

DEZAN SHIRA & ASSOCIATES

Your Partner for Growth in Asia



AN INTRODUCTION TO
DOING BUSINESS IN
HONG KONG 2016

Establishing and Running a Business
Tax, Audit and Accounting
Human Resources and Payroll
Industry Focus



 Join us on Facebook <Dezan Shira & Associates> <China Briefing>

 Visit us on LinkedIn <Dezan Shira & Associates> <China Briefing>

 Follow us on Twitter @DezanShira, @China Briefing



This edition of Doing Business in Hong Kong was produced by a team of professionals at Dezan Shira & Associates, with Samuel Wrest as managing editor and Steven Elsinga as technical editor. Creative design of the guide was provided by Jessica Huang and Estela Mi.

© 2016 Dezan Shira & Associates



DEZAN SHIRA & ASSOCIATES

Your Partner for Growth in Asia



ABOUT DEZAN SHIRA & ASSOCIATES

At Dezan Shira & Associates, our mission is to guide foreign companies through Asia's complex regulatory environment and assist them with all aspects of establishing, maintaining and growing their business operations in the region. Since its establishment in 1992, Dezan Shira & Associates has grown into one of Asia's most versatile full-service consultancies with operational offices across China, Hong Kong, India, Singapore and Vietnam, as well as liaison offices in Italy, Germany and the United States, and partner firms across the ASEAN region. With over 20 years of on-the-ground experience and a large team of professional advisers, we are your reliable partner in Asia

INTRODUCTION



ALBERTO VETTORETTI

Managing Partner
Dezan Shira & Associates

A handwritten signature in black ink, appearing to read 'Alberto Vettoretti'.

The People's Republic of China regained sovereignty over Hong Kong from Britain in 1997, from which point it has been a Special Administrative Region (SAR) of the country. However, the way in which the city is governed is still fundamentally different to the Chinese mainland – a fact that is reflected in its slogan of “One country, two systems”. Hong Kong is largely autonomous from China, and foreign companies will quickly discover that the rules of doing business in the mainland simply do not apply in Hong Kong, and vice versa.

For this reason, Hong Kong has long held a reputation as a popular “gateway” to invest in China. Its geographical proximity to the mainland, double taxation avoidance (DTA) network, modern banking system and transparent legal regime have made it an ideal location for foreign businesses to easily operate. While the Foreign Account Tax Compliance Act (FATCA) has stoked fears that this position may soon change – primarily because the act has caused some Hong Kong banks to turn away American corporations and individuals – Hong Kong remains the biggest source of foreign direct investment (FDI) into China, making up 81.2 billion of the country's total 119.5 billion FDI in 2014.

This publication, designed to introduce the fundamentals of doing business in Hong Kong, was created at the close of 2015 using the most up-to-date information at the time. It was compiled by Dezan Shira & Associates, a specialist foreign direct investment practice that provides corporate establishment, business advisory, tax advisory and compliance, accounting, payroll, due diligence and financial review services to multinationals investing in emerging Asia.

Since its establishment in 1992, Dezan Shira & Associates has grown into one of Asia's most versatile full-service consultancies with operational offices across China, Hong Kong, India, Singapore and Vietnam, partnership offices in Indonesia, Malaysia, the Philippines and Thailand, as well as liaison offices in Germany, Italy and the United States. Dezan Shira & Associates' experienced business professionals are committed to improving the understanding and transparency of investing in emerging Asia.



Contact Dezan Shira & Associates
asia@dezshira.com
www.dezshira.com



A BRIEF OVERVIEW OF HONG KONG

Political System

The Hong Kong Special Administrative Region (HKSAR) is currently ruled by China's Basic Law – the constitution adopted by the National People's Congress of the PRC on April 4, 1990. HKSAR was established on July 1, 1997, after Great Britain returned Hong Kong to the People's Republic of China (PRC).

Under the Basic Law, Hong Kong is allowed to retain the social, economic and legal systems present at the time of the handover for a 50 year period under the principle of "One Country, Two Systems." Additionally, the Basic Law designates a system of governance led by the Chief Executive, who is the head of the HKSAR, and the Executive Council, which assists the Chief Executive in policy-making issues.

Legal System

Due to its previous status as a British colony, Hong Kong's legal system is largely influenced by English Common Law. The constitutional framework for Hong Kong's legal system is provided by the Basic Law approved by the National People's Congress, which supplements the common law. The independent judiciary under the Basic Law ensures that Hong Kong remains within the common law system. The Court of Final Appeal is the highest court in HKSAR and is headed by the Chief Justice. Furthermore, reflecting its status as a Special Administrative Region, the HKSAR legal system is separate from the one governing the PRC under the principle of "One country, two systems."

Economic System

Hong Kong's economic system is defined as a free market economy and characterized by minimum intervention from the government. HKSAR is service oriented, and especially strong in the financial services, international trade, and tourism sectors. Additionally, it has strong economic links to mainland China and other major economies in the Asia Pacific region.

The lack of tariff and non-tariff barriers to trade has made Hong Kong an attractive destination for investors. Hong Kong SAR has no tariffs on imported goods, no import quotas, and applies excise duties to only four commodities. Furthermore, Hong Kong has no taxes on dividends generated from doing business in the country. Free trade and low taxation has helped Hong Kong to be ranked as the world's freest economy for 21 years in a row.

Financial System

The Hong Kong financial system is composed of four different financial regulators, each one governing different parts of the financial sector. These include the Securities and Futures Commission (SFC), an independent body set up to regulate the securities and future markets, and the Hong Kong Monetary Authority (HKMA), the government's agency responsible for maintaining monetary and banking stability.

Despite the HKMA's role as the currency board and de facto central bank, it does not print currency notes itself. Instead, it grants printing privileges to print the Hong Kong dollar to HSBC, Standard Chartered Bank and the Bank of China.

Under the Linked Exchange Rates System (LERS), the Hong Kong dollar has been pegged to the US dollar since 1983, at a rate of HK\$7.80 to US\$1, which has helped maintain monetary stability. Through the exchange rate system, the HKMA authorizes note-issuing banks to issue new banknotes, as long as an equivalent amount of US dollars is deposited with the HKMA.





ECONOMIC OUTLOOK

The economic outlook in 2016 will remain largely dependent on the global economy, in particular the slowdown in China and the U.S. interest rate rise in December, which are expected to shape the SAR's prospects over the coming year. Hong Kong's economy is forecasted to experience another slow year in 2016, with GDP growth likely to continue to hover at just above the 2.0 percent level. Stock market volatility remains a key risk in the region but confidence in the local bourse is expected to be buttressed by the launch of the Shenzhen-Hong Kong Stock Connect, which is scheduled to be implemented in 2016. This, together with other pioneering policies, will help support the sustainable growth of the banking and finance sector.

Trading volume will continue to fall along with the slowdown in demand from China, although the magnitude of the decline is expected to be smaller than that in 2015. The retail and tourism sectors are also expected to remain lackluster amid strong competition from cheaper destinations such as Japan, South Korea and the Eurozone, whose attractiveness to visitors has increased due to their devalued currencies. Hong Kong's competitiveness could further erode if China further devalues the RMB, as it did in 2015.

CBRE Research believes that any interest rate hikes in 2016 will be gradual and minimal. However, an increase in lending rates would reduce household spending power, leading to a fall in private consumption. A rise in U.S. interest rates would likely be followed by further currency appreciation, which would cause the HKD to follow suit. Any appreciation in the HKD would further damage exports and tourist consumption. Domestic spending could also face some headwinds as local shoppers opt to spend more overseas.

The employment sector will remain exposed to downside risks in 2016 as the trading and retail sectors continue to weaken. Oxford Economics forecasts that unemployment will edge up slightly from 3.3 percent in 2015 to 3.5 percent in 2016, although this level is still considered as near-full employment.

Looking beyond 2016, economic growth could pick as China re-emerges from its period of structural reform and the recovery in the U.S. picks up speed. In the longer term, the completion of massive new infrastructure works such as the Hong Kong-Zhuhai-Macau Bridge and the High Speed Rail (HSR) will provide new growth engines for Hong Kong.



This article and the "Industry Focus" section of this guide are provided by CBRE Group, Inc., a commercial real estate and property company with headquarters in Los Angeles, California. Hong Kong is CBRE's strategic regional hub and Asia Pacific headquarters.

For more information on CBRE and their services, please visit www.cbre.com.hk/ or contact: T +852 2820 2800 / F +852 2810 0830

TABLE OF CONTENTS

1 / Establishing and Running a Business	10
What are My Options for Investment?	11
• Different Entities That a Foreign Business Can Establish in HK	11
• Restrictions on Foreign Investment	12
How do I Establish a Business?	13
• Steps to Set up a Company in Hong Kong	13
• Minimum Requirements for Operating a Company	13
• Intellectual Property	14
• Opening a Bank Account in Hong Kong	16
• Recent Trends	17
How do I Make Changes to My Company?	18
• Dormant Company	18
• Changing a Company Name	18
• Changing the Company's Articles of Association	18
• Deregistering the Company	18
2 / Tax, Audit and Accounting	20
What are the Major Taxes in Hong Kong?	21
• Key Features of Hong Kong's Taxation System	21
• Salaries Tax (Individual Income Tax)	21
• Profits Tax (Corporate Income Tax)	23
• Property Tax	25
Offshore Status of Hong Kong Companies	26
• Contract Effectuated Test	26
• Operations Test	26
Key Compliance Requirements	28
• Accounting Standards	28
• Bookkeeping Requirements	28
• Financial Reporting Requirements	29

