



# **Hong Kong – Corporate and Individual tax guide 2020**

# HONG KONG

Hong Kong is located in Eastern Asia on the southeast coast of Mainland China. The official languages of Hong Kong are Chinese and English, and the currency is the Hong Kong dollar (HKD). Hong Kong continues to link its currency closely to the United States dollar (USD), maintaining an arrangement established in 1983.

Hong Kong was a self-governing British colony from 1841 to mid-1997. Pursuant to the 1984 Sino-British Joint Declaration, Hong Kong became a Special Administrative Region (SAR) of the People's Republic of China on 1 July 1997. According to the Basic Law (Hong Kong's constitutional document), Hong Kong is guaranteed a high degree of autonomy in all matters except foreign and defence affairs for the next 50 years after the sovereignty transfer under the 'one country, two systems' policy. The Basic Law ensures that Hong Kong's legal system is separate from the one of China and remains within the common law system. The Hong Kong SAR Government is committed to upholding the rule of law, which has played a vital role in Hong Kong's success in the past.

Hong Kong is one of the freest economies in the world. The Hong Kong SAR Government has long been endorsing the 'market driven with minimal government interference' policy in order to create a business-friendly environment in Hong Kong. Hong Kong became a member of the Asia Pacific Economic Cooperation in 1991 and a member of the World Trade Organization (WTO) on 1 January 1995.

Over the past few decades, Hong Kong has been transformed from a labour intensive manufacturing-based economy towards a high value-added and knowledge-based economy, with focus on international trade, financial services, tourism, etc. Since the handover in 1997, Hong Kong has become increasingly integrated with China through trade, tourism, and financial links. Hong Kong has also established itself as the premier stock market for Chinese firms seeking to list abroad and a prime renminbi (CNY) offshore centre.

## Corporate - Taxes on corporate income

Hong Kong adopts a territorial basis of taxation. Profits tax is payable by every person (defined to include corporation, partnership, and sole proprietorship) carrying on a trade, profession, or business in Hong Kong on profits arising in or derived from Hong Kong from that trade, profession, or business. In general, the tax residence of a person is irrelevant and there is no distinction between residents and non-residents when it comes to liability to profits tax, except in a tax treaty context. Non-residents are chargeable to tax on profits arising in or derived from Hong Kong unless they are from jurisdictions with which Hong Kong has a tax treaty and they are protected by the treaty.

Gains and receipts that are capital in nature are not subject to tax. Dividends from local companies chargeable to tax are exempt, whereas dividends from overseas companies are generally offshore in nature and not subject to tax in Hong Kong. The tax treatments of public and private companies are the same. Certain income that would not otherwise be subject to Hong Kong profits tax is deemed to arise in or be derived from Hong Kong from a trade, profession, or business carried on in Hong Kong and thus becomes taxable in Hong Kong. This includes royalties received by a non-resident for the use of or right to use a patent, design, trademark, copyright material, layout-design of an integrated circuit, performer's right, plant variety right, secret process or formula, or other property of a similar nature in Hong Kong, or for the use of such intellectual properties outside Hong Kong, but the royalties paid can be claimed as a deduction by a person for profits tax purposes.

Effective from the year of assessment 2018/19, there is a two-tiered profits tax rate in Hong Kong. The following table shows the applicable tax rates for companies and unincorporated businesses:

Rates of tax	Where the two-tiered rate applies * (%)	Where the two-tiered rate does not apply (%)
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Companies:

First HKD 2 million	8.25	
On the remainder	16.50	16.50

Unincorporated businesses:

First HKD 2 million	7.50	
On the remainder	15.00	15.00

\* As an anti-avoidance measure, a 'group of connected entities' can only nominate one entity within the group to enjoy the two-tiered tax rate for a given year of assessment.

There are special rules for determining the tax liabilities of certain industries, such as shipping, air services, and financial services. There is also a special tax framework for Islamic bonds (i.e. *sukuk*) that provides for the same tax treatments for *sukuk* vis-à-vis their conventional counterparts.

Incomes from certain qualifying debt instruments (QDIs) issued before 1 April 2018 are either tax exempt or subject to a concessionary tax rate (i.e. 50% of the regular profits tax rate) depending on the date of issue and maturity period of the QDIs. Incomes from QDIs issued on or after 1 April 2018 are tax exempt regardless of the maturity period, subject to the fulfilment of certain conditions. However, there is a specific anti-avoidance provision under which the concessionary tax rate/tax exemption does not apply to incomes derived from QDIs by a person who is an associate of the issuer of the QDIs.

Publicly offered funds that are regulated by the Securities and Futures Commission (SFC) of Hong Kong and other similar *bona fide* widely held investment schemes that comply with the requirements of a supervisory authority within an acceptable regulatory regime are exempt from profits tax in Hong Kong. Effective from 1 April 2019, both onshore and offshore privately offered funds are exempt from Hong Kong profits tax on profits derived from certain specified transactions provided that the specified transactions are carried out or arranged by 'specified persons' (i.e. SFC licensed fund managers) or the funds are a 'qualified investment fund' as defined. There are also specific anti-avoidance provisions in the Inland Revenue Ordinance (IRO) deeming certain resident persons to be subject to profits tax on their share of the non-resident person's tax-exempt profits.

Profits derived from the business of reinsurance of onshore and offshore risks and qualifying onshore and offshore captive insurance business are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate).

Qualifying profits derived by a qualifying corporate treasury centre are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate) under specified conditions. Qualifying profits derived from qualifying aircraft leasing activities and qualifying aircraft leasing management activities carried out in Hong Kong are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate) under specified conditions. In addition, the taxable net lease payments derived by a qualifying aircraft lessor from leasing of aircraft to an aircraft operator will be deemed as 20% of the gross lease payments less deductible expenses, excluding tax depreciation allowance.

Effective from the year of assessment 2018/19, the concessionary tax treatments under the following special tax regimes will be available only if certain threshold requirements for determining whether the profits producing activities are carried out in Hong Kong are met:

- Corporate treasury centres.
- Reinsurance business.
- Captive insurance business.
- Aircraft lessors and aircraft leasing managers.
- Shipping operations.

The threshold requirements will be specified by the Commissioner of Inland Revenue (CIR) by a notice published in the Gazette later and measured by various indicators (e.g. number of full time employees with the necessary qualifications in Hong Kong and the amount of operating expenditure incurred in Hong Kong).

## Corporate - Corporate residence

For Hong Kong profits tax purposes, corporate residency is not relevant in determining taxability of an entity except in a tax treaty context. Under the domestic tax law of Hong Kong, the decisive factors for taxability are (i) whether a corporation is carrying on a trade, profession, or business in Hong Kong, and (ii) whether profits are derived from such trade, profession, or business and arising in or derived from Hong Kong.

However, where it is necessary to determine the corporate residence, such as for the purpose of a comprehensive double tax agreement (CDTA), companies incorporated in Hong Kong and companies that are normally managed or controlled/centrally managed and controlled (depending on the provisions of the relevant CDTA) in Hong Kong are generally considered as a Hong Kong tax resident.

### Permanent establishment (PE)

For Hong Kong profits tax purposes, whether a foreign corporation is carrying on a trade, profession, or business in Hong Kong and the source of profits, rather than whether there is a PE in Hong Kong, are the decisive factors in determining taxability. A non-resident person, including a foreign corporation, having a PE in Hong Kong will be deemed as carrying on a trade, profession, or business in Hong Kong. The profits attributable to the PE will be subject to Hong Kong profits tax if such profits are arising in or derived from Hong Kong.

As a part of the new transfer pricing (TP) regulatory regime, a definition of PE has been incorporated into the IRO. For a CDTA territory resident person, the definition of PE follows that in the PE article of the CDTA that Hong Kong has with that territory. For a non-CDTA territory resident person, the definition of PE is specified in the IRO and largely follows that in the PE article of the latest 2017 OECD Model Tax Convention.

Effective from the year of assessment 2019/20, for a non-Hong Kong resident having a PE in Hong Kong, the TP rules on attribution of profits to a PE in Hong Kong (i.e. TP Rule 2) apply to determine the amount of profits attributed to the PE in Hong Kong (see the Branch income section for more details on profits attribution to a PE and the Group taxation section for more details on the TP rules).

## Corporate - Other taxes

### Value-added tax (VAT)

Hong Kong does not have a VAT, goods and services tax, or sales tax.

### Customs duties

There is no tariff on general imports in Hong Kong.

**Excise tax**

Duties are levied on limited categories of dutiable commodities (i.e. tobacco, liquor, methyl alcohol, and hydrocarbons), regardless of whether they are imported or locally manufactured.

**Property tax**

Property tax is charged annually to the owner of any land or buildings (except government and consular properties) in Hong Kong at the standard rate of 15% on the net assessable value of such land or buildings. Net assessable value of a property is the consideration payable to the owner for the right to use the land or buildings less rates paid by the owner and a 20% notional allowance.

Rental income derived by a company from a Hong Kong property is subject to profits tax. The company that is subject to profits tax may apply for an exemption from property tax in respect of the property. If no exemption is applied, the property tax paid can be used to offset against the profits tax payable by the company.

**Stamp duty**

Stamp duty is charged on transfer of Hong Kong stock by way of sale and purchase at 0.2% of the consideration (or the market value if it is higher) per transaction. Hong Kong stock is defined as stock the transfer of which must be registered in Hong Kong.

For conveyance on sale of immovable property in Hong Kong, the stamp duty payable depends on the type of property transferred (i.e. residential property vs. non-residential property) and the property consideration. Currently, stamp duty on transfer of properties is charged as follows:

- Transfer of residential property: A flat rate of 15%, with certain exemptions. One common exemption is acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition (*see 2 below*).
- Acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition and some other specified circumstances: Scale 2 rates ranging from HKD 100 (for property consideration of up to HKD 2 million) to 4.25% (for property consideration exceeding HKD 20 million).
- Transfer of non-residential property: Scale 1 rates ranging from 1.5% (for property consideration of up to HKD 2 million) to 8.5% (for property consideration exceeding HKD 20 million).

