11 March 2019
Global Tax Alert

Hong Kong passes new legislation to introduce use of fair value accounting treatment of financial instrument for tax purposes

Executive summary

Hong Kong's Legislative Council passed the bill (the Bill) for the new legislation (the New Law) to introduce the use of fair value accounting treatment of financial instrument for tax purposes. The New Law was enacted on 1 March 2019.

The Bill retains the original form, other than one amendment.[1]

In addition, the Hong Kong Government clarified certain provisions of the New Law during the legislative process.

Detailed discussion

Overview

Under the New Law, commencing from the taxable year ended on or after 1 April 2018, if taxpayers make an election, the accounting profits or losses, i.e., unrealized profits and losses, recognized on financial instruments would generally also be treated as the taxable profits or losses.

Amendment

Under the original bill, only accounts prepared under Hong Kong Financial Reporting Standard 9 (HKFRS 9), or its equivalent under the International Financial Reporting Standards (IFRS), i.e., IFRS 9, fell within the scope. The scope of the New Law has been extended to cover accounts which are prepared under the local equivalent to IFRS 9 in a foreign jurisdiction.

Clarification by the Government

Anticipated uncollectible amount associated with financial assets

The New Law specifies that a write-off loss under HKFRS 9 for loans made in the ordinary course of a money-lending business in Hong Kong and trade receivables would be deductible, provided that the financial assets are credit-impaired.

Several comments expressed the concern that certain financial instruments which are valued at amortized cost, or at fair value through other comprehensive income (FVOCI) would not be regarded as being loans or trade receivables, so the credit-impaired write-off loss in respect of such financial instruments would not be tax deductible before they are sold or realized.

The Government responded that the write-off loss in respect of financial instruments valued at amortized cost or FVOCI would be tax deductible provided that the Hong Kong Inland Revenue Department is satisfied that the relevant financial instruments were acquired for trading purposes.

Endnote

1. See EY Global Tax Alert, *Hong Kong introduces use of fair value accounting treatment of financial instrument for tax purposes*, dated 27 November 2018.

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