

International Tax Hong Kong Highlights 2018



Investment basics:

Currency – Hong Kong Dollar (HKD)

Foreign exchange control – No

Accounting principles/financial statements – Hong Kong Financial Reporting Standards. Financial statements must be filed annually.

Principal business entities – These are the public and private limited liability company, partnership, sole proprietorship and branch of a foreign corporation.

Corporate taxation:

Residence – A corporation (or other entity) is resident if it is incorporated in Hong Kong or managed and controlled in Hong Kong.

Basis – Generally, only Hong Kong-source income is subject to Hong Kong profits tax.

Taxable income – Profits tax is levied on the Hong Kong-source profits of businesses carried on in Hong Kong. In determining the source of profits, Hong Kong generally adopts the “operations test,” which involves identifying the activities that are most important in generating the profits and the place at which these activities are carried out. Expenses generally are deductible to the extent they are incurred in the production of profits that are chargeable to tax. However, domestic expenses, capital expenditure and losses, taxes and other expenses not incurred for the purpose of producing profits are not deductible. If a company's profits are derived from both Hong Kong sources and non-Hong Kong sources that are not assessable to profits tax, expenses attributable to the non-Hong Kong-source profits are not deductible.

Taxation of dividends – Dividends generally are exempt from profits tax.

Capital gains – Capital gains are not taxable. However, gains on the disposal of assets may be subject to profits tax if the disposal constitutes a transaction in the nature of trade (a factual determination).

Losses – Losses attributable to a business that earns profits subject to profits tax may be carried forward indefinitely and set off against future taxable profits of the company. There are specific anti-avoidance rules to prevent the purchase of a loss company for the sole or dominant purpose of using the company's losses. Losses cannot be carried back.

Rate – Profits tax is levied at a rate of 16.5% (15% for unincorporated businesses) where the company is carrying on business in Hong Kong and the relevant income is earned in or derived from Hong Kong.

Surtax – No

Alternative minimum tax – No

Foreign tax credit – Where there is a double tax agreement, foreign tax paid may be credited against profits tax on the same profits, but the credit is limited to the amount of Hong Kong tax payable on the same income.

Participation exemption – No

Holding company regime – No

Incentives – A profits tax exemption for offshore funds is available for specified transactions if certain conditions are satisfied. Concessionary tax rates are available for qualified corporate treasury centers, qualified aircraft lessors or leasing managers, offshore businesses of reinsurance companies and authorized captive insurance companies, etc.

Withholding tax:

Dividends – There is no withholding tax on dividend distributions from a Hong Kong entity.

Interest – There is no withholding tax on interest payments from a Hong Kong entity.

Royalties – Royalty payments made to a nonresident are deemed to be taxable in Hong Kong if made for the use of, or the right to use, intangibles in Hong Kong, or outside Hong Kong where the royalty payments are deductible for profits tax purposes. The amount deemed taxable is 30% of the gross amount of the royalties paid, resulting in an effective rate of 4.95% (16.5% x 30%) (or an effective rate of 4.5% for a noncorporate person (15% x 30%)). If the royalty is paid to an associated nonresident for the use of intangibles that previously were owned by a person carrying on business in Hong Kong, 100% of the royalty is deemed to be taxable, resulting in an effective rate of 16.5% (15% for a noncorporate person).

Technical service fees – No

Branch remittance tax – No

Other taxes on corporations:

Capital duty – Capital duty was abolished in 2012.

Payroll tax – No

Real property tax – Property owners are subject to property tax on rental income derived from property in Hong Kong. Property tax is charged at the standard rate of 15% of the net assessable value of the property as determined by rent, service charges and fees paid to the owner, less an allowance of 20% for repairs and maintenance. A company that derives rental income from property is subject to profits tax and may apply for an exemption from property tax.

Social security – For employees whose monthly income is HKD 7,100 or more, the employer is required to deduct 5% (capped at HKD 1,500) as the employee's contribution to the Mandatory Provident Fund (MPF) scheme, and then pay an additional 5% as its own contribution.

Stamp duty – Stamp duty is charged on documents connected with the lease, sale or transfer of immovable property in Hong Kong, and the sale of shares. If the above are transferred at less than market value, stamp duty may be imposed based on the market value at the date of transfer.

Stamp duty on the transfer of Hong Kong shares is 0.2% of the value of the shares transferred, which is shared equally between the buyer and seller. An exemption may

be available for an intragroup transaction if certain conditions are satisfied.

The rate on the lease of immovable property is 0.25% of the total rent payable for a short-term lease (one year or less); 0.5% of the annual or average annual rent for a one to three-year lease; and 1% of the annual or average annual rent for a lease exceeding three years.

The maximum *ad valorem* stamp duty on the sale and conveyance of nonresidential property is 8.5% of the value of property transferred. The *ad valorem* stamp duty rate for residential property is a flat rate of 15%, with certain exemptions and exceptions. In addition, for residential property acquired on or after 27 October 2012, a Special Stamp Duty (SSD) ranging from 5% to 20% is levied if the property is sold within 36 months of purchase. In addition to *ad valorem* stamp duty and SSD, a Buyer's Stamp Duty at a flat rate of 15% applies to residential property if it is acquired by any person (including a limited company), except a Hong Kong permanent resident, on or after 27 October 2012.

Transfer tax – No

Other – Other levies include betting duty (25%-75%) and the air passenger departure tax (levied on all air passengers departing Hong Kong (HKD 120)).

