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FINANCIAL MARKET UPDATE: TRENDS AND TECH

CONTENTS

While you may still be attracted by the stock price movements of the first ever weighted voting rights structured Initial Public Offering (IPO) in Hong Kong, the Hong Kong Monetary Authority (HKMA) issued new guidance and the Securities and Futures Commission of Hong Kong (HKSFC) took certain enforcement actions in Q2 2018. These new updates may shed light on your business or personal lending decisions. Here are some selective updates on recent regulatory changes in the financial market:

- Banking: The HKMA has revised the guidelines on applications made by virtual banks and has allowed the use of financial technology (FinTech) in the personal lending business.
- Financial market: In Q2 2018, the HKSFC took enforcement actions in 12 cases. Fines imposed exceeded HK$80 million in total.

Banking

Authorization of Virtual Banks

In May 2018, the HKMA revised its Guideline on the Authorization of Virtual Banks. This guideline sets out the requirements for: ownership, ongoing supervision, physical presence, technology risk, risk management, business plan, exit plan, customer protection, outsourcing and capital.

In particular, banks are required to engage a qualified independent expert to assess the adequacy of their plans for IT governance and their systems. Before commencing operations, banks must then undergo a more detailed independent assessment of the actual design, implementation and effectiveness of their computer hardware, systems, security and related procedures and controls.

In addition, banks must be able to present a credible and viable business plan. The HKMA will have concerns if a bank plans to build its market share aggressively with substantial losses during its initial years of operation. The HKMA also requires every bank to have an exit plan for unwinding its business operations in an orderly manner if its business model fails.

Use of FinTech in the personal lending business

In May 2018, the HKMA issued new guidelines to banks on Credit Risk Management for Personal Lending Business. In a bid to improve the customer experience in the digital environment, these guidelines allow banks to use innovative technology to manage the credit risks related to the personal lending business.

Under the new guidelines, banks may carve out a portion of their personal lending portfolio to which conventional lending practices will not apply. Instead of using proof of income to assess borrowers' ability to make repayments, banks may manage the related credit risks by adopting the techniques and practices made possible by innovative technology, such as big data and consumer behavioural analytics. To ensure the associated risks are managed appropriately, banks should limit this new portfolio to 10% of their capital base. In general, the amount of credit extended to individual borrowers should be smaller than that of conventional credit products. The HKMA will review these new arrangements at a later stage and consider the future scope of their application.

Financial market

The HKSFC took enforcement actions against listed issuers, licensed corporations and others for non-compliance with the Securities and Futures Ordinance (SFO), its codes and guidelines, and the related laws and regulations. There were 12 cases in Q2 2018 alone, which led to fines of more than HK$80 million altogether. In some cases, the HKSFC has proceeded to Market Misconduct Tribunal (MMT) or the higher courts. These cases are summarised below:

Ref	Non-compliance/breach	Fine (HK$)	No of cases	Remarks
1	Making false or misleading statements in the IPO or other announcement(s)	20K	2	The HKSFC has commenced MMT proceedings for 1 case (ie not yet fined)
2	Failure to (i) conduct adequate and reasonable due diligence in the IPO and (ii) properly supervise its staff when carrying out the sponsor work in the IPO	57M	1	
3	Late disclosure of inside information	-	2	The HKSFC has commenced MMT proceedings for these 2 cases (ie not yet fined)
4a	Other: a licence applicant providing false information	12K	1	
4b	Other: transfer of $61 million from the company's bank accounts to personal bank accounts	-	1	The HKSFC has commenced legal proceedings in the Court of First Instance to seek orders to disqualify former senior executives of the issuer
5	Other failure to comply with the code of conduct, Know-Your-Client (KYC), sales supervision, and failure to maintain an effective compliance function and satisfactory internal control among others	26.58M	5	
Total		**83.6M**	**12**	

In short, non-compliance with rules and regulations can lead to great losses in reputation and fines. The HKSFC has taken enforcement actions against not only fraudulent acts but also failure to supervise relevant staff or sales activities, maintain an effective compliance function, maintain internal controls or maintain a corporate governance structure according to the rules.

Based on the above snapshot of the regulatory developments, we encourage our clients to keep abreast of the recent regulatory changes and the regulators' enforcement actions. These will enhance your awareness of new business opportunities and regulatory practices. Independent IT governance and system assessment, business viability and exit plans are considered to be essential components of any virtual bank. An effective corporate governance structure and a robust internal control system, in particular for monitoring regulated activities, are important and should not be compromised. Otherwise, they may face huge risks in terms of penalties and reputation. If in doubt, please seek advice from a professional regulatory and risk advisor.

How can BDO Help?

BDO Risk Advisory in Hong Kong has a robust team of former banking practitioner, compliance, IT and risk professionals, which has helped our clients in applying licenses from HKMA, reviewing IT policies and systems, risk management processes and regulatory compliance. If you have any question in the above matters, please contact the author as shown below.

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DEVELOPMENT OF HONG KONG AS AN AIRCRAFT LEASING AND FINANCING HUB

In February 2017, the Financial Secretary stated in his budget speech: "… the government plans to introduce a bill into the Legislative Council in 2017 to amend the Inland Revenue Ordinance (IRO) to offer tax concession... [to] attract aircraft leasing companies to develop their business in Hong Kong, thereby creating job opportunities for both the financial and aviation industries."

The proportion of new aircraft being financed by leasing arrangement already exceeded 30% worldwide, according to Secretary for Transport & Housing of the Hong Kong Government in March 2017[1], while aircraft manufacturer Boeing forecast that over 39,000 new aircraft, valued at US$5.9 trillion, would be delivered over the next 20 years[2].

