Doing Business in Hong Kong

This document describes some of the key commercial and taxation factors that are relevant on setting up a business in Hong Kong.

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Background

Country overview

Hong Kong is located on the Southeast coast of China with a land area of about 1,100 square kilometres, comprising of Hong Kong Island, Kowloon Peninsula, the New Territories and the outlying islands. Hong Kong has a population of more than 7 million and three official languages which are English, Cantonese and Putonghua. Cantonese is the mother tongue in Hong Kong.

The People's Republic of China ("PRC") resumed its sovereignty over Hong Kong when the Hong Kong Special Administrative Region ("HKSAR") of the PRC was established on July 1, 1997. The head of HKSAR is the Chief Executive who is elected for a five-year term, with approval of the PRC.

The Basic Law, which was adopted on April 4, 1990, forms the written constitution of Hong Kong.

A number of business chambers in Hong Kong provide assistance on business opportunities and networking facilities, including:

- Australian Chambers of Commerce;
- American Chambers of Commerce; and
- British Chambers of Commerce.

There is no central bank in Hong Kong.

HSBC, Standard Chartered Bank and Bank of China are the only three note issuing banks in Hong Kong.

The financial and securities sectors are regulated by:

- The Hong Kong Monetary Authority;
- The Securities and Futures Commission; and
- The Stock Exchange of Hong Kong Limited.

Economic overview

Hong Kong operates under a "laissez-faire" economic system with minimal Government interference in all sectors of the economy, and there are no exchange controls. Hong Kong maintains its own monetary system and the Hong Kong dollar is pegged to the US dollar at the rate of 1US$ = 7.78 HKD.

The HKSAR Government welcomes foreign investment and there is no restriction on foreign ownership.

Key characteristics of Hong Kong's commercial environments are:

- a high degree of internationalization
- open and fair competition
- free flow of information
- well established financial networks
- good transport and communications infrastructure
- well educated workforce

- simple tax structure and low tax rates
- no tariffs adversely affecting international trade.

Hong Kong is a founding member of the World Trade Organisation (WTO) and is a strong supporter of the Anti-Dumping Code.

Since China's accession to the WTO and the signing of the free trade agreement between mainland China and Hong Kong, [i.e. the Closer Economic Partnership Agreement (CEPA)], Hong Kong has been well positioned to play an important role to companies wishing to expand businesses into mainland China.

In Hong Kong, commercial and industrial rights are protected through patents and trademark laws as well as consumer protection controls. However, there is little associated trade practices legislation.

Transport infrastructure

As a hub of finance and transport communications, Hong Kong plays an important role for business in the Asia Pacific region and acts as the gateway to mainland China.

Hong Kong has a well-developed road and railway transport infrastructure. Most of the Hong Kong people take their journeys on a public transport system which includes railways, trams, buses, minibuses, taxis and ferries. MTR Corporation Limited ("MTR") operates Hong Kong's railways including the Airport Express to the Hong Kong International Airport. The MTR's railway network covers most of the areas in Hong Kong Island, Kowloon and the New Territories, and is the backbone of Hong Kong's public transport system.

Choice of Legal Form

1. The most common types of business entities in Hong Kong are:

- a limited company
- partnership
- sole proprietorship
- Branch / Representative office

A limited company in Hong Kong requires at least one natural person appointed as director and a local company or person as company secretary.

2. Relevant legislation affecting business entities in Hong Kong include:

- The Companies Ordinance
- The Inland Revenue Ordinance
- The Business Registration Ordinance

Audit Requirements

All Hong Kong incorporated companies are statutorily required by the Companies Ordinance to have their financial statements audited annually in accordance with the Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants (HKICPA).

Financial statements for corporate entities need to comply with the disclosure requirements as set out in the Companies Ordinance, the Hong Kong Financial Reporting Standards (HKFRS) / Hong Kong Financial Reporting Standard for Private Entities (HKFRS-PE), Small and Medium-sized Entity Financial Reporting Standard (SME-FRS) issued by the HKICPA, and and the Rules of The Stock Exchange of Hong Kong Limited in the case of listed companies.