Anti-avoidance rules:

Transfer pricing – There are limited provisions in the tax law governing business carried on with closely connected nonresident persons.

Thin capitalization – There are no thin capitalization rules, but the deduction of interest expense is limited, especially with regard to interest paid to nonresidents.

Controlled foreign companies – No

Disclosure requirements – Certain related party transactions must be disclosed in the profits tax return.

Compliance for corporations:

Tax year – The tax year starts on 1 April and ends on 31 March of the following year. The basis period of tax computation is the accounting year ended in the tax year.

Consolidated returns – Hong Kong does not allow groups of companies to file consolidated returns and there is no group loss relief for members of a group of companies.

Filing requirements – Tax returns are issued annually on the first business day of April for companies to report their profits in the accounting year ended in the previous tax year, which ends on 31 March. Companies whose financial years end between 1 December and 31 March

normally are granted an extended period to file their tax returns. Assessments are issued once the Inland Revenue Department receives the tax return. Companies (and unincorporated businesses) also must pay a provisional profits tax for the following tax year, at a rate of 16.5% of the current year's profits. This payment is credited against the final profits tax liability, with any excess payment refunded.

Penalties – Penalties may be imposed for failure to comply with the Inland Revenue Ordinance (IRO). The Commissioner of Inland Revenue has the authority to initiate prosecution, to compound or to assess additional tax (which is a form of penalty) in respect of the offense.

Rulings – Taxpayers may request an advance ruling from the Inland Revenue Department on the application of provisions of the IRO. An advance pricing arrangement program has been introduced.

Personal taxation:

Basis – The Hong Kong personal income tax (salaries tax) covers all income arising in or derived from Hong Kong from an office, employment or pension. Interest income earned by an individual is exempt from tax in Hong Kong. Capital gains on financial transactions are also effectively exempt from tax.

Residence – Foreign residents who visit Hong Kong for no more than 60 days in a tax year (from 1 April to 31 March of the following year) are not liable to salaries tax on their employment income. Employees who already have paid tax of substantially the same nature as Hong Kong salaries tax in any territory outside Hong Kong are exempt in respect of income derived from services rendered in that territory outside Hong Kong.

Filing status – A married couple may opt for joint or separate assessment.

Taxable income – Individuals are taxed on their total Hong Kong income from employment, less deductible expenses, charitable donations and personal allowances. The source of employment income is determined by various factors, including the place where the contract was negotiated and concluded and where it is enforceable; the residence of the employer; and where the salary is paid. Income from non-Hong Kong employment is deemed to be sourced in Hong Kong if it is attributable to services rendered in Hong Kong. Directors' fees paid to directors of a company, the control and management of which is exercised in Hong Kong, are chargeable to salaries tax irrespective of where the director resides. Taxable income includes commissions, bonuses, cost of living allowances, stock option gains,

awards, gratuities, allowances (including those for education) and other perquisites derived from employment. Dividend income is not taxed, but gains from the exercise of share options are taxable.

Capital gains – Capital gains are not taxable in Hong Kong.

Deductions and allowances – In arriving at assessable income, the only deductions permitted are expenses that are wholly, exclusively and necessarily incurred in the production of assessable income. For general expenses, the scope for obtaining deductions is limited. Allowable deductions include mandatory contributions to a recognized occupational retirement scheme, self-education expenses, home loan interest, elderly residential care expenses and donations to approved charities.

Rates – Personal income is taxed in Hong Kong at progressive rates. The marginal tax rates range from 2% to 17% (on chargeable income less personal allowances), with a cap at the standard rate of 15% (on chargeable income without the deduction of personal allowances).

Other taxes on individuals:

Capital duty – No

Stamp duty – See above under "Corporate taxation."

Capital acquisitions tax – No

Real property tax – Property owners are taxed on rental income derived from property in Hong Kong. The tax is charged at the standard rate of 15% of the net assessable value of the property as determined by rent, service charges and fees paid to the owner, less an allowance of 20% for repairs and maintenance.

Inheritance/estate tax – No

Net wealth/net worth tax – No

Social security – For employees whose monthly income is HKD 7,100 or more, the employer is required to deduct 5% as the employee's contribution to the MPF scheme and then pay an additional 5% as its own contribution. Self-employed persons also contribute 5% of their relevant income and may choose to contribute on a monthly or annual basis. The maximum deduction is HKD 1,500 per month. All benefits derived from mandatory contributions must be preserved until the scheme member reaches the retirement age of 65, when he/she may withdraw the benefits in a lump sum.

Compliance for individuals:

Tax year – The tax year starts on 1 April of each year and ends on 31 March of the following year.

Filing and payment – The Inland Revenue Department issues tax returns to individual taxpayers on the first working day of May each year.

Penalties – Penalties may be imposed for failure to comply with the Inland Revenue Ordinance. The Commissioner of Inland Revenue has the authority to institute prosecution, to compound or to assess additional tax (which is a form of penalty) in respect of the offence.

Value added tax:

Taxable transactions – Hong Kong does not levy VAT.

Rates – N/A

Registration – N/A

Filing and payment – N/A

Source of tax law: Inland Revenue Ordinance and case law

Tax treaties: Hong Kong has signed 38 double tax agreements. Hong Kong signed the OECD MLI on 7 June 2017.

Tax authorities: Inland Revenue Department

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