The stamp duty payable is computed by applying the relevant rate to the consideration or market value of the property (whichever is higher). When Scale 1 or Scale 2 rates are applicable, marginal relief is available for transfer where the consideration is marginally above the lower bound of each rate band.

For lease of immovable property in Hong Kong, stamp duty is calculated at a specified rate of the annual rental that varies with the term of the lease. Currently, the applicable rate ranges from 0.25% (for lease period of not more than one year) to 1% (for lease period of more than three years).

Exemption is available for certain transactions, such as transfer of shares between associated corporate bodies, transfer of shares or units of exchange traded funds listed in Hong Kong, and certain stock borrowing and lending transactions, provided that the specified conditions for exemption (if any) are satisfied.

**Special Stamp Duty (SSD)**

There is an SSD on resale of residential property within 36 months from the date of acquisition. The SSD is imposed on top of the stamp duty payable on conveyance on sale or agreement for sale of residential property, with a few exemptions. The SSD payable will be calculated based on the stated consideration or the market value (whichever is higher) of the resold property at the regressive rates indicated below.

20% for residential properties held for six months or less.

15% for residential properties held for more than six months but for 12 months or less.

10% for residential properties held for more than 12 months but for 36 months or less.

**Buyer's Stamp Duty (BSD)**

A BSD is payable on acquisition of Hong Kong residential properties by any person (including Hong Kong and foreign companies) other than a Hong Kong permanent resident. The BSD is charged at a flat rate of

15% on the stated consideration or the market value of the property acquired, whichever is higher. The BSD is imposed on top of the stamp duty and the SSD (if applicable), with exemptions in certain situations.

#### **Business registration fees**

Every person who carries on a business in Hong Kong is required to apply for business registration with a fee within one month from the date of commencement of the business. The business registration certificate has to be renewed either on an annual basis or every three years with a payment of a business registration (renewal) fee. Special registration and licence fees are applicable to banks and deposit-taking companies.

#### **Capital duty**

There is currently no capital duty in Hong Kong.

#### **Government rates and rent**

Rates are an indirect tax levied on properties in Hong Kong. Rates are charged at 5% of the rateable value, which is the estimated annual rental value of a property at the designated valuation reference date of 1 October.

Privately owned land in Hong Kong is normally held by way of a government lease under which rent is payable to the Hong Kong Special Administrative Region (HKSAR) Government in return for the right to hold and occupy the land for the term (i.e. the duration) specified in the lease document. Currently, government rent is calculated at 3% of the rateable value of the property and is adjusted in step with any subsequent changes in the rateable value.

#### **Payroll taxes**

In Hong Kong, there are no payroll taxes other than the Mandatory Provident Fund (MPF) contribution (see *below*).

#### **Mandatory Provident Fund (MPF) contribution**

Under the MPF scheme, an employer is required to make a mandatory contribution for an employee in the amount equal to 5% of the monthly income of that employee. The maximum level of income for contribution purpose is HKD 30,000 per month. An employer may make voluntary contributions in addition to the mandatory contribution required.

### **Corporate - Branch income**

The two-tiered tax rate system that is applicable to corporations is also applicable to branches of foreign corporations in Hong Kong.

Under the Inland Revenue Rule 5 (IRR 5), the Hong Kong sourced profit of a Hong Kong branch of a foreign corporation, other than a financial institution, is determined according to the accounts maintained for the Hong Kong operation (or business). If the Hong Kong accounts do not disclose the true profits arising in or derived from Hong Kong attributable to the Hong Kong operation, the Hong Kong profit of the branch for profits tax purposes will be computed according to the ratio of turnover in Hong Kong to total turnover (or the proportion of Hong Kong assets over total assets) on the worldwide profits. Alternatively, the Hong Kong Inland Revenue Department (HKIRD) tax assessor may estimate the profits of the Hong Kong branch. In certain situations, the profits of the Hong Kong branch can be estimated based on a fair percentage of the turnover in Hong Kong.

Effective from the year of assessment 2019/20, the Authorized OECD Approach (i.e. the separate enterprises principle) (TP Rule 2) needs to be adopted for attributing income or loss to a PE of a non-Hong Kong resident person in Hong Kong. With the new TP Rule 2, the IRR 5 mentioned above will have effect only to the extent that it is not inconsistent with TP Rule 2.

### **Corporate - Income determination**

Inventory valuation

Inventory may be stated at the lower of cost or market value. Last in first out (LIFO) may not be used for

tax purposes. First in first out (FIFO) must be consistently applied.

The prevailing accounting standards require financial instruments to be carried at market value, with fluctuations in values of such assets and liabilities taken to the profit and loss accounts in the year they arise, irrespective of whether the revaluation gains or losses are realised (i.e. the 'fair value basis'). Following the court decision in the *Nice Cheer* case, the increases (unrealised gains) in the market values of trading securities are not taxable while the decreases (unrealised losses) may be deductible when they are recorded in the financial statements. For years of assessment of which the basis period begins on or after 1 January 2018, taxpayers may make a generally irrevocable election to adopt the above-mentioned fair value basis to account for their financial instruments for tax purpose, subject to certain conditions and with certain exceptions. Whether the amounts recognised in the profit and loss accounts are taxable or deductible will continue to be subject to the source rules and the nature (i.e. capital vs revenue) of the amounts.

There are special tax provisions for valuation upon cessation of a business under which inventory is valued at market value, unless it is sold to a person carrying on business in Hong Kong, who may deduct a corresponding amount as the cost of the inventory in computing the assessable profits.

There are also special tax provisions for valuation when (i) there is a change of intention for holding something as trading stock to capital asset or vice versa, or (ii) trading stock of a trade has been acquired or disposed of otherwise than in the course of the trade. In such circumstances, valuation based on the market value will apply.

### **Capital gains**

Gains from realisation of capital assets or receipts that are capital in nature are not taxed.

### **Dividend income**

Dividends from local companies chargeable to tax are exempt, whereas dividends from overseas companies are generally offshore in nature and not subject to Hong Kong profits tax. Hong Kong corporations may declare bonus issues (i.e. stock dividends), which are not taxable in the hands of the recipients.

### **Interest income**

Hong Kong sourced interest income received by or accrued to a corporation carrying on a trade or business in Hong Kong is subject to profits tax. Exemption is provided to interest income derived from any deposit placed in Hong Kong with a financial institution, unless the deposit secures a borrowing where the interest expense is deductible. This exemption, however, does not apply to interest accruing to a financial institution.

Interest accruing to a bank or financial institution will be deemed to be sourced and taxable in Hong Kong if the interest arises through or from the carrying on of business in Hong Kong by the bank or financial institution.

Interest income arising through or from the carrying on of an intra-group financing business in Hong Kong by a corporation (other than a financial institution) will be deemed to be sourced and taxable in Hong Kong.

### **Royalties**

Royalties paid or accrued to a non-resident for the use of or right to use in Hong Kong or outside Hong Kong (if the royalties are deductible in ascertaining the assessable profits of a person for Hong Kong profits tax purposes) a trademark, patent, design, copyright material, layout-design of an integrated circuit, performer's right, plant variety right, secret process or formula, or other property of a similar nature, or for the use in Hong Kong of cinema or television tape or any sound recording, are deemed to be taxable in Hong Kong. A total of 30% of the sum receivable is deemed to constitute profits subject to tax in normal situations. Where such royalties are received by or accrued to an associated corporation, however, 100% of the sum is deemed to constitute profits under certain circumstances.

In addition, royalties for the use of or right to use outside Hong Kong of any intellectual property (IP) or know-how generated from any R&D activity in respect of which a tax deduction for R&D expenditure is allowable in ascertaining the assessable profits of the recipient of the royalties are deemed to be taxable in Hong Kong.



**Partnership income**

Partnership business is taxed as a single entity, although an individual partner can use its share of losses incurred by a partnership to offset against the assessable profits of its other business. In general, there is no special registration requirement other than business registration for a partnership. The assessable profits of a partnership are basically determined in the same way as those of a corporation, with certain special rules (e.g. salaries or other remunerations paid to a partner or a partner's spouse are not deductible).

**Unrealised exchange gains/losses**

In general, unrealised exchange gains/losses are taxable/deductible if they are recognised in the profit and loss accounts in accordance with Generally Accepted Accounting Principles (GAAP), provided that they are revenue in nature and with a Hong Kong source. The nature and source of exchange gains/losses are determined by the nature and source of the underlying transactions. Exchange gains/losses arising from ordinary business transactions (e.g. trade receivables or payables) are taxable/deductible whereas exchange gains/losses arising from capital transactions (e.g. sale of capital assets) are non-taxable/non-deductible.

**Foreign income**

Hong Kong resident corporations are not taxed on their worldwide income. Foreign-sourced income, whether or not remitted to Hong Kong, is not taxed. As such, there is no specific tax provision dealing with deferral or non-remittance of foreign earnings. Nor does Hong Kong have any controlled foreign company (CFC) legislation.

**Corporate - Deductions**

Expenses that are incurred for producing profits chargeable to tax and that are not capital in nature are generally tax deductible. In addition, special tax relief is available for certain capital expenditure. There are special rules for deduction of certain expenses (e.g. interest expenses).

Accounting treatments are usually followed in determining the assessable profits, except when there is an explicit rule in the IRO. Accrued expenses recognised in the profit and loss accounts in accordance with GAAP are usually deductible if they are incurred for producing profits chargeable/subject to Hong Kong profits tax and are not capital in nature.

Expense items for which a tax adjustment is necessary in determining the amount of taxable profits from the accounting profits include: tax depreciation allowance vs. accounting depreciation, expenses that are capital in nature, general provisions that are non-deductible, and non-deductible interest expenses on borrowings used to finance non-income producing assets.

Set out below are the Hong Kong profits tax treatments of some common expense items.