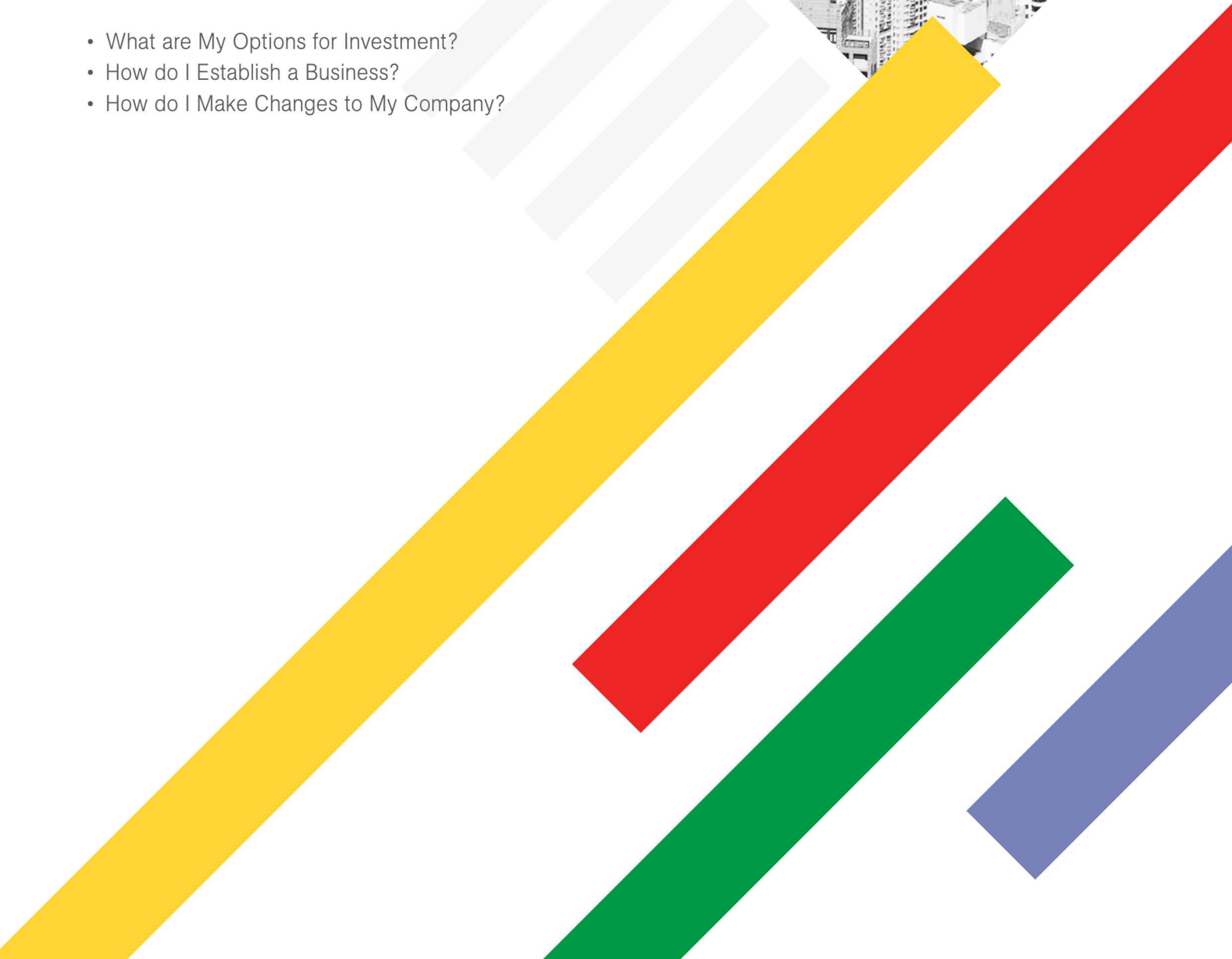
The Offshore Status of Hong Kong Companies	31
• How to Qualify for Offshore Tax Exemption	31
Hong Kong's Double Taxation Agreement Network	33
• Hong Kong's Existing Double Taxation Agreements	33
• Future DTAs under Current Negotiations	35
• The Benefits of Hong Kong's DTAs for Foreign Companies	36
3 / Human Resources and Payroll	37
How to Employ Workers in Hong Kong	38
• Registering Employees for Salaries Tax	38
Visa Procedures in Hong Kong	39
• Visitor's Visa	39
• Employment Visa	39
Employer's Obligation	40
• Social Security	40
• Leave	40
Terminating an Employee	42
• Types of Termination	42
• Severance Payment	43
• Long Service Payment	43
4 / Industry Focus	44
Retail Sector	45
Office Sector	47
Logistics Sector	49



1

ESTABLISHING AND RUNNING A BUSINESS

- What are My Options for Investment?
- How do I Establish a Business?
- How do I Make Changes to My Company?



WHAT ARE MY OPTIONS FOR INVESTMENT?



STEPHEN O'REGAN
Associate
International Business
Advisory

Different Entities That a Foreign Business Can Establish in HK

Hong Kong's Companies Ordinance recognizes several types of companies:

- Limited Company
 - » Company limited by shares, sub-divided into:
 - a. Private company
 - b. Public company
 - » Company limited by guarantee
- Unlimited Company

An unlimited company is one where the liability of its members is not limited.

Companies limited by guarantee do not have share capital, but the liability of its members is limited by the amount of assets they contribute. These entities are most commonly used as non-profits and NGOs.

There are three differences between a public and a private company. For a private company:

- The ability for members to transfer shares is restricted
- The number of members is limited to 50 (not including employees or former employees)
- The company may not issue invitations to the public to subscribe for shares or debentures of the company

If a company does not meet the above three conditions, it is a public company. The establishment procedure for a public company is much more complicated than for a private one.

“*The establishment procedure for a public company is much more complicated than for a private one. As such, for most purposes the private unlimited company is the most popular option for foreign investors.*”

Restrictions on Foreign Investment

Hong Kong allows foreign investment in almost all sectors, apart from two:

- **Television:** the Broadcasting Ordinance states that foreign ownership of a Hong Kong company with a license to broadcast domestic free television requires written consent from the Broadcasting Authority at three thresholds:
 - » Shareholding of 2-6 percent
 - » Shareholding of 6-10 percent
 - » Shareholding over 10 percent

In addition, if foreign entities in aggregate hold over 49 percent of voting control in such a company, their votes shall be subject to a formula as outlined in the Broadcasting Ordinance.

Companies with a license to broadcast domestic free television must be Hong Kong companies, and may not be the subsidiary of another company.

These restrictions do not apply to paid television, or non-domestic television.

- **Radio:** Foreign shareholding in a company with a sound-broadcasting license may not exceed 49 percent. Sound-broadcasting licenses can only be given to Hong Kong companies. Such companies may not be the subsidiary of another company.



Dezan Shira & Associates provides pre-investment market intelligence to foreign companies looking to establish a business in Hong Kong. For more information, please contact our experts at market.intelligence@dezshira.com

HOW DO I ESTABLISH A BUSINESS?

Steps to Set up a Company in Hong Kong

To set up a company in Hong Kong, investors need to follow the two steps below.

Step 1: Selecting a company name

The company's name can be either in Chinese or English, but may not contain both languages at the same time. Investors can look up whether the desired name already exists in the Company Registry. Also, the name may not infringe upon other parties' intellectual property rights. These too can be searched online, on the website of the Intellectual Property Department.

Step 2: Registering the company with the companies registry

Generally, companies can be fully registered online. However, preparing documents can be very time consuming in practice.

Besides completing two forms, the investor is required to submit the company's articles of association, signed by each founding member of the entity. Companies are generally not required to state their objectives in their memorandum, with certain exceptions such as companies incorporated to promote charitable objects. The articles should be in Chinese or English.

Once the documents have been submitted and the fees have been paid, the investor will receive the company registration certificate per email. Investors can choose to register for one year and pay a fee of HK\$2,250 or HK\$5,950 for three years (note that the registration fee is for 2016).

Investors can also file a paper company registration. However, registration will take longer. If paper documents were submitted, the investor may collect the certificate after four days at the Companies Registry. The paper and the electronic incorporation certificate have the same legal effect.

Note that some business activities may require an additional license, such as import and export.

Minimum Requirements for Operating a Company

Registered Capital

Most Hong Kong companies do not require a minimum registered capital.

Shareholding

With the new Companies Ordinance proclaimed in 2014, Hong Kong corporate law now allows investors to structure equity ratios independently from the amount of capital contributed. Voting rights and profit shares may also be separated, so that one shareholder may have a different voting share from its profit share.

Shares are considered personal property. Shareholders may transfer shares by notifying the company, which needs to register shareholding. Rules for transferring shares may be stipulated in the company's articles of association. When a transfer is lodged, the company needs to update its share register within two months.



VISIT US ON FACEBOOK
Dezan Shira & Associates

Alterations of share capital, such as the issuance of new shares or dilution must be notified to the Companies Registry within one month.

Corporate Governance

The company must have one director and one secretary. If the company has only one director, the sole director cannot be the secretary of the company at the same time. The sole shareholder can be a director.

As of 2014, at least one of the directors needs to be a natural person. If the company is part of a group of companies where one of these is a listed company, a director in the company may not be a corporate entity. Directors can be removed by ordinary resolution, i.e. by a simple majority of total shareholding rights.

The secretary can be an individual or a body corporate. If an individual, he/she should ordinarily reside in Hong Kong. If the secretary is a body corporate, its registered office or place of business should be in Hong Kong. When the corporate secretary is changed, the company needs to notify the Company Registry of the change.

Intellectual Property

Hong Kong offers a high level of protection for intellectual property (IP). According to the World Economic Forum, Hong Kong ranked 14th worldwide in terms of IP protection (2013-2014), and 10th according to the Intellectual Property Rights Index 2014. It is also a major global IP trading hub. Hong Kong recognizes several different classes of intellectual property: trademarks, patents, designs, copyright, trade secrets, plant variations and lay-out designs of integrated circuits.

Registering a Trademark

Trademarks are registered with the Hong Kong Trademarks Registry. Registration only covers the territory of the Hong Kong Special Administrative Region. Registration of a trademark in Hong Kong does not affect Mainland China, and vice versa.

To register a trademark in Hong Kong, the investor should first investigate whether the trademark is already registered in Hong Kong. This can be done online. If the trademark is available, the investor can apply for registration by filling in a form, with a graphic representation of the trademark attached. Along with the fee of HK\$2,000, these documents should then be sent to the Hong Kong Intellectual Property Department (IPD).

The IPD will then examine whether the trademark meets the requirements. There are four requirements:

- The trademark needs to be distinctive
- It cannot be a description of the goods or services the investor is providing
- It cannot be an industry or business term
- The trademark may not already exist

Provided there are no deficiencies in the form that was submitted, the trademark registration can be completed in six months. If the IPD has objections to the registration, it will notify the investor and give 6 months to rectify the application.

It should be noted that registering a company and registering a trademark are two separately distinct procedures with different legal outcomes.

Registering a Patent

Patents protect inventors by giving them the legal right to prevent others from manufacturing or selling their patented invention.

To register a patent in Hong Kong, the owner needs to already have a patent with the State Intellectual Property Bureau in Mainland China, the European Patent Office, or the United Kingdom Patent Office. These can then be extended to Hong Kong.

Hong Kong has two types of patents, a short-term patent and a standard patent. Standard patents are renewable every three years, for a maximum of twenty years. Short-term patents are valid for four months and renewable only once.

The application for a standard patent goes through two phases. The first is to request to record the existing patent (either from Mainland China, the EU or the United Kingdom). This needs to be done within six months after the patent has been published. Within two months, the IPD will give the applicant notice of any deficiencies in the application. If there are no deficiencies, or these have been corrected, the request will be published in the Hong Kong Intellectual Property Journal. Once the request has been published, the applicant needs to request registration and grant of the patent. Again, this needs to be done within six months after the request has been published. If the IPD finds no deficiencies, it will grant the standard patent.

The application for a short-term patent is more straightforward. The applicant needs only to file a request once, and attach a search report from either the State Intellectual Property Bureau in Mainland China, the European Patent Office, or the United Kingdom Patent Office.

Registering a Design

Designs are defined by the Registered Design Ordinance as “features of shape, configuration, pattern or ornament applied to an article by any industrial process, being features which in the finished article appeal to and are judged by the eye”.

