

INFORMATION PAMPHLET



A BRIEF GUIDE TO TAXES
ADMINISTERED BY THE
INLAND REVENUE DEPARTMENT
2003 - 2004

**INLAND REVENUE DEPARTMENT
THE GOVERNMENT OF
THE HONG KONG SPECIAL ADMINISTRATIVE REGION**

A BRIEF GUIDE TO TAXES
ADMINISTERED BY THE
INLAND REVENUE DEPARTMENT

This pamphlet is issued for the general information of persons unfamiliar with the tax legislation in Hong Kong. Being a brief guide, it can only cover the subject very broadly. For further details, reference may be made to our web site <http://www.info.gov.hk/ird> or the relevant legislation.

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INFORMATION PAMPHLET

TAXATION IN HONG KONG

The Inland Revenue Ordinance (Chapter 112) provides for the levying of three separate direct taxes for a year of assessment which ends on 31 March.

The taxes levied under the Ordinance are :

Profits Tax
Salaries Tax
Property Tax

PROFITS TAX

The Scope of the Charge

Persons, including corporations, partnerships, trustees and bodies of persons carrying on any trade, profession or business in Hong Kong are chargeable to tax on all profits (excluding profits arising from the sale of capital assets) arising in or derived from Hong Kong from such trade, profession or business. There is no distinction made between residents and non-residents. A resident may therefore derive profits from abroad without being charged to tax; conversely, a non-resident may be chargeable to tax on profits arising in Hong Kong. The questions of whether a business is carried on in Hong Kong and whether profits are derived from Hong Kong are largely questions of fact. However some guidance on the principles applied can be found in cases which have been considered by the courts in Hong Kong and in other common law jurisdictions.

The following sums are deemed to be receipts arising in or derived from Hong Kong from a trade, profession or business carried on in Hong Kong :-

- (1) Sums received from the exhibition or use in Hong Kong of cinematograph or television film or tape, any sound recording or any advertising material connected with such film, tape or recording.

- (2) Sums received for the use of or right to use in Hong Kong a patent, design, trademark, copyright material or secret process or formula or other property of a similar nature.
- (3) Sums received by way of hire, rental or similar charges for the use of movable property in Hong Kong or the right to use movable property in Hong Kong.

The profits tax rate for corporations is increased from 16% to 17.5% with effect from year of assessment 2003/04. For unincorporated businesses, the profits tax rate is increased from 15% to 15.5% in the year of assessment 2003/04 and to 16% in the year of assessment 2004/05.

The Basis of Assessment

Tax is charged on the assessable profits for a year of assessment. The assessable profits for a business which makes up annual accounts are calculated on the profits of the year of account ending in the year of assessment. For a business which commenced on or after 1 April 1974 and for which accounts are consistently made up to the same day in each year, assessments will equal in total the profits, as adjusted for tax, earned during the life of the business. In the year of assessment itself, a provisional tax is to be paid based on the profits assessed for the preceding year. The provisional payment is applied in the first instance against Profits Tax payable on assessable profits for that year of assessment when agreed in the following year. Any excess is then applied against the provisional Profits Tax payable for that succeeding year.

On cessation of a business (subject to certain circumstances where special treatment would apply), the assessable profits are generally based on the profits for the period from the end of the basis period for the previous year of assessment to the date of cessation.

Non-Residents and Agents dealing with Non-Residents

A non-resident is chargeable to tax either directly or in the name of his agent in respect of all his profits arising in or derived from Hong Kong from any trade, profession or business carried on here, whether or not the agent has the receipt of the profits, and the tax may be recovered out of the assets of the non-resident or from the agent. The agent is required to retain from the assets sufficient money to pay the tax.

A non-resident who receives sums described in sub-paragraphs (1) and (2) on pages 1 and 2 respectively is chargeable to tax in the name of any person in Hong Kong who paid or credited the sums to him; so is a non-resident who receives sums from the performance in Hong Kong of an activity by a non-resident entertainer or sportsman in his character as entertainer or sportsman. The person who pays or credits such sums is required at the time he makes the payment or credit to deduct from those sums an amount sufficient to meet the tax due.

Resident consignees are required to furnish quarterly returns to the Commissioner of Inland Revenue showing the gross proceeds from sales on behalf of their non-resident consignors and to pay to the Commissioner a sum equal to 1% of such proceeds, or such lesser sum as may have been agreed.

Where a non-resident carries on business with a resident and the business is so arranged that it produces to the resident either no profits or profits less than the ordinary profits that might be expected to arise to an independent concern, the business may be treated as carried on in Hong Kong by the non-resident through the resident as agent.

Where the true profits of a non-resident from a trade, profession or business carried on in Hong Kong cannot be readily ascertained, they may be computed on a fair percentage of the turnover in Hong Kong.

Where the accounts of a non-resident whose head office is outside Hong Kong do not disclose the true profits of a Hong Kong permanent establishment, the profit of the branch for tax purposes is taken to be the amount which bears to the taxpayer's total profits the same proportion as his turnover in Hong Kong bears to his total turnover.

Special provisions are made in the Ordinance for non-resident ship-owners and non-resident aircraft-owners whose vessels call at locations within Hong Kong waters or whose aircraft land at a Hong Kong airport. Further details may be obtained from the Department.

Exemptions and Deductions

Dividends received from a corporation which is subject to Hong Kong Profits Tax, as well as amounts already included in the assessable profits of other persons chargeable to Profits Tax (e.g. shares of profits from joint ventures) are excluded from the assessable profits of the recipient.