**Tax depreciation of fixed assets**

Tax depreciation allowances/deductions are available for capital expenditure incurred on the construction of buildings or structures and in the provision of machinery and plant for trade or business purposes, as follows:

- Industrial buildings and structures: An initial allowance of 20%, in addition to an annual allowance of 4%, of the cost of construction or cost of purchase from a developer is granted for an industrial building or structure occupied for the purpose of a qualifying trade. Provision is made for balancing allowance or charge in the year of assessment in which the building is disposed of to adjust the written-down value of the building to the disposal price. Balancing charges are restricted to the total of initial and annual allowances previously given.
- Commercial buildings and structures: An annual allowance of 4% of the capital expenditure incurred on the construction is applicable. A balancing allowance or charge applies upon disposal. Balancing charges are restricted to the total annual allowances previously given.
- Plant and machinery: An initial allowance of 60% of the capital expenditure on plant and machinery is given for the year of assessment during the basis period in which the expenditure is incurred. An annual allowance is also given for depreciation at three prescribed rates on the reducing value of each of the



- three depreciation rate 'pools'. The three prescribed rates are 10%, 20%, and 30%, and the reducing value of each of the three depreciation rate pools is original cost less initial and annual allowances and sales proceeds. Provision is made for balancing charges when plant and machinery within one of the three depreciation rate pools is sold or disposed of and the reducing value of that pool is less than the sale price, which is capped at the original amount incurred in the pool. In addition, balancing allowances or charges may be applicable upon cessation of business. Otherwise, sales proceeds are deducted in calculating the reducing value on which the annual allowance is calculated.

Book depreciation is adjusted for tax purposes in accordance with the above depreciation allowances granted under the IRO.

#### **Goodwill**

Cost of acquisition of goodwill/amortisation of goodwill is not deductible as it is capital in nature.

#### **Organisational and start-up expenses**

In general, company formation/start-up expenses that are incurred before the commencement of a trade, profession, or business and that are for the establishment of the overall income producing structure are capital in nature and not tax deductible.

#### **Research & development (R&D)**

A new R&D tax deduction regime is introduced in Hong Kong that applies to qualifying expenditure incurred or qualifying payment made on or after 1 April 2018. Under the new R&D tax deduction regime, there are two types of qualifying R&D expenditure, namely Type A expenditure and Type B expenditure. Subject to certain conditions, Type A expenditure (R&D expenditure other than Type B expenditure) will be granted a 100% normal deduction. Type B expenditure will be entitled to a 300% deduction for the first HKD 2 million of the expenditure and a 200% deduction for the remaining amount, without any limit on the amount eligible for the 200% deduction.

#### **Interest expenses**

There is no thin capitalisation rule in Hong Kong. However, except in some specified circumstances (e.g. interest expenses paid to an overseas associated corporation by a corporation carrying on an intra-group financing business in Hong Kong where certain conditions are met), interest expenses paid to an overseas recipient (whether a related or unrelated party) are generally not deductible if the overseas recipient is not subject to Hong Kong profits tax on the interest income. In addition, deduction of interest expense is subject to stringent and complicated rules that are designed to guard against loan arrangements with an intention to avoid Hong Kong profits taxes.

#### **Bad debts**

In general, a bad or doubtful debt incurred in any trade, business, or profession, proved to the satisfaction of the HKIRD to have become bad during the basis period for a year of assessment, is deductible. The deduction is limited to debts that were included as a trading receipt in ascertaining the taxpayer's assessable profits or debts in respect of money lent in the ordinary course of a money-lending business in Hong Kong.

If a taxpayer has elected to adopt the fair value basis to account for its financial instruments for profits tax filing purpose, a special deduction rule instead of the above general rule applies. Under the special rule, an impairment loss recognised in respect of a financial instrument that is not credit-impaired is not deductible. If any bad debt, doubtful debt, or impairment loss that has previously been allowed as a deduction is ultimately recovered, it will be treated as taxable profits of the basis period in which it is recovered.

#### **Charitable contributions**

A deduction is allowed for cash donations to approved charities made in the basis period for a year of assessment if the aggregate of such donations is not less than HKD 100. The deduction is limited to 35% of the assessable profits of the year of assessment.

#### **Pension expenses**

A deduction is allowed for regular/ordinary contributions to a mandatory provident fund scheme or recognised occupational retirement scheme made by an employer in respect of an employee to the extent

that the contributions do not exceed 15% of the employee's total emoluments for the period to which the contributions relate.

Special payments, other than the ordinary contributions to a mandatory provident fund scheme or recognised occupational retirement scheme, are capital in nature but can be deducted evenly over a five-year period under a specific provision of the IRO.

There are also specific rules for deduction of provisions for contributions to a mandatory provident fund scheme or recognised occupational retirement scheme.

### **Payments for directors**

Director fees or other remunerations paid by a corporation to its directors are generally deductible under the normal deduction rule. Nevertheless, no deduction is allowed on salaries or other remunerations paid to a sole proprietor or any partners or partners' spouses of a partnership business.

### **Contingent liabilities**

Generally speaking, general provisions for expenses are not deductible, whereas specific provisions are deductible if the HKIRD is satisfied that the amount has been incurred (i.e. the taxpayer has a legal/contractual obligation to pay such amount in the future) and that the provision represents a reasonably accurate estimate of the future liability.

### **Special deductions**

There are special deduction rules for expenditures incurred:

- for refurbishment of a building or structure, other than a domestic building or structure
- on environmental protection installation and machinery
- on environment-friendly vehicles
- on machinery or plant used specifically and directly for any manufacturing process, computer hardware (other than that which is an integral part of machinery or plant), computer software, and computer systems (collectively known as prescribed fixed assets)
- for registering trademarks, designs, or patents used in the production of taxable profits, and
- on the purchase of patent/know-how rights and specified intellectual property (IP) rights (i.e. copyrights, registered trademarks, registered designs, protected layout-design (topography) rights in respect of integrated circuits\*, protected plant variety rights\*, or performer's economic rights\*), provided certain specified conditions are met.

Effective from the year of assessment 2018/19.

### **Fines and penalties**

Fines and penalties are generally not deductible, as the HKIRD does not consider them to be expenses incurred for producing profits chargeable/subject to tax.

### **Taxes**

Taxes paid on corporate profits or income are generally not deductible for the purpose of calculating the assessable profits. The HKIRD may consider a foreign tax that is not calculated by reference to profits or income as deductible under the general deduction provision. Where interest income or gains from the sale of a certificate of deposit or bill of exchange are deemed to be subject to profits tax in Hong Kong, a deduction is allowed for foreign taxes of substantially the same nature of Hong Kong profits tax paid in respect of the same income, provided that the foreign taxes are not paid in a jurisdiction having a CDTA with Hong Kong. In the case where the foreign taxes are paid in respect of the above interest income or gains in a CDTA jurisdiction, a Hong Kong resident can only claim a tax credit for the foreign taxes paid on those interest income or gains.

### **Net operating and capital losses**

Net operating losses incurred in an accounting year can be carried forward indefinitely to offset future profits of the business. A corporation carrying on more than one business may have losses in one business offset profits of the others, with any balance being carried forward. Net operating losses cannot be carried backward.

Capital losses are not tax deductible.

#### **Payments to foreign affiliates**

Royalties and service fees paid/payable by a Hong Kong corporation to foreign affiliates are deductible, provided they are incurred for the production of profits chargeable/subject to tax. There is no special restriction on the deductibility of these payments.

In general, interest payable by a Hong Kong corporation to a foreign affiliate is not deductible if the recipient is not chargeable/subject to Hong Kong profits tax on the interest income received (except where either the payer or the recipient is a financial institution as defined in the tax law). Interest expenses on money borrowed from a non-Hong Kong associated corporation by a corporation in the ordinary course of its intra-group financing business carried on in Hong Kong are deductible, provided that certain specified conditions are met.

## **Corporate - Group taxation**

### **Transfer pricing (TP)**

Hong Kong has recently implemented a TP regulatory regime and TP documentation requirements. The key TP measures newly introduced and the respective effective dates are as follows:

#### **The TP regulatory regime**

There are two sets of TP rules. Under TP Rule 1, the HKIRD can impose TP adjustments on domestic or cross-border related-party transactions that are not entered into on an arm's-length basis and that result in a potential Hong Kong tax advantage, with exemptions for certain specified domestic transactions. Under TP Rule 2, the Authorised Organisation for Economic Co-operation and Development (OECD) Approach and the separate enterprises principle will be adopted for profit attribution to a PE of a non-Hong Kong resident in Hong Kong (see the Branch income section for more information).

TP Rule 1 applies to years of assessment beginning on or after 1 April 2018, whereas TP Rule 2 applies to years of assessment beginning on or after 1 April 2019. There is a grandfathering provision under which transactions entered into or effected before 13 July 2018 (i.e. the enactment date of the new TP law) will not be subject to the above TP rules. The HKIRD published Departmental Interpretation and Practice Notes (DIPNs) 59 and 60 in July 2019 to provide further guidance on the interpretation and application of TP Rule 1 and Rule 2, respectively.

In general, the HKIRD will apply the TP rules in the way that is best consistent with the OECD's Transfer Pricing Guidelines and the commentary on the business profits article and associated enterprise article of the OECD Model Tax Convention.

#### **The TP documentation requirement**

There is a mandatory 'three-tiered' TP documentation requirement consisting of Master File, Local File, and Country-by-Country (CbC) report.

For Master File and Local File, there are certain exemption thresholds based on the business size and the volume of different types of related-party transactions such that a Hong Kong enterprise is not required to prepare the Master File and the Local File if it meets either the business size threshold or all the volume-based, related-party transactions thresholds. Master File and Local File are required for accounting periods beginning from 1 April 2018 and have to be prepared within nine months after the accounting period end to which the files relate.

For CbC reports, please see the description of the CbC reporting regime below.

The HKIRD published DIPNs 58 in July 2019 to provide further guidance on the three-tiered TP documentation requirements, while DIPNs 46 on TP guidelines, which was issued back in 2009, serves as a reference in situations where the new TP Rules 1 and 2 are not applicable.

