and from a US tax perspective, LPs are treated as fiscally transparent and the income derived by them will flow up to their partners. Please refer to the Appendix for more details of the relevant laws and regulations in relation to the "widely held test" for offshore funds tax exemption in Australia, Singapore, the UK and the US for reference.

36. As Option 2 above mirrors the model adopted by two of the well-developed financial markets in the world (i.e. the Australia and the UK), we recommend that Option 2 be adopted as the test for "bona fide widely held" in Hong Kong as well. The current model of the "widely held test" in the UK has been in place since 2007 whereas Australia's "widely held test" which forms part of the third and final tranche of the Australia's Investment Manager Regime became law on 25 June 2015 and applies to 2015/16 and subsequent tax years.

37. In addition, we also recommend that:

(a) the "bona fide widely held test" in Option 2 be applied to all offshore funds (i.e. including hedge funds) for the sake of consistency/fairness and given that in Australia and the UK, the same "widely held test" also applies to hedge funds; and

(b) a 18-month grace period be provided to all offshore funds (i.e. including hedge funds and PE funds) for fulfilling the test in Option 2 since a fund may need certain time to establish its track record before new investors can be obtained. The 18 months can be counted from the date of launch of the fund or the commencement of trading or investment of the fund

2. Recommendations on specific types of widely held entities

38. In addition, similar to the Australian Investment Manager Regime, we recommend that the concession be extended to the following specified types of entities which are genuinely widely held entities, e.g.:

(a) sovereign wealth funds;
(b) pension funds that comply with the requirements/regulations of certain stipulated jurisdictions;
(c) central banks;
(d) government agencies; and
(e) the special purpose vehicles for investments set up and controlled by (a) to (d) above.

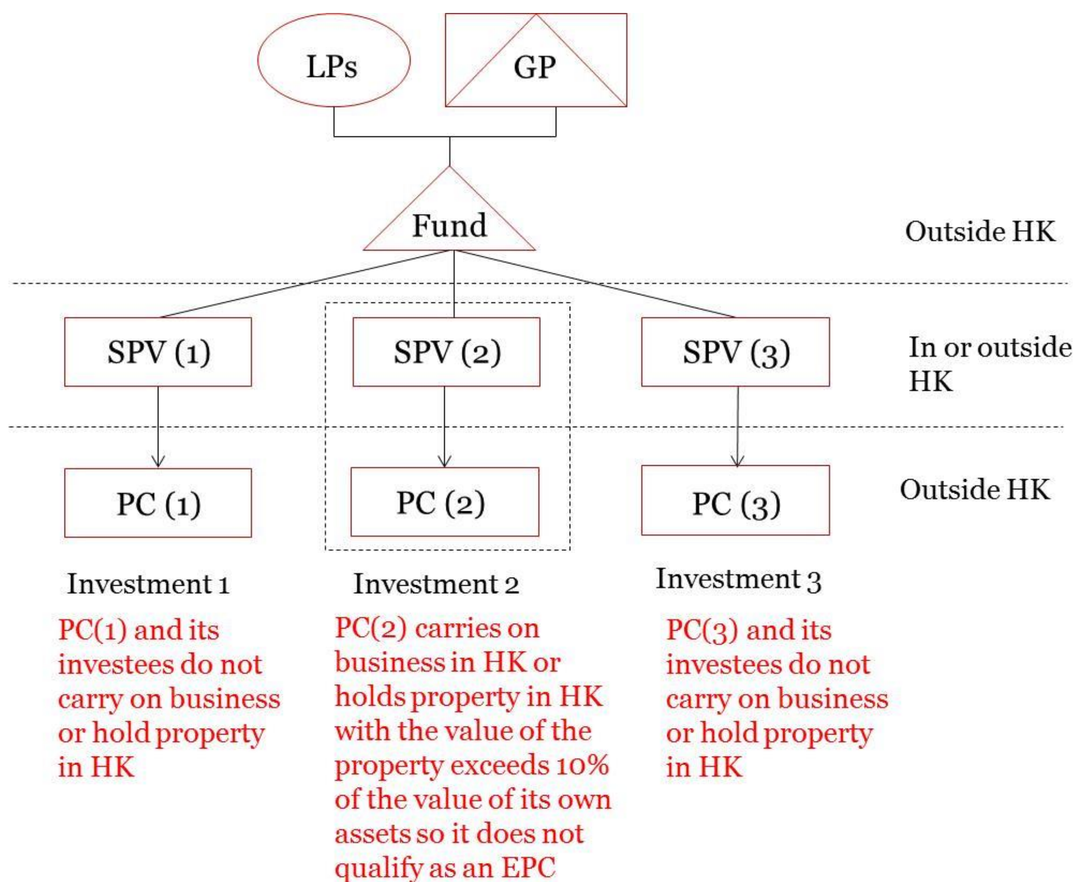
39. The above two recommendations, if being adopted, should be clearly spelt out in the revised DIPN 43 to be issued by the IRD to provide for clarity.