In July 2017, the Inland Revenue (Amendment) (No.3) Ordinance 2017 was enacted. In the same month, the Hong Kong Financial Services Development Council issued a paper, 'Recommendations for Developing Hong Kong as an Aircraft Leasing and Financing Hub', putting together recommendations on how Hong Kong can gradually develop itself into an international aircraft leasing and financing hub, complementing Tianjin Binhai New Area and Shanghai Pudong New Area to capture the robust aviation opportunities and enhancing economic and global influence of China.

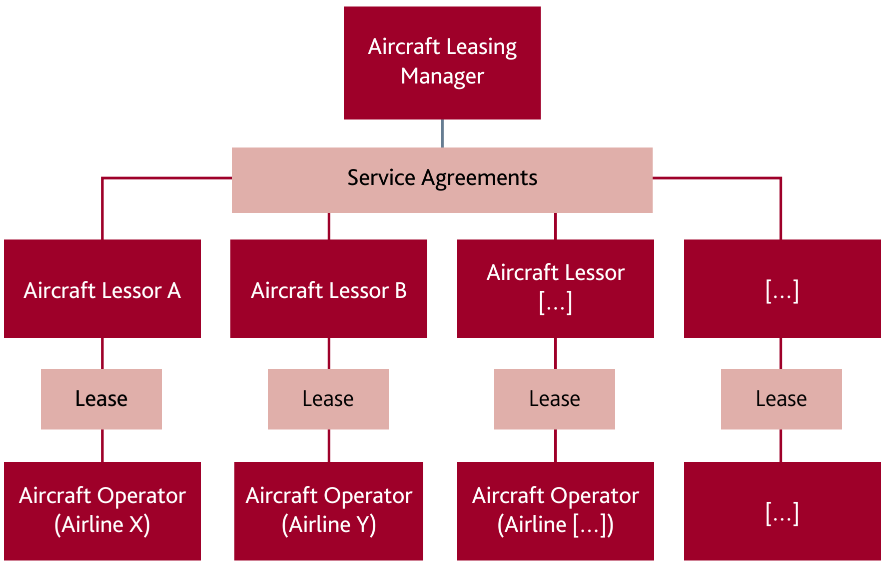
The Inland Revenue Department (IRD) issued the Departmental Interpretation and Practice Notes (DIPN) No.54, Taxation of Aircraft Leasing Activities in October 2017.

In November 2017, Carrie Lam, Chief Executive of HKSAR, spoke at the Hong Kong Aircraft Leasing and Aviation Finance Association inaugural ceremony. In her speech, Lam said: "… promoting high-value-added aviation services is one of the key areas that we are pressing ahead… Hong Kong already possesses favourable conditions necessary to thrive as an aviation financing hub in Asia… the withholding tax rate between Hong Kong and Mainland China has been lowered to five per cent... we have amended the relevant legislation to provide a dedicated tax regime."

In the past, the development of the aircraft industry has been constrained by: (i) a high corporate tax rate (16.5%); and (ii) no tax deduction for depreciation related to aircraft leased to non-Hong Kong airlines.

The new tax regime has:

i **set the profits tax rate for qualifying aircraft lessors and aircraft leasing managers at 8.25%, which is half of the standard profits tax rate; and**
ii **deemed the taxable amount of profits derived by qualifying aircraft lessors from leasing of aircraft to aircraft operators to be 20% of the gross lease payments less deductible expenses, excluding tax depreciation allowance.**



Qualifying aircraft lessors and qualifying aircraft leasing managers can enjoy half of the standard profits tax rate (ie 8.25%); and the taxable amount of profits derived by qualifying aircraft lessors from leasing of aircraft to aircraft operators under the new tax is deemed to be 20% of the gross lease payments and deductible expenses, excluding tax depreciation allowance.

1. Information from Secretary for Transport & Housing of the Hong Kong Government in his speech delivered in London on 4 March 2017 and quoted in DIPN 54 issued by Inland Revenue Department
2. Data quoted from 'Report on Current Market Outlook 2016–2035', issued by Boeing

Table 1: Professional services for aircraft leasing and financing companies that will significantly increase in the future

Service type	Services
Risk and other advisory	• Risk management: - Credit risk management (airlines/others) - Financial risk management (interest rate, foreign currency & derivative management) - Liquidity & funding management • Internal control: - Risk assessment and control analysis - Standard operating procedure/group policy and procedures - Control documentation/effectiveness testing - Internal audit outsourcing/co-sourcing • Restructuring & voluntary liquidations of SPVs • IT strategy, security/systems implementation
Outsourced financial accounting, company secretarial and payroll functions	• Maintenance of accounts, books and records • Preparation of statutory financial statements • Provision of company secretarial services • Recruitment and placement of staff
Tax compliance and advisory	• Corporation tax compliance • Transaction support and advice • Tax structuring • Executive and employee tax planning and compliance
Audit	• Provision of statutory audits for HK and other overseas entities

The effective tax rate (including effect of (ii) above) will be lower than that in Ireland (12.5%) and Singapore (8%).

The government's initiative to introduce this concessionary tax regime is highly visionary and pragmatic, aiming to transform Hong Kong into an aircraft financing hub within a short period.

According to government estimates, with the introduction of the new tax regime:

i. Hong Kong's market share in the global aircraft leasing business will reach 18% in 20 years, offering over HK$700 billion for aircraft financing (based on a total of 3,240 airplanes).
ii. 1,640 employees will be hired directly, and over 13,700 jobs will be created indirectly.
iii. The profits tax generated will exceed HK$10 billion, and over HK$430 billion will be added to the GDP of Hong Kong.