**Country-by-country (CbC) reporting regime**

Key features of the CbC reporting regime in Hong Kong are summarised as follows:

The Hong Kong ultimate parent entity of a multinational enterprise group with annual consolidated group revenues of 750 million euros (EUR) (i.e. about HKD 6.8 billion) or above (i.e. a reportable group) will be required to file a CbC report in Hong Kong.

A Hong Kong entity of a reportable group that is not the group's ultimate parent entity will also be required to file a CbC report in Hong Kong if the ultimate parent entity is not required to file a CbC report in its own jurisdiction of tax residence or if Hong Kong is not able to obtain the CbC report from that jurisdiction.

The CbC report filing requirement will apply retrospectively to accounting periods beginning on or after 1 January 2018.

Generally speaking, the deadline for filing a CbC report is within 12 months after the end of the accounting period to which the report relates. Where surrogate parent filing applies and a later deadline for filing CbC reports is prescribed in the laws or regulations of the jurisdiction of tax residence of the surrogate parent entity, the later deadline will be taken as the filing deadline in relation to the CbC report concerned.

**The advance pricing arrangement (APA) regime**

A statutory APA programme has been introduced for the year of assessment 2018/19. The objectives of the APA programme are to help taxpayers obtain tax certainty on their complex or significant TP arrangements and reduce the risk of double taxation arising from related-party transactions. Any Hong Kong resident enterprise or a non-resident enterprise with a PE in Hong Kong, chargeable to Hong Kong profits tax and having related-party transactions, may apply for an APA, provided that certain conditions (including the threshold for an APA application) are met. Under the statutory APA regime, enterprises can apply for unilateral, bilateral, or multilateral APA.

Prior to the year of assessment 2018/19, the HKIRD accepts APA application as part of the advance ruling application. DIPN 48 was issued by the HKIRD and provides guidance on the APA application, such as the timeframe and threshold for an APA application, the various stages involved in the APA process, an audit involving years covered by a concluded APA, and possible rollback of the TP methodology agreed under an APA to prior years. The appendices of the DIPN include various sample documents for use in an APA application. It is expected that the HKIRD will revise certain guidance in DIPN 48 as a result of the recent introduction of the statutory APA regime in Hong Kong.

**Thin capitalisation**

Hong Kong does not have thin capitalisation rules. For restrictions on deduction of interest expenses, see Interest expenses in the Deductions section.

**Controlled foreign companies (CFCs)**

Hong Kong does not have a CFC regime.

**Corporate - Tax credits and incentives****Foreign tax credits**

Foreign tax credits are available if foreign taxes are payable/paid on income derived from a jurisdiction that has entered into a CDTA with Hong Kong and the same income is subject to tax in Hong Kong. Effective from the year of assessment 2018/19, taxpayers are required to take all reasonable steps to minimise the foreign tax payable before making a claim for tax credit in Hong Kong. *See the Withholding taxes section for a list of jurisdictions that have entered into a CDTA with Hong Kong.*

**Foreign investment incentives**

Hong Kong does not have any specific incentives for foreign investment, except that offshore funds may be exempt from profits tax under certain circumstances.

**Other tax incentives**

*Please refer to the Taxes on corporate income section for other tax incentives that can be enjoyed by both foreign and Hong Kong companies.*

### Corporate - Withholding taxes

There is no withholding tax (WHT) on dividends and interest. Royalties received by non-residents (see Royalties in the Income determination section) are subject to a WHT (see the applicable WHT rates for corporations below).

Resident consignees are required to furnish quarterly returns to the HKIRD showing the gross proceeds from sales on behalf of their non-resident consignors and to pay to the CIR a sum equal to 0.5% of such proceeds. The HKIRD normally accepts this as satisfying the Hong Kong tax obligations of the non-resident. Hong Kong has so far entered into 43 treaties with different jurisdictions. The following table shows the applicable WHT rates for payments made from Hong Kong payers to non-treaty and treaty country corporate recipients. The rates shown in the table are the lower of the domestic and treaty rates. For WHT rates on payments received by Hong Kong recipients from treaty country payers, please refer to the summaries of the respective treaty countries. All of the following treaties have been ratified and become effective unless indicated otherwise in the notes below.

Recipient	WHT (%)		
	Dividends (1)	Interest (1)	Royalties (2)
Non-treaty	0	0	2.475 to 4.95 (2)
Treaty:			
Austria	0	0	2.475 to 3 (3)
Belarus	0	0	2.475 to 3 (4)/2.475 to 4.95 (5)
Belgium	0	0	2.475 to 4.95 (5)
Brunei	0	0	2.475 to 4.95 (5)
Cambodia (8)	0	0	2.475 to 4.95 (5)
Canada	0	0	2.475 to 4.95 (5)
China, the People's Republic of	0	0	2.475 to 4.95 (5)
Czech Republic	0	0	2.475 to 4.95 (5)
Estonia (8)	0	0	2.475 to 4.95 (5)
Finland	0	0	2.475 to 3 (3)
France	0	0	2.475 to 4.95 (5)
Guernsey	0	0	2.475 to 4 (6)
Hungary	0	0	2.475 to 4.95 (5)
India	0	0	2.475 to 4.95 (5)
Indonesia	0	0	2.475 to 4.95 (5)
Ireland	0	0	2.475 to 3 (3)
Italy	0	0	2.475 to 4.95 (5)
Japan	0	0	2.475 to 4.95 (5)
Jersey	0	0	2.475 to 4 (6)
Korea	0	0	2.475 to 4.95 (5)
Kuwait	0	0	2.475 to 4.95 (5)
Latvia	0	0	0/2.475 to 3 (7)
Liechtenstein	0	0	2.475 to 3 (3)
Luxembourg	0	0	2.475 to 3 (3)
Macau (9)	0	0	2.475 to 3 (3)
Malaysia	0	0	2.475 to 4.95 (5)
Malta	0	0	2.475 to 3 (3)
Mexico	0	0	2.475 to 4.95 (5)

The Netherlands	0	0	2.475 to 3 (3)
New Zealand	0	0	2.475 to 4.95 (5)
Pakistan	0	0	2.475 to 4.95 (5)
Portugal	0	0	2.475 to 4.95 (5)
Qatar	0	0	2.475 to 4.95 (5)
Romania	0	0	2.475 to 3 (3)
Russia	0	0	2.475 to 3 (3)
Saudi Arabia	0	0	2.475 to 4.95 (5)
South Africa	0	0	2.475 to 4.95 (5)
Spain	0	0	2.475 to 4.95 (5)
Switzerland	0	0	2.475 to 3 (3)
Thailand	0	0	2.475 to 4.95 (5)
United Arab Emirates	0	0	2.475 to 4.95 (5)
United Kingdom	0	0	2.475 to 3 (3)
Vietnam	0	0	2.475 to 4.95 (5)

## Notes

1. Hong Kong does not impose WHT on dividends and interest currently. However, the treaties provide for a maximum WHT rate on dividends and interest should Hong Kong impose such WHT in the future. Some of the treaties also provide for a reduced WHT rate on dividends and interest if conditions specified in the treaties are met.

2. With the introduction of two-tier profits tax rates, there are two possible sets of domestic WHT rates on royalties paid to non-resident corporations:

- i. If the two-tier tax rates apply, the WHT rates are 2.475% for the first HKD 6.67 million of gross royalty income (i.e. the deemed profit rate of 30% times the tax rate of 8.25% for the first HKD 2 million of assessable profits) and 4.95% for the remaining amount of gross royalty income (i.e. the deemed profit rate of 30% times the tax rate of 16.5% for the remaining amount of assessable profits).
  - ii. If the two-tier tax rates do not apply, the WHT rate for the whole amount of gross royalty income is 4.95%.
- The 2.475% and 4.95% rates are determined by applying the relevant two-tier rates, which are 8.25% and 16.5%, respectively, on the deemed assessable profits of the royalties. In the normal situation, the deemed assessable profits are 30% of the royalties received by or accrued to a non-resident corporation. Hence, the effective WHT rate on the royalties ranges from 2.475% (when the deemed assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the deemed assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two-tier rates are not applicable).

In the situation where a person carrying on a trade or business in Hong Kong has, at any time, wholly or partly owned the IP in respect of which the royalties are paid and the non-resident corporation is an associate of the Hong Kong payer, the deemed assessable profits are 100% of the royalties received

by or accrued to a non-resident corporation. Hence, the applicable WHT rates are 8.25% for the first HKD 2 million of assessable profits and 16.5% for the remaining amount if the two-tier rates are applicable.

3. The domestic WHT rate on the gross royalty income ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 3% according to the treaty.

4. For payments for the use of, or the right to use, aircraft, the effective WHT rate ranges from 2.475% on the gross payments (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 3% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable). For other cases, the effective WHT rate on the gross royalty income ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable).

5. Since a rate specified in the treaty is higher than the domestic WHT rates, the effective WHT rate on the gross royalty income ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable).

6. The domestic WHT rate on the gross royalty income ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 4% according to the treaty.

7. The 0% rate applies to payments for the use of, or the right to use, industrial, commercial, or scientific equipment or for information concerning industrial, commercial, or scientific experience. For other cases, the WHT rate on the gross royalty income ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (in relation to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 3% according to the treaty.

8. Ratified and will be effective from year of assessment 2020/21 in Hong Kong.

9. Not yet ratified.

## Corporate - Tax administration

### Taxable period

A year of assessment (or tax year) begins on 1 April of a year and ends on 31 March of the following year. The period that is used to compute the taxable profits for a year of assessment is called the basis period, which is normally the financial year ended in the year of assessment.

### Tax returns

Tax returns are issued on the first working day of April each year. Effective from year of assessment 2018/19, there are ten supplementary forms for profits tax filing purpose, and taxpayers are required to file the supplementary forms that are applicable to them together with the tax return issued.