Designs can be registered and protected if the designer can show that they are new. A design is new if it has not been previously registered, or has never before been published or disclosed. To file for the registration of a design, the applicant needs to submit the prescribed form, provide a representation and statement of novelty, and pay the registration fee. If the application is in order, the Designs Registry will publish the registration in the Hong Kong Intellectual Property Journal. The design will be protected for a maximum of 25 years, and needs to be renewed every five.

Copyright

Unlike the other intellectual property rights in Hong Kong, copyright arises automatically and does not need to be registered. It differs from design in that design protects the shape of an object. A copyright applies to:

- Literary, dramatic, musical or artistic work
- Sound recordings, films, broadcasts or cable programs
- The typographical arrangement of published editions

With the copyright, the owner has the exclusive right to:

- Copy the work
- Issue or make available copies of it to the public
- Rent out copies of it to the public
- Perform the work
- Broadcast the work

- Make an adaptation to the work

Others are restricted from copying the work, which is defined as reproducing the work in any material form.

The protection for copyright differs from that of registered design in that copyright only protects against reproduction of the works, whereas a registered design also protects against the independent creation of a new design that is not substantially different from the registered design. The bar to prove a copyright infringement is also higher than for a registered design, in that for copyright infringement, the owner needs to show there is a reproduction in material form, whereas for registered design infringement, the designer needs to establish that the design is the same as or not substantially different from the registered design.

The owner of a copyright may seek a court injunction to prevent the reproduction and distribution of copyrighted materials, as well as claiming financial compensation.

Opening a Bank Account in Hong Kong

When a foreign investor wishes to set up a bank account in Hong Kong, the bank will usually require the directors and authorized signatories to come to the bank office in person for a Know Your Client meeting. This is required under Hong Kong anti-money laundering legislation. Financial regulations have been tightened in recent years, in order to combat the designation of the city as a tax haven.

As part of these regulations, the Hong Kong Monetary Authority has released a Guideline requiring banking institutions to implement a background check on applications for business accounts. Specifically, the banking institution needs to verify the identity of the primary shareholders, at least two directors (including the managing director) and the authorized signatories.

These individuals will need to come in person to the meeting. Sending another individual on an absentee's behalf is considered a red flag. The attendants of the meeting need to bring their passport (not a copy), their Hong Kong work permit (if applicable), and a proof of address. This can be a recent utility or something of the like.

Under the Guideline, the bank is also required to examine the nature of the business. The bank will therefore commonly enquire about the intended use of the bank account, the company's objectives (such as expected turnover), detailed information about operations (such as what products are being traded, the mark-up, etc.) its business scope and the source of funds. Often, the bank will request supporting documentation and review these in a process that may take between two to four weeks.

Evidence of the nature of the business can include the company website, a business plan, proposed contracts, brochures etc. If these are not available for the local company, information of this nature can be provided about the parent company or the corporate group instead.

In any case, the applicants will need to submit:

- The Certificate of Incorporation and Business Registration Certificate
- The memorandum and articles of association
- A resolution of the board of directors to open an account, stating who is authorized to open and operate it
- The company file at the Company Registry



FABIAN KNOPF

Senior Associate
International Business
Advisory

“Key to using a Hong Kong corporation to establish a Chinese subsidiary is the ability to open and maintain a corporate bank account in Hong Kong, since a Chinese subsidiary may only receive a capital injection from a bank account held in the name of the parent company.”

Please note that when a company is marked as a 'shell company', it will be subject to a higher level of scrutiny. Here, a shell company is understood to be a corporation that does not conduct business activities itself, but channels funds for group companies. Here, the identity documents of the beneficial owners is required as well.

Once the bank account has been approved, the investor will receive the bank account number, bank cards and access codes. The account will become fully active once the first deposit has been made.

Recent trends

In recent years, Hong Kong has been blacklisted by many governments for being a safe haven for sheltering or laundering money, tax evasion and other criminal behavior. In order to rid itself of this status, the Hong Kong government has stepped up regulation of its banking and financial sector. This includes its acceptance of the Foreign Account Tax Compliance Act (FATCA). This American law intends to combat tax evasion committed by American citizens who hide their funds abroad by enlisting the cooperation of foreign governments. These governments then implement FATCA into their own law, establishing a regulatory framework that requires banks in that country to monitor all the transactions engaged in by American citizens. Since Hong Kong acceded to FATCA and implemented its stipulations into Hong Kong law, local banks are now required to set up a complex monitoring mechanism for American clients.

The costs of this mechanism have prompted many Hong Kong banks to refuse predominantly American clients – both corporate and individual – altogether. Even where Hong Kong banks still accept American clients, the compliance requirements have increased substantially, as has the red tape involved in opening accounts.

HOW DO I MAKE CHANGES TO MY COMPANY?

Dormant Company

A company can become dormant when it passes a special resolution (resolution approved by at least 75 percent of shareholders) to go dormant, and the Companies Registry has been notified.

If a company is dormant, many of its compliance requirements are reduced or lifted. The company no longer needs to:

- Hold annual meetings
- Deliver annual returns
- Prepare financial statements and Directors' Reports
- Appoint auditors and undergo annual audits
- Publish financial statements to the shareholders before general meetings
- Prepare summary financial reports

A company returns from dormancy the moment it engages in an accounting transaction. Despite all the benefits, a dormant company still needs to maintain a registered office, corporate secretary, and fulfil annual business registration.

Changing a Company Name

To change the company name, the board needs to pass a special resolution to do so. Within 15 days of the resolution, the company must inform the Companies Registry of the change.

Changing the Company's Articles of Association

To change the articles of association, the company again needs to pass a special resolution. The company then needs to notify the Companies Registry and submit a copy of the altered articles. The holders of at least 5 percent of shares can appeal to the court to cancel the alteration.

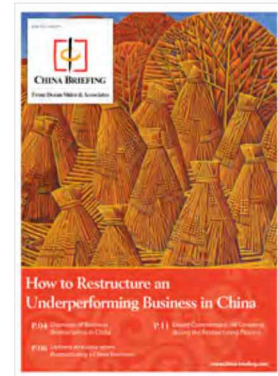
Deregistering the Company

The company, a director or a shareholder can request deregistration. To do so, the following conditions need to be met:

- All shareholders agree
- The company has not yet commenced operations, or has ceased operations three months ago
- The company has no outstanding liabilities
- The company is not involved in any ongoing legal proceedings
- The company has no subsidiary around the world and holds no asset (i.e., immovable property) in Hong Kong.

The board should first pass a resolution to deregister the company.

RELATED READING



How To Restructure an Underperforming Business in China

June, 2015

- See more [here](#)

Before the company can be deregistered, it first needs to show a written notice from the tax office stating it has no objection against the deregistration. Directors and shareholders can apply for such a letter, or a person authorized to do so by the company. To apply for this letter, the applicant has to fill in a form, retrievable from the tax office website, and pay a fee of HK\$ 270. It takes up to 21 days to process the request.

With the Notice of No Objection, the investor should then apply for deregistration with the Companies Registry within three months. To apply for deregistration, the investor has to fill in the designated form and pay a fee. The Notice of No Objection needs to be included in the submission. Where the applicant is a company, it must designate a natural person to give notice to the Companies Registry.

The deregistration will then be published in the Company Gazette. If no objections are made in the following three months - such as by alleged creditors - the deregistration is effectuated.

Former directors must keep the books and papers of the company for seven years after deregistration.



2

TAX, AUDIT AND ACCOUNTING

- What are the Major Taxes in Hong Kong?
- Offshore Status of Hong Kong Companies
- Key Compliance Requirements
- Hong Kong's Double Taxation Agreement Network

WHAT ARE THE MAJOR TAXES IN HONG KONG?



JENNIFER LU
Senior Manager
Corporate Accounting
Services

According to the Basic Law of Hong Kong, the taxation system of PRC China is not applicable to Hong Kong, which essentially means that Hong Kong enjoys an independent taxation system. Generally speaking, because the city only imposes three direct taxes, Hong Kong has one of the most simple tax economies in the world. There are also generous allowances and deductions to reduce the burden of taxpayers. Apart from direct taxes, certain indirect taxes are also collected, such as stamp duty and betting duty.

One thing to be noted is that Hong Kong doesn't have any turnover taxes, including sales tax or value added tax, making it a favorable location for profit shifting and conducting re-invoicing activities. In this part of the guide, we firstly introduce the unique features of HK's taxation system and then concentrate on its three direct taxes, which constitute a major part of the government's fiscal revenue. Tax administration is charged by the Inland Revenue Department. The tax assessment year usually runs from April 1 to March 31 each year. A company may also choose their fiscal year on their own discretion.

Key Features of Hong Kong's Taxation System

Compared to the taxation systems of other jurisdictions, Hong Kong's tax system has some special features.

Firstly, taxes in Hong Kong are only levied on a territorial basis, unlike most countries which apply both residential jurisdiction and territorial jurisdiction in determining tax liability. That is to say, only income arising in or derived from Hong Kong is taxable, whereas worldwide income is not taxable, irrespective of the residence status of the taxpayers.

Secondly, there is no comprehensive system of income taxation in Hong Kong. Instead, a taxpayer is liable to tax on three different types of income. If an income fails to fall within any of the three specific tax provisions, then it shall not be subject to tax.

Salaries Tax (Individual Income Tax)

All individuals earning income arising in or derived from Hong Kong from an office, employment or pension are subject to salaries tax in Hong Kong. Tax payable is calculated at a progressive rate on the "net chargeable income" or at a standard rate on the "net income" (before deduction of the allowances), depending on which is lower. It is further reduced by a tax reduction, subject to a maximum.

Net Chargeable Income = Total Income – Deductions – Allowances

Net Income = Total Income – Deductions

“Hong Kong doesn't have any turnover taxes, including sales tax or value added tax, making it a favorable location for profit shifting and conducting re-invoicing activities.”

Tax Rates

PROGRESSIVE RATES (YEAR OF ASSESSMENT 2016/17 ONWARDS)		
Net Chargeable Income(HKD)	Rate	Tax (HKD)
On the first 40,000	2%	800
On the next 40,000	7%	2,800
On the next 40,000	12%	4,800
Remainder	17%	
STANDARD RATE OF TAX		
15%		

Allowance

YEAR OF ASSESSMENT 2016/17 ONWARDS, IN HKD	
Basic allowance	132,000
Marriage allowance	264,000
Child allowance (for each dependent): the 1 st to 9 th child	100,000
For each child born during the year, the Child allowance will be increased by	100,000
Dependent brother or sister allowance (for each dependent)	33,000
Dependent parent and dependent grandparent allowance (for each dependent)	
Parent/grandparent aged 60 or above or is eligible to claim an allowance under the Government's Disability Allowance Scheme	40,000
Parent/grandparent between the age of 55 to 60	23,000
Additional dependent and dependent grandparent allowance	
Parent/grandparent aged 60 or above or is eligible to claim an allowance under the Government's Disability Allowance Scheme	46,000
Parent/grandparent between the age of 55 to 60	23,000
Single parent allowance	132,000
Disabled dependent allowance (for each dependent)	66,000

Deductions (Maximum Limits)

YEAR OF ASSESSMENT 2016/17 ONWARDS, IN HKD	
Expenses of self-education	80,000
Elderly residential care expense	92,000
Home loan interest	100,000
Mandatory contribution to recognized retirement schemes	18,000
Approved charitable donations (income-allowable expenses-depreciation allowance)×percentage	35%



VISIT US ON LINKEDIN
Dezan Shira & Associates

Maximum Tax Reductions:

Profits tax, salaries tax and tax under personal assessment for the year of assessment 2015/16 are reduced by 75 percent, subject to a ceiling of HK\$20,000 per case.