Tainting

Background

40. The new legislation provides profits tax exemption to transactions conducted by qualified offshore PE funds in respect of securities of eligible private companies outside Hong Kong. To qualify for the tax exemption, the overseas private companies must meet the definition of an "excepted private company" (EPC) as specified in the law. An EPC is a private company (1) incorporated outside Hong Kong; (2) that did not carry on any business / hold any immovable property in Hong Kong and (3) that did not hold (whether directly or indirectly) any private companies carrying on a business or holding immovable property in Hong Kong where the aggregate value of such shareholding exceeds 10% of the value of its own assets. A three-year look-back period commencing from the time the tax exempt transaction is carried out will be applied in assessing compliance with the requirements in (2) and (3) above.

41. However, in the case where a qualified offshore PE fund holds multiple investments by holding (directly or indirectly) more than one EPC, a question arises as to whether the disqualification for tax exemption in one investment will taint other investments which otherwise would qualify for the tax exemption. The tainting issue can be illustrated by the example in the following diagram.



42. In the above example, the fund holds three investments. PC(1) in Investment 1 and PC(3) in Investment 3 all along qualify as an excepted private company but PC(2) in Investment 2 (which is not under the control of the fund) fails to qualify as an excepted private company because say for example, it carries on a business in Hong Kong or holds immovable property in Hong Kong with the value of the property exceeding 10% of the value of its own assets.

43. On a strict interpretation of the legislation, the profits derived by the fund from the disposal of Investments 1 and 3 may not enjoy the tax exemption because Investment 2 does not qualify as an EPC. If this interpretation was followed in practice, this would not be within the spirit of the new exemption which is designed to promote the PE fund industry in Hong Kong. If the new exemption would apply to the investments in EPCs (i.e. Investments 1 and 3) but not to investments in non-EPCs (i.e. Investment 2), then the expenses of the fund would need to be apportioned to determine the proper amount of net profits subject to tax.

Recommendations

44. As the policy intent of the new legislation is to provide the PE fund industry with the tax certainty that the profits derived from transactions in securities of EPCs will not be subject to tax in Hong Kong so as to attract more PE fund managers to set up or expand their business in Hong Kong, we recommend that the revised DIPN 43 include a non-

tainting rule and clarify that in the above situation, the profits derived by the fund from a disposal of Investment 1 and/or 3 (either through disposal of the SPV or disposal of the EPC) will continue to be eligible for the profits tax exemption. The assessiability of the profits from Investment 2 would be subject to the ordinary assessing provisions of the IRO.

45. In addition, for computing the assessable profits of Investment 2, we recommend that (1) all direct expenses that can be readily identified as wholly attributed to the taxable investment should be allowed for tax deduction in full and (2) the portion of indirect expenses that is attributed to the taxable investment should also be deductible. The apportionment should be made on a basis that is most reasonable and equitable given the circumstances of the case. The basis of apportionment may be on turnover (sales proceeds), gross profits, income or value of the assets, etc. Reference should also be made to the principles stated in Inland Revenue Rules 2A and 2C as well as revised DIPN 3.