The filing deadline is usually within a month from the date of issue of the tax return. However, corporations whose financial year ended after 30 November and are represented by a tax representative are normally granted with an extension for filing their returns. The exact filing due date depends on the accounting year-end date of the taxpayer.

The basis of assessment is the accounting profits of the financial year ending within the year of assessment, with appropriate adjustments for tax purposes. A tax return is usually filed together with a tax



computation showing the tax adjustments to the accounting profits in arriving at the taxable profits or allowable tax losses for a given year of assessment.

Corporate taxpayers are also required to attach their audited accounts as supporting documents when filing a profits tax return, unless they qualify as a small corporation as defined by the HKIRD (i.e. mainly those with gross income for a basis period of not exceeding HKD 2 million plus a few other conditions). Small corporations are not required to attach supporting documents with their profits tax returns but are still required to keep those documents and submit them upon request. A branch of a foreign corporation doing business in Hong Kong is required to file a profits tax return annually, and the HKIRD may require audited accounts of the foreign corporation to support the Hong Kong branch's profits tax return.

Notice of assessment will be issued after the tax return has been examined by the HKIRD. Taxpayers may be subject to post-assessment investigation or field audit under the computerised random selection procedures of the HKIRD at a later date.

#### **Payment of tax**

Tax is usually payable in two instalments. The dates of payment of tax, which generally fall between November of the year in which the return is issued and April of the following year, are determined by the CIR and specified in an assessment notice. A system of provisional tax payments applies whereby estimated tax payments are made during the current year. The provisional profits tax payable is normally estimated based on the previous year's profits tax liability. The provisional profits tax already paid is credited against the final profits tax assessed for a year of assessment, which is determined after filing of the return.

Taking a company with an accounting year end date of 31 December as an example, the final tax payment for the company for a given tax year is usually due in November of the year in which the return is issued, whereas the provisional tax payments (to be paid in two instalments) are usually due in November of the current year and January of the next year.

#### **Tax audit process**

There is no specific tax audit cycle in Hong Kong. Tax audit targets are selected with reference to certain criteria determined by the HKIRD.

#### **Statute of limitations**

An additional assessment may be made by an HKIRD tax assessor if a taxpayer chargeable to tax has not been assessed to tax or has been assessed at less than the proper amount. The assessment must be made within the relevant year of assessment or within six years after the end of that year of assessment. The time limit for making additional assessments is extended when a taxpayer either has not been assessed, or is under-assessed, due to fraud or wilful evasion. In that case, an additional assessment may be made up to ten years after the end of the relevant assessment year.

A statement of loss is not an assessment, and the above six-year time limit does not apply to issue or revision of a statement of loss. A tax loss year remains technically open until the sixth year after the first year in which the taxpayer has an assessable profit after utilising all the tax losses brought forward.

#### **Topics of focus for tax authorities**

Profits tax issues that are often subject to close scrutiny of the tax authority include offshore claim of profits, capital claims of income, transactions with related parties and closely connected non-residents, and deductibility of expenses (e.g. interest expenses, share-based payments, intra-group management/service fees).

#### **General anti-avoidance rules (GAARs)**

The IRO includes a GAAR (i.e. section 61A) allowing the HKIRD to disregard a transaction or counteract the tax benefit conferred by a transaction if the sole or dominant purpose of entering into such a transaction is to obtain a tax benefit. Whether the sole or dominant purpose of entering into a transaction is for obtaining a tax benefit will be assessed according to a set of factors stipulated in section 61A. Another GAAR in the IRO is section 61, which empowers the HKIRD to disregard a transaction that reduces or would reduce the amount of tax payable by any person if that transaction is considered artificial or fictitious. Although both GAARs could be used, in practice, section 61A is more often invoked by the HKIRD in tackling tax avoidance schemes.

## Corporate - Other issues

### Base Erosion and Profit Shifting (BEPS)

Hong Kong has enacted domestic tax legislation to implement the following minimum standards under the BEPS Action Plan: (i) introducing a TP regulatory regime and a mandatory three-tiered TP documentation requirement in Hong Kong, (ii) implementing a statutory APA regime in Hong Kong, and (iii) removing the ring-fencing features in certain concessionary tax regimes in Hong Kong.

### Multilateral Instrument (MLI)

Hong Kong, as represented by mainland China, was one of the signatories to the MLI. In implementing the MLI, Hong Kong has taken a pragmatic approach by (i) opting in the provisions of the MLI that represent the BEPS minimum standards (e.g. the principal purpose test for preventing treaty abuse and the requirement for allowing a minimum three-year period for a person to present its case for Mutual Agreement Procedure) and (ii) opting out of the other provisions that are not mandatory, for instance, those provisions addressing hybrid mismatches and artificial avoidance of PE. Hong Kong is currently going through the necessary domestic legislative process to implement the MLI as domestic legislation, and the MLI is not yet effective for Hong Kong.

**Automatic exchange of financial account information (AEOI) / Common Reporting Standard (CRS) regime**  
Under the AEOI/CRS regime in Hong Kong, reportable financial institutions are required to identify the reportable financial accounts held by (i) tax residents of reportable jurisdictions or (ii) passive non-financial entities whose controlling persons are tax residents of reportable jurisdictions in accordance with the specified due diligence procedures, collect the required information of those reportable accounts, and furnish such information to the HKIRD. Such information will be exchanged on an annual basis. Hong Kong will only conduct AEOI with a reportable jurisdiction when an arrangement is in place with the reportable jurisdiction concerned to provide the basis for exchange.

There are currently 75 reportable jurisdictions, but the number of reportable jurisdictions has been increased to 126 effective from 1 January 2020. As of May 2019, Hong Kong has activated exchange relationships for CRS purposes with 59 jurisdictions based on either a bilateral or multilateral competent authority agreement for CRS.

### Tax information exchange agreements (TIEAs)

Currently, Hong Kong has entered into seven TIEAs with different jurisdictions as shown in the following table:

Faroese	Sweden
Greenland	United States
Iceland	

All of the above TIEAs are ratified and effective.

In addition to the signing of the Hong Kong-United States TIEA, Hong Kong signed a Model 2 intergovernmental agreement (IGA) with the United States in November 2014 to facilitate financial institutions in Hong Kong to comply with the Foreign Account Tax Compliance Act (FATCA).

### Foreign investment restrictions

In general, Hong Kong does not impose restriction to foreign investors to make investments in Hong Kong, and wholly foreign owned companies are allowed. The only exception is the restriction on foreign ownership of Hong Kong's licensed television/sound broadcasters, of which the collective foreign ownership ceiling is 49% of the voting power. In addition, an approval from the Broadcasting Authority must be obtained for holding, acquisition, or exercise of voting control by a foreign investor of more than 2% of a licensee.

**Exchange controls**

Hong Kong does not have any foreign exchange control. There is no restriction on entry or repatriation of capital or remittance of profits from investments. Funds can be freely remitted to persons outside Hong Kong by various means (e.g. dividends, interest, royalties, service fees, branch profits).

**Choice of business entity**

The principal forms through which a business can be conducted in Hong Kong are as follows:

- Company incorporated in Hong Kong (either private or public via listing on the Stock Exchange of Hong Kong).
- Branch of a foreign company.
- Representative or liaison office of a foreign company.
- Joint venture (can be set up either as a company or partnership).
- Partnership.
- Sole proprietorship.

Of the above, privately incorporated companies and branches of foreign companies are most commonly used by foreign investors, as limited liability is usually desirable.

**Intellectual property (IP) regulations**

The Intellectual Property Department is responsible for monitoring the IP regime and ensuring the protection and enforcement of IP rights in Hong Kong. The Department is also responsible for investigating complaints against infringements and has extensive powers of search and seizure. Registration and protection of patents, copyrights, trademarks, and registered designs are each governed by a separate ordinance.

**Merger and acquisition (M&A) activities**

There are no specific restrictions on M&A activities in Hong Kong. The following tax considerations are relevant in the M&A context:

- Dividends or other forms of distribution of profits (e.g. distribution of branch profits to the head office) are generally not taxable.
- Capital gains arising from an M&A transaction are not taxable in the hands of the transferor, whereas amortisation of the goodwill in the transferee's accounts is not tax deductible due to its capital nature.
- Gains derived from transfer of revenue items (e.g. trade receivables) in an asset deal will be subject to profits tax.

For a share deal, stamp duty is payable on the transfer of Hong Kong shares at 0.2%, unless an exemption applies; for an asset deal, stamp duty is payable on conveyance of immovable property in Hong Kong at various rates up to 15%, depending on the type of immovable property transferred and the date of the transfer (see *Stamp duty in the Other taxes section*).

There is no special tax concession/incentive relating to M&A transactions.

Tax losses in the acquired company can generally be carried forward indefinitely to set off against future assessable profits. However, there are specific anti-avoidance provisions in the IRO that prevent the transfer of shares of a company with accumulated tax losses to owners of a profitable company for the sole or dominant purpose of utilising the tax losses (i.e. offsetting the tax losses against the profits generated from other trade, profession, or business of the transferee).

Pending the enactment of specific tax legislation dealing with corporate amalgamation, the HKIRD has issued some guidance on the profits tax treatment of various issues arising from corporate amalgamation on its website. In addition to the utilisation of tax losses, the guidance also covers issues such as the profits tax treatment of fixed assets and trading stocks transferred, and the profits tax return filing positions of the amalgamating and the amalgamated companies in the year of amalgamation, etc.

## Individual - Taxes on personal income

Hong Kong does not impose income tax based on an individual's total income. Instead, the three main types of income derived by individuals are taxed under different income taxes. That is, business or trading profits are taxed under profits tax, income from employment, office or pension is taxed under salaries tax, and rental income from immovable property is taxed under property tax. The residence status of an individual is not a determinative factor in examining his/her liability to salaries tax except in a tax treaty context.

*A resident individual with different types of income can elect 'personal assessment' which is an assessment on the total income of the individual (see the Tax administration section for more information).*

### Territorial basis of taxation

A person's residence, domicile or citizenship is not relevant in determining liability to Hong Kong salaries tax under the domestic law. The term 'resident' is defined in each of the comprehensive double tax agreements (CDTAs) signed by Hong Kong and is used in applying a CDTA.