The HKFRS and HKFRS-PE are, in all material respects, converged with International Financial Reporting Standards and International Financial Reporting Standards for small and medium-sized entities respectively, whereas SME-FRS is a 'local' accounting standard applicable to entities which are entitled to take advantage of the reporting exemption as set out in the Companies Ordinance.

The financial statements of private companies are not published or required to be filed on public record in Hong Kong.

Under the Hong Kong Companies Ordinance, every company shall keep proper accounting records regarding:

a) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place;

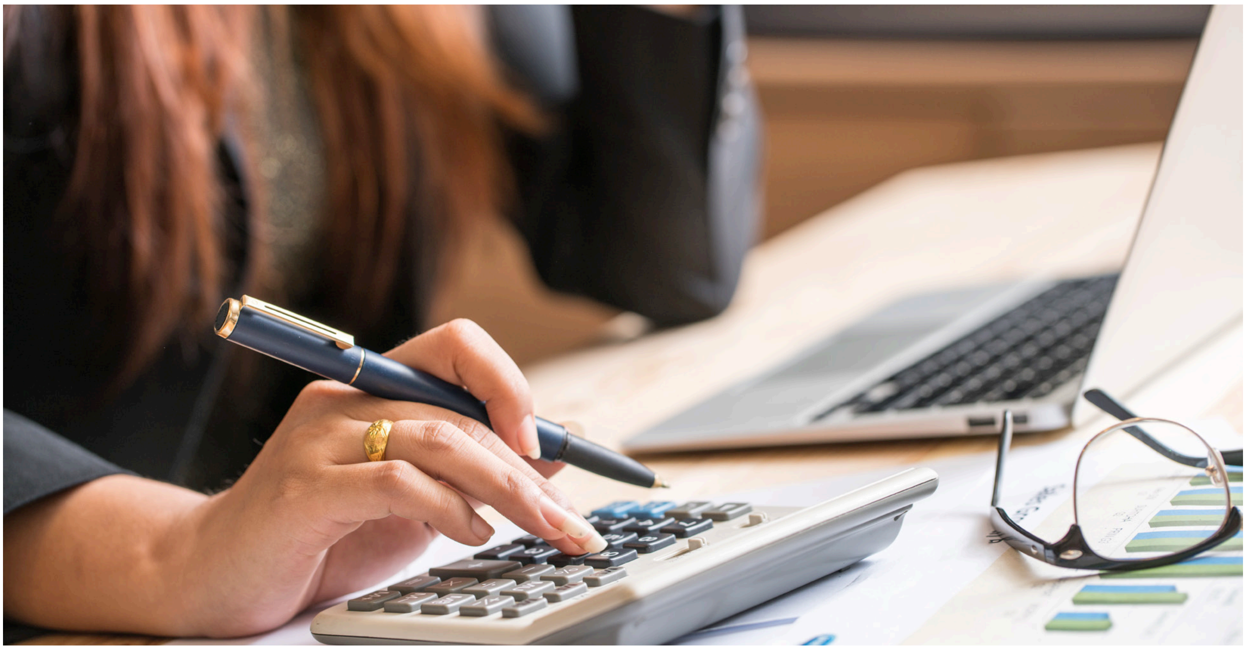
b) all sales/service income and direct operating costs of the company; and

c) the assets and liabilities of the company.

The accounting records are to be kept for seven years from the end of the financial year in which the last entry was made, or to which the last recorded matter relates.

Business entities are also required under the Hong Kong Inland Revenue Ordinance to maintain sufficient records of their income and expenditure to enable the assessable profits (if any) to be readily ascertained. Even if the business operations are conducted offshore, the relevant supporting invoices and receipts, together with other relevant records, are still required to be kept.

