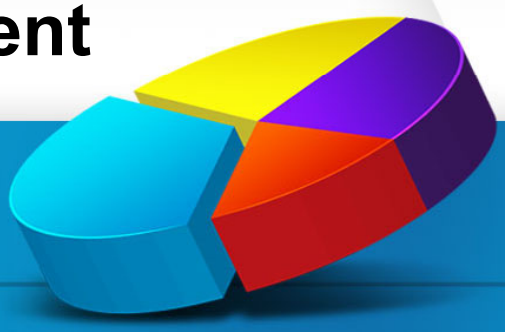
CTA – P5
Advanced Taxation Practice
Hong Kong Tax Resident

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Hong Kong Tax Resident

Hong Kong Tax Resident

- Individual
  - (a) he/she ordinarily resides in Hong Kong; or
  - (b) he/she stays in Hong Kong for more than 180 days during a year of assessment or for more than 300 days in two consecutive years of assessment one of which is the relevant year of assessment.
- An individual is generally considered "ordinarily residing" in Hong Kong if he/she has a permanent home in Hong Kong where he/she or his/her family lives.
  - (a) "Ordinary residence" connotes residence in Hong Kong with some degree of continuity and apart from accidental or temporary absence.
  - (b) To be an ordinary resident of Hong Kong, the person must be habitually and normally resident in Hong Kong, apart from temporary or occasional absences of long or short duration. The concept of ordinary resident refers to a person's abode in Hong Kong which he/she has adopted voluntarily and for settled purposes, with a sufficient degree of continuity, as part of the regular order of his/her life for the time being, whether of short or of long duration.
- In ascertaining the number of days a person stays in Hong Kong, part of a day will be counted as one day.

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Hong Kong Tax Resident

- Entity
  - (a) (where the entity is a company) the company is incorporated in Hong Kong; or if the company is incorporated outside Hong Kong, being normally managed or controlled in Hong Kong; or
  - (b) (where the entity is not a company) the entity is constituted under the laws of Hong Kong; or if the entity is constituted outside Hong Kong, being normally managed or controlled in Hong Kong.
- The legal concept "normally managed or controlled" does not require that both management and control be exercised in Hong Kong. "Management" refers to the management of daily business operations, or implementation of the decisions made by top management, etc. "Control" refers to the control of the whole business at the top level, including formulating the central policy of the business, making strategic policies of the entity, choosing business financing, evaluating business performance, etc.

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Permanent Establishment in Hong Kong

Authorised OECD Approach (AOA)

- Two-step approach
  - use functional and factual analysis to hypothesize the permanent establishment as a distinct and separate enterprise;
  - apply the arm's length principle to the hypothetical enterprise in accordance with the OECD Transfer Pricing Guidelines for Multilateral Enterprises and Tax Administrations (the TPG) by analogy.

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Key Entrepreneurial Risk-Taking (KERT)

- KERT function/ Significant People Function (SPF) concept
  - Relates to the active day-to-day decision makers and management, rather than the formalizing of the outcome of decision making.
  - refers to functions performed below the strategic level of senior management and often middle management, but it depends on decision making process within the enterprise

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Hong Kong's Attribution Rules

- Permanent establishment as defined in DTA or Schedule 17G
  - Rule 2, section 50AAK
    - the income or loss of a non-Hong Kong resident person attributable to the person's permanent establishment in Hong Kong to be determined as if the permanent establishment were a distinct and separate enterprise.
- If the non-Hong Kong resident person is a tax resident of a jurisdiction which has a DTA with Hong Kong, it is necessary to refer to the relevant DTA to determine whether the non-Hong Kong resident person has a permanent establishment in Hong Kong.
- If the non-Hong Kong resident person is not a tax resident of a jurisdiction which has a DTA with Hong Kong, it is necessary to refer to Part 3 of Schedule 17G to determine whether the non-Hong Kong resident person has a permanent establishment in Hong Kong

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Permanent establishment deemed carrying on business

- The non-Hong Kong resident person is regarded as carrying on a trade, profession or business in Hong Kong for the purposes of charging profits tax.

- Profits arising in or derived from Hong Kong in respect of a business carried on in Hong Kong by a non-DTA territory resident person, without a permanent establishment in Hong Kong, remain chargeable to profits tax under section 14.

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Basic Premise of Rule 2

- Sec 50AAK(2). It were a distinct and separate enterprise
  - (a) engaged in the same or similar activities under the same or similar conditions; and
  - (b) dealt wholly independently with the person.

- Sec 50AAK(3). Account is to be taken of the functions performed, assets used and risk assumed by the person
  - (a) through the permanent establishment; and
  - (b) through the other parts of the person.

- Sec 50AAK(3). The permanent establishment
  - (a) has the same credit rating as the person; and
  - (b) has the equity and loan capital that it could reasonably be expected to have in the circumstances set out in section 50AAK(2).

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Permanent Establishment (under DTA)

- "Permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on. Includes especially:
  - a. a place of management;
  - b. a branch;
  - c. an office;
  - d. a factory;
  - e. workshop, and
  - f. a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

- Two critical components
  (a) a certain degree of permanence at geographical point (the duration test); and
  (b) A specific geographical point (the location test).

- Building site or construction or installation project:
  - continue for a period more than 12 months; (the period may be varied between different Contracting States)

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Permanent Establishment (under DTA)

- Preparatory or auxiliary activities:
  - The 1st set of conditions
    (a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
    (b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;
    (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;
    (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;
    (e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character;
    (f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.
  - The 2nd set of conditions
    (a) the activities carried on for the enterprise through the place consist solely of any combination of the activities mentioned in subparagraph (a) of the 1st set of conditions; and
    (b) the overall activity of the place resulting from the combination of the activities is of a preparatory or auxiliary character.

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Permanent Establishment (under DTA)

- Agent as permanent establishment
  - Have and habitually exercise, authority to conclude contracts on behalf of an enterprise.
- Independent agents
  - Who act for an enterprise in the ordinary course of their business do not constitute a permanent establishment of that enterprise.
- Commissionnaire arrangement
  - A person sells products in Hong Kong in its own name but on behalf of an enterprise resident outside Hong Kong that is the owner of these products.

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END

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