

# How Good Hong Kong Is In Business and Tax Planning ?

Celia Hui [September 2008]

There is a growing trend that many overseas clients request our associate, Hongkong Managers & Secretaries Limited (“HKM”), to assist them in setting up corporations in Hong Kong (“HKCo”) to conduct the so-called “re invoicing business”. The rationale behind is driven by commercial motives. Overseas investors prefer Hong Kong to other locations is largely connected with her strategic location of being a stepping-stone to the mainland China market and the well-developed infrastructure including free repatriation of profits, free exchange control, excellent banking, transportation and telecommunication systems.



## 1. Tax-Exempt Business Operation

If the following conditions are fulfilled, HKCo can also get tax exemption agreement from the Hong Kong Inland Revenue Department (“IRD”) on its profits generated from the re invoicing business.

- a. HKCo does not establish any office nor employ any staff in Hong Kong. It simply appoints a professional service company (e.g. HKM) to provide the secretarial services in order to comply with the minimum statutory requirements of the Hong Kong Companies Ordinance.
- b. HKCo's related company or associate at overseas (“Overseas Associate”) is fully responsible for marketing, sourcing of goods, negotiation and conclusion of business contracts.
- c. When Overseas Associate negotiates and finalizes the terms of sales with overseas customers, it notifies the overseas suppliers to deliver the goods directly to the customers. Then, it instructs the HKM to:
  - ♦ make payments to the suppliers;
  - ♦ type the relevant invoices;
  - ♦ operate HKCo's bank account;
  - ♦ arranging letters of credit; and
  - ♦ record the transactions in HKCo's accounts.

If HKCo conducts business in the above manner, the IRD will accept that the company does not generate any Hong Kong sourced profits. It simply acts as a “bookkeeping centre” (through HKM) following instructions from Overseas Associate. The administrative works performed by HKM in Hong Kong are purely incidental functions, which are not instrumental in earning the company's trading profits and, of course, give no indication of a source of profits in Hong Kong.

## 2. Acting As Special Investment Vehicle



By changing the investment vehicle into HKCo to hold the Chinese investments, benefits under the “Arrangement Between The Mainland Of China And The Hong Kong Special Administrative Region For The Avoidance Of Double Taxation And The Prevention Of Fiscal Evasion With Respect To Taxes On Income” could be enjoyed.

The Arrangement confers benefits that are greater than or comparable to the other tax treaties China has entered into, including those with Mauritius. The withholding tax rates on repatriation of interest, dividends and royalties under the Arrangement are amongst the lowest available in the double tax treaties signed by China. A comparison of the rates of withholding tax is summarized as follows:

Income \ Location	No Treaty	Hong Kong	Mauritius	Barbados	Singapore
Interest	10%	7%	10%	10%	10%
Dividends	10%	10% / 5%	5%	5%	12% / 7%
Royalties	10%	7%	10%	10%	10%
Capital gains on shares	Taxable	Exempt	Exempt	Exempt <sup>4</sup>	Taxable

Any advice included in this communication was not intended to be used, and it cannot be used, for avoiding tax and penalty that may be imposed by any tax authorities. Being one of the major business centers in the world, it is easy to put commercial substance into transactions and invoke fewer questions from tax authorities than elsewhere. But, of course, commercial considerations always dictate the final choice of how to operate HKCo in real life. Overseas investors therefore should consult their qualified advisors, particularly where unusual or complex situations are involved, before taking any action.

Our Tax & Business Advisory Division takes care of China and Hong Kong tax compliance, cross-border tax planning advisory, corporate restructuring, company formation in China, pre-investment consultation, due diligence review for mergers and acquisition, pre-listing tax review and tax investigation, etc. She is responsible for serving a portfolio of diversified local and international clients including construction, financial institutions, information technology, investment holding, logistics, manufacturing, professional service and trading companies.

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