- For profits tax, the ceiling of the tax reduction is applied to each business.
- For salaries tax, the ceiling is applied to each individual taxpayer; but for couples jointly assessed, the ceiling is applied to each couple.
- For personal assessment, single taxpayers will each be subject to the ceiling. Married couples must make their personal assessment election together and the ceiling will therefore apply to each couple.
- The tax reduction is not applicable to property tax.

Profits Tax (Corporate Income Tax)

Any party, including corporations, partnerships, trustees and organizations involved in any trade, profession or business in Hong Kong, is subject to tax on all profits (excluding profits arising from the sale of capital assets).

Profits tax is levied based on assessable profits, which is determined by excluding deductible expenses and tax-exempt incomes.

Profits Tax Rate

- Normal rate (for the year of assessment 2008/09 onwards)
 - » Corporations: 16.5 percent
 - » Unincorporated businesses: 15 percent
- Concessionary rate
 - » Half of the normal profits tax rate is applied to trading profits and interest income received or derived from qualifying debt instruments issued in Hong Kong, and to offshore businesses of professional reinsurance companies

Exemptions

The following sums can be exempted from the assessable profits of a company:

- Dividends received from a corporation which is subject to Hong Kong Profits Tax;
- Amounts already included in the assessable profits of other persons chargeable to Profits Tax;
- Interest on Tax Reserve Certificates;
- Interest on, and any profit made in respect of, a bond issued under the Loans Ordinance (Cap. 61) or the Loans (Government Bonds) Ordinance (Cap. 64), or in respect of an Exchange Fund debt instrument or in respect of a Hong Kong dollar-denominated multilateral agency debt instrument;
- Interest income and trading profits derived from long term debt instruments; and
- Sums received or accrued in respect of a specified investment scheme by or to the person as:
 - » A person chargeable to Profits Tax in respect of a mutual fund, unit trust or similar investment scheme that is authorized as a collective investment scheme under section 104 of the Securities and Futures Ordinance (Cap. 571); or
 - » A person chargeable to Profits Tax in respect of a mutual fund, unit trust or similar investment scheme where the Commissioner is satisfied that the mutual fund, unit trust or investment scheme is a bona fide widely held investment scheme which complies with the requirements of a supervisory authority within an acceptable regulatory regime.

Deductions

• Deductible Expenses

Generally, all outgoings and expenses, to the extent to which they have been incurred by the taxpayer in the production of chargeable profits, are allowed as deductions. However, the following items are non-deductible:

- » Domestic or private expenses;
 - » Any loss or withdrawal of capital, the cost of improvements and any expenditure of a capital nature;
 - » Any sum recoverable under insurance or contract of indemnity;
 - » Rent of or expenses relating to premises not occupied or used for the purpose of producing the profits;
 - » Taxes payable under the I.R.O., except Salaries Tax paid in respect of employees' remuneration;
 - » Any remuneration or interest on capital or loans payable to section 16AA; contributions made to a mandatory provident fund scheme in respect of the proprietor or the proprietor's spouse or, in case of a partnership, to its partners or their spouses.
- Expenditure on Building Refurbishment
- » A person who incurs capital expenditure on the renovation or refurbishment of business premises is allowed to deduct that expenditure over a period of five years in equal installments commencing the year in which the expenditure is made.
- Expenditure on plant and machinery specially related to manufacturing, and on computer hardware and software
- » For this kind of expenditure, a full deduction is allowed during the basis period in which the expenditure was incurred.
- Expenditure on Environmental Protection Facilities
- » Expenditure on environmental protection machinery –With effect from the year of assessment 2008/09, a full deduction is allowed during the basis period in which the expenditure is incurred.
 - » Expenditure on environmental protection installation –With effect from the year of assessment 2008/09, a deduction at 20 percent of the expenditure is allowed during the five years that follow the year in which the expenditure is incurred.
 - » Expenditure on environmentally friendly vehicles –With effect from the year of assessment 2010/11, a full deduction is allowed during the basis period in which the expenditure is incurred.
- Depreciation Allowances
- » Industrial Building Allowances on Industrial Buildings and Structures
 - › Initial allowance: 20 percent on the cost of construction of the premises
 - › Annual allowance: four percent on the cost of construction of the premises
 - › Balancing allowance or charge will be due upon disposal of the premises
 - » Commercial Buildings Allowances on Commercial Buildings and Structures
 - › Annual allowance: four percent on the cost of construction of the premises
 - › Balancing allowance or charge will be due upon disposal of the premises
 - » Plant and Machinery
 - › Initial allowance: 60 percent on the cost
 - › Annual allowance: at rates of 10 percent, 20 percent or 30 percent as prescribed by the Board of Inland Revenue in the Inland Revenue Rules, on the reducing value of the asset. Items qualifying for the same rate of annual allowance are grouped under one "pool".
 - › A balancing allowance is available only on cessation of a business to which there is no successor. A balancing charge can, however, arise whenever the disposal proceeds of one or more assets exceed the reducing value of the whole "pool" of assets to which the disposed items belong.

» Donations

Charitable donations made to approved charitable institutions or trusts of a public character or to the Government of the Hong Kong Special Administrative Region, amounting in aggregate not less than HK\$100 but not exceeding 35 percent (10 percent for years of assessment up to and including 2002/03; and 25 percent for years of assessment 2003/04 to 2007/08) of the adjusted assessable profits before deduction of donations, are allowable for deduction in computing the assessable profits.

Property Tax

Property tax is levied on income arising from the letting of immovable property in Hong Kong. Property Tax is payable by the owner(s) at the standard rate of the year of assessment on “net assessable value”. Under the provisions of the “Inland Revenue Ordinance” (IRO), each and every joint owner or owner in common is responsible for reporting rental income on tax returns and paying Property Tax as if he/she is the sole owner.

Where the owner receives only rent and no other benefit, the annual rent is the “assessable value” (AV). Rent receivable (due but not yet received) should be included in the AV. Irrecoverable rent can be excluded from tax charge in the year in which it became irrecoverable. Any amount subsequently recovered is assessable to tax as income in the year of recovery.

The property tax is paid on 15 percent of the net assessable value.

- If the tenant pays rates, the net assessable value is less than a standard allowance of 20 percent for repairs and outgoings.
- If the owner is responsible for paying rates, rates paid can be deducted before allowing for the 20 percent deduction.



For assistance navigating Hong Kong's various tax compliance requirements, please contact our tax experts at tax@dezshira.com

OFFSHORE STATUS OF HONG KONG COMPANIES

A company in Hong Kong can be established without substance. This means that the business operation can be run in name only with no office or staff and can be operated remotely. Under the current practices if no income is sourced from the Hong Kong company, meaning that all the income is sourced from abroad, then the company will not be liable for tax in Hong Kong. Generally, there are two common types of tests to determine a company's offshore status:

Contract Effected Test

The contract effected test is used for determining the taxability of the income accruing to the taxpayer from trading transactions. The important factor here is whether or not the contract of purchase or sale is made in Hong Kong. This includes negotiation, conclusion and execution of the terms of the contract. The following factors should also be taken into consideration:

- How were the goods shipped?
- How were the sales solicited and orders processed?
- How were the goods procured and stored?
- How was financing arranged?
- How was the payment made?

Operations Test

The operations test is for cases other than trading and money lending (manufacturing income and passive income). For commission income, when applying for tax exemptions, one should take the following questions into consideration:

- What is the originating cause of the income?
- Did the originating cause take place in Hong Kong?
- What has been done to earn profits and where was it done?

Essentially enterprises should be aware of the following needs when applying for offshore status:

- No operations office in Hong Kong
- No staff hired and working in Hong Kong
- No customers/client from Hong Kong
- No suppliers from Hong Kong
- Income contract not negotiated or concluded in Hong Kong
- Goods not entering Hong Kong
- Services agreements or sales/purchases invoices should avoid involving any Hong Kong parties
- The actual operations take place outside Hong Kong

Once these basic requirements are met, the tax authority will check the supporting documents and decide whether the company should pay tax or not. However, once the exemption is granted the company should prepare annual accounting and audit reports, as well as tax returns in the jurisdictions where it operates outside of Hong Kong.

It is common for the tax authority to wait 2-3 years before questioning companies regarding their offshore status. At that point the company should prepare for a review of their books starting from incorporation. Obtaining an offshore status was quite popular up to five years ago, but now the tax authority is becoming quite strict.

Documentary evidences including but not limited to the following documents are critical to the success of the claim:

- Organization chart with full details of the company's establishments in Hong Kong and overseas which should include the location and size of the office, the number of employees and their respective names, post titles, duties and remuneration packages.
- Travelling schedule and passport of the directors and the persons who are involved in the business of the Hong Kong company.
- A detailed description of the businesses carried out by the company in order to earn income. For each of the activities identified, the company should specify the name of the responsible person and the place where such activity was performed.
- With regard to the income, especially high-income, the investor needs to provide the following documents:
 - » Correspondence of negotiation with the customer and suppliers (email, fax etc.,)
 - » Distribution agreement or master sales agreement should be provided if any
 - » The purchase/sales order, sales confirmation, shipping documents and invoice of sales and purchase
 - » Relevant banking documents

KEY COMPLIANCE REQUIREMENTS



LINDA CHEN

Manager
Corporate Accounting
Services

Accounting Standards

As one of the two Special Administrative Regions of China, Hong Kong enjoys the rights to develop its own accounting standards, rather than applying the relative standards of mainland China. The Hong Kong Institute of Certified Public Accountants (HKICPA) is the only organization authorized by law to promulgate financial reporting and auditing standards for professional accountants in Hong Kong.

The accounting standards of Hong Kong are known as the Hong Kong Financial Reporting Standards (HKFRS), which have been fully converged with International Financial Reporting Standards (IFRS) since January 1, 2005. According to the HKICPA, HKFRS are designed to apply to general purpose financial statements and other financial reporting of all profit-oriented entities.

On April 30, 2010, the HKICPA issued the Hong Kong Financial Reporting Standard for Private Entities (HKFRS for Private Entities) as a financial reporting option for Private Entities to relieve the reporting requirements under full HKFRS of qualifying private entities. Section 1 of HKFRS for Private Entities presents the qualifying criteria for applying this standard. However, entities are not mandated to adopt this standard, even if they are eligible to do so. This means that such eligible entities can apply for the full HKFRS only if they wish.