Generally, all expenses, to the extent to which they have been incurred by the taxpayer in the production of chargeable profits, are allowed as deductions including :-

- (1) Interest on funds borrowed (provided certain conditions are satisfied) and rent of buildings or land occupied for the purpose of producing the profits.
- (2) Bad and doubtful debts (any recoveries to be treated as income when received).
- (3) Repairs of articles, premises, plant and machinery used in producing the profits.
- (4) Expenditure for registration of a trade mark, design or patent and expenditure on the purchase of patent rights or rights to any know-how for use in Hong Kong in the production of chargeable profits. No deduction is, however, allowable in respect of patent rights or rights to any know-how purchased by a person wholly or partly from an associated or related person.
- (5) Expenditure on scientific research including market, management and business research and payments for technical education subject to certain rules.
- (6) An employer's annual contribution to a fund under a recognized occupational retirement scheme, or annual premium payment in respect of a contract of insurance under such a scheme, or regular contributions paid to a mandatory provident fund scheme, or any provision for these purposes, but limited in respect of any one employee to 15% of his total emoluments for the relevant period.
- (7) Any mandatory contributions paid by a sole proprietor or a partner in a partnership in respect of his liability to pay such contributions as a self-employed person under the Mandatory Provident Fund Schemes Ordinance (Cap. 485) not exceeding \$12,000 in a year of assessment, taking into account deductions already allowed under any other sections in the Ordinance. However, contributions made for spouses are not deductible.

In computing the profits, deduction is specifically prohibited in respect of the following :-

- (1) Domestic or private expenses and any sums not expended for the purpose of producing the profits.
- (2) Any loss or withdrawal of capital, the cost of improvements and any expenditure of a capital nature.
- (3) Any sum recoverable under insurance or contract of indemnity.
- (4) Rent of or expenses relating to premises not occupied or used for the purpose of producing the profits.
- (5) Taxes payable under the Inland Revenue Ordinance, except Salaries Tax paid in respect of employees' remuneration.
- (6) Any remuneration or interest on capital or loans payable to or, subject to section 16AA, contribution 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.

A transfer of certain allowable head office administrative expenses by means of a charge to a local branch or subsidiary in Hong Kong would be allowed as a deduction for Hong Kong tax purposes, to the extent to which they were incurred during the basis period for the year of assessment in the production of profits chargeable to tax.

Tax Incentives

There are tax incentives in specific areas where this may be necessary to enable us to compete in the region on a level playing field. They include:-

- (1) Immediate writing off to be allowed for capital expenditure on plant and machinery specially related to manufacturing, and on computer hardware and software.
- (2) Capital expenditure on refurbishment of business premises to be allowed to be written off over five years of assessment.
- (3) Concessionary tax rate for gains derived from qualified debt instruments.
- (4) Concessionary tax rate for offshore business of reinsurance companies.
- (5) Exemption from payment of tax on interest (accrued on or after 22 June 1998) derived from any deposit placed in Hong Kong with an authorized institution (not applicable to interest received by or accrued to a financial institution).

Losses

Losses made in an accounting year are to be carried forward and set off against future profits of that trade but a corporation carrying on more than one trade may have losses in one trade offset against profits of the other. An individual who incurs a trading loss and who claims Personal Assessment will have the loss allowed as a deduction from his total income.

Any unallowed losses brought forward from the year 1974/75 remain available for set-off against future profits.

For gains or losses which are subject to concessionary tax rate, there are special provisions on the adjustment of losses between concessionary trading activities and normal trading activities.

Depreciation Allowances

◆ Industrial Buildings and Structures

Special allowances are given in respect of capital expenditure incurred on the construction of industrial buildings and structures used in certain trades such as transport, dock, water and electricity undertakings, the manufacture, processing or storage of goods and trades carried on in mills and factories and in farming. An initial allowance of 20% of such capital expenditure is given in the year of expenditure and an annual allowance of 4% of the expenditure is given until the total expenditure is written off. When the asset is disposed of, a balancing allowance or balancing charge is made based on the difference between the disposal price and the written down value on disposal.

◆ Commercial Buildings and Structures

Up to the year of assessment 1997/98, a building or structure which is not an industrial building or structure but is nevertheless used for the purposes of a trade, profession or business (other than as stock in trade) can qualify for an annual “rebuilding allowance” of 2% of the capital expenditure incurred on the construction of such building or structure.

From the year of assessment 1998/99, a new provision becomes effective. Under the new legislation, an annual “commercial building allowance” of 4% of the cost of construction is granted in respect of an eligible commercial building or structure. At the same time, provisions for balancing allowance and charge similar to industrial buildings and structures have been introduced.

◆ Plant and Machinery

Allowances on capital expenditure incurred on the provision of plant and machinery for the purpose of producing chargeable profits, except those assets referred to under 'Tax Incentive' above, are deducted in arriving at assessable profits :-

- (1) An initial allowance on the cost of the item of plant and machinery. As from the year 1989/90, the allowance is 60% of the cost.
- (2) Annual allowances at rates prescribed by the Board of Inland Revenue on the reducing value of the asset. As from the year 1980/81, the rates are 10%, 20% and 30% according to the estimated working life of the particular category of plant or machinery. Items qualifying for the same rate of annual allowance are grouped under one "pool".
- (3) A balancing allowance based on the unallowed expenditure compared with moneys received on disposal of the plant and machinery is available 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.

Books & Records

All persons carrying on business in Hong Kong are required to keep sufficient records, in English or Chinese, of their income and expenditure to enable their assessable profits to be readily ascertained. There are statutory requirements to record certain specified details of every business transaction. Business records must be retained for at least **7** years after the date of the transaction to which they relate.

In the financial year 1995/96 the law has been amended to the effect that any person who fails to keep sufficient records can be subject to penalty up to **\$100,000**.

SALARIES TAX

The Scope of the Charge

This tax is imposed on all income arising in or derived from Hong Kong from an office or employment or any pension. In deciding whether income “arises in or is derived from Hong Kong”, it is necessary to establish where the employment, the source of income is located. "Income arising in or derived from Hong Kong" includes all income derived from services rendered in Hong Kong. Special provisions apply to crew of ships and aircraft who visit Hong Kong for short spans of time and persons who have paid tax of substantially the same nature as Hong Kong Salaries Tax in any territory outside Hong Kong.

“Income from any office or employment” includes all forms of income from the employer and others. Income also includes “rental value” in respect of a place of residence provided rent-free by the employer (including cases of reimbursements of rent paid by employees directly to their landlords). The “rental value” to be included in the assessment is 10% of the total income (after deducting outgoings, depreciation, etc.) from the employer or any person associated with the employer.