Hong Kong adopts a territorial basis of taxation. All individuals, whether a resident or non-resident of Hong Kong, are subject to Hong Kong salaries tax on (i) Hong Kong-sourced employment income, (ii) income from an office held in Hong Kong, and (iii) income from a Hong Kong pension.

### Employment income

A person has Hong Kong-sourced employment income if the employment is a Hong Kong employment or in case the employment is a non-Hong Kong employment, the employment services are rendered by the person in Hong Kong.

The Hong Kong Inland Revenue Department (HKIRD) will generally accept that an employment is a non-Hong Kong employment if all of the following three conditions are met:

- The contract of employment was negotiated and entered into, and is enforceable outside Hong Kong.
- The employer is a resident outside Hong Kong.
- The employer's remuneration is paid outside Hong Kong.

If any of the above conditions is not met, the employment will likely be considered by the HKIRD as Hong Kong employment.

For a Hong Kong employment, employment income is not taxable if all of the employment services for a year of assessment are rendered outside Hong Kong. In determining whether all the services are rendered outside Hong Kong for a given year of assessment, no account is taken of services rendered in Hong Kong during visits not exceeding 60 days in the basis period for the year of assessment (the so-called '60-day rule').

For a non-Hong Kong employment, only income attributed to services rendered in Hong Kong is subject to Hong Kong salaries tax (the so-called 'time apportionment basis'). Similar to Hong Kong employment, the 60-day rule will apply in considering whether there are any services rendered in Hong Kong in a given year of assessment under a non-Hong Kong employment (i.e. services rendered in Hong Kong during visits not exceeding 60 days in the basis period for the year of assessment will be ignored).

*Where the employment income of an individual is subject to tax both in Hong Kong and an overseas jurisdiction that does not have a CDTA with Hong Kong, a unilateral income exemption may be available under the domestic tax law to provide relief from double taxation (see the Foreign tax relief section for more information).*

There are special rules for taxing employment income derived by seafarers and aircrew.

### Income from an office

The source of income from an office (e.g. directors' fees) is determined by the location at which the company paying the fees is centrally managed and controlled. The '60-day rule' and 'time apportionment basis' discussed above do not apply to income from an office.

**Pensions**

Pensions are, in practice, subject to Hong Kong salaries tax if the funds out of which the payment is made are managed and controlled in Hong Kong, and the pensions (other than a government pension) are related to services rendered in Hong Kong. Similar to income from an office, the '60-day rule' and 'time-apportionment basis' discussed above do not apply to income from a pension.

**Personal income tax (salaries tax) rates**

In general, a person's income from employment, less allowable deductions and personal allowances, is chargeable to Hong Kong salaries tax at progressive rates ranging from 2% to 17% as follows:

For 2019/20:

Net taxable income (HKD)		Tax on column 1 (HKD)	Percentage on excess (%)
Over (column 1)	Not over		
0	50,000	-	2
50,000	100,000	1,000	6
100,000	150,000	4,000	10
150,000	200,000	9,000	14
200,000		16,000	17

The maximum tax for 2019/20, however, will be limited to tax at the standard rate (15%) on the net assessable income (after any business deductions) less concessionary deductions and charitable donations but without the deduction of personal allowances.

In rare cases where the total amount of allowable deductions exceeds the assessable income of an individual taxpayer in any year of assessment, the excess can be carried forward indefinitely to set off against the taxpayer's assessable income in subsequent years of assessment.

**Local income taxes**

Hong Kong does not impose any local, state, or provincial income taxes.

**Individual – Residence**

A person's residence, domicile or citizenship is not relevant in determining liability to Hong Kong salaries tax under the domestic law.

However, where it is necessary to determine an individual's residence, such as for the purpose of a CDTA, individuals who (i) ordinarily reside in Hong Kong or (ii) stay in Hong Kong for more than 180 days during a year of assessment or for more than 300 days in two consecutive years of assessment are generally considered as a Hong Kong tax resident.

**Individual – Other taxes****Payroll taxes****Mandatory provident fund (MPF) scheme**

Hong Kong's MPF system came into operation on 1 December 2000. The MPF scheme is designed to

provide a formal, compulsory system of retirement protection by way of a privately managed contribution scheme. An employee is required to contribute 5% of their monthly income, and the employer must make a monthly contribution matching this amount. The maximum level of income for contribution purpose is HKD 30,000 per month. Accordingly, the maximum mandatory contribution for each of the employee and employer is HKD 1,500 per month. The employee's mandatory contributions will be withheld from monthly income by the employer.

An employee whose income is less than HKD 7,100 per month is not required to make mandatory contributions. However, the employer of such employee is required to contribute an amount that is equal to 5% of the employee's monthly income.

Exemption from joining the MPF scheme is available for some very limited categories of employees, including people from overseas who enter Hong Kong for employment for not more than 13 months or who are covered by an overseas retirement scheme.

An employee or an employer may make voluntary contributions in addition to the mandatory contributions required.

#### **Profits tax**

Business profits with a Hong Kong source derived by individuals are taxable under profits tax irrespective of whether they are residents. While there is no capital gains tax in Hong Kong, gains from disposal of assets in Hong Kong may be considered as trading gains which are taxable under profits tax. Hong Kong sourced royalties received by resident individuals are taxable as business profits under profits tax.

Withholding tax is applicable to royalties received by non-resident individuals if the use of the relevant intellectual property is in Hong Kong or the use is outside Hong Kong and the royalties paid can be claimed as deduction under profits tax by the payer.

#### **Consumption taxes**

##### **Value-added tax (VAT)/Good and services tax/Sales tax**

Value-added, good and services, and sales taxes do not apply in Hong Kong.

##### **Net wealth/worth taxes**

There are no net wealth/worth taxes in Hong Kong.

##### **Estate and gift taxes**

Hong Kong does not have an estate duty or a gift tax.

##### **Property taxes**

Property tax is charged to the owner of any land or buildings (except government and consular properties) in Hong Kong at the standard rate of 15% on the net assessable value of such land or buildings. Net assessable value of a property is the consideration payable to the owner for the right to use the land or buildings less rates paid by the owner and a 20% notional allowance. Property occupied by the owner for self-use is not subject to property tax as no rent is receivable with respect to that property.

##### **Government rates and rent**

Rates are an indirect tax levied on properties in Hong Kong. Rates are charged at 5% of the rateable value which is the estimated annual rental value of a property at the designated valuation reference date of 1 October.

Privately owned land in Hong Kong is normally held by way of a government lease under which rent is payable to the government of the Hong Kong Special Administrative Region (HKSAR) in return for the right to hold and occupy the land for the term (i.e. duration) specified in the lease document. Currently, government rent is calculated at 3% of the rateable value of the property and is adjusted in step with any subsequent changes in the rateable value.

##### **Treatment of foreign owned real estate**

Offshore rental income or capital gain from disposal of foreign real estate owned by a Hong Kong resident individual is not subject to Hong Kong tax.

**Customs duties**

Custom duties are levied on limited categories of dutiable commodities (i.e. tobacco, liquor, methyl alcohol, and hydrocarbons) regardless of whether they are imported or locally manufactured. As far as individuals are concerned, the duties are usually included in the sale prices of such commodities by the retailers.

**Stamp duties**

Stamp duty is charged on transfer of Hong Kong stock by way of sale and purchase at 0.2% of the consideration (or the market value if it is higher) per transaction. Hong Kong stock is defined as stock the transfer of which must be registered in Hong Kong.

For conveyance on sale of immovable property in Hong Kong, the stamp duty payable depends on the type of property transferred (i.e. residential property vs non-residential property) and the property consideration. Currently, stamp duty on transfer of properties is charged as follows:

- Transfer of residential property: A flat rate of 15%, with certain exemptions. One common exemption is acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition (see 2 below).
- Acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition and some other specified circumstances: Scale 2 rates ranging from HKD 100 (for property consideration of up to HKD 2 million) to 4.25% (for property consideration exceeding HKD 20 million).
- Transfer of non-residential property: Scale 1 rates ranging from 1.5% (for property consideration of up to HKD 2 million) to 8.5% (for property consideration exceeding HKD 20 million).
- The stamp duty payable is computed by applying the relevant rate to the consideration or market value of the property (whichever is higher). When Scale 1 or Scale 2 rates are applicable, marginal relief is available for transfer where the consideration is marginally above the lower bound of each rate band.
- For lease of immovable property in Hong Kong, stamp duty is calculated at a specified rate of the annual rental that varies with the term of the lease. Currently, the applicable rate ranges from 0.25% (for lease period of not more than one year) to 1% (for lease period of more than three years).

**Special stamp duty (SSD)**

There is an SSD on resale of residential property in Hong Kong within 36 months from the date of acquisition. The SSD is imposed on top of the *ad valorem* stamp duty payable on conveyance on sale or agreement for sale of residential property, with a few exemptions. The SSD payable will be calculated based on the stated consideration or the market value (whichever is higher) of the resold property at the regressive rates indicated below.

- 20% for residential properties held for six months or less.
- 15% for residential properties held for more than six months but for 12 months or less.
- 10% for residential properties held for more than 12 months but for 36 months or less.

**Buyer's stamp duty (BSD)**

A BSD is payable on acquisition of Hong Kong residential properties by any person other than a Hong Kong permanent resident. The BSD is charged at a flat rate of 15% on the stated consideration or the market value of the property, whichever is higher. The BSD is imposed on top of the *ad valorem* stamp duty and the SSD (if applicable), with exemptions in certain situations.

**Transfer tax/Turnover tax/Registration tax**

Transfer, turnover, and registration taxes do not apply in Hong Kong.

**Individual - Income determination****Employment income**

Taxable employment income includes any wages, salary, leave pay, fees, commissions, bonuses, gratuities, perquisites, and allowances, with certain specific exemptions. Set out below are the tax treatment of some common items.