This initiative will certainly have a significant impact on the finance and aviation industries and a positive impact on the general economy.

The demand for high quality talent and services in aviation, financing, tax, accounting and risk advisory will significantly increase in the near future (**see Table 1**).

How can BDO Help?

BDO in Hong Kong has multi-disciplinary teams to help our clients in risk advisory, accounting and secretarial, tax advisory and audit matters. If you have any question in aircraft financing and risk related matters, you can contact **Peter Pang** (peterpang@bdo.com.hk) in risk advisory. You may also contact **Celestine Yeung** (celestineyeung@bdo.com.hk) for specific issues in tax, **Andrew Lam** (andrewlam@bdo.com.hk) for audit issues, **Dorothy Pak** (dorothypak@bdo.com.hk) for accounting and secretarial assistance and **Kenneth Yeo** (kennethyeo@bdo.com.hk) for valuation matters.

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SENIOR PARTNER OF BDO IN CHINA LUO ZHENBANG REACHED THE TOP OF MOUNT EVEREST

Luo Zhenbang, Senior Partner of BDO in China reached the peak of Mount Everest on 19 May 2018. By reaching the peak at the height of 8,848 metres above the sea level, Luo becomes the first person ever to reach the top of Mount Everest among accountants, financial officers and auditors in China.

As Luo Zhenbang accomplished his adventure and stood on the top of Mount Everest, he raised the flags of the firm and The Chinese Institute of Certified Public Accountants. Congratulations to Luo Zhenbang on his successful conquest to the top of Mount Everest.

BDO, A CATALYST FOR GROWTH IN THE GIG ECONOMY

Traditionally, 'match making' is a concept all about love, relationships and marriage. But, in today's commercial world, BDO adopts the concept of 'match making' in its delivery of professional services. BDO's Professional Resources Solutions (PRS) deploys professionals of all levels who are well experienced with diversified portfolios that are ready to serve in the gig economy.

What is the gig economy?

The 'gig economy' is a labour market characterised by the prevalence of short-term contracts or freelance work, as opposed to permanent jobs[1].

In APAC, Hong Kong is seen to be embracing the free agent trend the most, with 55% of respondents agreeing that most people are looking for a flexible contract-based role rather than a traditional permanent full-time role[2]. We have seen many multinational companies extensively increase their hiring of contract workers to complement and bridge the gap in the skills and capacities of their existing workforce. A recent survey confirmed that 54% of employers in Hong Kong indicated that they had hired contingent staff in the past year[3].

Three reasons why the gig economy has a positive effect on a company's growth

1. Diversity and Inclusion (DNI)

Workplace diversity and inclusion involves understanding, accepting and valuing differences regardless of an employee's background, gender, race, language, religion, etc, and providing an environment where employees feel valued and supported to participate and contribute.

The gig economy allows companies to recruit from a diverse pool of candidates either for particular projects or on a contractual basis. As such, employers can recruit candidates based specifically on their prior work/project experience, calibre, expertise and talent. This creates a diversified workforce with different backgrounds and perspectives appropriately qualified to work on projects and arrive at winning business solutions when working as a team.

This facilitates the promotion of DNI which, in turn, also:

- Provides a bigger talent pool as it attracts a wider range of qualified candidates
- Increases the vitality of employees, ie workers' efficiency, and creates a competitive advantage for the company
- Promotes innovation and cultivates a creative workplace
- Includes more diversified sets of skills, which means new business opportunities
- Improves the company's business reputation

And the final result will be an increase in business opportunities and profitability for the company.

2. Agile and flexible hiring model

In the past, work tasks were very much operationally-oriented. Each employee had a certain number of tasks to accomplish every day, which are repetitive throughout his/her entire career. However, amidst changes such as evolvement of the market and business environment, updates of regulation and compliance requirements, automation and digitalisation of working process, employees' jobs are no longer operational (most of them are now automated or outsourced). Instead, they are more strategically and project-oriented.

Companies without resources or talent to cater for such changes tend to hire workers with more diversified skillsets and expertise to bring in value and the best practices to their existing team. This, therefore, promotes the rising trend of the gig economy.

The gig economy not only offers the flexibility of employment on demand, but also helps bringing in talent to bridge resource and talent gaps through the supply of experienced giggers (independent workers who are employed to work on short-to-medium-term projects/ engagements on a non-permanent basis).

These giggers will have accumulated a diversified range of and/or some specific knowledge and experience from working on different projects in different types of companies and organisations across various industries. Such experience and knowledge will be of great value to the hiring companies as the giggers are able to share their past experience and give examples of good practice which, in turn, will enhance the company's overall capability, enrich the team's knowledge and help them overcome/prevent project-related hurdles.

This agile and flexible hiring model also helps companies lower their sink-in costs since the gig economy expedites the decision-making process. It is easy for companies to terminate an employment relationship with a gigger if that worker is not performing well. Meanwhile, if a gigger has a good performance, they can also consider hiring him/her to become a permanent staff without the additional cost of a recruitment process.

3. Cost, cost, cost

Maintenance cost

When hiring giggers, companies are not required to pay orientation costs or benefits such as study, annual, sick, maternity or paternity leave etc, nor to provide any ongoing training and continual professional

1 https://www.bbc.com/news/business-38930048
2 'Gig Economy: How Free Agents are Redefining Work' survey published in 2018 by PERSOLKELLY, the regional headquarters of Kelly Services HK.
3 2016 Hays Asia Salary Guide

development. Also, there are no future obligations in providing longer-term benefits, such as long service leave entitlement or severance-related expenditure.