From 1 April 2003, provisions relating to tax exemptions in respect of holiday passage and warrant provided by the employer have been repealed. From this date onwards, all holiday journey benefits provided by the employer are chargeable to tax.

The Basis of Assessment

Liability to Salaries Tax is based on the chargeable income of the year of assessment, but the total amount of income for the year cannot be ascertained until the year is past. Hence, the Inland Revenue Department will first demand for payment of Provisional Salaries Tax during the year of assessment and then make adjustments in the following year. Any provisional tax paid for a year of assessment is applied firstly against the Salaries Tax payable on the income for that year and if there is excess, apply the excess against the following year’s provisional tax liability.

For example, a taxpayer who commenced employment on 1 July 2002, and earned income for 9 months during year of assessment 2002/03, his provisional tax liability for 2003/04 will be estimated by grossing up to 12 months’ income. If after receipt of the tax bill this taxpayer suffered a reduction in income of more than 10% (for instance, he ceased to be employed on 31 October 2003), he may apply for the holdover of provisional tax – at least 28 days before tax falls due.

Under Salaries Tax, taxpayers may claim deductions and allowances. Entitlement to a new allowance is also a ground for applying holdover of tax.

Income of Husband and Wife

A married person is responsible for all aspects of his or her own salaries tax affairs including lodgement of returns and payment of tax assessed. However, if the total tax liability of a married couple is greater than it would have otherwise been when their incomes are aggregated, they may elect to be jointly assessed in much the same way as before.

Deductions Allowed

The following deductions are allowable:

- (a) Expenses wholly, exclusively and necessarily incurred in the production of assessable income, not being expenses of a private or domestic nature;
- (b) Donations paid to approved charities if the amount is not less than \$100 and with the limitation that such allowance shall not exceed 25% (10% for years of assessment prior to 2003/04) of the income after allowable expenses;
- (c) Expenses of self-education paid on fees (including tuition and examination fees) in connection with a prescribed course of education undertaken to gain or maintain qualification for use in employment. The maximum amount of deduction is \$40,000 from year of assessment 2001/02.
- (d) Elderly residential care expenses paid by the person or his/her spouse in the year of assessment 1998/99 and after to a residential care home in respect of the person's or his/her spouse's parent or grandparent. The maximum amount that can be deducted is \$60,000 for a year of assessment for each parent or grandparent. (To be eligible for the deduction, the parent/grandparent must be aged 60 or above at any time in the year of assessment, or under 60 but entitled to claim an allowance under the Government's Disability Allowance Scheme; and the residential care home must be one specified in the Inland Revenue Ordinance. Should the deduction be allowed to a person, he or any other person is not entitled to claim dependent parent/grandparent allowance and additional dependent parent/grandparent allowance for the same parent/grandparent for the same year of assessment.);
- (e) As from the year of assessment 1998/99, taxpayer can, for any 5 years of assessment of choice (continuous or otherwise), claim deductions for "home loan interest" paid on a home loan for the acquisition property unit used as his dwelling. The following conditions must be satisfied before deduction is granted:
 - the property concerned must be situated in Hong Kong,
 - the property must be used as his place of residence during the year of assessment,
 - if he is the sole owner of the property, the maximum amount deductible is:

<u>Year of Assessment</u>	<u>Amount</u>
1998/99 to 2000/01	\$100,000
2001/02 and 2002/03	\$150,000
From 2003/04 onwards	\$100,000
 - if he is a joint owner or tenant in common of the property, the maximum amount deductible for each year is to be apportioned amongst the joint-tenants or tenants-in-common, respectively in accordance with the number of joint-tenants or his/her share of ownership in the dwelling.
- (f) Mandatory contributions paid to Mandatory Provident Fund Scheme (MPFS) in the year of assessment 2000/01 and after. The maximum deduction for a year of assessment is \$12,000.

- (g) Contributions paid to a Recognized Occupational Retirement Scheme (RORS) in the year of assessment 2000/01 and after, subject to the following restrictions :
- (i) the amount deductible is the lesser of the actual amount contributed to the RORS or the amount of mandatory contribution that person would have been required to pay had that scheme been a Mandatory Provident Fund Scheme; and
 - (ii) the maximum deduction is \$12,000 for a year of assessment.

Allowances

In addition to or as an alternative to a Basic Allowance, a taxpayer may claim the following allowances if appropriate :

◆ Married Person's Allowance

- (a) If the taxpayer has income chargeable to Salaries Tax : -

A taxpayer is entitled to the Married Person's Allowance if he/she was, at any time during the year: -

- married and not living apart from his/her spouse ; or
- living apart from his/her spouse but was maintaining or supporting him/her,

and his/her spouse did not derive any income chargeable to Salaries Tax; or the couple has elected for Joint Assessment.

- (b) If the taxpayer has elected Personal Assessment : -

A taxpayer is entitled to the Married Person's Allowance if he/she was, at any time during the year : -

- married and not living apart from his/her spouse ; or
- living apart from his/her spouse but was maintaining or supporting him/her;

◆ Child Allowance

Child allowances are granted to taxpayers in respect of their unmarried child(ren) maintained by them. The child must be under 18 of age during the year of assessment or if 18 and over but under 25 during the year of assessment and receiving full-time education at a university, college, school or other similar educational establishment. In addition, child allowance is granted for a child of any age who is incapacitated for work by reason of physical or mental disability (disregarding his/her age). Under separate taxation, all child allowances must be claimed by either the husband or the wife.