There is an additional standard that applies to small and medium sized entities, the Hong Kong Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (SME-FRF & SME-FRS). This standard was initially issued in August 2005 and revised in March 2014. Again, the standard is not mandatory. The qualifying criteria is set out in Division 2 of the Hong Kong Company Ordinance and highlighted in Paragraphs 22-43 of this standard.

Bookkeeping Requirements

According to part 9 of the Hong Kong Companies Ordinance, the most recent version of which came into effect March 3 2014, companies incorporated in Hong Kong must maintain proper books of accounts and must also satisfy statutory audit requirements on an annual basis.

Detailed requirements for bookkeeping are stipulated in the Subdivision 2 of the Company Ordinance, according to which:

A company must keep accounting records that comply with

- Accounting records that are sufficient to show and explain the company's transactions; to disclose the company's financial position and performance with reasonable accuracy; and to enable directors to ensure that the financial statements comply with the Company Ordinance.
- In particular, the accounting records must contain:
 - » daily entries of all sums of money received and expended by the company, and the matters in respect of which the receipt and expenditure takes place; and,
 - » the assets and liabilities of the company

* Section 51C of the Inland Revenue Ordinance provides a more specific list of the records to be kept

“Hong Kong enjoys the rights to develop its own accounting standards, rather than applying the relative standards of mainland China.”

Where to keep the accounting records

- A company's accounting records must be open to inspection by the directors at all times
- If a company's accounting records are kept in a location outside Hong Kong, the accounts and returns must be sent to a place within Hong Kong. Those accounts and returns must disclose with reasonable accuracy the financial position of the business in question at intervals of not more than 6 months

How long accounting records are to be preserved

- The company must preserve the records for seven years after the end of the financial year to which the last entry was made
- Penalties for not complying with the bookkeeping requirements:
- A director of a company who fails to take all reasonable steps to secure compliance with the bookkeeping requirements commits an offence and is liable to a fine of HK\$300,000

Financial Reporting Requirements

Statutory reports are required annually for companies incorporated in Hong Kong. The reports must contain audited financial statements for the current year, with corresponding amounts for the preceding year, including a balance sheet, profit and loss account, and a cash flow statement. Audited financial statements must be prepared and signed off by a certified public accountant on behalf of a business or non-profit organization, to provide financial accountability and accuracy to a company's stakeholders and people with a vested interest in the company.

Companies incorporated outside Hong Kong but have a place of business there should register as a foreign company with the Registry. If required to publish their financial statements under the laws or regulations of their incorporated place, the foreign company should file its financial statements in the annual return to the Registry.

Foreign companies whose securities are publicly traded in the Hong Kong Stock Exchange may prepare financial statements in accordance with either the HKFRS or the IFRS, or under certain limited conditions of other reporting frameworks, such as the China Accounting Standards for Business Enterprises (ASBE) and Generally Accepted Accounting Principles in the United States of America (US GAAP).

To prepare financial statements, certain documents might be required according to the instructions by Inland Revenue Department. These are as follows:

TYPE	RECORD TO BE MAINTAINED
Sales	Sales invoice
	Goods return note
	Receipt slip
	Daily receipt record
Purchases	Purchases invoice
	Petty cash voucher
	Payment slip
	Check stub
	Statement
General expenses	Expenses invoice
	Payment receipt
	Check stub
	Salary record
Bank transaction	Bank statements
	Bank paid-in slip and related receipt details
	Check stub and copy
Tangible assets	Purchase and sale agreement
	Invoice and receipt
	Check stub and copy
Inventory	Purchase and sale agreement
	Invoice and receipt
	Check stub and copy
	Inventory list (including quantity and unit cost on every item)
	Obsolete or slowing-moving inventory
Investment	Security ask/bid confirmation slip
	Purchase and sale agreement
	Capital inspection report (Apply for PRC investment)

THE OFFSHORE STATUS OF HONG KONG COMPANIES

How to Qualify for Offshore Tax Exemption

A company in Hong Kong can be established without substance. This means that the business operation can be run in name only with no office or staff and can be operated remotely. Under current practices, if no income is sourced from the Hong Kong company – meaning that all income is sourced from abroad – then the company will not be liable for tax in Hong Kong. Generally, there are two common types of tests to determine a company's offshore status:

1. Contract Effected Test

The contract effected test is used for determining the taxability of the income accruing to the taxpayer from trading transactions. The important factor here is whether or not the contract of purchase or sale is made in Hong Kong. This includes negotiation, conclusion and execution of the terms of the contract. The following factors should also be taken into consideration:

- How were the goods shipped?
- How were the sales solicited and orders processed?
- How were the goods procured and stored?
- How was financing arranged?
- How was the payment made?

2. Operations Test

The operations test is for cases other than trading and money lending (manufacturing income and passive income). For commission income, when applying for tax exemptions, one should take the following questions into consideration:

- What is the originating cause of the income?
- Did the originating cause take place in Hong Kong?
- What has been done to earn profits and where was it done?

Essentially, enterprises should be aware of the following needs when applying for offshore status:

- No operations office in Hong Kong
- No staff hired and working in Hong Kong
- No customers/client from Hong Kong
- No suppliers from Hong Kong
- Income contract not negotiated or concluded in Hong Kong
- Goods not entering Hong Kong
- Services agreements or sales/purchases invoices should avoid involving any Hong Kong parties
- The actual operations take place outside Hong Kong

Once these basic requirements are met, the tax authority will check the supporting documents and decide whether the company should pay tax. If and when the exemption is granted, the company should prepare annual accounting and audit reports, as well as tax returns in the jurisdictions where it operates outside of Hong Kong.

It is common for the tax authority to wait 2-3 years before questioning companies regarding their offshore status. At that point the company should prepare to review their books starting from incorporation. Obtaining an offshore status was quite common around five years ago, but now the tax authority is becoming quite strict.

Documentary evidences including but not limited to the following documents are critical to the success of the claim:

- Organization chart with full details of the company's establishments in Hong Kong and overseas which should include the location and size of the office, the number of employees and their respective names, post titles, duties and remuneration packages
- Travelling schedule and passport of the directors and the persons who are involved in the business of the Hong Kong company
- A detailed description of the businesses carried out by the company in order to earn income. For each of the activities identified, the company should specify the name of the responsible person and the place where such activity was performed.
- With regard to the income, especially high-income, the investor needs to provide the following documents:
 - » Correspondence of negotiation with the customer and suppliers (email, fax etc.);
 - » If applicable, distribution agreement or master sales agreement;
 - » The purchase/sales order, sales confirmation, shipping documents and invoice of sales and purchase;
 - » Relevant banking documents.

HONG KONG'S DOUBLE TAXATION AGREEMENT NETWORK

Hong Kong's Existing Double Taxation Agreements

COUNTRY / TERRITORY	DATE OF SIGNATURE OF AGREEMENT	EFFECTIVE FROM
Austria	25.05.2010	Year of Assessment 2012/2013
Austria (Protocol)	25.06.2012	03.07.2013
Belgium	10.12.2003	Year of Assessment 2004/2005
Brunei	20.03.2010	Year of Assessment 2011/2012
Canada	11.11.2012	Year of Assessment 2014/2015
Czech	06.06.2011	Year of Assessment 2013/2014
France	21.10.2010	Year of Assessment 2012/2013
Guernsey	22.04.2013	Year of Assessment 2014/2015
Hungary	12.05.2010	Year of Assessment 2012/2013
Indonesia	23.03.2010	Year of Assessment 2013/2014
Ireland	22.06.2010	Year of Assessment 2012/2013
Italy	14.01.2013	Year of Assessment 2016/2017
Japan	09.11.2010	Year of Assessment 2012/2013
Japan (Exchange of Notes)	10.12.2014	Year of Assessment 2016/2017
Jersey	22.02.2012	Year of Assessment 2014/2015
Korea	08.07.2014	Pending
Kuwait	13.05.2010	Year of Assessment 2014/2015
Liechtenstein	12.08.2010	Year of Assessment 2012/2013

COUNTRY / TERRITORY	DATE OF SIGNATURE OF AGREEMENT	EFFECTIVE FROM
Luxembourg	02.11.2007	Year of Assessment 2008/2009
Luxembourg (Protocol)	11.11.2010	Year of Assessment 2012/2013
Mainland China	11.02.1998	Year of Assessment 1998/1999
Mainland China	21.08.2006	Year of Assessment 2007/2008
Mainland China (2nd Protocol)	30.01.2008	11.06.2008
Mainland China (3rd Protocol)	27.05.2010	20.12.2010
Mainland China (4th Protocol)	01.04.2015	Pending
Malaysia	25.04.2012	Year of Assessment 2013/2014
Malta	08.11.2011	Year of Assessment 2013/2014
Mexico	18.06.2012	Year of Assessment 2014/2015
Netherlands	22.03.2010	Year of Assessment 2012/2013
New Zealand	01.12.2010	Year of Assessment 2012/2013
Portugal	22.03.2011	Year of Assessment 2013/2014
Qatar	13.05.2013	Year of Assessment 2014/2015
South Africa	16.10.2014	01.04.2016
Spain	01.04.2011	Year of Assessment 2013/2014
Switzerland	04.10.2011	Year of Assessment 2013/2014
Thailand	07.09.2005	Year of Assessment 2006/2007
United Arab Emirates	11.12.2014	Pending
United Kingdom	21.06.2010	Year of Assessment 2011/2012
Vietnam	16.12.2008	Year of Assessment 2010/2011
Vietnam (Protocol)	13.01.2014	Year of Assessment 2016/2017

Future DTAs Under Current Negotiations

COUNTRY / TERRITORY	NEGOTIATIONS SCHEDULED	SCHEDULED NEGOTIATIONS COMPLETED ON
Bahrain	15.04.2013 - 17.04.2013 (1st round)	16.04.2013
	11.12.2013 - 12.12.2013 (2nd round)	12.12.2013
Bangladesh	22.08.2011 - 25.08.2011 (1st round)	25.08.2011
	31.07.2014 - 01.08.2014 (2nd round)	01.08.2014
Finland	06.07.2010 - 08.07.2010 (1st round)	08.07.2010
	20.09.2011 - 22.09.2011 (2nd round)	21.09.2011
Germany	16.06.2014 - 20.06.2014 (1st round)	20.06.2014
	02.03.2015 - 06.03.2015 (2nd round)	06.03.2015
India	03.08.2010 - 05.08.2010 (1st round)	05.08.2010
	18.04.2011 - 21.04.2011 (2nd round)	21.04.2011
Israel	20.01.2014 - 24.01.2014 (1st round)	23.01.2014
Latvia	18.11.2013 - 22.11.2013 (1st round)	21.11.2013
Macao SAR	05.07.2005 - 06.07.2005 (1st round)	06.07.2005
	09.02.2007 (2nd round)	09.02.2007
Macedonia	09.06.2015 - 12.06.2015 (1st round)	12.06.2015
Mauritius	14.01.2013 - 17.01.2013 (1st round)	16.01.2013
Pakistan	24.09.2007 - 28.09.2007 (1st round)	28.09.2007
	15.01.2014 - 17.01.2014 (2nd round)	17.01.2014
Romania	27.10.2014 - 30.10.2014 (1st round)	29.10.2014
Russian Federation	18.12.2013 - 19.12.2013 (1st round)	19.12.2013
Saudi Arabia	25.05.2010 - 28.05.2010 (1st round)	28.05.2010
	22.05.2011 - 25.05.2011 (2nd round)	25.05.2011
	12.05.2015 - 14.05.2015 (3rd round)	13.05.2015