**Benefits in kind**

If the employer has sole and primary liability for payment of the benefit, and no other person including the



employee acts as a surety in respect of the liability, the employee will generally not be taxed on such benefit, except in three situations:

- if the benefit is capable of being converted into money by the employee, or
- if the employer pays any amount in connection with the education of a child of an employee, or
- if the employer pays any amount in connection with the holiday journey of an employee.

In the first situation above, the taxable benefit is the second-hand value of the benefit obtained and in the second and third situations the taxable benefit is the cost to the employer of providing the benefit.

### **Housing benefits**

Housing that is provided or subsidised by an employer or its associated corporation is taxable. However, instead of taxing the amount of rents paid by the employer, the taxable amount is the rental value of the housing quarters in excess of the rents actually paid by the employee for the quarter (if any). The rental value of housing quarters provided by an employer is computed as a percentage of the employee's assessable income less any allowable outgoings and expenses and depreciation allowances on capital expenditure incurred on machinery or plant, as follows:

Type of accommodation	Rate (%)
Hotel, one bedroom	4
Hotel, not more than two bedrooms	8
Other accommodation	10

Where an employer refunds all or part of the rents paid by an employee, the treatment will be similar to cases in which the employer provides accommodations to the employee rent-free or at a reduced rent. A cash allowance for housing is fully taxable where the employer has no control over how it is spent by the employee.

### **Retirement benefits**

Any sums received by way of commutation of pension under a recognised occupational retirement scheme upon death, incapacity, retirement, terminal illness, or termination of service are exempt, with certain exceptions where there is a termination of service of less than ten years with an employer. Any sums received by way of commutation of pension under the Pensions Ordinance are also exempt.

Any sums received by an employee in connection to the employer's mandatory contributions to an MPF scheme are exempt from salaries tax. Sums related to the employer's voluntary contributions received from an MPF scheme upon death, incapacity, retirement, terminal illness, or termination of service of the employee are also exempt, with certain exceptions where there is a termination of service of less than ten years with an employer. Sums related to the employer's voluntary contributions received at times other than those mentioned above are taxable.

Sums related to employer's contributions received from a retirement scheme that is not a recognised occupational retirement scheme or an MPF scheme are subject to Hong Kong salaries tax.

### **Termination payments**

Compensation for termination of employment that does not represent a payment for past, present, or future services is not taxable in general. Such payment should be distinguished from termination gratuities that relate to services previously rendered by the employee, which are therefore taxable. Taxable termination payments may be spread backward over the final three years of employment for Hong Kong salaries tax purposes.

Long service or severance payments made in accordance with the Employment Ordinance are not subject to Hong Kong salaries tax.

Payment in lieu of notice that is specified in an employment contract is taxable.

#### **Equity compensation**

Gains from any employee share options are taxable when the options are exercised, assigned or released. There are specific provisions governing the taxation of employee stock options. Other employee share-based benefits (such as share awards) are also subject to Hong Kong salaries tax.

#### **Business income**

Business income is taxed under profits tax (*see Profits tax in the Other taxes section for more information*).

#### **Capital gains**

*All capital gains derived by an individual are not subject to tax in Hong Kong (see Profits tax in the Other taxes section for more information).*

#### **Dividend income**

Dividends derived by an individual are not subject to tax in Hong Kong.

#### **Interest income**

Interest on bank deposits derived by an individual is not subject to tax in Hong Kong.

#### **Rental income**

Rental income from immovable property in Hong Kong is taxed under property tax (*see Property tax in the Other taxes section for more information*).

#### **Treatment of intellectual property**

Neither royalty nor gain from sale of intellectual property is within the scope of Hong Kong salaries tax. Such income, however, may be taxable under profits tax (*see Profits tax in the Other taxes section for more information*).

#### **Exempt income**

Certain benefits in kind and retirement benefits received by employees are exempt from salaries tax (*see Benefits in kind and Retirement benefits above for more information*).

#### **Future rates**

No more information is available on future rates.

#### **Hybrid tax systems**

Hong Kong does not have an applicable hybrid system.

### **Individual - Deductions**

Outgoings and expenses other than those of a domestic, private or capital nature are allowable under salaries tax insofar as they are incurred wholly, exclusively, and necessarily in the production of income subject to salaries tax. In practice, very few expenses can meet the above restrictive requirements.  
Employment expenses

Some business travel expenses (excluding private travel expenses such as home to place of work) and entertainment expenses may qualify for deduction under salaries tax subject to the restrictive requirements above. Depreciation allowances may be allowed on capital expenditure incurred on plant and machinery where the use of which is essential in the production of assessable income.

#### **Concessionary deductions**

A few concessionary deductions are specifically provided for under the Inland Revenue Ordinance.

**Qualifying premiums paid under the Voluntary Health Insurance Scheme (VHIS)**

Qualifying premiums paid under the HKSAR Government's VHIS are allowed for deduction starting from the year of assessment 2019/20. The maximum amount to be deducted in respect of qualifying premiums paid for each insured person for each year is HKD 8,000, with no cap on the number of insured persons for whom the taxpayer is eligible for claiming the concessionary deductions in a given year of assessment.

**Charitable donations**

Charitable donations made in cash to approved charitable institutions are allowable if the aggregated amount for a year of assessment is not less than HKD 100. For year of assessment 2018/19, the deduction for charitable donations is restricted to 35% of the assessable income after allowable deductions of the year of assessment.

**Elderly residential care expenses**

Elderly residential care expenses paid to a residential care home in respect of a parent or grandparent of a taxpayer or spouse are deductible up to a maximum of HKD 100,000 for each tax year for each parent or grandparent for year of assessment 2018/19.

**Self-education expenses**

A deduction is allowed for self-education expenses paid for employment-related courses. The maximum amount of deduction allowed for each tax year is HKD 100,000 for year of assessment 2018/19.

**Mandatory contributions to an MPF scheme and contributions to other retirement schemes**

Mandatory contributions to an MPF scheme and contributions to other recognised occupational retirement schemes are deductible up to a maximum of HKD 18,000 for year of assessment 2018/19.

**Voluntary contributions to an MPF scheme and qualifying annuity premiums**

Effective from year of assessment 2019/20, a deduction is allowed for (i) employee's MPF voluntary contributions made to a designated MPF account and (ii) qualifying annuity premiums paid for a qualifying deferred annuity policy (essentially those policies certified by the Insurance Authority).

The maximum total tax deduction allowed for (i) and (ii) above is HKD 60,000 for each year of assessment. If an employee is entitled to tax deduction for both qualifying annuity premiums and MPF voluntary contributions for a year of assessment, deductions will firstly be allowed for MPF voluntary contributions and then for qualifying annuity premiums.

**Home loan interest expenses**

Home loan interest paid can be deducted by a person if the property is owned by that person and is occupied by that person as their place of residence during the year of assessment. The place or residence must be situated in Hong Kong in order to qualify for the deduction. The maximum deduction for each tax year is HKD 100,000 for 20 years of assessment.

**Standard deductions**

There is no blanket or standard deduction although a few concessionary deductions are available (see *Concessionary deductions above for more information*).

**Personal allowances**

Under salaries tax and personal assessment (if elected), allowances are granted for each taxpayer provided that the applicable conditions for the allowances are satisfied. The amounts allowed for year of assessment 2019/20 are shown below.

Personal allowances	2019/20 (HKD)
Basic allowance (for single persons) (1)	132,000
Married person's allowance (for married couples) (1)	264,000
Child allowances (2):	
1st to 9th child (each):	
Year of birth	240,000
Other years	120,000
Dependent parent or grandparent allowance (each):	
Aged 60 or above:	
Not residing with taxpayer	50,000
Residing with taxpayer throughout the tax year	100,000
Aged 55 to 59:	
Not residing with taxpayer	25,000
Residing with taxpayer throughout the tax year	50,000
Dependent brother or sister allowance (for whom no child allowance is claimed)	37,500
Single parent allowance (for single parent with sole or predominant care of a child)	132,000
Disabled dependant allowance (in addition to any allowances already granted for the disabled person)	75,000
Personal disability allowance (in addition to any allowances already granted for the disabled person)	75,000

#### Notes

If a married couple both have income chargeable to salaries tax and no joint assessment or personal assessment is elected, they are taxed as two single persons and each will be entitled to the basic allowance. The married allowance is given only if one spouse has no income liable to salaries tax, or where joint assessment or personal assessment is elected by the couple.

Child allowances are only available to one of the spouses of a married couple. The couple must state which spouse will claim the child allowance.

**Business deductions**

Business expenses incurred for producing assessable profits are allowable under profits tax (see Profits tax in the Other Taxes section for more information).

**Losses**

Business losses may be used to offset against assessable business profits from the same trade under profits tax. If an individual elects personal assessment (see the Tax Administration section for more information), business losses can be used to offset employment income or business profits from other trades. Capital losses are not allowable under either salaries tax or profits tax.

**Fine and penalties**

Fine and penalties are not deductible as they do not meet the conditions of being incurred wholly, exclusively and necessarily in the production of income subject to salaries tax.

**Individual - Foreign tax relief and tax treaties****Foreign tax relief**

As a relief from double taxation, unilateral income exemption is available for employment income derived from services rendered outside Hong Kong and where tax similar to the nature of Hong Kong salaries tax has been charged and paid on that income in the territory in which the services are rendered. This is applicable up to the year of assessment 2017/18.

Starting from the year of assessment 2018/19, the income exclusion claim is only available where foreign tax has been paid in a non-CDTA jurisdiction for services rendered in that jurisdiction.

Technically, this income exemption applies to both Hong Kong and non-Hong Kong employments. However, such exemption is practically not applicable to taxpayers with a non-Hong Kong employment as only income of services rendered in Hong Kong is taxable in cases of non-Hong Kong employment.