Another point to highlight is that giggers do not expect to receive these types of benefits from the hiring companies as they seek other advantages provided by the flexibility of work.

Lower fixed costs

The new resourcing model in the gig economy will inevitably help companies lower their fixed costs. For example, when it comes to property rental, companies can operate in a smaller office area suitable for the size of their core workforce.

Giggers are only recruited when companies have resourcing or project needs. Therefore, instead of committing to rent a larger office space permanently, companies could consider using a serviced office or additional workspace only for the duration of the giggers' employment.

Cost efficiency

The gig economy allows companies to hire at value-for-money. They are able to pay workers based on the market price and are not subjected to the expectations of consistent salary increments of permanent and long service employees. Most of the time, salary increments for permanent staff are due to length of service and are not based on the employees' contribution at work.

The gig economy does not consider factors such as employees' loyalty towards companies and their past contribution, but focuses purely on a cost perspective. Companies can pay market rates based on the candidate's experience, capabilities and/or expertise.

How can BDO help?

The gig economy represents a challenge regarding the effective match between giggers and those corporations that have demands for talent/resources in a critical and timely manner. So, how do you find the right candidate for your business?

BDO Hong Kong's PRS team acts as a dock and provides a platform that bridges the supply and demand of the gig economy. We have been diligently servicing clients who have significant demands for professional resources and talents over the last half a decade.

As a professional firm, we differentiate ourselves by adopting a consultative and advisory model in the provision of our 'match making' services. In all instances, we will meet our clients to obtain a good and thorough understanding of their needs and/or problems, as well as to look into their expectations regarding calibre, skillsets and so forth.

Members of our PRS team are all seasoned professionals and advisors who have experience in diagnosing the problems and issues that clients face. They will then work with the talent acquisition team to identify either one individual or a team of potential consultants to work on the client's projects. In addition to experience and skillsets, we will also take into account whether the potential candidate(s) will fit into the client company's culture, along with various aspects such as language capability and other expertise. Our mission is to bridge, or even close, the expectation gap between our clients and potential candidates to create a 'perfect match'.

PRS is not merely about executive search and recruitment service, which we also provide to our existing clients. Rather, our main focus is on a professional secondment and advisory service, where we will deploy consultants to clients' projects on a short-to-medium-term basis. In addition, since we are a fully-fledged accounting and advisory firm, we are able to provide comprehensive business solutions to best fit our clients' needs. Our clients can benefit from PRS by releasing the pressure of human resource and talent shortages, which, in turn, allows them to become more focused on business development and the strategic growth of their businesses.

A further benefit to be gained from BDO is our comprehensive and close-knit international network. With our presence extending across 160 countries globally, we are basically '*Where you want us to be*'. We strongly believe that we are your ideal business partner to work with on resourcing-related solutions around the globe.

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GLOBAL RISK LANDSCAPE 2018 REPORT

BDO Global Risk Landscape 2018 report has been published to announce the survey results of over 500 C-suite and senior risk experts across the globe regarding their latest views towards the possible business risks in coming future.

According to the survey results, there is a divide opening up between those businesses that embrace change and actively engage in it, and those that are being forced to change. That gap is increasingly obvious when innovation levels are correlated with commercial success. As a result, agility and innovation are the keys to manage the potential risks, especially in technological terms.

With the greatest challenge that all businesses face is to understand how the customer being an agent of change, innovation must allow a business to support the feedback loop with its customer base and to push that information into the change process, ie the capacity to analyse data and provide insights for future improvement.

Three white papers have also been published by our global Risk Advisory teams across the Americas, Asia-Pacific and EMEA to deliver insight and advice on the local risks affecting their markets.

If you would like to obtain a copy of Global Risk Landscape 2018 report and the three white papers, please visit: https://www.bdo.global/insights/advisory/ras/global-risk-landscape-2018

WHAT MATTERS TO EMPLOYERS IN 2018/19 AND BEYOND?

The article we have published in the APERCU issue December 2017 has updated readers on the latest employment-related legislative amendments. So what legislative or proposed changes will affect employers in 2018/19 and beyond?

Controversy about the government's proposal to abolish the Mandatory Provident Fund (MPF) offsetting arrangement

In our December APERCU article on the Chief Executive's 2017 Policy Address, we highlighted Mrs Lam's pledge to abolish the rules that allow employers to offset severance payments (SPs) or long service payments (LSPs) against their MPF contributions within her term of office. To facilitate a consensus among the various stakeholders on this controversial issue and eventually abolish the offsetting mechanism as Mrs Lam promised, the government has recently announced the following preliminary proposal:

1. An incremental subsidy amounting to at least HK$17.2 billion (double the original sum proposed by the ex-Chief Executive) to ease the additional burden on SMEs making SPs or LSPs following the ban on the offsetting arrangement.
2. The introduction of a two-tier government subsidy system. For the first three years, the government will subsidise up to 50 per cent of employers' SPs or LSPs. After that, the subsidy will reduce by five per cent a year, until it falls to five per cent in the twelfth year. (In the previous proposal, the government subsidy was limited to ten years.) After that, employers will be responsible for the full amount of the payments. (Details of the two-tier government subsidy system are shown in **Table 1**.)
3. The calculation of SPs and LSPs will stay unchanged at two-thirds of an employee's salary for the final month, multiplied by their reckonable years of service, and capped at HK$390,000.
4. The introduction of a designated saving account (DSA) to which employers will contribute the equivalent of one per cent of an employee's salary as a reserve for SPs and LSPs. The contribution to the DSA is limited to 15 per cent of an employee's total salary (which means employers would contribute for only 15 years per employee).
5. The government will provide a second layer of subsidy, to be used if a business's contributions to the DSA fail to cover its SPs or LSPs.