Taxation



The Inland Revenue Ordinance (IRO) imposes three separate types of direct taxes on company profits and income of partnerships and individuals. The three direct taxes levied are:

a) Profits tax;

b) Salaries tax; and

c) Property tax

Based on the territorial concept, a liability to tax will arise only when the income has a source in Hong Kong. Income which arises or is derived from outside Hong Kong will not be assessed for tax by the Hong Kong Inland Revenue Department. Under normal circumstances, the claim for exemption from Hong Kong tax needs to be lodged with, and agreed by, the Hong Kong Inland Revenue Department.

Provisional tax is payable for all three taxes and is usually based on the assessable income of the previous year.

Profits tax

Individuals and entities carrying on a trade, profession or business in Hong Kong are subject to profits tax if the source of profits arises in or is derived from Hong Kong from the carrying on of that trade, profession or business.

Whether a taxpayer is carrying on a trade, profession or business in Hong Kong is largely a matter of fact and will depend upon the circumstances of each case.

In broad terms, a trade, profession or business is being carried on or performed in Hong Kong if:

a) its central management is located in Hong Kong;

b) its continuous commercial activities are in Hong Kong; or

c) its activities are conducted through an agent in Hong Kong where the agent has a general authority to negotiate and conclude contracts.

Dividend and bank interest income as well as capital gains are non-taxable in Hong Kong.

Profit tax losses can be carried forward indefinitely subject to the anti-avoidance rule on change of ownership. There is no group loss relief available.

Anti-avoidance legislation is also in place aiming at transfer pricing arrangements between overseas and Hong Kong entities who are closely connected.

Hong Kong has signed double tax treaties or double tax agreements with a number of countries including, inter alia, Belgium, Thailand, Vietnam, Indonesia, the Netherlands, Luxembourg, Japan, France, United Kingdom, Austria, Canada, Italy, Korea, South Africa and mainland China.

Most agreements concluded so far cover airline and shipping income although certain bilateral agreements provide relief from double tax on other types of income. Double tax agreements also seek to clarify on the rules for division of revenue between Hong Kong and the contracting countries.

In addition, Hong Kong has agreed to implement the OECD tax model of Common Reporting Standard with effect from 2018.

Profits tax rates in Hong Kong for the year of assessment 2017/18 are:

Incorporated businesses	- 16.5%
Unincorporated businesses	- 15%

Salaries tax

Salaries tax is charged on every person in respect of his income arising in or derived from Hong Kong from any office, employment or pension. In order for the income to give rise to salaries tax, the duties must be rendered in Hong Kong and the number of days spent in Hong Kong by the individual should be over 60 days per year.

Income is deemed to include all wages, salary, leave pay, perquisites, bonuses and allowances. A common type of taxable benefits-in-kind is in respect of rent free accommodation provided to the employees by the employers (or associated entities). In general, the taxable amount of rent free accommodation is calculated at 10% of the assessable income derived from the employment.

Salaries tax is payable at:

a) the standard rate (15% for 2017/18) on the chargeable income; and

b) the sliding rates (between 2% and 17% for 2017/18) on the chargeable income after personal allowances.

Property tax

Property tax is charged on rental income derived by persons owning buildings or land in Hong Kong.

However, rental income received by corporations is assessed as profits tax, instead of property tax, by bringing the rental income into charge for profits tax purpose.

The rate of property tax is 15% on the chargeable income for the year of assessment 2017/18. Property in Hong Kong is also subject to rates based on an assessed rateable value for each property.

Other taxes

Currently there are none of the following taxes in Hong Kong:

Wealth tax / Gift tax / VAT / Capital gains tax / Dividend income / Interest income / Turnover

Allowances

Depreciation

Depreciation allowances for tax deduction purpose are available for qualifying capital expenditure on plant and machinery, and industrial and commercial buildings.