◆ **Dependent Parent or Dependent Grandparent Allowance**

- (a) To be eligible for claiming a Dependent Parent or Dependent Grandparent Allowance, the taxpayer must have maintained at any time during the year a parent or grandparent who :-
- (i) is ordinarily resident in Hong Kong;
 - (ii) is aged 60 years or more or eligible to claim an allowance under the Government's Disability Allowance Scheme; and
 - (iii) has either resided with the taxpayer, otherwise than for full valuable consideration, for a continuous period of 6 months or has received from him/her or his/her spouse not less than \$12,000 (\$1,200 prior to year of assessment 1998/99) in money towards his/her maintenance.
- (b) An Additional Dependent Parent/Grandparent Allowance will be granted in respect of each dependent parent/grandparent actually living with the taxpayer otherwise than for full consideration continuously throughout the year.
- (c) Only one individual can be granted the allowance in respect of any one parent/grandparent (the dependent). In the event that more than one taxpayers wish to claim the allowance in respect of the same dependant for the same year of assessment, only one allowance will be given in respect of that dependent person. The Inland Revenue Department will request the claimants to reach an agreement among themselves so as to decide which one of them is to have the allowance for that year.
- (d) For the purpose of Dependent Parent Allowance, the word "parent" means-
- (i) a parent of whose marriage the person or his/her spouse is a child;
 - (ii) a parent by whom the person or his/her spouse was legally adopted;
 - (iii) a step-parent;
 - (iv) the person's or his/her spouse's natural parent; or
 - (v) a parent of the person's deceased spouse.
- (e) As for the purpose of Dependent Grandparent Allowance, the word "grandparent" means :-
- (i) a natural grandfather or grandmother of the person or his/her spouse;
 - (ii) an adoptive grandparent of the person or his/her spouse;
 - (iii) a step grandparent of the person or his/her spouse; or
 - (iv) a grandparent of the person's deceased spouse.

◆ **Single Parent Allowance**

A Single Parent Allowance is granted if an individual had at any time during the year of assessment the sole or predominant care of a child in respect of whom the individual was entitled during the year of assessment to claim a Child Allowance. The allowance is not due if the individual was married and not living apart from his/her spouse at any time during the year. No Single Parent Allowance is allowable in respect of any second or subsequent child.

◆ **Disabled Dependant Allowance**

A Disabled Dependant Allowance is granted if an individual is maintaining a dependant who is eligible to claim an allowance under the Government Disability Allowance Scheme. This allowance is granted in addition to any allowance already being claimed.

◆ **Dependent Brother or Dependent Sister Allowance**

Commencing from the year of assessment 1996/97, a Dependent Brother or Dependent Sister Allowance is granted if an individual or his/her spouse maintains an unmarried brother/sister of his/her own or of his/her spouse and the person so maintained at any time in the year of assessment was -

- (a) under the age of 18 years;
- (b) of or over the age of 18 years but under the age of 25 years and was receiving full time education at a university, college, school or other similar educational establishment; or
- (c) of or over the age of 18 years and was, by reason of physical or mental disability, incapacitated for work.

A Dependent Brother or Dependent Sister allowance may be granted for each brother/sister maintained. A brother/sister is only treated as maintained by the person or by the spouse of the person if, at any time during the year, the person or the spouse had sole or predominant care of the brother/sister. A Dependent Brother or Dependent Sister Allowance and a Child Allowance shall not both be given in any year of assessment in respect of the same dependent person.

Various allowances for recent years are summarized as follows :-

Year of Assessment	<u>1997/98</u>	<u>1998/99</u> <u>to 2002/03</u>	<u>2003/04</u>	<u>2004/05</u>
	\$	\$	\$	\$
<u>Basic allowance</u>	100,000	108,000	104,000	100,000
<u>Married Person's Allowance</u>	200,000	216,000	208,000	200,000
<u>Child Allowance</u>				
For the 1st & 2nd child (For each qualified child)	27,000	30,000	30,000	30,000
For the 3rd to 9th child (For each qualified child)	14,000	15,000	30,000	30,000
<u>Dependent Brother / Dependent Sister Allowance</u>				
(For each qualified brother/sister)	27,000	30,000	30,000	30,000
<u>Dependent Parent / Dependent Grandparent Allowance</u>				
(For each qualified parent/grandparent)	27,000	30,000	30,000	30,000
<u>Additional Dependent Parent/Grandparent Allowance</u>				
(For each qualified parent/grandparent)	8,000	30,000	30,000	30,000
<u>Single Parent Allowance</u>	75,000	108,000	104,000	100,000
<u>Disabled Dependant Allowance</u> (For each qualified dependant)	25,000	60,000	60,000	60,000

Tax Rates

Income after deductions and allowances (net chargeable income) is charged at the following rates :-

Year of Assessment	1997/98 (the year with a 10% tax rebate)					1998/99 to 2000/01 & 2002/03		
	Net Chargeable Income \$	Rate	Tax \$	(Note) Effective Rate	(Note) Net Tax \$	Net Chargeable Income \$	Rate	Tax \$
On the First	30,000	2%	600	1.8%	540	35,000	2%	700
On the Next	$\frac{30,000}{60,000}$	8%	$\frac{2,400}{3,000}$	7.2%	$\frac{2,160}{2,700}$	$\frac{35,000}{70,000}$	7%	$\frac{2,450}{3,150}$
On the Next	$\frac{30,000}{90,000}$	14%	$\frac{4,200}{7,200}$	12.6%	$\frac{3,780}{6,480}$	$\frac{35,000}{105,000}$	12%	$\frac{4,200}{7,350}$
Remainder		20%		18%			17%	

Year of Assessment	2001/02 (the year with a 50% tax rebate, subject to upper limit of \$3,000)					2003/04			2004/05		
	Net Chargeable Income \$	Rate	Tax \$	(Note) Effective Rate	(Note) Net Tax \$	Net Chargeable Income \$	Rate	Tax \$	Net Chargeable Income \$	Rate	Tax \$
On the First	35,000	2%	700	1%	350	32,500	2%	650	30,000	2%	600
On the Next	$\frac{35,000}{70,000}$	7%	$\frac{2,450}{3,150}$	3.5%	$\frac{1,225}{1,575}$	$\frac{32,500}{65,000}$	7.5%	$\frac{2,437}{3,087}$	$\frac{30,000}{60,000}$	8%	$\frac{2,400}{3,000}$
On the Next	$\frac{23,750}{93,750}$	12%	$\frac{2,850}{6,000}$	6%	$\frac{1,425}{3,000}$	$\frac{32,500}{97,500}$	13%	$\frac{4,225}{7,312}$	$\frac{30,000}{90,000}$	14%	$\frac{4,200}{7,200}$
On the Next	$\frac{11,250}{105,000}$	12%	$\frac{1,350}{7,350}$	12%	$\frac{1,350}{4,350}$						
Remainder		17%		17%			18.5%			20%	

Net Chargeable Income = Total Income - Deductions – Allowances

Tax charged shall not exceed the standard rate of tax applied to the net total income without Allowances, i.e. total assessable income less total deductions only:

<u>Year of Assessment</u>	<u>Standard Rate</u>
1997/98 to 2002/03	15 % (see Note below)
2003/04	15.5%
From 2004/05 onwards	16 %

Note (1) Year of Assessment 1997/98

Pursuant to the Tax Exemption (1997 Tax Year) Order, there is a 10% tax rebate for the year of assessment 1997/98. The effective standard rate for this year of assessment is therefore 13.5%.

