Client Alert
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Financial Services and Treasury Bureau proposes new tax deductions for voluntary contributions and deferred annuity policies

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In line with the Hong Kong government's commitment to further develop the local pension system to address the aging population, the Financial Services and Treasury Bureau (**FSTB**) recently submitted a paper to the Legislative Council (**Legco**) proposing to offer tax deductions to taxpayers who make mandatory provident fund (**MPF**) voluntary contributions and/or purchase deferred annuity policies (the **Proposal**).

1. What's the expect timeline?

The amendment bill to introduce the Proposal is expected to be discussed at Legco sometime during the last quarter of this year and the FSTB will likely consult the industry again before finalizing the legislative amendments. Once the bill is passed, the proposed deductions are slated to take effect in the 2019-20 assessment year.

2. Which MPF contributions are currently tax deductible?

Hong Kong's MPF system is funded by both mandatory and voluntary contributions from employers and employees. At present only mandatory contributions made by employers and employees as well as voluntary contributions made by employers are tax deductible (**Deductible Contributions**). However, Deductible Contributions are by statute, subject to preservation requirements whereby the benefits of such contributions may only be paid out to scheme members when they reach the age of 65 unless other exceptional circumstances apply[1] (**Withdrawal Restrictions**). On the other hand, voluntary contributions made by scheme members (or employees) are only subject to restrictions imposed by the various MPF service providers and thus enjoy no tax benefits.

3. How will the Proposal change the current position?

Under the Proposal, scheme members will have the added option of making tax deductible voluntary contributions **provided that** such amounts contributed are also made subject to the abovementioned Withdrawal Restrictions.

Scheme members wanting to benefit from voluntary contribution tax deductions must deposit contribution amounts in a new separate tax deductible voluntary contribution (**TDVC**) account and may select any MPF service provider to handle the account. Similarly, members of an ORSO (Occupational Retirement Schemes Ordinance) scheme may open a TDVC account with an MPF service provider to enjoy the same tax benefits.

[1] The other exceptional circumstances are: (i) early retirement; (ii) permanent departure from Hong Kong; (iii) total incapacity or terminal illness; or (iv) death.

4. What type of deferred annuities will be tax deductible?

To specifically address certain age groups and varying risk profiles of workforce individuals, the Proposal provides tax deductions for premiums paid for deferred annuity products that satisfy the following criteria:

- a minimum total premium value of HKD180,000;
- a minimum accumulation period (i.e. the period of time during which the purchaser of the annuity is to pay premiums) of five years;
- a minimum annuity period (i.e the period of time during which the guaranteed income is payable on a regular basis) of ten years;
- a minimum annuitization age of 50 or above; and
- additional disclosure requirements, including but not limited to a clear presentation of the deferred annuity product's: (i) internal rate of return; (ii) guaranteed payment; and (iii) variable payment.

5. Is there a cap on the tax deductions?

In its current form, the Proposal caps the maximum amount of deductible tax for each taxpayer at HKD36,000 per year, and both MPF voluntary contributions as well as deferred annuities will share the same aggregate limit. Accordingly, a taxpayer may allocate annual tax deduction amounts between MPF voluntary contributions and deferred annuity premiums paid, up to the annual maximum limit.

6. What are the implications?

- If you are an MPF service provider: The Proposal will necessitate changes to the constitutive and offering documents of your MPF schemes, policies and procedures (including risk assessments) and operations and systems, e.g. the creation of new TDVC accounts. You'd better act fast given that the Proposal is set to take effect in less than a year!
- If you are an insurance provider, you should start revisiting your annuity product features, brochures, websites and education materials as well as enhancing training on annuity products for intermediaries.

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