Table 1: Details of the proposed two-tier government subsidy

Number of years after abolition	Tier 1 of government subsidy (% of employers' SPs and LSPs)	Tier 2 of government subsidy (% of employers' SPs and LSPs)	Maximum government subsidy (tier 1 plus tier 2)
1	50%	25% (50% x 50%)	75%
2	50%	25% (50% x 50%)	75%
3	50%	25% (50% x 50%)	75%
4	45%	24.75% (55% x 45%)	69.75%
5	40%	24% (60% x 40%)	64%
6	35%	22.75% (65% x 35%)	57.75%
7	30%	21% (70% x 30%)	51%
8	25%	18.75% (75% x 25%)	43.75%
9	20%	16% (80% x 20%)	36%
10	15%	12.75% (85% x 15%)	27.75%
11	10%	9% (90% x 10%)	19%
12	5%	4.75% (95% x 5%)	9.75%
13	0%	0%	0%

Notes

1. Employers are allowed to offset the pre-effective date SPs and LSPs with their MPF contributions made both before and after the effective date of abolition of MPF offsetting arrangement (efficient date) (please see example 1 for further details).
2. The abolition of the offsetting arrangement should also apply to occupational retirement schemes under Occupational Retirement Schemes Ordinance (ORSO). The employers concerned, and those who make voluntary contributions under the MPF system in excess of the compulsory 5%, can make use of the accrued benefits derived from their voluntary contributions to offset SPs and LSPs. Likewise, gratuity based on length of service as a voluntary payment by employers to employees should also continue to be used to offset SPs and LSPs.

Example 1
Company A began operating five years before the offsetting arrangement was abolished. It has employed eight employees, of which three were dismissed five years after the abolition.

Assumptions
1. The employees' average monthly salary was HK$12,000. Immediately after the offsetting arrangement was abolished, their salary was increased to HK$15,000.
2. Five years after the abolition, Company A dismissed three employees, each with ten years' service (five years before the abolition and five years after it). The final monthly salary of the dismissed employees was HK$15,000.

Summary of the amounts involved on dismissal of three employees

I) Before the abolition of offsetting SPs and LSPs (five years) (in HK$)			
Calculations	SPs/LSPs payable	Employer's 5% MPF contribution to dismissed employees	
Amount	(12,000 x 2/3) x 5 years x 3 employees = 120,000 (a)	i Made before abolition (600 x 12) x 5 years x 3 employees = 108,000 (b)	ii Made after abolition (750 x 12) x 5 years x 3 employees = 135,000 (c)
Total employer's MPF contribution to the three dismissed employees, and conclusion for (I)		243,000 [(b) + (c)] (No top-up payment by Company A is required, because the employer's total contribution to the MPF, made before and after the abolition, is sufficient to cover the SPs and LSPs payable to the three dismissed employees)	

II) After the abolition of offsetting SPs and LSPs (five years) (in HK$)				
Calculations	SPs/LSPs payable	Accrued balance of DSA	Tier 1 [(d) x subsidy rate in the relevant year]	Tier 2 [(d) – (f) – (e)] x subsidy rate in the relevant year]
Amount	(15,000 x 2/3) x 5 years x 3 employees = 150,000 (d)	(150 x 12) x 8 employees x 5 years = 72,000 (e)	150,000 x 40% = 60,000 (f)	(150,000 – 60,000 – 72,000) = 18,000 x 40% = 7,200 (g)
Total subsidy amount and conclusion for (II)	Total government subsidy = 67,200 [(f) + (g)] Top-up payment by employer = 10,800 [150,000 (d) – 60,000 (f) – 72,000 (e) – 7,200 (g)]			

Source: Preliminary idea on abolishing the offsetting arrangement under MPF system published by the Legislative Council Panel on Manpower

The above example shows that the proposed government subsidy that employers can get is fairly complicated to calculate. Despite receiving the subsidy, employers will still be required to incur additional expenditure on the termination of employees after the offsetting arrangement is abolished.

The business sector has raised complaints about the government's proposal. Representatives from the sector have expressed concerns that those SMEs that hire a small number of employees would not be able to afford the extra cost of contributing to the new DSA, let alone the additional cost of the top-up payment for SPs and LSPs after the abolition. SMEs would have to dig into their own pockets or seek external finance to meet the cost of the top-up payment. Such extra costs may lead some SMEs to make the decision to close their business.

Representatives of the business sector have made alternative proposals to the government, calling for more subsidies as follows:

1. To consider the two-tier profits tax system and to further subsidise companies by matching one per cent of the employers' contribution to the new DSA.
2. To extend the subsidy on SPs and LSPs beyond the 12-year grace period (or indefinitely).

Meanwhile, representatives from the employment sector have welcomed the government's proposal to stop this offsetting arrangement swallowing up employees' retirement funds. In addition, the employment sector finds the government's proposal acceptable, as it does not reduce the cap of HK$390,000 on SPs and LSPs (despite the fact that the proposal still allows employers to offset the pre-effective date SPs and LSPs against MPF contributions made both before and after the effective date).