The Benefits of Hong Kong's DTAs for Foreign Companies

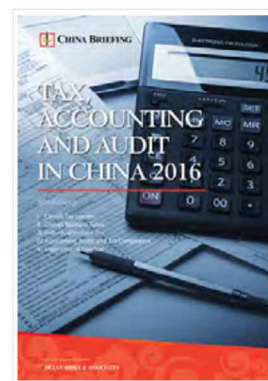
Double taxation arises when two or more tax jurisdictions overlap, resulting in the same item of income or profit being taxed in each. Hong Kong adopts the territoriality basis of taxation, whereby only income/profit sourced in Hong Kong is subject to tax, and that derived from a source outside Hong Kong by a local resident is in most cases not taxed in Hong Kong. Therefore, Hong Kong residents generally do not suffer from double taxation. Many countries which tax on a worldwide basis also provide their residents who operate a business in Hong Kong with unilateral tax credit relief. Hong Kong allows a deduction for foreign tax paid on a turnover basis in respect of an income which is also subject to tax in Hong Kong. Businesses operating in Hong Kong therefore do not generally have problems with double taxation of income.

Notwithstanding this, the Hong Kong Special Administrative Region Government (HKSARG) recognizes that there are merits in concluding comprehensive double taxation agreements (DTAs) with their trading partners. A DTA provides certainty to investors on the taxing rights of the contracting parties; helps investors to better assess their potential tax liabilities on economic activities; and provides an added incentive for overseas companies to do business in Hong Kong, and likewise for Hong Kong companies doing business overseas. Up to now, Hong Kong has signed 32 comprehensive DTAs with other countries. In addition, Hong Kong is in the process of negotiating 13 comprehensive DTAs with other countries such as Germany, India and Russia.

Hong Kong's onshore-offshore tax regime often results in a reduced tax burden for those that operate through Hong Kong companies by pricing intra-group transactions. This has led to heightened transfer pricing scrutiny from the Hong Kong Inland Revenue Department in recent years. Consequently, the Advance Pricing Arrangement (APA) program¹ was introduced to Hong Kong in 2012, which was widely regarded as a welcome development for multinational companies, as it offers a non-adversarial approach in which taxpayers can engage with tax authorities in a transparent manner to achieve an optimal tax outcome. Importantly, Hong Kong can only start an APA program with another country after having signed a DTA with that country.

¹ An APA is an agreement that determines an appropriate set of criteria (e.g. transfer pricing method, external data, appropriate adjustments, critical assumptions as to future events) to determine the pricing of related party transactions over a fixed period of time. This is either three or five years.

RELATED READING



Tax, Accounting, And Audit in China 2016 (8th Edition)
February 2016

- See more [here](#)

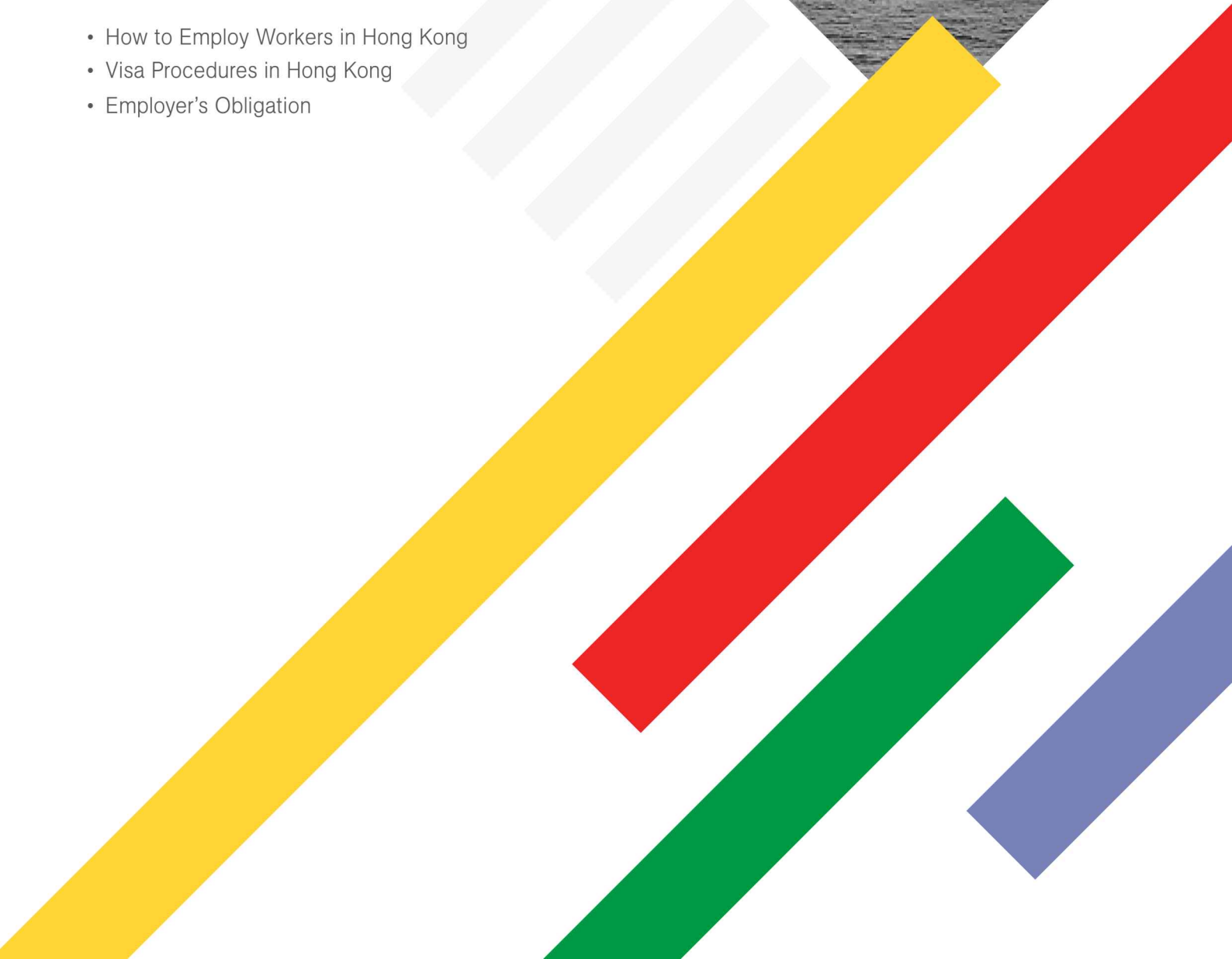


FOR MORE INFORMATION
Tax, Accounting, and
Audit in China

3

HUMAN RESOURCES AND PAYROLL

- How to Employ Workers in Hong Kong
- Visa Procedures in Hong Kong
- Employer's Obligation



HOW TO EMPLOY WORKERS IN HONG KONG



FEDERICO PAOLUCCI
Associate
International Business
Advisory

Registering Employees for Salaries Tax

Unlike most countries, individual income tax, or Salaries Tax as it is known in Hong Kong, is not withheld by the employer. Instead, individuals need to pay their tax themselves.

As such, there are only two administrative requirements applicable to employers in Hong Kong.

Employer's Return

On April 1 every year, the Internal Revenue Department (IRD) will issue a document called the Employer's Return to companies. Companies need to fill in and file these returns for:

- Unmarried individuals that are paid an annual income of HK\$120,000 or more
- Married individuals
- Part-time staff
- Directors
- Individuals that are to receive a pension of HK\$120,000 or more

Employees are defined as:

- Persons employed by a Hong Kong company, including:
 - » Part time and full time staff
 - » Hong Kong and non-Hong Kong residents
 - » Persons who provide services for the company in or outside Hong Kong
- Employees assigned or seconded to a Hong Kong company by its overseas holding company

New Hires

When the company hires a new employee, it needs to inform the IRD within 3 months.

Employers need to keep records of the following information concerning their employees:

- Personal details
- Full or part-time
- Position
- Amount of cash remuneration, non-cash remuneration and other fringe benefits
- Contributions to the Mandatory Provident Fund
- Amendments to the contract
- Length of employment

The IRD needs to be informed of:

- Changes in the employee's particulars (change of residential address, marital status etc.)
- Changes in the terms of employment
- The identity document number of the employee

“ Individual income tax, or Salaries Tax as it is known in Hong Kong, is not withheld by the employer. Instead, individuals need to pay their tax themselves.”

VISA PROCEDURES IN HONG KONG

Visitor's Visa

Citizens of most developed countries may stay in Hong Kong for 90 days without a visa; British nationals may stay for 180 days.

Employment Visa

The type of visa that is most applicable to foreign investors is the Employment Visa under the General Employment Policy. Other work visas are for entrepreneurs and semi-skilled workers, like technicians. Applicants for the Employment visa must possess skills, knowledge or experience that are not readily available in Hong Kong. Note that different rules apply for Mainland Chinese. The requirements are:

- The applicant has no record of a serious crime, nor poses a security risk.
- Good background, such as a degree in a relevant field, or technical qualifications, proven professional abilities or experience, backed by documentary evidence.
- The applicant has a confirmed job offer.
- Remuneration is broadly in line with market levels.

Apart from the application form, the employee needs to submit the following documents:

- Passport
- Copy of academic qualifications and relevant work experience
- Recent photo

The employer needs to submit:

- The company's employment contract or letter of appointment to the applicant containing information about post, salary, other fringe benefits and employment periods
- Photocopy of the Business Registration Certificate
- Photocopy of proof of financial standing, such as an audited financial report
- Documents with details of company background such as business activities
- Detailed business plan

These documents need to be collected and delivered to the Immigration Department in Hong Kong. Foreigners residing in Mainland China at the time of application need to submit these documents to the Immigration Division of the Hong Kong Government in Beijing. The processing of the work visa application takes about 2-3 months.

If the visa application is granted, a permit label will be issued to the applicant, who has to affix it onto their passport. At this point, the fees need to be paid as well. With the label affixed onto the passport, the applicant can enter Hong Kong.



FOLLOW US ON TWITTER
@DezanShira

EMPLOYER'S OBLIGATION

Social Security

Pension

Employers and employees must contribute 5 percent of the employee's salary to a retirement scheme that is registered with the Mandatory Provident Fund. For both parties, the amount is capped at HK\$18,000. The first HK\$12,000 per year is tax deductible. Please note that the figures may vary from year to year according to the government policy.

