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AN INTRODUCTION TO

# Doing Business in Hong Kong 2023





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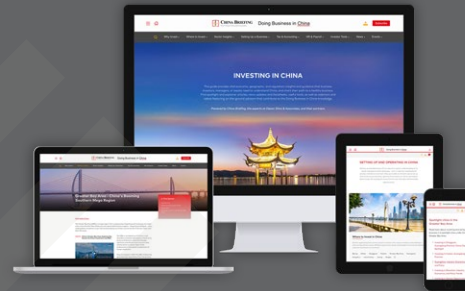
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This Investing Doing Business in Hong Kong guide was produced by a team of professionals at Dezan Shira & Associates, with Zhou Qian as technical editor, and Gigi Wong, Katrina Huang, and Sandy Zhang, and Jennifer Lu as contributors. Creative design of the guide was provided by Aparajita Zadoo.

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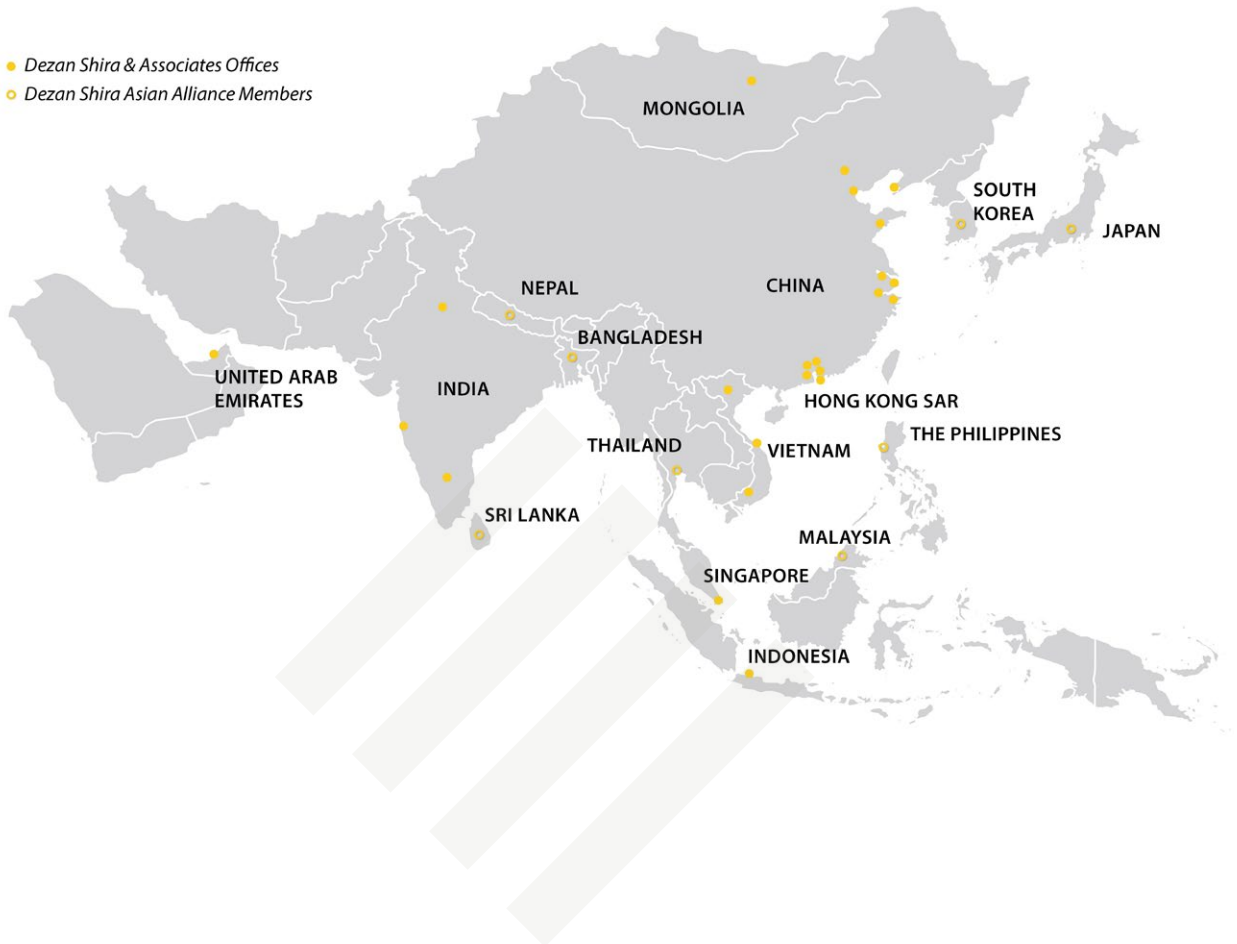
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## About Dezan Shira & Associates

Dezan Shira & Associates is a pan-Asia, multi-disciplinary professional services firm, providing legal, tax and operational advisory to international corporate investors. Operational throughout China, India, and ASEAN, 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. With more than two decades of on-the-ground experience and a large team of lawyers, tax experts, and auditors, in addition to researchers and business analysts, we are your partner for growth in Asia.



# Preface

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 from 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 served as a dominant “gateway” to the Chinese Mainland. Its geographical proximity to the Chinese mainland, low taxes, business-friendly environment, free flow of capital, rule of law, independent judiciary, and robust intellectual property protection have made it an ideal place for foreign investment. Despite the hardships of the pandemic, Hong Kong remains strong as ever and will continue to function as a free global financial hub, strengthened by the development of the Guangdong-Hong Kong-Macao Greater Bay Area (GBA).

This publication, designed to introduce the fundamentals of doing business in Hong Kong, was created in April 2023 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, as well as liaison offices in Italy, Germany and the United States, and partner firms across the ASEAN region. Dezan Shira & Associates' experienced business professionals are committed to improving the understanding and transparency of investing in emerging Asia.



**ALBERTO VETTORETTI**  
Managing Partner  
Dezan Shira & Associates



## CONTACT

**Dezan Shira & Associates**  
Hongkong@dezshira.com  
www.dezshira.com



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# What's New in This Guide?

Doing Business in Hong Kong 2023 introduces the fundamentals of investing in Hong Kong. Compiled by professionals at Dezan Shira & Associates in April 2023, this comprehensive guide is ideal for businesses looking to enter the Hong Kong market as well as companies who already have a presence there and want to stay updated with the most recent and relevant policy changes.

To be more specific, the below topics have been updated:

**Why Hong Kong:** We provide a comprehensive roundup of Hong Kong and discuss Hong Kong's key advantages as a dynamic investment gateway to the Chinese and Asia, including its business-friendly environment, low taxes, rule of law, free economy, independent judiciary, modern infrastructure, I&T capabilities, and robust intellectual property protection.