The government hopes that the proposed bill will be approved by 2020 and take effect by 2022. However, the business sector remains unconvinced, as demonstrated by its counter-proposals. In view of the controversy surrounding the issue, government officials must study the counter-proposals from the business sector and the employment sector to reach a consensus in both sectors, win support and move forward. It seems unlikely that the government will be able to proceed to legislation in 2018. We will monitor developments concerning this topic.

Updates on proposed amendments to maximum and minimum levels of relevant income for contributions to the MPF

The Mandatory Provident Fund Schemes Authority (MPFA) has recently reviewed the minimum and maximum levels of relevant income. (The previous review took place in 2014.) At present, the minimum and maximum relevant income levels are HK$7,100 and HK$30,000, respectively. According to the statutory adjustment factor, the MPFA proposes adjusting the above levels to HK$8,000 and HK$48,000 (the threshold would first be adjusted to HK$39,000 and then to HK$48,000 two years later), and will submit this proposal to the government in July this year. If the proposal is passed by the Legislative Council later this year, the cap on the employer's contribution for an employee may increase from HK$1,500 to HK$2,400 when calculated at the 5% contribution rate.

Details before and after the proposed amendments are summarised in **Table 2**.

Updates on proposed amendments to the statutory minimum wage

The Minimum Wage Commission launched a six-week public consultation to invite views from the community, including members of the public and stakeholders, on the review of the statutory minimum wage. The consultation ran from 9 April to 20 May 2018.

The Labour leaders have called for the minimum wage to be raised to HK$42 per hour from the current HK$34.5 per hour, and claimed that such an increase is needed to guarantee a reasonable standard of living for people on low pay.

Since Hong Kong brought in the statutory minimum wage at HK$28 per hour in 2011, it has gone up every two years; it is currently HK$34.5 per hour. The government will announce the new rate on Labour Day, 1 May 2019.

The above proposals would have a significant impact on Hong Kong's entrepreneurs, employees and wider economy; particularly the proposals for abolishing the offsetting arrangement. In view of the complexity of and controversy surrounding these proposals, further reviews and discussion among stakeholders are needed before the proposals can receive legislative approval. We will keep readers informed about the latest developments.

Proposal for increment of statutory paternity leave

A proposal to increase statutory paternity leave (SPL) in Hong Kong from three to five days has formally put forward by the government and the relevant amendment bill has recently introduced into the Legislative Council for approval of the SPL legislation. The increment of SPL would expect to take effect in February 2019.

Speak to our payroll professionals

Feel free to get in touch to find out how we can help you with a tailored payroll outsourcing solution.

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Table 2: Proposed amendments to minimum and maximum levels of relevant income

	Proposed minimum level of relevant income		Proposed maximum level of relevant income	
	Contribution (from 1 June 2014)	**Proposed contribution under review (may be adjusted)**	**Contribution (from 1 June 2014)**	**Proposed contribution under review (may be adjusted)**
Employees paid monthly	HK$7,100 per month	HK$8,250 per month	HK$30,000 per month	HK$48,000 per month (the threshold would first be adjusted to HK$39,000 and then to HK$48,000 two years later)
Self-employed	HK$7,100 per month or HK$85,200 per year	HK$8,250 per month or HK$99,000 per year		
Casual employees in industry schemes	HK$280 per day	HK$315 per day (to be confirmed)		

Notes
1. The amendments to the relevant income levels would not change the current employer's share of the MPF contributions, as employers are required to contribute regardless of the employee's relevant income. However, employers must calculate their contributions according to the new minimum level of relevant income as shown in **Table 3**.

Table 3: MPF contribution calculations under the new proposals

Proposed monthly relevant income (under review and may be adjusted)	Proposed mandatory contributions (under review and may be adjusted)		
	Employer's contribution	**Employee's contribution**	**Self-employed person's contribution**
Less than HK$8,000	Relevant income x 5%	Not required	Not required
HK$8,000 to HK$48,000	Relevant income x 5%	Relevant income x 5%	Relevant income x 5%
More than HK$48,000	Capped at HK$2,400 per month	Capped at HK$2,400 per month	Capped at HK$2,400 per month or HK$28,800 per year

Notes
1. With the above in mind, it is important to understand what is included under relevant income. According to the definition provided by the MPFA, relevant income refers to any wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite or allowance (including housing allowance and other housing benefits), expressed in monetary terms, paid or payable by an employer (directly or indirectly). However, relevant income excludes SPs or LSPs under the Employment Ordinance.

DEAL VALUE AND VOLUME INCREASED IN Q2 AS THE CHINESE ECONOMY CONTINUES TO GROW

- Deal volume and deal value increased by 10% and 26% respectively in Q2 2018 compared to Q1 2018
- Business confidence among Chinese entrepreneurs continued to improve in Q2 2018. Chinese entrepreneurs are still optimistic about the economic growth and future market conditions as the country's economy continues to grow, supported by strong economic fundamentals
- To mitigate the trade war with the US, the Chinese government has reduced value-added tax rates and further eased restrictions on foreign investment. It is expected that the Chinese government will introduce more reform policies in the next quarter and continue to promote the Belt and Road initiative.

Mid-market M&A levels in the Greater China region recorded 11% growth in deal volume from 743 deals in the first half of 2017 to 826 deals in the first half of 2018. A similar trend was noted for deal value, which grew 9% from US$67.1 billion in the first half of 2017 to US$73 billion in the first half of 2018.