(2) Year of Assessment 2001/02

Pursuant to the Tax Exemption (2001 Tax Year) Order, there is a 50% tax rebate for the year of assessment 2001/02, subject to upper limit of \$3,000.

Examples (for Year of Assessment 2002/03)

	<u>EXAMPLE A</u>		<u>EXAMPLE B</u>	
<u>Single Income Family</u>	<u>Taxed at</u> <u>Marginal Rates</u>		<u>Taxed at</u> <u>Standard Rate</u>	
	\$	\$	\$	\$
Employment income of husband		360,000		3,300,000
Income of wife		<u>Nil</u>		<u>Nil</u>
		360,000		3,300,000
<u>Less</u> : Husband's deductible outgoings		<u>3,000</u>		<u>4,000</u>
		357,000		3,296,000
<u>Add</u> : Value of quarters 10% on \$(360,000-3,000)	35,700		Nil	
Rent paid to employer	<u>5,000</u>	<u>30,700</u>	<u>Nil</u>	<u>Nil</u>
		387,700		3,296,000
<u>Less</u> : Donations	4,000		5,000	
Mandatory Contributions to Mandatory Provident Fund Scheme	12,000	16,000	12,000	17,000
	<u> </u>	<u>371,700</u>	<u> </u>	<u>3,279,000</u>
<u>Less</u> : Married person's allowance	216,000		216,000	
Child allowance for 2 children	60,000		60,000	
Dependent parent allowance for 1 parent	<u>30,000</u>	<u>306,000</u>	<u>30,000</u>	<u>306,000</u>
Net chargeable income		65,700		2,973,000
		=====		=====
Tax thereon	35,000 @ 2% =	700	35,000 @ 2% =	700
	30,700 @ 7% =	2,149	35,000 @ 7% =	2,450
			35,000 @ 12% =	4,200
			2,868,000 @ 17% =	487,560
		<u>2,849</u>		<u>494,910</u>
		=====		=====
Tax payable		2,849	[Restricted to 15% on \$3,279,000]	491,850
		=====		=====

Both Spouses Earning Income

EXAMPLE C

Separate Taxation applies :

	<u>Mr A</u>	<u>Mrs A</u>
	\$	\$
Assessable income after deductions	204,000	112,000
<u>Less : Allowances</u>	<u>168,000</u>	<u>108,000</u>
Net chargeable income	36,000	4,000
	=====	=====
Tax payable	770	80
	====	==

- Note :
- (1) All child allowance for 2 children claimed by Mr A.
 - (2) Mr A and Mrs A are to be assessed separately and served with separate notices of assessment.

EXAMPLE D

Joint assessment may be elected if one spouse has income that is less than the Basic Allowance :

	<u>Separate Taxation</u>		<u>Joint Assessment</u>	
	<u>Mr B</u>	<u>Mrs B</u>		\$
	\$	\$		
Assessable income				
after deductions	300,000	55,000	Mr B's assessable income	300,000
<u>Less : Allowance</u>	<u>168,000</u>	<u>108,000</u>	Mrs B's assessable income	<u>55,000</u>
Net chargeable income	132,000	Nil	Less : Allowance	<u>355,000</u>
	=====	====		<u>276,000</u>
Unabsorbed allowance	Nil	53,000	Aggregated net chargeable	
	====	=====	income	79,000
				=====
Tax payable	11,940	Nil		
	=====	====		
Total tax payable	11,940		Total tax payable	4,230
	=====			=====

Note : All child allowance for 2 children claimed by Mr B

The couple may elect to be jointly assessed and reduce their total tax payable from \$11,940 to \$4,230.

Both Spouses Earning Income

EXAMPLE E

An example in which one spouse earns a substantial amount of income.

(1) Child Allowances claimed by Mr C

	<u>Mr C</u>	<u>Mrs C</u>
	\$	\$
Assessable income after deductions	1,900,000	180,000
<u>Less : Allowances</u>	<u>168,000</u>	<u>108,000</u>
Net chargeable income	1,732,000	72,000
	=====	=====
Tax payable	283,940	3,390
	=====	=====
Total tax payable		\$287,330
		=====

(2) Child Allowances claimed by Mrs C

	<u>Mr C</u>	<u>Mrs C</u>
	\$	\$
Assessable income after deductions	1,900,000	180,000
<u>Less : Allowances</u>	<u>NIL</u>	<u>168,000</u>
Net chargeable income	1,900,000	12,000
	=====	=====
Tax payable	285,000	240
	=====	=====
Total tax payable		\$285,240
		=====

Note: (1) All child allowance should be claimed by Mrs C in this case.

(2) The total amount of tax to be paid by Mr and Mrs C can be reduced from \$287,330 to \$285,240.

PROPERTY TAX

The Scope of the Charge

Property Tax is charged on the owners of land and/or buildings in Hong Kong and is computed at the standard rate on the net assessable value of the property. The standard rate for years of assessment 1997/98 to 2002/03 is 15%, for 2003/04 is 15.5% and will be 16% for 2004/05 and onwards.

The Basis of Assessment

The assessable value is computed by reference to the actual consideration payable to the owner in respect of the right of use of the property. Examples of consideration to be included in the assessable value are rent, payment for the right of use of premises under licence, lump sum premium, service charges and management fee paid to the owner, and the owner's expenditure (e.g. repairs) borne by the tenant. The net assessable value is the assessable value (after deduction of rates paid by the owner) less an allowance of 20% for repairs and outgoing. Deduction is allowed for irrecoverable rent.