**Incorporation and business registration:** We include updates to the incorporation and business registration process, including changes in the business registration fee in 2023-24.

**The Companies (Amendment) Ordinance 2023:** We add a new section introducing the new Companies (Amendment) Ordinance 2023, which comes into operation on April 28, 2023. Fully virtual general meetings without the requirement for presence of members at any physical locations, as well as a mixed mode of such virtual general meetings and members attending at physical location(s), i.e., hybrid general meetings, are allowed under this regime.

**Taxes, audit, and accounting:** We update this chapter with the tax measures introduced in Hong Kong's 2023-24 Budget, including the reduction of profits tax, salaries tax, and tax under personal assessment for the year of assessment 2022/23. We also add a new section introducing Hong Kong's new rules on foreign source income exemption and amend the section on territorial source principle of taxation accordingly. Moreover, we introduce the application of the global minimum effective tax rate in Hong Kong.

**Human resources and payroll:** We update the calculation of salaries tax and amend the section on termination pay. We also briefly introduce the Employment and Retirement Schemes Legislation (Offsetting Arrangement) (Amendment) Bill 2022, which will be effective in 2025.

# Why Hong Kong?

A highly dynamic city that serves as a gateway to the Chinese Mainland and Asia, Hong Kong is the ideal base for your investment in Asia. Hong Kong's business-friendly environment, low taxes, rule of law, free economy, independent judiciary, modern infrastructure, I&T capabilities, and robust intellectual property protection allow businesses and individuals to succeed in this most competitive and international city.

## Why Choose Hong Kong for Your Business?



### Largely autonomous political system under the “One Country, Two systems”

Hong Kong is allowed to retain its capitalist economic system and own currency, legal system, legislative system, and governmental system for 50 years till 2047.



### Proximity to markets in Asia, including the Chinese Mainland

Hong Kong enjoys an ideal location in Asia that enables businesses to tap into the various opportunities in the Guangdong-Hong Kong-Macao GBA and throughout the rest of the region.



### Low, simple, and competitive tax regime

Hong Kong enjoys one of the most tax-friendly systems in the world. It adopts the territorial basis of taxation and does not have any turnover taxes, making it a favorable location for profit shifting and conducting re-invoicing.



### Open, fair, and efficient business environment

The absence of exchange controls, corruption-free government, free flow of information, capital, and talents, and low taxation has enabled Hong Kong to maintain a free and efficient environment for business activities and commerce.



### A leading international financial hub and a prime location for financial services

Hong Kong's financial markets operate under effective and transparent regulations that are in line with international standards.



### Excellent legal and dispute resolution services under rule of law

Hong Kong's strict maintenance of the rule of law and judiciary independence, its common law tradition, and its established English Chinese bilingual legal system has made it an ideal hub for dispute resolution worldwide.



### World-class infrastructure with sophisticated support services

Hong Kong provides some of the most advanced business infrastructure in the world. The city is easily accessible with efficient and affordable public transport systems.



### Improving data privacy protection

Hong Kong has been ramping up efforts to improve data privacy protection within its jurisdiction. The Personal Data (Privacy) Ordinance, Cap 486 was amended in 2021 to cope with new privacy challenges.



### Highly skilled and multicultural talent pool

Hong Kong has a diverse talent pool, equipped with the skills and knowledge to drive business in Hong Kong and beyond. The HKSAR government is also ramping up efforts in pooling more high-quality talents in 2023.



### Active participation in the global transition to a green economy

Hong Kong pledges to reach carbon neutrality by 2050. It has been trying to lead by example and making it easier for green bond issuers to come to Hong Kong to raise funds.



## Political system

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

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 separated from the one governing the PRC under the principle of “One Country, Two Systems.”

The PRC national laws will be applied to Hong Kong only if they are listed in Annex III to the Basic Law, after consultation with the Hong Kong Basic Law Committee. For example, in June 2020, the PRC Law on Safeguarding National Security in Hong Kong was added to Annex III.

## 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 the Chinese Mainland and other major economies in the Asia Pacific region.

The absence of exchange controls, corruption-free government, and free flow of information, capital, and talents has enabled Hong Kong to maintain a free and efficient business environment for business activities and commerce. Further, Hong Kong has a good reputation due to its “free port” and straightforward customs clearing procedure. The city has no tariffs on imported goods, no import quotas, no dumping tax laws, and applies excise duties on only four commodities – hard alcohol, tobacco, oil, and methyl alcohol. Moreover, Hong Kong does not impose taxes on dividends generated from doing business in the region.



Free trade and low taxation have helped Hong Kong become one of the world's freest economies and among the easiest places in the world to do business.

## 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), the Mandatory Provident Fund Schemes Authority (MPFA, a statutory body set up to assist Hong Kong's workforce to accumulate savings for their retirement), the Insurance Authority (IA, a body set up to protect the interests of policyholders and promotes the general stability of the insurance industry), 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 Hong Kong dollar printing privileges 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.

## Tax regime

Hong Kong offers one of the most tax-friendly systems in the world. It imposes only three kinds of direct taxes – profits tax (for incorporated body), salaries tax (for personal income), and property tax (for income sources from Hong Kong property). There are also generous allowances and deductions to reduce the burden of taxpayers.

Hong Kong does not have sales tax, value added tax, capital gain tax, estate tax, and tax on dividends, making it a favorable location for profit shifting and re-invoicing.

## Data privacy protection

Like other major economies, Hong Kong has been ramping up efforts on improving data privacy protection within the jurisdiction.

In Hong Kong, the Personal Data (Privacy) Ordinance, Cap 486 of the Laws of Hong Kong (PDPO) protects the privacy of individuals in relation to personal data, and was recently amended in 2021 to cope with new privacy challenges and address public concerns.





When the PDPO was drafted, reference was made to the relevant requirements under the 1980 OECD Privacy Guidelines and the European Union (EU) Directive 95/46/EC. It may be noted that the EU's GDPR, in effect since 2018, contains significant new regulatory provisions impacting data protection and introduced major changes to its 1995 Directive. However, these new requirements are not found under the PDPO.

## Geographical proximity to China and the Greater Bay Area

Hong Kong's geographic position enables businesses to easily tap into the various opportunities in the Guangdong-Hong Kong-Macao Greater Bay Area (GBA) and the Chinese Mainland market.

Hong Kong enjoys a highly active and cooperative business relationship with the Mainland. It is both the country's leading conduit for foreign investment and its primary offshore capital raising center – the city, as one of the world's largest IPO markets, is expected to attract more Chinese companies to list amid tensions between the US and China.