Other issues to be addressed / clarified in revised DIPN 43 (Profits Tax Exemption for Offshore Funds)

46. We recommend that the following issues be addressed / clarified in the revised DIPN 43:

(a) Paragraph 37 of the existing DIPN 43 states that where the trading receipts from the incidental transactions carried out by an offshore fund do not exceed 5% of the total trading receipts from both the specified transactions and the incidental transactions of the fund, the fund will still qualify for the tax exemption. It further states that typical incidental transactions include, among others, *"receipts of interest or dividend on securities acquired through the specified transactions"*.

In this regard, we consider that dividend income or interest income on securities (e.g. bonds) acquired by the fund through specified transactions should not be treated as "trading receipts from incidental transactions". Can the IRD clarify if this is correct?

(b) In the case where an offshore PE fund invested (directly or through a SPV) in an overseas company that was originally a private company and subsequently disposed of after it became a listed company, can the IRD clarify whether the tax exemption under the offshore PE funds exemption regime will still be available? This is similar to the case for hedge funds that invest in a private company prior to IPO, whereby they sell the investment upon or after IPO. The IRD has accepted that such transactions are qualifying transactions for the purposes of the Offshore Funds Exemption.

(c) The current definition of "special purpose vehicle" states that a SPV means, among others, *"a corporation, partnership .... or any other entity that is wholly or partially*

owned by a non-resident person". In the case where the SPV is owned by a fund, can the IRD clarify whether the owner (i.e. the non-resident person) here refers to the fund itself or the ultimate beneficial owners of the fund?

(d) The current definition of "excepted private company" states that an EPC means *"a private company incorporated outside Hong Kong that, at all times within the 3 years before a* ***transaction*** *falling within subsection (1)(a), (b) or (c) is carried out ...*". From a practical perspective, the transaction in question should be the transaction that gives rise to the profit. In this regard, can the IRD clarify whether the "transaction" above refers to the sale transactions only and does not include purchase transactions?

	Australia	**Singapore**	**United Kingdom**[5]	**US Delaware**
Test	Broadly, the test is that no member of the entity holds a participation interest of 20% or more, or there are no five or fewer members with a combined participation interest of at least 50% (the "**widely held test**").	Singapore Resident Fund Scheme (section 13R) and Offshore Fund Tax Exemption Scheme (section 13CA) - fund cannot be owned 100% by "Singapore persons" (any Singapore resident individual or entity). If a Singapore resident non-individual investor (either alone or with certain 'associates') owns more than the "prescribed percentage" of issued securities in the fund, that investor will be subject to a tax penalty equal to 17% of its share of the fund's profits per the accounts. For funds with fewer than 10 investors, the "prescribed percentage" is 30%; otherwise it will be 50%.	A fund will be regarded as widely held if either no majority interest in the fund is ultimately held by five or fewer persons and persons connected with them, or no interest of more than 20% is held by a single person and persons connected with that person. This forms part of the "**independent capacity test**".	US LPs are fiscally transparent and the income derived by the LP flows up to its partners. As such, there are no "widely-held" or "closely-held" tests applicable to the fund from a US tax perspective.
Concessions	If the entity does not satisfy the widely held test, but is being actively marketed to meet the requirements, the entity is taken to have met the test.		If the fund is not a widely held collective fund but is either being actively marketed with the intention that it becomes one or is being wound up or dissolved, the test is also met.	

[5] UK Investment Manager Exemption - Statement of Practice 1/01 (http://webarchive.nationalarchives.gov.uk/20140603144422/http:/customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageLibrary_ConsultationDocuments&propertyType=document&columns=1&id=HMCE_PROD1_027709).

