

# EXECUTIVE COUNCIL

## CONFIDENTIAL

**Title of Report:** Clarification of Expenses for Individual Transferable Quota (ITQ) for taxation purposes

**Paper No:** 281/10

**Date:** 25 November 2010

**Report of:** Taxation Officer / Commissioner of Taxation  
Legislative Drafter / Attorney General

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### 1.0 Purpose

To present to Honourable Members an amendment to section 2 of the Taxes Ordinance 1997 to clarify the meaning of Expenses for ITQ.

### 2.0 Recommendation

It is recommended that Honourable Members:

- (a) approve the amendment to section 2 of the definition of Expenses for ITQ
- (b) the clarification is legislated by the AG's office as soon as possible as we have two outstanding objections on this matter
- (c) that we inform the parties concerned immediately after a decision has been made, in advance of any changes to legislation, to allow them to submit correct company accounts.

### 3.0 Summary of Financial Implications

See paragraph 6.

### 4.0 Background

**4.1** There was an ExCo paper 308/05 that introduced the Taxes (Amendment) Bill 2006 that deemed "expenses" includes any expenditure **incurred** by any person in acquiring the whole or any part of an individual transferable quota, or of a charge on such a quota, (and, accordingly, the quota or charge represented by any such expenditure shall not be depreciated in the computation of that person's chargeable income for any chargeable period);'

**4.2** The issue is that as the legislation currently stands if a company purchases ITQ it is treated as a revenue item and not a capital one. Therefore, instead of getting capital allowances or no relief it gets a revenue deduction. The legislation is silent about WHEN it gets the revenue deduction as it states

**incurred** so we follow accountancy principles. The accountancy principles will dictate where and when the expense is written off. So that if it is in the Profit and Loss (P&L) in full in the year of purchase it is allowed then, and if it is written off over say 20 years to the P&L (amortised) it is allowed in that way for tax.

**4.3** It is highly likely that proper accountancy is to amortise over the remaining life of the ITQ and so the tax deduction will be over the remaining life too.

**4.4** It is clear that this was NOT what the legislation intended and that the ITQ should be allowed for tax when 'paid', EXCO paper 308/05, paragraph 3.3.2, attached. Therefore legislation as it stands does not do this, it allows the relief when 'incurred' and incurred means as per the accounts.

## **5.0 Proposed amendment**

### **5.1 Expenses**

It is proposed that the legislation is amended so that the expense of ITQ is allowed when it is paid, regardless of how it is treated for accounting purposes.

### **6.0 Financial Implications**

Under the current legislation we would give tax relief for the expense when it is claimed in the accounts. Therefore, this could be over a number of years where the cost of ITQ is amortised in the accounts and under the proposal it would be given tax relief in one lump (albeit the same total).

### **7.0 Legal Implications**

The Taxes Ordinance will need to be amended to give legal effect to this change. It was not possible to include this in the Taxes (Amendment) Bill being submitted for Executive Council's approval under ExCo paper 278/10, so it will need to be included in a future Taxes (Amendment) Bill. Unless Executive Council decide otherwise, this will not be given special priority but will be done as soon as possible, to the extent that competing priorities allow.

### **8.0 Human Resources Implications**

None

# EXECUTIVE COUNCIL

## RESTRICTED

**Title of Report:** The Taxes (Amendment) Bill 2005  
**Paper No:** 308/05  
**Date:** 15 December 2005  
**Report of:** Taxation Officer

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### 1.0 Purpose

To present to Honourable Members the Taxes (Amendment) Bill 2005 and Explanatory Memorandum, which have been drafted by Miss Lesley Furlonger, Parliamentary Draftsperson, to include the proposals agreed by ExCo at their meeting 24 November 2005.

### 2.0 Recommendations

That His Excellency the Governor is advised to approve the remission of the Taxes (Amendment) Bill 2005 to the Legislative Council.

### 3.0 Background

3.1 The policy proposals, which have previously been agreed by ExCo at their meeting held 24 November 2005, have now been incorporated into the Taxes (Amendment) Bill 2005.

3.2 The Explanatory Memorandum sets out the detail contained in the Bill succinctly and clearly and no further background information to clauses 1, 3, 4, 6, 8 and 9 is considered necessary.

3.3 The taxation of the new rights contained in the Fisheries (Conservation and Management) Ordinance 2005 is covered under clauses 2, 5 and 7 of the Bill and is summarised as follows:

3.3.1 Clause 2 introduces a revised definition of income and a new definition of expenses to cover those new rights.

3.3.2 As a result of these definitions the cost, in monies paid, of acquiring an individual transferable quota is to be treated as a revenue expense allowable in

the company accounts at the time as it is paid. Any monies received on any disposal of that quota then becomes income arising at the time of sale.

- 3.3.3 The acquisition or disposal of any unquoted shares, by a company or an individual, deriving their value because of the individual transferable quota held by a company will be dealt with differently.
- 3.3.4 The income or loss arising on the sale of any such shares will be treated as such in the company or individual accounts at the time of sale.
- 3.3.5 It is necessary therefore that all incidental acquisition or disposal costs are notified to the Taxation Office within 28 days on the appropriate form, which will be available from the Taxation Office. Failure to comply with this requirement will incur a mandatory penalty under Clause 5 at section 100B(3).
- 3.3.6 Any incidental costs incurred in the acquisition or sale of such shares will also be allowable. These costs are defined at Schedule 2 Taxes Ordinance 1997, paragraph 1(3). That section is reproduced below:

“(3) ...the incidental costs to the person making the disposal of the acquisition of the asset or of its disposal shall consist of expenditure wholly and exclusively incurred by him for the purposes of the acquisition or, as the case may be, the disposal, being fees, commission or remuneration paid for the professional services of any surveyor or valuer, or auctioneer, or accountant, or agent or legal adviser and costs of transfer or conveyance together with—

(a) costs of advertising to find a seller or a buyer, and

(b) costs reasonably incurred in making any valuation or apportionment required for the purposes of the computation of the gain, including in particular expenses reasonably incurred in ascertaining market value where required by this Ordinance.”

- 3.3.7 To ensure that companies and individuals provide the correct information to the Taxation Office it is necessary that the information provided to the Director of Fisheries, under the Fisheries (Conservation and Management) Ordinance 2005, is readily available to the Taxation Office. Clause 7 introduces that requirement, as explained in the Explanatory Memorandum.