The Mainland and Hong Kong Closer Economic Partnership Agreement CEPA provides Hong Kong products and services easier access to the vast Mainland market. The CEPA goes beyond China's WTO commitments, eliminating tariffs and allowing earlier or preferential access to some services sectors. Overseas companies can also benefit from CEPA. For trade in goods, foreign investors can set up production lines in Hong Kong to produce goods that meet the CEPA rules of origin (ROO) requirements. For trade in services, companies incorporated in Hong Kong by foreign investors can make use of CEPA as long as they satisfy eligibility criteria of a "Hong Kong Service Supplier".

In the financial sector, Hong Kong and the Chinese Mainland have made remarkable progress in opening new channels to enhance their financial connectivity, such as establishing the Shanghai-Hong Kong Stock Connect, Shenzhen-Hong Kong Stock Connect and Bond Connect, Mainland-Hong Kong Mutual Recognition of Funds arrangement, and the two-way cross-boundary Wealth Management Connect in the GBA. Thus, Hong Kong's status as an international financial hub is expected to be further strengthened under the GBA development plan.

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## **Establishing and Running a Business**

- ◆ **What are my options for investment?**
- ◆ **How do I establish a business?**
- ◆ **What are the key compliance requirements?**
- ◆ **How do I make changes to my company?**
- ◆ **How do I deregister my company?**
- ◆ **How do I solve legal disputes?**



# What are my options for investment?

Foreign investors can carry on business in Hong Kong through multiple business vehicles, including:

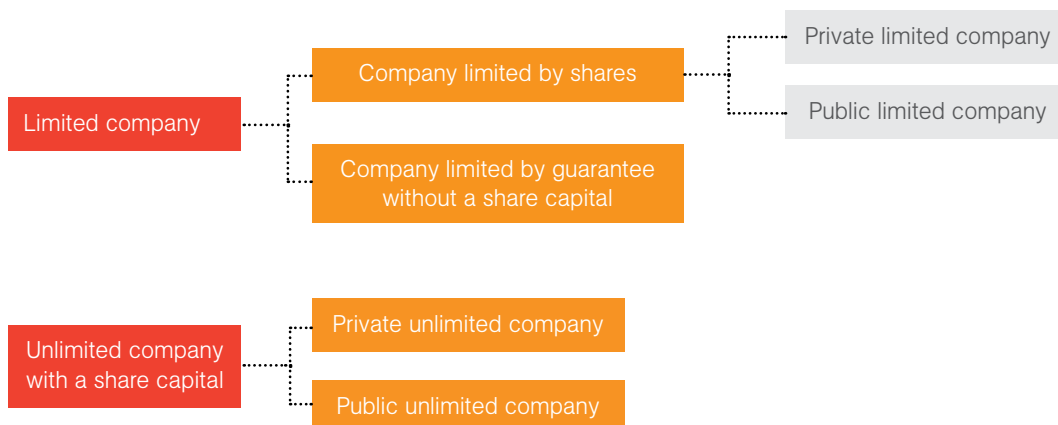
- A company incorporated in Hong Kong
- A branch office registered in Hong Kong of the foreign corporation
- A representative office established in Hong Kong
- Sole proprietorship
- Partnership

While some options are more commonly adopted than others, investors are advised to choose the most appropriate business structure based on the pros and cons of each option.

## Hong Kong companies

Foreign investors can establish their presence in Hong Kong by setting up a Hong Kong company. Companies incorporated in Hong Kong can be limited or unlimited and can be public or private. To be more detailed, there are five types of companies that may be formed under the Companies Ordinance (Cap. 622):

- Private companies limited by shares (private limited company)
- Public companies limited by shares (public limited company)
- Companies limited by guarantee without a share capital
- Private unlimited companies with a share capital (private unlimited company)
- Public unlimited companies with a share capital (public unlimited company)





**GIGI WONG**

Manager  
Business Advisory Services  
Hong Kong Office

**A company limited by guarantee** does not have share capital, but the liability of its members is limited by the amount of assets they have undertaken to contribute. This is the type of company that is most suitable for nonprofit activities, such as operating a nonprofit research institute. It is not a suitable structure for a business undertaken for profit making purposes.

**A company limited by shares** has a share capital that is divided into a number of shares. The shares are issued to shareholders and the liability of its shareholders will be limited to the unpaid subscription price for the shares. This is most suitable for a company that carries on a business for profit making purposes.

**A private limited company** is a company limited by shares which:

- restricts the ability of its members to transfer shares;
- limits the number of members to 50 (not including employees or former employees); and
- does not issue invitations to the public to subscribe for shares or debentures of the company.

It is the most dominant type of business entity in Hong Kong, accounting for 99 percent of all companies incorporated in Hong Kong. Most small to medium sized companies are set up as private limited companies due to its many advantages, such as its separate legal entity, its limited liability to members, its positive image among banks and investors, and the convenience of ownership transfer.

**A public limited company** is a company whose shares and debentures are offered to the public. If a company is a limited liability company but does not fall into the scope of a private limited company or a company limited by guarantee, then it is a public limited company. Many public companies are listed on the Stock Exchange of Hong Kong Limited and the statutory requirement for a public company is much stricter as it raises capital from the public. A medium to large private limited company may decide to transfer the company structure to that of a public limited company (and thereby expanding its share base) – when they achieve significant growth in the industry.

**An unlimited company** is one where the liability of its members is not limited. This business structure is rarely adopted by investors.

## Branch offices

A branch office has no separate legal identity and is treated as an extension of the overseas parent company in Hong Kong. As such, the overseas parent company is liable for all the debts and liabilities of the branch office.

A foreign corporation wishing to establish a Hong Kong branch office must register with the Companies Registry as a non-Hong Kong company and obtain a Business Registration Certificate.

*“The statutory requirement for a public company is much more stricter than for a private one. As such, for most purposes, the private limited company is the most popular option for foreign investors.”*

---

In general, branch offices of foreign companies registered in Hong Kong are subject to similar legal and tax requirements and consequences as companies incorporated in Hong Kong. The business activities that can be carried on in Hong Kong and the profit tax rate are the same for branch offices of foreign companies and locally incorporated companies.

While this option is generally not recommended for that parent company assumes larger liability for branch offices, foreign investors may prefer a branch over a subsidiary considering:

- A branch office might be more tax efficient for the parent company under certain circumstances, such as when losses incur in the Hong Kong branch.
- Generally, the transfer of the shares of a foreign company operating a branch in Hong Kong are not subject to stamp duty in Hong Kong.
- A branch office is subject to limited compliance requirements under the Companies Ordinance.
- A branch office is not required to conduct separate audit.
- A branch office can be terminated easily by notifying the Company Registry.