	Australia	Singapore	United Kingdom[5]	US Delaware
	There is also relief for funds winding down and for circumstances outside the control of the entity. A foreign entity can also be an IMR widely-held entity if it is a specified widely held entity as described in the legislation. Broadly, these include foreign life insurance companies, certain complying foreign superannuation / pension funds, managed investment trusts, foreign government pension funds, investment funds wholly owned by a foreign government agency, amongst others. Also, for the purposes of the widely held test, the participation interests of these entities and widely held foreign collective investment vehicles are treated as nil.		Actively marketed means that there must be evidence of ongoing genuine attempts to obtain third party investment into the fund in order to meet the widely held test and that the terms on which interests in the fund are offered are not prohibitive or discriminatory for that class of business.	
Other notes	Entitlements to remuneration of an independent fund manager and its connected entities are disregarded for the purposes of the determining the total participation interest (under the widely held test) to		The fund may need to establish a track record before new investors are obtained and will therefore have 18 months from the commencement of trading in the UK to meet the widely held test.	

	Australia	Singapore	United Kingdom[5]	US Delaware
	the extent the remuneration is brought to tax in Australia or under foreign law. The tests are applied on a trace-through basis. However, note that for the purposes of these tests, an entity and each of the entity's affiliates is treated as together being one entity that has all of the interests and rights of the affiliated entities. For fund of funds, the underlying foreign fund would be the "test entity", from which you would apply the tests on a trace-through basis. Note that the IMR widely-held test is most relevant for applying the Direct Investment Concession (i.e. direct investment by a foreign fund). The Indirect Investment Concession (i.e. investment made on behalf of foreign fund by independent Australian fund manager) may be available for a foreign fund, which does not meet the widely-held tests, provided no more than 70% of the income		Where invest management services are provided to a collective investment scheme constituted as a partnership, participants in the scheme will not be regarded as connected persons for this purpose if their only connection is membership of the partnership. This means that if the investment manager is a partner in the fund it will not be treated as connected with the other partners in the fund for the purposes only of the 'Independent Capacity Test'. The independent capacity test will also be met (i) where the provision of services to the non-resident and persons connected with the non-resident is not a substantial part of the investment management business. Where that part does not exceed 70% of the investment manager's business, either by reference to fees or to some other measure, it will not be regarded as substantial. Further, if in the first 18 months from the start of a new investment	

	Australia	Singapore	United Kingdom[5]	US Delaware
	of the independent Australian fund manager is to be received from the foreign fund (and other requirements are met).		management business the services provided to the non-resident exceed 70% of the business, they will not be treated as a substantial part of the business provided that they are consistently below 70% in subsequent periods; or (ii) where the provision of services to the non-resident represents more than 70% of the investment manager's business 18 months after the start of a new investment management business but that was for reasons outside the manager's control and the manager had taken all reasonable steps to bring it below 70%. The investment manager will be expected to provide all relevant information to support a contention that the services are a substantial part of the manager's business for reasons beyond the manager's control and to demonstrate what steps have been taken to rectify that position. The HMRC will also have regard to the overall circumstances of the	

	Australia	Singapore	United Kingdom[5]	US Delaware
			relationship between the non-resident and the investment manager in determining whether they are carrying on independent businesses that deal with each other on arm's length terms. For master/feeder structures, the independence test will be applied as if the master fund were transparent by looking at the beneficial ownership of each feeder fund to determine whether the master fund is independent. Similarly, if the investment manager acts for one or more sub-funds owned by an umbrella fund, the beneficial ownership of the umbrella fund will determine whether the independence test is met. A subsidiary may be considered independent of its parent company for the purposes of the test, notwithstanding the parent's ownership of the share capital.	

About the Financial Services Development Council

The Hong Kong SAR Government announced in January 2013 the establishment of the Financial Services Development Council (FSDC) as a high-level and cross-sector platform to engage the industry and formulate proposals to promote the further development of Hong Kong's financial services industry and map out the strategic direction for development. The FSDC advises the Government on areas related to diversifying the financial services industry, enhancing Hong Kong's position and functions as an international financial centre of our country and in the region, and further consolidating our competitiveness through leveraging the Mainland to become more global.

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