



Hong Kong Tax Newsflash: IRD revises guidance on deduction of foreign taxes

The Inland Revenue Department (IRD) in July 2019 released an updated [Department Interpretation and Practice Notes \(DIPN\) No. 28 \(revised\)](#) on the deduction of foreign taxes. This replaces the DIPN issued in July 1997.

Following the enactment of the [Inland Revenue \(Amendment\) \(No. 6\) Ordinance 2018](#), a Hong Kong tax resident person can only apply for a tax credit, instead of claiming a tax deduction, in respect of the foreign tax paid on specified interest and gains in a jurisdiction that has concluded a double taxation agreement (DTA) with Hong Kong ("DTA territory"). The IRD has updated DIPN No. 28 to provide more guidance in this respect.

Tax on profits is not deductible

In DIPN No. 28 (revised), the IRD reiterates the position under the old DIPN that tax on profits generally is not deductible because it is not an outgoing or expense incurred in generating chargeable profits.

Other taxes and duties considered for deduction

However, the IRD also restates that foreign taxes and duties not calculated by reference to profits will be considered for deduction. Examples given in the updated DIPN include rates levied on property, vehicle license fees and duties on commodities.

Deduction of foreign tax on specified interest and gains

An exception to the non-deduction rule for tax on profits is provided under section 16(1)(c) of the Inland Revenue Ordinance (IRO), which allows the deduction of foreign tax paid that is substantially the same in nature as tax imposed under the IRO in respect of specified interest and gains (i.e. profits chargeable to tax under section 15(1)(f), (g), (i), (ia), (j), (k), (l) or (la) of the IRO). Such interest and gains include interest income derived by financial institutions, funds or intragroup financing businesses, and gains from the disposal or redemption of certificates of deposit, bills of exchange or regulatory capital securities, etc.

Before the enactment of the Inland Revenue (Amendment) (No. 6) Ordinance 2018, section 16(1)(c) of the IRO provided unilateral relief from double taxation for foreign tax paid on specified interest and gains in the form of a deduction, regardless of whether there was a DTA between Hong Kong and the foreign jurisdiction. With effect from the year of assessment 2018/19, section 16(2J) of the IRO restricts the application of section 16(1)(c) of the IRO. A Hong Kong tax resident no longer may claim a deduction for the foreign tax paid in a DTA territory in respect of specified interest and gains, but only a tax credit under the applicable DTA and section 50 of the IRO. The IRD indicates in DIPN No. 28 (revised) that this is in line with the international practice that where a DTA is in place, relief from double taxation should be allowed under the DTA only to the extent contemplated by the agreement.

Although DIPN No. 28 (revised) is not legally binding, it provides a good indication of the IRD's position. Taxpayers may wish to review their situations to determine whether they are aligned with the IRD's practice.

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