## Representative offices

Like a branch office, a representative office also has no separate legal identity, and the overseas parent company shall bear full responsibility for its debts and liabilities. Nevertheless, a representative office is not allowed to conduct any profit generating business activities (or else it is required to register as a branch office). It can only engage in promotion, liaison, and market research activities.


Representative offices need not be registered with the Companies Registry but are required to file for a Business Registration Certificate with the Inland Revenue Department.

Foreign investors who seek to study the market in Hong Kong may prefer representative offices over branches considering representative offices are exempted from filing profit tax returns if it does not conduct profit-generating businesses in Hong Kong.

## Sole proprietorship

A sole proprietorship is the easiest and simplest form of business that is owned and operated by a sole person. It has no separate legal identity, and the sole proprietor is entitled to all the profits from the business and is personally responsible for all the liabilities. The only procedural step in establishing a sole proprietorship is to obtain a Business Registration Certificate.

In addition to easy setup, the sole proprietorship has certain tax advantages. The sole proprietor can elect for “Personal Assessment” in their tax return filed for the tax year, so that the profits from the sole proprietorship will be assessed under the salaries tax scheme, which are subject



to generous allowance and deductions and the progressive rate of which may be lower than the corporate tax rate. Moreover, the business losses of the sole proprietorship can be offset against other income of the proprietor.

On the other hand, sole proprietorship is considered to be the riskiest business form as the sole proprietor shall bear joint liability for the debt that the business incurs. There is no protection of their personal assets. Thus, sole proprietorship is generally not recommended for investors.

## Partnership

Partnership is a form of business where two or more people carry on business in common with a view of sharing profits. There are two types of partnerships in Hong Kong—general partnership and limited partnership.

In a general partnership, the partners enjoy all the property rights and are personally liable to other partners' debts and obligations of the partnership. The only procedural step in establishing a partnership is to obtain a Business Registration Certificate.

In a limited partnership, there should be one or more general partners, who are responsible for the management of the partnership and liable for all its debt, and one or more limited partners, who are liable for the debts of the partnership within the amount they contribute to the capital of the partnership. A limited partner is not allowed to manage or control the partnership. A limited partnership is required to be registered with the Companies Registry and obtain a Business Registration Certificate.

Partnerships are generally easier to set up, maintain, and dissolve as compared to companies. There are fewer compliance requirements imposed on partnerships. Besides, partnerships might be more efficient in attracting talents as employees with skills, knowledges, and expertise have the chance to be promoted to partners.

## Restrictions on foreign investment

Hong Kong does not subject foreign investments to special regulatory regimes or requirements per se. However, on the basis of public interest, there are restrictions on voting control by non-Hong Kong residents and corporations in the broadcasting sector. Such restrictions are set out in the Broadcasting Ordinance (Cap. 562) and the Telecommunications Ordinance (Cap. 106). The government's special industrial-land policy features somewhat more complex rules, but it is still less demanding than the policies of many other Asian investment centers.

### • 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 5-10 percent;
- » Shareholding of 10-15 percent; or
- » Shareholding of over 15 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.



#### RELATED SERVICES

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 [hongkong@dezshira.com](mailto:hongkong@dezshira.com)



# How do I establish a business?

## Requirements and steps to set up a company in Hong Kong

For the purpose of this guide, we only introduce the setup requirements and process of a private limited company in this chapter, as it is the most popular option for foreign investors.

The registration of a company in Hong Kong usually starts with the creation of the company name and ends with the issue of a business registration certificate. During the whole process, there are mainly two government departments involved, namely the Companies Registry and Business Registration Office under Inland Revenue Department. The detailed procedures are set out below.

- **Step 1: Selecting a company name**

A company may be registered with an English name, a Chinese name, or an English and Chinese name. But a company name with a combination of English words/letters and Chinese characters are not allowed. Investors can look up whether the desired name already registered (or if there is a similar name already registered) in the Companies Registry. Also, the name may not infringe upon other parties' intellectual property rights. This can be searched on the website of the Intellectual Property Department. Moreover, a limited company must include the word "Limited" at the end of its name unless a special application is submitted for not including the word "limited" to the Companies Registry.

- **Step 2: Deciding the organizational structure, amount of capital, company secretary, and registered office address**

After selecting a company name, the investor should decide the member of the board of directors of the intended company. The first shareholder (i.e., founder member) should obtain a written consent from the director.

It should be noted that since March 3, 2014, all companies registered in Hong Kong should appoint at least one natural person to act as its director. However, there are no restrictions on the nationality of the director.

At the same time, the investor should determine the amount of capital and the number of shares to be issued to the first shareholder(s). The Companies Ordinance (Cap. 622) does not impose any restrictions on the minimum and maximum amounts of capital. It is the sole discretion of the investor to determine the amount of capital for the company based on the need of the operation and whether an extra license is required for the intended business activity. Since March 3, 2014, par values are not attached to shares. The Articles of Association ("AA") should only state the number of shares and the amount of capital. The investor should contribute whatever amount stated in the AA immediately after the company is registered.

The investor should also decide the company secretary, the designated representative of the significant controllers register, and address of the registered office before registration. If there are two or more directors, one of the directors could act as company secretary. However, if the investor will be the sole director of the intended company, another person should be appointed to act as company secretary. A written consent to act as company secretary should be obtained. The investor could also engage the service of a professional firm, duly registered in Hong Kong, to provide company secretarial service with a fixed annual fee.

#### **Requirements of Acting as Company Secretary and Designated Representative**

The secretary of a company may be:

- An individual - must ordinarily reside in Hong Kong; or
- A body corporate - must have its registered office or a place of business in Hong Kong.

A company's designated representative must be either:

- A director, employee, or member of the company who is a natural person resident in Hong Kong; or
- An accounting professional, a legal professional, or a person who possesses a Trust or Company Service Provider (TCSP) license.

The address of the registered office should be located in Hong Kong. There is not other particular limitation on the registered office address, but a postal box number cannot be used as registered office address of a Hong Kong company. If the founder does not plan to lease a physical office, he can utilize the service of a professional firm. But it should be ensured that the service provider must possess a TCSP license.