The Chinese government has been pushing for economic structural reform, including the following recent actions:

- From May 2018, the Ministry of Finance has reduced the value-added tax rate from 17% to 16%
- The Ministry of Commerce has further promoted and encouraged acquisitions in the e-commerce and business services sectors along the Belt and Road countries
- The National Development and Reform Commission announced on 28 June 2018 that it would be further easing restrictions on foreign investment in various sectors, including agriculture, automotive and banking
- China's central bank has cut the banks' reserve ratio requirement by 1.25% over Q2 2018 to encourage business lending and support economic growth.

Outbound investment

China's outbound investments continued to increase in Q2 2018 following the introduction in 2017 of specific guidelines and regulations for outbound investment. Industries that benefitted in the first half of 2018 were mainly in the industrials chemicals, technology & media and consumer sectors.

Due to the heightened tensions from the trade war with the US, Chinese entities have become more restricted in terms of accessing the US market. While these are still early days, more focus has been placed on outbound investments in the Belt and Road regions. It is expected that outbound investments led by Chinese entities in this region will continue to rise in the second half of 2018. However, this may limit the overseas industries in which China can invest. For example, there may be less opportunities in the advanced technology space in the Belt and Road regions.

Inbound investment

China's inbound investments were stable in Q2 2018 compared to the same period in 2017. The Ministry of Commerce indicated in June 2018 that foreign direct investment into China only rose 2.3% year-on-year.

The consumer and business services were the key sectors for foreign investment, accounting for around 70% of total foreign investment in the first half of 2018, followed by industrials & chemicals. Inbound investments in the technology sector increased in Q2 2018, particularly in e-commerce and software companies.

It is expected that the trend of inbound investment in Chinese high-tech companies will continue in the second half of 2018.

Figure 1: PE/Trade volume & value

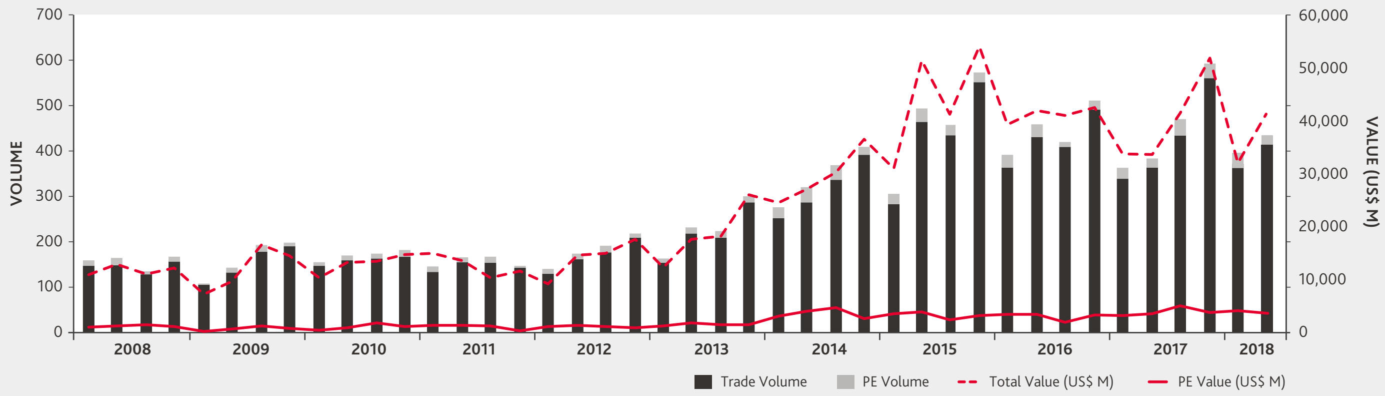

Figure 2: Mid-market volumes by sector in China

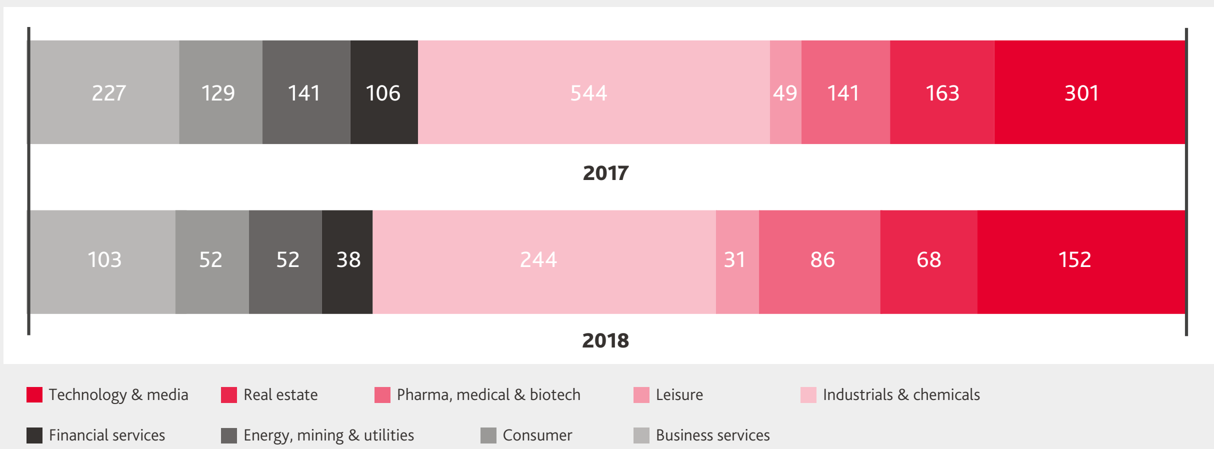

Figure 3: Heat chart by sector in China

Industrials & chemicals	320	28%
Technology & media	218	19%
Business services	132	12%
Consumer	121	11%
Financial services	103	9%
Pharma, medical & biotech	95	8%
Energy, mining & utilities	60	5%
Real estate	47	4%
Leisure	42	4%
TOTAL	**1,138**	**100%**