Employee compensation

By law, employers are required to take insurance to compensate employees for work related incidents or deaths. For companies with less than 200 employees, the minimum coverage is HK\$100 million per event. Companies with over 200 employees need a minimum coverage of HK\$200 million per event.

Leave

All employees are entitled to leave on statutory holidays, irrespective of length of services. Hong Kong's statutory holidays are as follows:

- New Year's (January 1)
- First three days of Lunar New Year (late January or early February)
- Ching Ming Festival (April 4, 5 or 6)
- Labor Day (May 1)
- Dragon Boat Festival (in June)
- Establishment of the Hong Kong SAR (July 1)
- The day following Chinese Mid-autumn Festival (in September)
- Chung Yeung Festival (in October)
- Chinese National Day (October 1)
- Chinese Winter Solstice Festival (21 or 22 December) or Christmas (at the option of the employer)

Annual Leave

Employees are entitled by law to a maximum of 14 days paid annual leave, depending on their years of service with the company. The amount of annual days leave owed an employee is as follows:

YEARS OF SERVICE	1	2	3	4	5	6	7	8	9 or more
DAYS LEAVE	7	7	8	9	10	11	12	13	14

Sick Leave

Employees may only take paid sick leave if they have accumulated enough paid sickness days. Paid sickness days are accumulated at the rate of two paid sickness days for each completed month of the employee's employment during the first 12 months, and four paid sickness days for each completed month of employment thereafter. Paid sickness days can be accumulated throughout the whole employment period.

The employee is not entitled to sickness allowance if:

- The employee refuses treatment without reasonable excuse
- The sickness day falls on a statutory holiday
- Compensation is payable by law (Employees' Compensation Ordinance)

During sickness leave, the employee's wage is reduced to 4/5 of the daily average wage as earned in the past 12 months.

Maternity Leave

An employee who becomes pregnant must notify her employer. She is then entitled to:

- A continuous period of ten weeks' maternity leave
- If child birth occurs later than expected, added leave until the child is born
- An additional leave of maximum four weeks for illness or disability due to the childbirth

The employee may decide to take leave two to four weeks prior to the expected date of childbirth, with the agreement of the employer. In absence of such a decision, leave starts four weeks prior to birth. If childbirth occurs earlier than expected, that day is the starting day of the maternity leave. The employee is eligible for maternity leave pay if she has been working at least 40 weeks before the commencement of the maternity leave, and has given notice and produced a medical certificate with the expected date of birth. Maternity leave pay is set at 4/5 of the employee's regular pay over the past 12 months.



For assistance with automating
your Hong Kong HR processes
or advice on drafting labor contracts,
please contact us
at hr.admin@dezshira.com

TERMINATING AN EMPLOYEE

Types of Termination

An employment contract in Hong Kong can be terminated in two ways: termination by notice, or immediate termination.

Immediate Termination

The employer may terminate the contract without notice in case of:

- Willful disobedience of a lawful and reasonable order
- Misconduct
- Fraud or dishonesty
- Habitual neglect of duties

The employee may terminate the contract without notice for:

- Reasonable fear of physical danger by violence or disease
- Ill-treatment by the employer
- Becoming permanently unfit for the type of work engaged in, as judged by a medical practitioner

Termination with Notice

An employment contract may be terminated by either side by giving the other party notice, or paying one month's wages instead of notice. The default time within which to give notice is one month. Parties may contractually agree upon shorter notice, but no less than seven days.

During the first month of a probation period – if one is agreed upon – no notice is required.

The one month's pay is calculated by taking the employee's daily salary as earned over the past 12 months, and multiplying this by the number of days the wages would actually have been payable.

Termination Prohibited

In five cases, an employee cannot be terminated:

- An employee who is confirmed to be pregnant and has submitted a pregnancy notice
- An employee on paid sick leave
- For reasons of giving evidence or information related to court proceedings, or an inquiry related to the enforcement of employment laws
- For trade union membership or activities
- An employee injured at work, without having first come to an agreement on compensation

Severance Payment

When an employee is dismissed, the employer needs to pay:

- Outstanding wages
- Wages in lieu of notice, if applicable
- Payment in lieu of untaken leave
- Severance pay

Employees who have worked for over 24 months with a company are entitled to severance pay. It is payable if the employee is dismissed by reason of redundancy, the contract is not renewed by reason of redundancy, or the employee is otherwise laid off.

Here, redundancy means that the employer either decided to close the business, the employer ceases to do business in that area, or the type of work the employee is involved in is expected to diminish or cease.

Lay off is a specific term that applies when the employee is hired under terms where remuneration depends on specific tasks that the employer provides. If during half of the total number of working days in any consecutive four weeks, no work has been provided, this is a lay off. It is also a lay off if, in one third of any 26 consecutive weeks, no work has been provided.

Long Service Payment

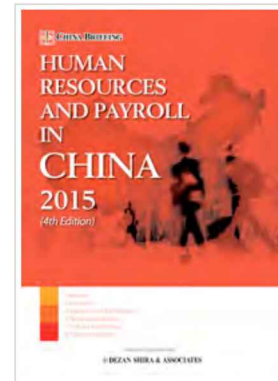
If the length of service has been five years or more, the employee may also receive payment if:

- Terminated for reasons other than serious misconduct
- Terminated for reasons other than redundancy

The employee may take long service payment if:

- The contract expires and is not renewed
- The employee dies (money goes to spouse, children or parents)
- The employee resigns for health reasons
- The employee is aged above 65 and is retiring

RELATED READING



Human Resources and Payroll in China 2015(4th Edition)
March, 2015

- See more [here](#)

4

INDUSTRY FOCUS

- Retail Sector
- Office Sector
- Logistics Sector





RETAIL SECTOR

The ongoing change in the Hong Kong retail landscape is structural rather than temporary, unlike previous downturns during SARS in 2003 and the Global Financial Crisis of 2008. The ongoing anti-corruption campaign and economic slowdown in China are influencing Chinese tourists' consumption patterns and inhibiting their demand for high-value goods. This is likely to remain the case for the foreseeable future.

A substantial improvement in demand is not expected in 2016 as a number of additional headwinds could emerge. The U.S. Federal Reserve raised interest rates in December 2015, but any further increases are expected to be progressive and measured. However, this will eventually place a greater financial burden on households and may ultimately reduce their spending power. The USD will also likely appreciate further as demand for the currency rises along with higher interest rates. As a result, the HKD will likely follow suit, meaning that tourists will find shopping in Hong Kong even more expensive.

Sales of discretionary products are coming under pressure while retailers selling basic necessities near the border will see competition from the new shopping mall in Qianhai dedicated to selling Hong Kong-based goods. The mall, called CTFHOKO, will be operated by Chow Tai Fook and prices there are reported to be more expensive than those in Hong Kong. With more brand and product varieties in Hong Kong and malls like this are not extremely competitive in pricing, any impact on Hong Kong's retail market is set to be minimal.

However, new tourist attractions in Hong Kong will remain limited. Shanghai Disneyland will open in 2016, further intensifying competition between the two cities. This could further impact tourist arrivals in Hong Kong. However, with terrorist attacks and natural disasters occurring more frequently elsewhere in the world, Hong Kong is still considered to be a safe place to visit.

In September 2015 CBRE Research published *The Changing Retail Landscape: How to Survive the Slowdown in Hong Kong?* This special report explained how shifting tourist spending patterns are impacting the local retail market. Hong Kong's transformation from a luxury goods oriented retail market to a mid-range market, as discussed in the report, will continue in 2016. Mid-market retailers will benefit from the change in spending patterns and remain the main driver for retail



space. Some of them will use this window of opportunity to re-establish themselves in prime locations and/or expand their store networks. Whilst Hong Kong will remain a key market for luxury goods retailers and no groups are expected to exit the market completely, the trend of consolidation will continue. However, they will remain focused on prime shops along tier I streets in core districts for opportunities to consolidate or upgrade, although they will not bid as aggressively for such locations as they did in previous years.

The number of surrender leases could increase towards the end of Q1 2016 following the end of the festival period. As such, rents may face higher pressure as early as late Q1 2016. The rental down-cycle could persist for the next two years as downward adjustments gradually occur upon lease expiry. Street shops will bear the brunt of lower rents while shopping malls will fare comparatively better due to their more balanced trade mix. Street shop landlords are expected to become more willing to accept rents lower than the previous lease term, in order to guard against vacancy and secure rental income. Retailers will prioritize securing space along tier I streets, resulting in higher rental pressure on lower-tier streets.

Most available space in Causeway Bay has now been absorbed and any drop in rents in 2016 will be milder than that which was recorded in 2015. However, many leases in other core areas such as Tsim Sha Tsui are scheduled to expire in 2016, meaning that the pace of rental decline will be more rapid in those districts. Overall, given the lower base of comparison, CBRE Research forecasts that rents will decline by between 10-15 percent in 2016.



OFFICE SECTOR


The office market was the best performing commercial property sector in 2015 and is expected to remain the bright spot in the coming year. Net take-up in 2015 amounted to three times the combined total of 2013 and 2014, thanks largely to strong demand from the banking, finance and insurance sectors.

Following the implementation of the Shanghai-Hong Kong Stock Connect and announcement of the mutual fund recognition scheme in 2015, Mainland Chinese firms emerged as the major driver of demand, particularly in the CBD. This drove down vacancy rates across the SAR, particularly in Central, where vacancy fell from 4.0 percent at the end of 2014 to just 1.2 percent at the end of 2015. As of Q4 2015, citywide average rents had rebounded to levels before the Global Financial Crisis in 2008.

The expected launch of the Shenzhen-Hong Kong Stock Connect in 2016 will continue to support the growth of the Hong Kong financial sector. As a result, leasing activity in Central is expected to remain robust, with companies from Mainland China once again comprising a major source of leasing demand.

Some financial sector entrants from Mainland China may continue to display a strong preference for space in prestigious buildings and will remain willing to pay premium rents. However, landlords may exercise more due diligence on potential tenants who have not yet established a strong reputation in their industry. In contrast, established companies in Hong Kong could adopt a different approach by seeking space in cost effective buildings as they look to keep real estate expenses down.

The insurance sector will also likely remain a key demand driver as the asset management industry expands. Insurance companies are seeking space both in the CBD and elsewhere around the city. The lack of available space, both in the primary and secondary market, will remain the main challenge for occupiers. There are only two small office buildings scheduled for completion in Central in 2016, one of which has a proportion of space reserved for self-use by its developer. Multinational corporations will generally remain cautious and cost sensitive, both inside and outside the CBD, and will continue to be on the lookout for consolidation or decentralization opportunities. However, finding cost effective space will remain a challenge. CBRE therefore



expects to see more pre-leasing activity for both new and secondary space from companies seeking large contiguous spaces.

The impact of the weaker retail market on office demand may not be substantial as many retailers' offices in Hong Kong also house purchasing and management functions for the wider region.