#### • **Step 3: Preparing registration documents and registering with the Companies Registry**

In this step, the investor should prepare the registration documents, including mainly the AA, the incorporation form, and a Notice to Business Registration Office, and submit the aforesaid documents to the Companies Registry for registration. At the same time, the investor should pay the application fee for incorporation and business registration fee and levy. The application fee for incorporation is HK\$1,720 (subject to a 10% reduction for incorporation through the "e-Registry" portal). The business registration and levy fee is HK\$2,150 for one-year certificate and HK\$5,650 for three-year certificate, in the period from April 1, 2023 onwards. Investors can choose to register for one year or three years. If the documents are prepared in accordance with the prevailing laws and regulations, the Companies Registry will issue the Certificate of Incorporation together with the Business Registration Certificate, which signifies that the company legally exists.

Generally, companies can be fully registered online if the founder members are individuals and the individual user accounts have been registered with the e-Registry, but investors can also file a paper company registration. Excluding the time needed to prepare the registration documents, the whole registration process will take one to five working days.

Note that some business activities may require additional permits, certificates, and approvals, the details of which can be checked on the Business License Information Service under the Trade and Industry Department.

- **Step 4: Making company chop and printing the AA (Optional)**

After the company is officially incorporated, the investor could find a service provider to make the company chop and print the AA. After March 3, 2014, the new Companies Ordinance (Cap. 622) has simplified the execution of documents by companies. It is now optional for companies to keep and use the common seal and the AA of the company can be in electronic form.

## Opening a bank account in Hong Kong

Opening a bank account in Hong Kong is often a vital first step to establishing business presence. However, many investors believe it is more difficult to open an account in Hong Kong now as compared to before. This is mostly because financial regulations have been tightened in order to combat the designation of the city as a tax heaven.

Common issues faced by investors relate to producing required documents and conditions on maintaining fixed deposits. For many banks, it is common to impose a monthly charge for failing to maintain a balance above a certain minimum amount.

It is therefore important for foreign investors to understand the procedures and documents required. The internal practices of the bank may vary from one to another, but generally the following procedures can be expected:

- Most banks will require an initial appointment, via phone, email, or physical visit;
- Following this, a preliminary review is usually conducted by phone interview, electronic questionnaires, or physical meeting with directors, or by sending supporting documents to bank manager;
- If the preliminary review is passed, both parties will meet to sign the relevant bank application forms and documents, as well as pay the initial deposit and application fee:
  - » Deposit differs according to the bank and is subject to change from time to time.
  - » Signatories also differ according to the bank and time. While some banks accept certified and true copy of shareholders' ID, others require the director/shareholder/ beneficial owner/ nominee to be physically present. In most cases, banks require the same number of people present as that forms quorum in a board meeting according to the AA to satisfy their Know Your Customer procedure.



**GIGI WONG**

Manager  
Business Advisory Services  
Hong Kong Office

- At this stage, the bank manager will send the application for the department review, which normally takes approximately one to two months. It is not uncommon for the review department to require further supporting documents before finally opening a new bank account on your behalf.

Generally, the following documents are required during the application:

- Company documents: Business Registration Certificate, Certificate of Incorporation, AA, and NNC1 form.
- Proof of business: Documents required varies from bank to bank, but generally include evidence of the nature of the business, experience in the industry etc. For example, issued/received invoices, business plan description, agreement with suppliers, bank reference letter, and website.
- Personal documents: Passport and residency proof (for example, utility bill, electricity bill, or bank statement which are issued within three months and include the holder's address and name).
- Source of Funds: The bank would ask for the source of fund of the investment to the Hong Kong company. For example, investor's bank statements.

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. To open a bank account for a shell company, 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.

## Virtual banks and money service operators

In addition to traditional banks, another emerging option is using virtual banks, which have no physical branches and focus on digital services. This concept is still very new to Hong Kong and for now, the HKMA only granted eight licenses for virtual banking.

These banks are a good alternative for tech-savvy people and remote operations. However, it should be noted that some banks are not yet offering corporate bank accounts, or cater only to Hong Kong residents.

Advantages of virtual banks include better rates and lower fees, integrations with enterprise software, a high set up convenience, and a heavy focus on small- and medium-sized enterprises (SMEs). Disadvantages include less personal relationship development, lack of ATM network, deposit inflexibility, and unavailability of specific services.

*“Companies that have a physical office or employee located in Hong Kong usually have a much higher chance of success.”*

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Another digital banking solution are money service operators. They usually offer services, such as dedicated payment instructions, the ability to receive money via domestic or international bank transfers, and linking to third party services or currency exchange.

For foreign SMEs operating in Hong Kong, virtual banks could offer a more convenient and cheaper service. This is particularly true for business owners who operate subsidiaries in Hong Kong that primarily function as holding companies. But it should be noted that the virtual banking industry is still very new and growing and as of now, not reliable enough for companies. Nevertheless, the market is expanding, and this might be a valuable option in the future.

## Gradual improvements to the banking environment

The HKMA has announced that it has taken steps to improve its internal banking environment – taking the time to engage with various stakeholders to gather details of specific incidents relating to difficulties around bank account opening.

As a result, the HKMA has cautioned financial institution against a one-size-fits-all approach and encouraged them to take a risk-based approach that differentiates the “risk levels of individual customers in accordance with their backgrounds and circumstances”.

The situation is improving, but there is still a long way to go. Hong Kong needs to continue to ease its administrative red-tape in order to stay competitive with other international financial hubs in the region, such as Singapore – which like Hong Kong, serves as a financial gateway to Asia, but benefits from a more relaxed banking environment for foreign businesses.

## Intellectual property


Hong Kong offers a high level of protection for intellectual property (IP), ranking 16<sup>th</sup> according to the Intellectual Property Rights Index 2022. It is also a major global IP trading hub. Hong Kong recognizes several different classes of IP, including trademarks, patents, designs, copyright, trade secrets, plant variations, domain names, and lay-out designs of integrated circuits.

### Registering a trademark

For the benefits of a registered trademark, an application for registration must be made to the Trade Marks Registry, Intellectual Property Department (IPD). Registration only covers the territory of the Hong Kong SAR. Registration of a trademark in Hong Kong does not affect the Chinese Mainland, and vice versa.

To register a trademark in Hong Kong, the investor should first investigate whether the trademark is already registered. This can be done online on the Trademark Online Search System (<https://esearch.ipd.gov.hk/nis-pos-view/#/>). The investor can also use the Search and Preliminary





Advice services provided by the Trade Marks Registry by simply completing Forms T1 and submitting the appropriate fee.

If the trademark is available, the application to register a trademark can be made online through the IPD Electronic Filing Services, or it can be filed physically with the Trade Marks Registry by filling Form T2, with a graphic representation of the trademark attached.