Top deals

The largest mid-market deal in Q2 2018 was in the pharma, medical & biotech sector (**Figure 2**). The top three major mid-market deals were:

- NWS Holdings Limited, AIA Group Limited and China Capital Zhongcai Fund Management Co.,Ltd. together invested US$500 million in online healthcare firm We Doctor Group Limited – announced in May 2018;
- China FAW Group Corporation, together with Tus-Holdings Co., Ltd. and Contemporary Amperex Technology Co., Ltd., acquired Chinese electric car start-up Byton for US$500 million – announced in June 2018; and
- Multiple bidders (Sequoia Capital, Tencent Holdings Ltd., Coatue Management, L.L.C and Yunfeng Capital) invested in online education firm VIPKID for US$500 million – announced in June 2018.

Looking ahead

The latest heat chart for Greater China (**Figure 3**) indicates that there are a total of 1,138 deals planned or in progress with 320 (28%) related to industrials & chemicals and 218 (19%) related to technology & media. Other key sectors include business services, consumer and financial services.

Going forward, deals could be impacted by current geopolitical issues and macroeconomic factors.

How can BDO help?

BDO's Specialist Advisory Services team in Hong Kong offer a wide range of tailor-made transaction support solutions including financial due diligence, business valuations and M&A advisory. We have assisted hundreds of clients in this respect in their transactions in the past few years.

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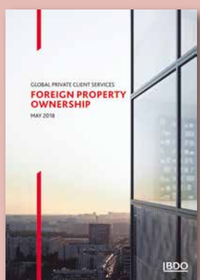

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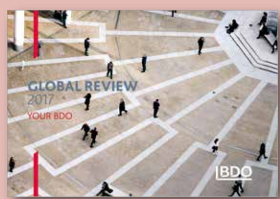

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NEW APPOINTMENT

ENOCH HSU PhD
Director
Tax Services

Enoch Hsu has been appointed as Director of Transfer Pricing in our Tax Department with effect from 27 August 2018.

Enoch has extensive global transfer pricing experience as he had been a transfer pricing economist at big four accounting firms in China, Hong Kong, and US offices since 1999. The clients Enoch served are in various industries, such as consumer products (apparel, electronics, and retail), financial services, technology and telecommunication, software. He is highly proficient in assisting multinational enterprises in preparing global transfer pricing exercises for both compliance and advisory purposes.

Enoch has assisted multinational corporations in restructuring their business organisations by performing robust financial and economic analyses for business operations. In doing so, he helps the companies to design and construct effective business structures and supply chain models to achieve operational efficiency. Enoch has also conducted wide range of intangible valuation projects from tax and transfer pricing perspective. Through negotiating with tax authorities, he has aided clients to obtain advantageous outcomes in cost sharing arrangements and advance pricing agreements. Moreover, while working in Mainland China, Enoch has built his rapport with tax authorities to resolve tax controversies and disputes.

Prior to his transfer pricing profession, Enoch was an adjunct professor of Economics at Santa Clara University for three years. He taught principles of microeconomics, corporate finance, and intermediate microeconomics. He also taught international economics at the MBA level of Leavey School of Business. Enoch has obtained his doctoral degrees in Economics from Claremont Graduate University in 1998.

PETER PANG
Principal
Risk Advisory Services

Peter Pang has been appointed as Principal of Risk Advisory with effect from 2 May 2018.

Peter has extensive experience in managing corporate governance, risk management, internal control review, internal audit, Sarbanes-Oxley and other assurance projects for local, regional and international clients.

Peter has more than 20 years of risk and assurance experience. Prior to joining BDO, he was the Head of Risk of a listed aircraft leasing company with operations in Asia, Europe and America. He also worked in a large international accounting and advisory firm as head of department.

Peter served clients in various industries with a focus on financial services, including banking, securities, fund and asset management, trust operation, investment banks, aircraft leasing, airlines, regulatory and professional organisations, public services, property development, trading, manufacturing and retailing.

Peter is a Fellow of the Hong Kong Institute of Certified Public Accountants, a Fellow of Institute of Chartered Accountants in England and Wales and a certified FRM of Global Association of Risk Professionals (GARP).

ABIGAIL LI
Principal
Tax Services

Abigail Li has been appointed as Principal of Tax with effect from 1 May 2018.

Abigail has extensive experience in Hong Kong and international tax and in a wide range of industries including asset management and financial services, corporate treasury, commodities, shipping, industrial and consumer products. Her clients range from well-established large multinational companies (MNCs) to start-ups or new economy companies.

Abigail is experienced in advising on sophisticated technical tax issues in Hong Kong, and also in respect of cross border transactions involving Hong Kong including tax planning, group structuring, M&A and cross border financial products or transactions.

Abigail is also experienced in assisting clients in various applications with the Hong Kong Inland Revenue Department and Stamp Office including application for advance ruling, certificate of tax residency and stamp duty relief.

Abigail has in-house experience as an Asia Pacific tax manager in a US listed Fortune 500 MNC, resolving local and regional tax issues from operations, treasury, etc.

Abigail's recent projects include structuring tax advice in respect of fund formation and asset management group, tax due diligence for M&A, legal entity rationalisation, financial assets sale and purchase, securitisation, aircraft and ship leasing, etc.

Abigail is a fellow of the Association of Chartered Certified Accountants (ACCA) and a member of its Tax subcommittee.