A foreign tax credit is available to Hong Kong tax residents in respect of income derived from and taxable in a jurisdiction that has entered into a CDTA with Hong Kong and the same income is subject to tax in Hong Kong. Effective from the year of assessment 2018/19, salaries taxpayers are required to take all reasonable steps to minimise the foreign tax payable before making a claim for tax credit in Hong Kong.

**Tax treaties**

Currently, Hong Kong has entered into 43 tax treaties with different jurisdictions. All of the following treaties have been ratified and become effective unless indicated otherwise in the notes below.

**Estate and gift tax conventions**

Hong Kong has not entered into any estate and gift tax conventions because the estate duty was abolished in 2006 and it does not have a gift tax.

**Tax information exchange agreements (TIEAs)**

Currently, Hong Kong has entered into seven TIEAs with different jurisdictions.

In addition to the signing of the Hong Kong-United States TIEA in March 2014, Hong Kong signed a Model 2 intergovernmental agreement (IGA) with the United States in November 2014 to facilitate financial institutions in Hong Kong to comply with the Foreign Account Tax Compliance Act (FATCA).

**Automatic exchange of information (AEOI)/Common Reporting Standard (CRS) regime**

Hong Kong has put in place a legislative framework to implement the AEOI/CRS regime. Reportable financial institutions are required to identify the reportable financial accounts held by (i) tax residents of reportable jurisdictions or (ii) passive non-financial entities whose controlling persons are tax residents of reportable jurisdictions in accordance with the specified due diligence procedures, collect the required information of those reportable accounts, and furnish such information to the HKIRD. Such information will then be exchanged on an annual basis.

There are currently 75 reportable jurisdictions for AEOI purposes, but the number of reportable jurisdictions has been increased to 126 effective from 1 January 2020. However, Hong Kong will only conduct AEOI with a reportable jurisdiction when an agreement is in place with that reportable jurisdiction to provide the basis for exchange.

As of May 2019, Hong Kong has activated exchange relationships for CRS purposes with 59 jurisdictions based on either a bilateral or multilateral competent authority agreement for CRS.

## Individual - Other tax credits and incentives

There is no special tax incentive for individuals under Hong Kong salaries tax. Hong Kong has no tax holidays.

## Individual - Tax administration

### Taxable period

An assessment year (or tax year) begins on 1 April of a year and ends on 31 March of the following year.

### Basis of assessment

The basis of assessment is the total assessable income accrued to a person in a given year of assessment with appropriate adjustments for allowable deductions and personal allowances.

### Personal assessment

An individual who is a Hong Kong resident may elect for personal assessment whereby income chargeable to salaries tax, profits tax and property tax is aggregated in a single assessment. Personal assessment enables an individual to offset a business loss against income subject to salaries tax or property tax and to claim deduction of loan interest on rental properties which is not available under property tax. Losses brought forward from previous tax years under personal assessment may be used to offset against income in current year or subsequent years. Allowable deductions and appropriate personal allowances are granted under personal assessment and the tax is calculated on the balance in the same manner as for salaries tax. The maximum tax payable is, however, limited to tax at the standard tax rate on the person's total assessable income less allowable deductions, but without a deduction for personal allowances.

Effective from the year of assessment 2018/19, a married person may elect for personal assessment on his/her own rather than jointly with his/her spouse as far as he/she is an individual who (i) is of or above the age of 18 years or is under that age if both parents are deceased and (ii) is either ordinarily resident in Hong Kong or a temporary resident of Hong Kong.

However, if a married couple has elected for joint assessment for salaries tax purposes, then an election for personal assessment must be made jointly by the husband and the wife.

### Joint assessment for married couples

Although married persons who both earn taxable income are normally taxed separately, they may elect to be taxed jointly (i.e. election for joint assessment) where it is beneficial to them.

Under joint assessment, the total income of both spouses will be aggregated under one assessment, with adjustments for allowable deductions and appropriate personal allowances. The total tax liability will then be apportioned between the spouses based on each individual's respective share of the total aggregated income.

### Tax returns

Individual tax returns are issued on the first working day of May each year. The filing deadline is usually within a month from the date of issue. However, individuals who are represented by a tax representative are normally granted with an extension of an additional month for filing their returns. Further extensions for return filing may be possible upon application and will be considered on a case-by-case basis.

In the more complicated cases (e.g. those involving time apportionment claim), a tax return is usually filed together with a tax computation showing how the net chargeable income is computed. In general, no supporting documents (e.g. donation receipts) are required to be submitted together with a tax return. However, the HKIRD may request for such supporting documents subsequent to filing of the return.

Notice of assessment will be issued after the tax return has been examined by the HKIRD. Taxpayers may be subject to post-assessment investigation of the HKIRD at a later date.

#### **Payment of tax**

Tax is usually payable in two instalments. The dates of payment of tax, which generally fall between January and April of the year following the year in which the tax return is issued, are determined by the Commissioner of Inland Revenue and specified in an assessment notice. A system of provisional tax payments applies whereby estimated tax payments are made during the current year. The provisional salaries tax payable is normally estimated based on the previous year's salaries tax liability. The provisional salaries tax already paid is credited against the final salaries tax assessed for a year of assessment, which is determined after filing of the return.

#### **Withholding requirements**

An employer is not obliged to withhold salaries tax from the remuneration paid to an employee except in cases where an employee is about to leave Hong Kong for more than one month other than on a normal business trip. In such cases, the employer may be required to withhold payments from the departing employee.

As dividends and interest derived by individuals are not subject to Hong Kong income tax, there is no withholding requirement on such income derived by an individual.

Withholding tax is applicable to royalties received by non-resident individuals for the use of the relevant intellectual property in Hong Kong or for the use outside Hong Kong and the royalties paid can be claimed as deduction under profits tax by the payer.

#### **Audit cycle**

The name of the tax authority is the Hong Kong Inland Revenue Department (HKIRD).

There is no specific tax audit cycle in Hong Kong. Tax investigation targets are selected based on specific facts and circumstances of individual cases and certain criteria (e.g. income level) determined by the HKIRD.

#### **Statute of limitations**

An additional assessment may be made by a HKIRD tax assessor if a taxpayer chargeable to tax has not been assessed to tax or has been assessed at less than the proper amount. The assessment must be made within the relevant year of assessment or within six years after the end of that year of assessment. The time limit for making additional assessments is extended when a taxpayer either has not been assessed, or is under-assessed, due to fraud or wilful evasion. In that case an additional assessment may be made up to ten years after the end of the relevant assessment year.

#### **Topics of focus for tax authorities**

Salaries tax issues that are often subject to close scrutiny of the tax authority include: time apportionment claim, income exclusion claim, taxability of termination payments, taxation of employee share benefits, and taxation of carried interest.



## Individual - Sample personal income tax calculation

Below is a sample salaries tax computation for year of assessment 2019/20 for illustrative purposes.

### Assumptions:

The individual is a married person with two children both below age 18.

The individual's wife is not working and the two children are maintained by the individual.

The total assessable income of the individual consists of salaries of HKD 600,000 and year-end bonus of HKD 50,000.

The individual made contributions of HKD 18,000 to an MPF scheme during the year.

The individual made qualified charitable donations of HKD 3,000 during the year.

Salaries tax computation	HKD	HKD
Salaries	600,000	
Bonus	50,000	
Total assessable income		650,000
<b>Less: Concessionary deductions</b>		
Charitable donations	(3,000)	
Retirement scheme contributions	<u>(18,000)</u>	<u>(21,000)</u>
Net income		629,000
<b>Less: Allowances</b>		
Married person's allowance	(264,000)	
Child allowances (HKD 120,000 x 2)	<u>(240,000)</u>	<u>(504,000)</u>
Net chargeable income		125,000
<b>Tax at progressive rates:</b>		
First HKD 50,000 @ 2%	1,000	
Next HKD 50,000 @ 6%	3,000	
Remainder HKD 25,000 @ 10%	2,500	
<b>Tax payable (1)</b>		<u>6,500</u>

### Note

The tax amount calculated based on the standard rate (i.e. HKD 629,000 @15% = HKD 94,350) is higher than that computed at progressive rates so the standard rate would not apply.

## Individual - Other issues

### Treatment of business entities

A business can be conducted in Hong Kong through the following principal forms:

- Company incorporated in Hong Kong (either private or public via listing on the Stock Exchange of Hong Kong).
- Representative or liaison office of a foreign company.
- Joint venture (can be set up either as a company or partnership).
- Partnership.
- Sole proprietorship.

An entity in any of the above forms is subject to Hong Kong profits tax in the name of the entity itself on any profits arising in or derived from Hong Kong from a trade, profession or business carried on in Hong Kong.

### Visa and work permit

Foreigners are generally required to obtain a work permit before taking employment in Hong Kong.

Visa applications may be submitted to the nearest Chinese diplomatic and consular mission at the individual's place of residence, or applications may be sent directly to the Hong Kong Immigration Department, or through the sponsor in Hong Kong. The application must be supported by certain specified documents (e.g. resume, letter of contract of employment, letter from employer).

The Hong Kong Immigration Department will contact the individual and/or the sponsor for verification upon receiving the application.

### Tax equalisation or reimbursement plans

A tax reimbursement program is usually provided by employers to expatriate employees to alleviate any tax increases which may be incurred as a result of an overseas assignment. A tax reimbursement program may either be a 'tax protection' or 'tax equalisation' plan.

A tax protection plan makes provision for the employee's total tax liability not to exceed the amount they would have paid in their home country had the employee not been posted overseas. If the employee's actual tax liabilities exceed the hypothetical home country tax, the employer reimburses the difference to the employee. If the actual tax liabilities are less than the hypothetical home country tax, the employee keeps the difference.

In contrast, a tax equalisation plan aims to maintain the employee's tax burden as if they had remained in the home country. If the employee's actual taxes are greater than they would have incurred in the home country, the employer reimburses the excess, and if the actual taxes are less, the employee is required to pay the difference to the employer.

The hypothetical home country tax must be calculated under either plan. The hypothetical tax is generally computed on the base salary and other remuneration as if the employee had remained in the home country.

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