After filing, the Trade Mark Registry will examine whether the application meets the requirements laid out in the Trade Marks Ordinance (Cap. 559) and the Trade Mark Rules (Cap. 559A), including the following:

- The trademark needs to be distinctive;
- It cannot be a description of the goods or services the investor is providing or seeking to provide;
- It cannot be an industry or business term; and
- The trademark has not been registered or applied for by another trader.

Provided that the application is complete and correct, the trademark registration can be completed within six months, upon which it will be published in the Hong Kong Intellectual Property Journal. If the IPD objects the registration, it will notify the investor in writing. The applicant will have six months to ratify the application. A further period of three months extension may be granted.


## Registering a patent

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

Hong Kong has two types of patents: standard and short-term. Protection under standard patents is renewable annually after the end of the first third year, for a maximum of 20 years. Protection under short-term patents is renewable after four years from first filing, for a maximum term of eight years.

Applying for a patent elsewhere in the world or in other regions of China does not automatically give you protection in Hong Kong. Investors need to file an application with the Patents Registry of the IPD, which conducts only a formal examination of the patent paperwork. However, in order to be granted an effective patent in Hong Kong, the investor must have first registered the patent in one of three designated patent offices - the State Intellectual Property Office of the PRC, the European Patent Office, or the United Kingdom Patent Office.

The application for a standard patent goes through two phases. The first phase is to file a request to record the existing patent (either from the Chinese Mainland, the EU, or the United Kingdom). This needs to be done within six months after the designated patent application. Within two months after the request, the IPD will give the applicant notice of any issues with



the application. If there are no issues, or if these have been corrected, the request will be published in the Hong Kong Intellectual Property Journal. The second phase is to file a request for registration and grant of the Chinese, European, or UK granted patent in Hong Kong, which should be conducted within six months after publication of the request to record, or the grant of the patent by the designated patent office.

The grant of a short-term patent is based on a search report from an international searching authority or one of three designated patent offices. The application for a short-term patent only needs to be submitted once and there is generally no time limit for filing. But if the applicant wishes to claim priority from a first application in a Paris Convention country or World Trade Organization member territory, the short-term patent application should be filed in the Hong Kong SAR within 12 months of filing the first application. Within two months after the submission of the application, the IPD will examine the application and give the applicant notice to correct any issues. If there is no issue or the issues are corrected, a short-term patent for the invention will be granted and published in the Hong Kong Intellectual Property Journal.

## Registering a design

The Registered Design Ordinance (Cap. 522) defines designs 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”.

Registered designs protect only the appearance of products, for example the look of a computer monitor. Registration of the design does not protect the way in which the product relating to the design works.

Designs can be registered and protected if the designer can show that they are new at the filing date of the application, or the priority date (if claimed). A design is new if it has not been previously registered, or has never been published or disclosed before. 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 of IPD will publish the registration in the Hong Kong Intellectual Property Journal. The design will be protected for a maximum of 25 years from the filing date, and needs to be renewed every five years.



## Copyright

Unlike the other IP 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 the following:

- Literary, dramatic, musical, or artistic work;
- Sound recordings, films, broadcasts, or cable programs; and
- 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; and
- 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 threshold to prove a copyright infringement is also higher than for a registered design. 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.

# What are the key compliance requirements?

## Annual compliance requirements

A company is a separate legal entity, that is to say, it is a legal person in its own right and separate from its owners. The benefit of limited liability through operating as a limited company also brings with it obligations in so much as the company must comply with the various provisions in the Companies Ordinance (Cap. 622).

These obligations include the timely disclosure and reporting of specified information about the company, its officers and shareholders, etc. and any changes in such information to the Registrar of Companies so that members of the public can have ready access to the latest information of the company kept by the Registrar of Companies.

Basically, annual compliance of a Hong Kong company includes:

- Filing of annual return;
- Renewal of business registration;
- Holding of annual general meeting;
- Appointment of auditor;
- Arrangement of audited financial statements; and
- Update of changes of company particulars/structure with Companies Registry.

## New regime of significant controller register

Under the Companies (Amendment) Ordinance 2018 (“the Amendment Ordinance”), all companies incorporated in Hong Kong (except listed companies) need to comply with the significant controllers register requirements starting from March 1, 2018.

Some of the key requirements prescribed by the Amendment Ordinance include:

- Identify and ascertain a person/ persons who has / have significant control over the company;
- Maintain a significant controllers register to be accessible by law enforcement officers upon demand;
- Designate at least one person as its representative to provide assistance relating to the company’s significant controllers register to the law enforcement officers;
- Keep the significant controllers register at the company’s registered office or a prescribed place in Hong Kong; and
- Keep the significant controllers register updated.

Failure to comply with the significant controllers register requirements set forward in the Amendment Ordinance could qualify as a criminal offense. The company and every responsible person in breach of the Amendment Ordinance could liable for a fine levied at HK\$25,000, and where applicable, a further daily fine.

A significant controller is a person or legal entity who meets one or more of the following conditions:

- Holds, directly or indirectly, more than 25 percent of the company's issued shares or a right to share more than 25 percent of the capital or profits of the company;
- Holds, directly or indirectly, more than 25 percent of the voting rights of the company;
- Holds, directly or indirectly, the right to appoint or remove the majority of the board of directors of the company;
- Has the right to exercise, or actually exercises, significant influence or control over the company; or
- Has the right to exercise, or actually exercises, significant influence or control over the activities of a trust or a firm that is not a legal person, but whose trustees or members satisfy any of the above four conditions in relation to the company.

To identify a significant controller, companies can review their register of members, articles of association, shareholders agreements or other relevant agreements, and issue notice(s) to any person who is believed to be the significant controller and any person who is believed to know the identity of the significant controller and obtain their required particulars.

## **Compliance of anti-money laundering and counter-terrorist financing requirements for trust or company service providers**

According to the Anti-Money Laundering and Counter-Terrorist Financing Ordinance Ordinance (Cap. 615) (AMLO) issued by the Companies Registrar, starting from March 1, 2018, person carries on trust or company services are required to possess a TCSP license.

In general, TCSP licensees are required to:

- Take all reasonable measures to mitigate the risk of money laundering and terrorist financing; and
- Ensure that, among other things, the anti-money laundering and counter-terrorist financing requirements under the AMLO are complied with.

To fulfil the above-mentioned obligations, TCSP licensees must assess the money laundering and terrorist financing risk of their businesses, develop, and implement policies and procedures on:

- Risk assessment;
- Customer due diligence measures;
- Ongoing monitoring of customers;
- Suspicious transactions reporting;
- Record keeping; and
- Staff training.

Accordingly, companies are required to provide the due diligence documents to the service provider (TCSP licensee) due to this new requirement.