The depreciation rates in Hong Kong are:

- 4% for commercial building
- 20% initial and then 4% for industrial buildings
- 60% initial and then 10%-30% on written down value for plant and machinery furniture and equipment etc.
- 100% for prescribed fixed assets

Employment

Generally speaking, the employment climate in Hong Kong is very stable. The highly educated, skilled and dedicated workforce has been very appealing to foreign investors.

The government is endeavouring to promote harmonious labour relations and safeguard employees' rights and benefits through implementation of appropriate labour policy and labour legislation.

The Employment Ordinance is the main legislation prescribing the minimum rights, benefits and protection for employers and employees in Hong Kong.

The Minimum Wage Ordinance protects the rights of the employees employed in Hong Kong. The current statutory minimum wage rate is HK$34.50 per hour.

Under the Mandatory Provident Fund Schemes Ordinance, each of the employers and the employees is required to make monthly contributions to the scheme at 5% of the employee's earnings (subject to a cap of HK$1,500), contributions over and above which are voluntary.

Employment conditions are usually provided for in the contracts of service entered into between employers and employees, but for certain industries, there are collective agreements entered into between employers and the trade unions representing these employees.

Any person wishing to enter Hong Kong for employment, investment, education, training or residence must obtain the appropriate entry visas before coming to Hong Kong unless that person is the holder of a Hong Kong Permanent Identity Card or has the right of abode or unconditional stay in Hong Kong. Significant penalties will be imposed if the employer is found guilty of employing persons without proper visa requirements.

Dependents (including spouses and children) who accompany individuals taking up employment in Hong Kong must apply for dependent visas. Certain nationalities are granted visa free access to Hong Kong but only up to a stipulated period of time.

No compulsory medical insurance is required in Hong Kong.

Payroll tax is covered by the Salaries Tax mentioned above and is to be paid by the employee directly, who should submit the Individual Income Tax Return each year.

Withholding Taxes

Royalties

Royalties are taxable in Hong Kong if they are related to the use, or right to use, in Hong Kong of any patent, design, trade mark, copy right material or other property of a similar nature.

The assessable profit is deemed to be 30% of the sum paid to the non-resident who is not connected with the payer and 100% if connected. The withholding tax is computed at 16.5% of the deemed assessable profits. The tax (4.95% for third party or 16.5% for connected party) is to be withheld by the payer for payment on behalf of the non-resident (as its agent in Hong Kong) to the Inland Revenue Department in Hong Kong.

There are no withholding taxes on interest and dividends which are not taxable in Hong Kong.

Miscellaneous

1. Estate Duty
   – Abolished in February 2006

2. Stamp Duty

Stamp duty is chargeable under the Stamp Duty Ordinance on documents effecting the transfer of shares and securities registered in Hong Kong and the transfer or lease of land and buildings situated in Hong Kong.

Buyer's Stamp Duty on the acquisition and Special Stamp Duty on disposal of residential properties on top of ad valorem stamp duty is chargeable on the individual or company which acquires a residential property on or after October 27, 2012 and resells it within 36 months.

The maximum rates of stamp duty for 2017/18 are:

Conveyances of immovable property	8.5% of consideration over HK$21,739,120
Lease of more than 3 years	1% of annual rent
Transfer of shares or securities	0.2% of the consideration paid or of the market value (whichever is higher)
Special Stamp Duty on reselling residential properties	10% - 20%
Buyer's Stamp Duty on the acquisition of residential properties	15%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This document is provided by AMA CPA Limited as a general overview of matters to be considered when setting up an overseas business in Hong Kong. It is essential to take advice on specific issues. No liability can be accepted for any action taken or not taken arising from the information provided in this publication.

If you are setting up a business in Hong Kong, the members of DFK International can help you to achieve this efficiently. You will receive practical advice on business issues, tailored to meet your objectives, from experienced business advisers.

For further information on the services available from the DFK member firms in Hong Kong please contact:

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