Properties for Owner's Business Use

If the income from property chargeable to Property Tax is included in the taxpayer's profits for Profits Tax purposes, or if the property owned by the taxpayer is occupied by him/her for business purposes, the amount of Property Tax paid may be deducted from the amount of Profits Tax assessed. Corporations carrying on a trade, profession or business in Hong Kong, on application made in writing to the Commissioner, may be exempt from paying Property Tax which would otherwise be set off against their Profits Tax.

PERSONAL ASSESSMENT

What is Personal Assessment and how it may work to reduce tax liability

The Inland Revenue Ordinance provides for the levying of three separate direct taxes for a year of assessment, viz, Profits Tax, Salaries Tax and Property Tax. Individuals ordinarily resided in Hong Kong may be able to reduce their tax liability by electing Personal Assessment. Under Personal Assessment, income from the above sources is aggregated and from this total, the following may be deducted :-

- (a) interest payments on money borrowed for the acquisition of properties on a property-by-property basis (i.e. the amount of interest deduction for each property should not exceed the assessed income from that property),
- (b) approved charitable donations (capped at 25% of income as from the year of assessment 2003/04; previously 10%)
- (c) elderly residential care expenses (from year of assessment 1998/99 onwards),
- (d) home loan interest (from year of assessment 1998/99 onwards),
- (e) mandatory contributions paid to Mandatory Provident Fund Scheme (MPFS) as an employee (from year of assessment 2000/01 onwards),
- (f) contributions paid to a Recognized Occupational Retirement Scheme (from year of assessment 2000/01 onwards),
- (g) business losses incurred in the year of assessment,
- (h) losses brought forward from previous years under Personal Assessment, and
- (i) personal allowances (see Allowances under SALARIES TAX).

Tax at progressive rates (same as those used for Salaries Tax) will then be imposed on the balance. Credit will be given for any tax already paid on the income included in the assessment. If the total of the tax already paid exceeds the tax chargeable under Personal Assessment, a refund will be made.

Who may elect for Personal Assessment

An individual may elect for Personal Assessment if :-

- (a) he/she is 18 years of age or over, or under that age if both his/her parents are dead; and
- (b) the individual is or, if he/she is married, whose spouse is a permanent or temporary resident in Hong Kong.

For the purpose of Personal Assessment :

“permanent resident” means an individual who ordinarily resides in Hong Kong;

“temporary resident” means an individual who stays in Hong Kong for a period or a number of periods amounting to more than 180 days during the year of assessment in respect of which the election is made or for a period or periods amounting to more than 300 days in 2 consecutive years of assessment, one of which is the year of assessment in respect of which the election is made.

Where an eligible individual is married and not living apart from his or her spouse and both of them have income assessable under the Inland Revenue Ordinance, that individual may not elect for Personal Assessment unless his or her spouse also elects.

Time limit for electing Personal Assessment

Election for Personal Assessment must be made in writing not later than 2 years after the end of the year of assessment in respect of which the election is made or 1 month after an assessment of income or profits forming part of the individual’s total income for such year of assessment becomes final and conclusive under Section 70, whichever is the later.

Treatment of a Married Couple under Personal Assessment

Unlike Salaries Tax, separate taxation for husband and wife is not applicable under Personal Assessment. A husband and wife are assessed jointly under Personal Assessment. The total income of an individual, as appropriately reduced, will be aggregated with that of his/her spouse to arrive at the joint total income of the couple for assessment purposes. Normally, the tax payable on the joint assessment is apportioned between the husband and the wife proportional to their respective reduced total income, and each will be issued with a Notice of Assessment. However, where an additional assessment is issued, the whole of the tax payable under this assessment shall be charged on the spouse assessed in respect of that income.

OBLIGATIONS OF TAXPAYERS (SALARIES, PROFITS & PROPERTY TAX) UNDER THE INLAND REVENUE ORDINANCE

- ◆ **Section 5 (2) (c)** - Where a corporation has been exempted from Property Tax and a change of ownership or of use takes place which might affect such exemption, the corporation must notify the Commissioner in writing within 30 days after the event.
- ◆ **Section 51(2)** - Every person (whether an individual, a partnership or a corporation) who is chargeable to Salaries, Profits or Property Tax for any year of assessment and who has not received a Return Form is required to notify the Commissioner of Inland Revenue in writing that he is so chargeable within four months after the end of the basis period for the year of assessment concerned.
- ◆ **Section 51(6)** - Any person who ceases to carry on a trade, profession or business or ceases to hold an office or employment in respect of which Salaries Tax is chargeable or ceases to own any source of income or ceases to be the owner of any land and buildings must advise the Commissioner of Inland Revenue in writing within one month of the date of the event.
- ◆ **Section 51(7)** - Any person chargeable to Salaries Tax, Profits Tax or Personal Assessment who is leaving Hong Kong for a period exceeding one month must notify the Commissioner of Inland Revenue at least one month before he is due to leave. If he intends to return to Hong Kong the approximate date of return must be given. This does not apply to persons who are required to leave frequently in the course of business or employment.
- ◆ **Section 51(8)** - Any person chargeable to Salaries Tax, Profits Tax, Personal Assessment or Property Tax who changes his address must notify the Commissioner of Inland Revenue in writing within one month. The Inland Revenue Ordinance also provides that anything sent from the Inland Revenue Department is properly served if sent by post to a person's last known address. In other words although a person failed to receive a notice from the Department, he is deemed to have received it if it was sent by post to his last known address. The Department usually sends all mail by ordinary post and it is important therefore that notification of change of address is promptly made.
- ◆ **Section 51C** - Every person carrying on a trade, profession or business in Hong Kong must keep sufficient records of his income and expenditure (either in English or in Chinese) to enable his assessable profits to be readily ascertained. There are statutory requirements to record certain specified details of every business transaction. Business records must be retained for at least seven years after the date of the transaction to which they relate. This does not apply to a corporation which has been dissolved.
- ◆ **Section 51D** - Owners of properties must keep sufficient records of rent received, such as lease agreements and duplicates of rent receipts to enable their tax liability to be readily ascertained. Such records should be retained for a period of not less than 7 years.