The forthcoming demolition of Warwick House in Hong Kong East will continue to generate relocation demand. Tenants forced to leave the building will either stay in Hong Kong East or may choose to relocate across the harbor to Kowloon East due to the comparatively greater availability of cost effective space.

A total of 14 million sq. ft. (NFA) of Grade A office space is due for completion in 2016, with only one scheme in Kowloon East larger than 500,000 sq. ft. (NFA). Vacancy is expected to remain extremely low across the major submarkets and 2016 is set to remain a landlords' market. Rents will continue to rise over the course of the year but will reach the peak of the current market upcycle by the year-end, when pre-leasing for new projects due for completion in 2017 will intensify.

Rental growth in 2016 should decelerate from 2015 due to the higher base of comparison and economic uncertainty that is set to endure for much of the year. Rents in Central will continue to outperform, with growth projected at 5-10 percent for 2016, following an increase of 14 percent in 2015. Other submarkets are expected to see rents climb by up to 5.0 percent in 2016.

LOGISTICS SECTOR


The global trade slowdown dampened sentiment in the logistics market over the course of 2015. Internal and external demand will not improve in short-term. The Trans-Pacific Partnership (TPP) and recent Free Trade Agreements among countries in the region will have a negative long-term impact on Hong Kong's status as a global logistics hub. Currently, nearly 5.0 percent of Hong Kong's re-exports in terms of value are trades between China and South Korea through Hong Kong. China is expected to launch more trade policies and reduce tariffs with other trading partners. These will threaten Hong Kong's external trade as China is its largest trading partner, accounting for half of total merchandise trade.

The slow economy along with sluggish trade and retail sales growth will result in subdued leasing demand for warehouse space in 2016. Demand from 3PL operators will remain soft and is unlikely to reverse until global trade improves, which is not expected to occur in 2016. This will exert a stronger impact on demand for direct ramp access space, rather than those facilities with cargo lift access, as such space is generally preferred by 3PL operators. CBRE Research expects warehouse space with cargo lift access to outperform those facilities with direct-ramp access. This will offset the potential correction in rents in the latter.

Over the course of 2015, leasing demand shifted from 3PL operators to mid-range retailers, a trend that will likely continue this year in spite of the weaker retail market. Mid-range retailers, which continue to display relatively solid leasing demand for retail space, will continue to upgrade and expand their logistics operations in 2016.

Mapletree Logistics Hub in Tsing Yi is expected to be ready for occupation in early 2016 and will supply the market with 1.6 million sq. ft. of direct access stock. Around 40 percent is pre-committed to logistics operations including grocery e-retailer RedMart from Singapore. Elsewhere, China Merchants' logistics project in Tsing Yi is expected to be finished in 2017, with pre-leasing activity scheduled to begin this year. This new supply, coupled with weaker demand for this type of product due to the slower economy, will continue to put downward pressure on rents for direct access property in 2016.

Landlords remained active in submitting planning applications under the industrial revitalization



scheme, which ends in March 2016. The approved buildings will likely be removed from industrial stock in 2016 or even 2017 depending on their tenants' lease expiries. Vacancy in flatted factories and I/O buildings is expected to remain low as more stock will be taken off the market. However, I/O rental growth will be curbed by the incoming office supply boom from revitalized industrial properties and new office premises, especially in Kowloon East.

Data centers remain a bright spot in the market as more landlords and occupiers upgrade warehouses from storing physical goods to storing data. Examples of this trend include Cargo Consolidation Complex, which has seen most floors converted for data center use by the tenant PCCW Solutions. The building was sold in December 2015 to a fund for a figure close to HK\$14 billion after a very competitive bidding process. Sun Hung Kai Logistics Centre in Sha Tin will complete its conversion to a data center in 2016. Equinix are continuing to expand within the buildings they occupy in Tsuen Wan.

The e-commerce wave in Asia is stimulating warehouse demand around the region and Hong Kong is benefitting for both domestic consumption and as a facilitator for cross-border goods movements. International e-commerce operators have already expanded operations to Hong Kong while some local operators have invested in technology to specifically cater to the e-commerce industry, which is focused on high volumes of small and irregular orders.

Even with some new supply, warehouse vacancy will remain tight and hence warehouse rents will remain fairly flat in 2016 despite subdued demand. This trend is likely to continue until 2017 but may pick up sooner depending on the external trade environment.



DEZAN SHIRA & ASSOCIATES

Your Partner for Growth in Asia

CONTACT

HONG KONG

- +852 2376 0334
hongkong@dezshira.com

CHINA

- Beijing: +86 10 6566 0088
beijing@dezshira.com
- Dalian: +86 411 3957 3311
dalian@dezshira.com
- Qingdao: +86 532 6677 5461
qingdao@dezshira.com
- Tianjin: +86 22 5830 7666
tianjin@dezshira.com
- Shanghai: +86 21 6358 8686
shanghai@dezshira.com
- Hangzhou: +86 571 5685 9956
hangzhou@dezshira.com
- Ningbo: +86 574 8733 8682
ningbo@dezshira.com
- Suzhou: +86 512 8686 8717
suzhou@dezshira.com
- Guangzhou: +86 20 3825 1725
guangzhou@dezshira.com
- Shenzhen: +86 755 8366 4120
shenzhen@dezshira.com
- Dongguan: +86 769 3381 8020
dongguan@dezshira.com
- Zhongshan: +86 760 8826 9592
zhongshan@dezshira.com

INDIA

- Delhi: +91 12 4401 1219
delhi@dezshira.com
- Mumbai: +91 22 6700 4843
mumbai@dezshira.com

SINGAPORE

- +65 6521 2933
singapore@dezshira.com

VIETNAM

- Ho Chi Minh City: +84 8 6299 8294
hcmc@dezshira.com
- Hanoi: +84 4 3942 0443
hanoi@dezshira.com

DEZAN SHIRA & ASSOCIATES ASIAN ALLIANCE

Indonesia: Winnindo Business Consult

- +62 21 3193 7020
indonesia@dezshira.com

Malaysia: Christopher Heng & Peng Sam

- +603 6257 1130
malaysia@dezshira.com

The Philippines: Machica Group

- +63 2 562 8190
philippines@dezshira.com

Thailand: Honor Audit & Advisory Co.

- +662 684 1299
thailand@dezshira.com

DEZAN SHIRA & ASSOCIATES LIAISON OFFICES

Germany Liaison Offices

- Stuttgart: +49 (0) 711 34 18 02 - 0
- Cologne: +49 (0) 221 940 21 00
germandesk@dezshira.com

Italy Liaison Office

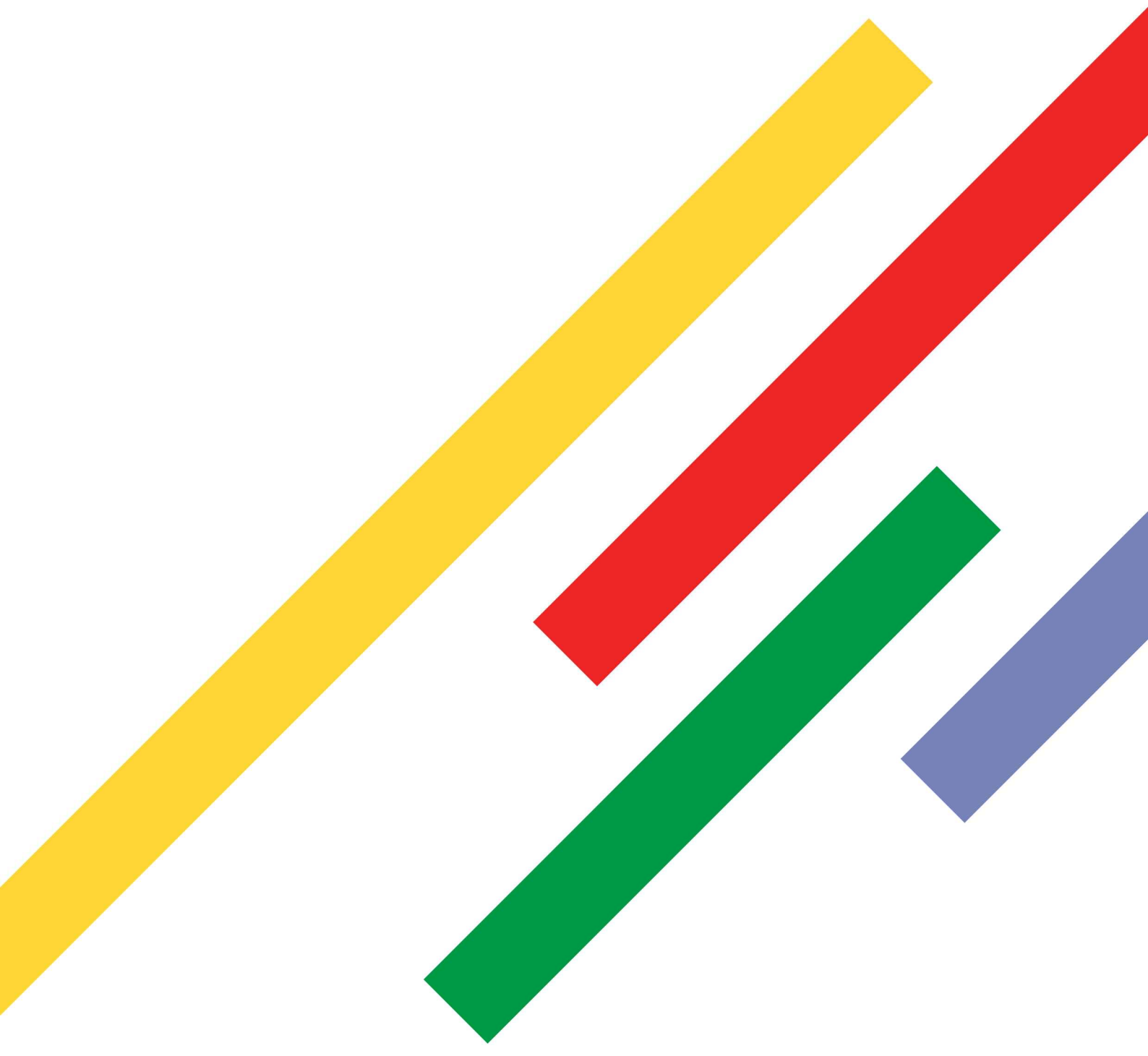
- Treviso: +39 0422 264026
italiandesk@dezshira.com

United States Liaison Office

- Boston: +1 617 236 8098
usa@dezshira.com

Disclaimer

The contents of this guide are for general information only. For advice on your specific business, please contact a qualified professional advisor. Copyright 2015, Asia Briefing Ltd. No reproduction, copying or translation of materials without prior permission of the publisher.



CORPORATE ESTABLISHMENT · DUE DILIGENCE · BUSINESS ADVISORY · TAX · ACCOUNTING · PAYROLL · AUDIT · COMPLIANCE

 hongkong@dezshira.com

 www.dezshira.com