## New inspection regime

A new inspection regime is being implemented under the Hong Kong Companies Ordinance (Cap. 622), which provides additional protection to the personal information of directors and other relevant individuals who appear on the Companies Register.

Under the new inspection regime, (a) correspondence addresses instead of usual residential addresses (URAs) of directors and (b) partial identification numbers (IDNs) instead of full IDNs of directors, company secretaries, and other relevant persons like liquidators, will be made available on the Companies Register for public inspection.

Meanwhile, companies can withhold the URAs and full IDNs (except the first part) on the registers where the information is maintained from public inspection. (The first part of the IDN is decided by an established rule, which is usually the first half of the sequence number if the IDN is an even number, or the part that begins with the first character in the sequence and ends with the character that falls on the middle of the sequence if the IDN is an odd number.) The URAs and full IDNs are regarded as “Protected Information” under the new inspection regime. Previously, the URAs and full IDNs of any company’s director, company secretaries, or other relevant persons could be accessed by the public.

By replacing URAs and full IDNs with correspondence addresses and partial IDNs, the protection of personal information will be enhanced. At the same time, it will ensure the transparency of the Companies Register by allowing the public to access it for the purposes stipulated under the Companies Ordinance (Cap. 622).

Since substantial modifications are being made to the integrated Companies Registry Information System (“ICRIS”), the new inspection regime will be implemented in three phases. The respective commencement dates of each phase are August 23, 2021 (phase 1); October 24, 2022 (phase 2); and December 27, 2023 (phase 3).

Under **phase 1**, companies may replace URAs of directors with correspondence addresses and full IDNs of directors and company secretaries with their partial IDNs on their own registers for public inspection.

Under **phase 2**, Protected Information on the Index of Directors on the Companies Register will be replaced with correspondence addresses and partial IDNs for public inspection. Documents containing Protected Information that are filed for registration – after the commencement of this phase, i.e., October 24, 2022 – will not be provided for public inspection, except for “specified persons” upon application.

Under **phase 3**, data subjects (i.e., individuals whose URA and full IDNs are contained in documents filed with the Companies Registry before the new inspection regime’s commencement) can apply to the Companies Registry for withholding their Protected

Information contained in documents registered with the Companies Registry from public inspection and replace such information with their correspondence addresses and partial IDNs. Same as phase 2, only specified persons can apply to the Registry for access to the Protected Information of directors and other persons.

To meet the requirements of this new regime, and if data subjects and Hong Kong registered companies want to withhold their Protected Information from public inspection, they should contact their service provider to update their personal information accordingly and make corresponding applications.

### **The Companies (Amendment) Ordinance 2023**

The Companies (Amendment) Ordinance 2023 (“the Amendment Ordinance”) comes into operation on April 28, 2023.

The Companies Ordinance (Cap. 622) provides that a company must hold an annual general meeting within the prescribed time. A company may also hold a general meeting out of its own initiatives from time to time as necessary. The manner of holding a general meeting is governed by the provisions in the Companies Ordinance (Cap. 622) and the Companies (Model Articles) Notice (Cap. 622H) as well as provisions of the company’s own AA.

The Amendment Ordinance seeks to modernize the Companies Ordinance (Cap. 622) and the Companies (Model Articles) Notice (Cap. 622H) to expressly cater for the scenario of companies holding fully virtual general meetings without the requirement for presence of members at any physical locations, as well as a mixed mode of such virtual general meetings and members attending at physical location(s), i.e., hybrid general meetings.



#### **RELATED SERVICES**

Dezan Shira & Associates provides compliance assistance to foreign companies operating in Hong Kong. For more information, please contact our experts at [hongkong@dezshira.com](mailto:hongkong@dezshira.com).

# How do I make changes to my company?

## Dormant company

A dormant company is a company that has no significant accounting transactions during a fiscal year. “Accounting transaction”, in relation to a company, means a transaction that is required to be entered in the company’s accounting records, excluding a transaction arising from the payment of any fee that the company is required by an Ordinance to pay.

A company can become dormant when it passes a special resolution (resolution approved by at least 75 percent of shareholders), and the resolution is delivered to the Registrar of Companies.

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

- Hold annual general meetings;
- Deliver annual returns\*;
- Prepare financial statements and Directors’ Reports;
- Appoint auditors and undergo annual audits; or
- Publish financial statements to the shareholders before general meetings.

Despite all the benefits, a dormant company still needs to maintain a registered office, corporate secretary, designated representative of significant controller(s), fulfill annual business registration, and comply with the taxation requirements of the Inland Revenue Department.


A company ceased to be dormant if the company passes a special resolution declaring that the company intends to enter into an accounting transaction and the resolution is delivered to the Registrar of Companies or there is an accounting transaction in relation to the company.

## Changing a company name

To change the company name, the company needs to pass a special resolution, a resolution that is passed by a majority of at least 75 percent. The special resolution and the AA as altered need not be delivered to the Companies Registry, but a “Notice of Change of Company Name” (Form NNC2) should be filled and delivered within 15 days after the passing of the special resolution together with the required fee (HK\$295) either electronically through the “e-Registry” portal ([www.eregistry.gov.hk](http://www.eregistry.gov.hk)) or in hard copy form to the Shroff on the 14<sup>th</sup> floor of the Queensway Government Offices.

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\* However, a private company is still required to deliver an annual return for the year in which it declares itself to be dormant if the effective date on which the company becomes dormant falls after the 42<sup>nd</sup> day after the anniversary of its date of incorporation.



Electronic Certificate of Change of Name will normally be issued within an hour by email. But if the Form NNC2 is delivered in hard copy, the Certificate of Change of Name will normally be issued within four working days, and has to be collected in person. The change of name will be effective from the date on which the Certificate of Change of Name is issued.

Please note that the intended company name should not be the same as or too similar to a name appearing in the index of company names kept by the Registrar of Companies, or in conflict with a trademark in the Trademark Register maintained by the Intellectual Property Department. Or else the change may be rejected by the Registrar, or the company may be subject to a change of name direction by the Companies Registry after change of name.

## Changing the company's Articles of Association

A company may alter most of its AA except:

- Articles on the liability of its members as stated in Section 83 and 84(1) of the Companies Ordinance (Cap. 622);
- Articles that are inconsistent with any rights attached to shares in a class of shares (for company with shared capital) or any rights of a class of members (for company without a share capital); and
- Articles related to the contributions of members of a company limited by guarantee under Section 84(2) of the Companies Ordinance (Cap. 622) other than to increase the specified amount.