OBLIGATIONS OF EMPLOYERS UNDER THE INLAND REVENUE ORDINANCE

- ◆ **Section 52(4)** - An employer is required to furnish, within three months of engagement, particulars of any new employee who is likely to be chargeable to Salaries Tax.
- ◆ **Section 52(5)** - An employer must advise the Commissioner of Inland Revenue not less than one month before the termination of service of any employee who is likely to be chargeable to Salaries Tax.
- ◆ **Section 52(6)** - An employer must, not later than a month before the employee actually leaves, advise the Commissioner of Inland Revenue whenever an employee who is chargeable to Salaries Tax is about to leave Hong Kong for more than a month. This does not apply to an employee who is required, in the course of his employment, to leave Hong Kong at frequent intervals.
- ◆ **Section 52(7)** - An employer who is required by Section 52(6) to give notice to the Commissioner of Inland Revenue the expected departure of an employee must not, except with the consent in writing of the Commissioner, make any payment to the employee for a period of one month from the date of that notice.
- ◆ **Sales Personnel** If employed or treated to be employed under Section 9A of the Inland Revenue Ordinance, or holding an office are chargeable to Salaries Tax, employers are required to report their earnings even if these are by way of a variable commission.
- ◆ **Freelance brokers** holding no set office and not bound in a master-servant employment relationship are held to be carrying on business and to be chargeable to Profits Tax. Persons employing such agents are asked to give details of commissions they pay and employers making Employer's Returns are required to include this information in Form IR 56M.

Penalties may be imposed on taxpayers/employers who, without reasonable excuse, fail to comply with requirements of the Inland Revenue Ordinance.

COMPLETION OF TAX RETURN

Previously, a taxpayer who is an individual had to complete one tax return for employment income and one for each of the properties or businesses owned. Much of the information completed on each form was repeated. To help simplifying the taxation reporting, the Department introduced in 1994 the Composite Tax Return System, consolidating the tax reporting by individuals of different sources of income in one single return. Owners of jointly-owned properties, partnerships and corporations continue to report their rental income and profits in their respective returns.

CHARITABLE DONATIONS

A person who is chargeable to Salaries Tax or Profits Tax or who elects to be personally assessed can deduct from assessable income or assessable profits or total income for Personal Assessment the aggregate (not less than HK\$100) of donations made to approved charitable institutions or trusts of a public character or to the Government for charitable purposes up to a limit of 25% (10% for years of assessment prior to 2003/04) of the assessable income or assessable profits or total income for Personal Assessment.

DOUBLE TAXATION

An Arrangement between the Mainland of China and Hong Kong for the Avoidance of Double Taxation on Income has been implemented. It has effect in respect of income derived from the Mainland on or after 1 July 1998 and income derived from Hong Kong in any year of assessment commencing on or after 1 April 1998. The Arrangement covers business profits through permanent establishment, airline/shipping/land transport operations and personal services. In addition, we have concluded double taxation relief arrangements on airline and shipping income with other countries. Our legislation has also been amended to provide reciprocal exemption of taxation on shipping income with effect from 1 April 1998.

COLLECTION OF TAXES

A notice of assessment served to a taxpayer stipulates the amount of tax payable and the due date. Taxpayer should use the attached payment voucher or the detachable payment slip to pay tax by the following means :-

- (1) By phone. PPS account holders may use the tone phone to dial 18011 for bill registration and then 18031 for bill payment. The merchant code for Inland Revenue Department is '10'.
- (2) By Bank Automated Teller Machine (ATM). Taxpayers may use ATM card to pay at any of those HSBC/Hang Seng Bank ATMs with the "Bill Payment" signage or JETCO ATMs with the "JET PAYMENT" logo.
- (3) Via the Internet. Taxpayers may visit our web site < <http://www.info.gov.hk/ird> > through a PC with Internet connection. Under the "Tax Information" menu, select "Payment" and then "Payment Methods" which will provide further details and link them to the various payment web sites to effect tax payment. Under the Electronic Service Delivery Scheme, taxpayers may also access the various payment web sites on ESD kiosks by selecting the IRD's "Payment of Tax Bills" service.
- (4) By post with crossed cheque and payment voucher or payment slip addressed to "Inland Revenue Department, P.O. Box 28282, Gloucester Road Post Office, Hong Kong." The cheque should be payable to "The Government of the Hong Kong Special Administrative Region" or "The Government of the HKSAR".
- (5) In person by cash, cheque or EPS at post offices. Taxpayers should bring along the payment voucher or payment slip.

To pay tax by electronic means, taxpayers should enter the "Shroff Account Number for electronic payments" printed on the payment voucher or payment slip and observe the daily transaction limit of the relevant banks.

If tax is not fully paid by the specified due date, the unpaid tax including the second installment, if any, will be deemed to be in default and immediately recoverable. A surcharge of 5% will be added to the unpaid amount. The Commissioner is empowered to take recovery actions which include the institution of civil action in the District Court, or the issue of a notice to a third party who owes or is about to pay money to the defaulting taxpayer requiring him to pay such moneys not exceeding the amount of tax in default to the Department. A defaulter will be liable to the following costs and interest in addition to the outstanding tax due upon entry of judgment :

- (1) Court fee (\$630)
- (2) Fixed costs - service of writ (\$300)
 - additional amount for every defendant after the first defendant (\$40)
- (3) Interest on the judgment sum from the date of commencement of proceedings to the date of full settlement. The judgement interest rate is available for reference on the IRD homepage on the internet. The rate as at 1 April 2003 is 8.0%.

If tax including a 5% surcharge continues to be in default for a period of 6 months after the due date, a further 10% surcharge may be added to the total unpaid amount (including the 5% surcharge).

To build up funds for tax payment, taxpayers are encouraged to join our Electronic Tax Reserve Certificates Scheme. They can purchase Tax Reserve Certificates (TRCs) monthly by bank autopay or at any time by telephone, automated teller machine, via the Internet, by post or in person at the post office. The Scheme offers "Auto Tax Payment Service" which ensures on-time tax payment. The TRCs held in the account will be automatically redeemed, on a First-In-First-Out basis, for payment of the holder's tax.

MISCELLANEOUS LEVIES

STAMP DUTY

Stamp duty is chargeable on certain documents specified in the First Schedule to the Stamp Duty Ordinance which imposes fixed duty on some documents and an ad valorem duty on others. Fixed duties vary from \$3 to \$100 whereas ad valorem duties range from 0.1% to 3.75%.

In the case of conveyances of immovable property, the following duties are chargeable :-

- (1) a fixed duty of \$100 where sale price does not exceed \$1,000,000;
- (2) 0.75 per cent where the sale price exceeds \$1,000,000 but does not exceed \$2,000,000;
- (3) 1.5 per cent where the sale price exceeds \$2,000,000 but does not exceed \$3,000,000;
- (4) 2.25 per cent where the sale price exceeds \$3,000,000 but does not exceed \$4,000,000;
- (5) 3 per cent where the sale price exceeds \$4,000,000 but does not exceed \$6,000,000; or
- (6) 3.75 per cent where the sale price exceeds \$6,000,000.

There is provision for marginal relief at the commencement of the higher rates. With effect from 31 January 1992, stamp duty at the same rates as conveyances of immovable property is chargeable on agreements for the sale and the purchase of residential property. After the agreement has been so stamped, the related conveyance will be chargeable with a fixed stamp duty of \$100 only.

With effect from 1 April 1999, there are provisions for a dutypayer to apply for deferring payment of stamp duty on residential properties and certain uncompleted agreements are exempt from payment of stamp duty.

Leases granted in consideration of premium only attract the same duties as for conveyances of land. For leases granted in consideration of both premium and rent, the premium attracts an ad valorem duty of 3.75% while the rate of duty on rents varies with the period of the lease (from 0.25% to 1% of the annual rent).

Transactions in Hong Kong Stock require the preparation of contract notes on which buyers and sellers have each to pay ad valorem duty at the rate of 0.1% of the consideration.

In all cases, the Collector of Stamp Revenue is empowered to charge duty based on the market value of the property conveyed or shares transferred if he is of the opinion that the consideration is inadequate.

ESTATE DUTY

For persons who pass away on or after 1 April 1998, estates valued at \$7,500,000 or below are exempt from estate duty. The rate of duty is 5% for estates valued at over \$7,500,000 but not exceeding \$9,000,000. It rises to 10% for estates over \$9,000,000 but not exceeding \$10,500,000 and 15% for estates beyond \$10,500,000. There is a marginal relief at the commencement of each higher band. Assets situated outside Hong Kong are not subject to duty. In some countries, double taxation relief is granted for estate duty paid in Hong Kong.

BETTING DUTY

Duty is chargeable on bets on horse racing made on authorized totalizators or parimutuels, at 12% on standard bets which include win, place, double, quinella and quinella place and at 20% on extoic bets which include six-up, treble, tierce, trio, double trio and triple trio. Duty is also charged, at 30% on contributions or subscriptions to authorized cash sweeps and at 25% on bets made on lotteries conducted by the Hong Kong Lotteries Board. With effect from 18 July 2003, duty is charged at 50% on the net stake receipts from the conduct of authorized betting on football matches by an authorized company.

REGISTRATION OF BUSINESSES

Except for a limited number of exempt businesses (e.g. businesses carried on by charitable institutions), every person carrying on any business in Hong Kong must register his business within one month of the commencement of the business and pay the business registration fee AND the levy when required. The fee and levy payable for main/branch business registration certificates commencing on or after 1 April 2003 are as follows:-

1-Year Certificate

	<u>Fee</u>	<u>Levy</u>	<u>Total</u>
Main	\$2,000	\$600	\$2,600
Branch	\$73	\$600	\$673

3-Years Certificate

	<u>Fee</u>	<u>Levy</u>	<u>Total</u>
Main	\$5,200	\$1,800	\$7,000
Branch	\$189	\$1,800	\$1,989

Every company incorporated in Hong Kong under the Companies Ordinance and every overseas company which has established a place of business in Hong Kong is deemed to be a person carrying on business and is liable to be registered and pay the required fee & levy.

Excepting companies incorporated or registered under the Companies Ordinance, exemption from payment of the annual registration fee and levy for a very small business may be granted if its average monthly sales or receipts do not exceed the following limits: -

- For businesses deriving profits mainly from the sales of services \$10,000
- For other businesses \$30,000

An application for exemption will only be considered after the formal application for registration has been submitted. [For details, please refer to the leaflet titled “Application for Exemption of Business Registration Fee & Levy” (Form IRBR168).]

HOTEL ACCOMMODATION TAX

This tax is imposed on hotel and guest house accommodation and is levied on the accommodation charges paid by guests. The rate of tax is 3%.

EVASION OF TAX – A CRIMINAL OFFENCE

CONSEQUENCE OF INCORRECT RETURN

All tax returns contain a declaration to the effect that the information returned therein is true, correct and complete. Understatement/omission of profits or income or submission of false information constitutes an offence.

Submission of an incorrect tax return without reasonable excuse is an offence carrying a fine of \$10,000 and a further fine of treble the amount of tax which has been undercharged. The imposition of penalty may, however, be dealt with administratively by the Commissioner.

Submission of an incorrect tax return wilfully with intent to evade tax is a serious offence. On conviction, the maximum penalty is a fine of \$50,000 plus a further fine of treble the amount of tax undercharged and to imprisonment for 3 years. The Court of Appeal of the High Court has warned that a defendant, once convicted, may be liable to immediate custodial sentence.

ADVANCE RULINGS

A person may apply to the Commissioner, subject to payments and certain regulations, for a ruling on how any provision of the Inland Revenue Ordinance applies to him or the arrangement specified in the application.

FURTHER INFORMATION

If you need more information, please call our information hotline 187 8088, visit our web site: <http://www.info.gov.hk/ird> or e-mail to taxinfo@ird.gov.hk.

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