Under most circumstances, the alteration of the AA can only be done by passing a special resolution. However, an alteration in articles to the maximum number of shares that the company may issue may be made by ordinary resolution.

Within 15 days after the alteration is made, the following documents are required to be delivered to the Companies Registry:

- A copy of the special resolution for alteration of the AA;
- A notice of alteration in the relevant specified forms, namely Forms NAA1, NAA2, NAA3, or NAA4;
- A certified copy of the AA as altered (for Forms NAA1, NAA2, and NAA3); and
- Other relevant documents required to be delivered with the specified forms for registration as appropriate.

To be noted, the holders of at least five percent of the shares or five percent of the company's members can appeal to the court to cancel an alteration of the objects of a company.

# How do I deregister my company?

A private company or a company limited by guarantee, other than those companies specified in Section 749(2) of the Companies Ordinance (Cap. 622), may apply for deregistration when it is defunct. To do so, the following conditions need to be met:

- All shareholders agree to the deregistration;
- The company has not yet commenced operations or business, or has ceased operations or business during the three months before the application;
- The company has no outstanding liabilities;
- The company is not involved in any ongoing legal proceedings;
- The company holds no assets consisting of any immovable property situated in Hong Kong; and
- If the company is a holding company, its subsidiaries' assets do not consist of immovable property situated in Hong Kong.

Before the company can be deregistered, it first needs to obtain a letter of “Notice of No Objection to a Company being Deregistered” (Notice of No Objection) from the Commissioner of Inland Revenue Department (IRD), the Hong Kong tax office. Directors and shareholders, or a person authorized by the company, can apply for such a letter. To apply for this letter, the applicant has to fill in a form, retrievable from the tax office website, and pay a prescribed fee.

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 Gazette on the website of the Government Logistics Department. If no objections are made within the following three months – such as by alleged creditors – the Registrar may deregister the company by publishing in the Gazette another notice declaring it to be deregistered on the date of publication of that other notice.

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

## Deregister a Company in Hong Kong



**1** Assess whether the Company fulfils the conditions of deregistration



**2** Confirm the date of cessation of business, if applicable



**3** Preparation of last audit, if applicable  
*Lead time: case by case*



**4** Confirmation of tax clearance with the IRD  
*Lead time: case by case*



**5** Application of Notice of No Objection to a Company Being Deregistered with the IRD –  
*Lead time: around 1 month*



**6** Application of deregistration with the Companies Registry –  
*Lead time: around 1 month*



**7** Publication of Gazette for the proposed deregistration  
*Lead Time: 5 months*



**8** Officially dissolved by deregistration

# How do I solve legal disputes?

Located in the center of Asia, Hong Kong prides itself as an ideal location for dispute resolution not only in Asia, but also worldwide. Given its geographic and economic proximity to the Chinese Mainland, Hong Kong acts as a bridge for cross-border disputes that involve this region. Thanks to Hong Kong's reputation for its strict maintenance of the rule of law and judiciary independence, its common law tradition, and its established English-Chinese bilingual legal system, Hong Kong has also become an ideal hub to resolve international disputes for foreign investors doing business in Hong Kong.

Below we introduce the common dispute resolution methods in Hong Kong.

## Alternative Dispute Resolution (ADR)

Alternative Dispute Resolution (ADR) is a voluntary and private dispute resolution process in which the parties agree to appoint a neutral third party to assist them to settle or resolve their dispute.

Under the new High Court and District Court rules, which came into effect on April 2, 2009, the courts are required to actively manage cases and facilitating dispute resolution. Such case management includes, where appropriate, encouraging the parties to use procedures alternative to litigation to resolve their dispute, i.e., ADR.

ADR has certain advantages over litigation. In addition to cost and time saving, parties have more control over how the dispute is solved. Because of its confidential nature, it can sometimes preserve business relationship between the disputed parties. Unlike litigation in open courts, trade terms are not disclosed to the public.

Mediation and arbitration are the most commonly used forms of ADR.

### Mediation

Mediation is a voluntary, confidential, and private dispute resolution process in which a neutral person, the mediator, helps the parties to reach their own negotiated settlement agreement. The mediator has no power to impose a settlement, other than the power of persuasion. A successful mediation results in an agreement signed by the parties. Despite being widely supported and recognized as having the potential to resolve disputes in a quick, cheap, and confidential way, mediation remains under-utilized when compared to arbitration.

### Arbitration

Arbitration is a private process where disputing parties agree that one or several individuals can make a binding decision about the dispute after receiving evidence and hearing arguments. In an arbitration, the arbitrator investigates the legal rights and wrongs of a dispute and makes a decision. Once the arbitrator has arrived at a decision, it is binding on parties, whether they agree with it or not. This is how arbitration is different from mediation.



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Arbitration is very much like the way a court case is decided by a judge, except that the process does not take place in a court room, and it is not open to the public.

As a leading seat of arbitration, Hong Kong maintains several the world's top arbitral institutions, such as:

- Hong Kong International Arbitration Centre (HKIAC);
- The International Court of Arbitration of the International Chamber of Commerce (ICC-ICA);
- China International Economic and Trade Arbitration Commission (CIETAC);
- China Maritime Arbitration Commission (CMAC);
- Permanent Court of Arbitration (PCA); and
- The Hong Kong Maritime Arbitration Group (HKMAG).

For parties who wish to commence an arbitration to resolve disputes, there must be a valid arbitration agreement, and as an arbitration friendly jurisdiction, Hong Kong adopts a broad definition of what constitutes a valid arbitration agreement. It could be a clause in the main contract, or a separate agreement made prior to or after the dispute happens. Among others, an arbitration agreement should set out how a party commences arbitration and the procedural guidelines of the arbitration. It must be made in writing or recorded in any written form to be enforceable in Hong Kong.

Arbitral awards made in Hong Kong can be enforced in all state parties to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Besides, in order to complete the network for recognition and enforcement of arbitral awards, the HKSAR has respectively entered into reciprocal arrangements with the Mainland and the Macao SAR. In 2019, HKSAR and the Chinese Mainland, signed the *Arrangement Concerning Mutual Assistance in Court-ordered Interim Measures in Aid of Arbitral Proceedings by the Courts of the Mainland and of the Hong Kong Special Administrative Region*, according to which parties to arbitral proceedings seated in the HKSAR and administered by designated arbitral institutions may apply to the Mainland courts for interim measures, including property preservation, evidence preservation, and conduct preservation. Notably, Hong Kong has become the first jurisdiction outside the Chinese Mainland where, as a seat of arbitration, parties to arbitral proceedings administered by its arbitral institutions would be able to apply to the Mainland courts for interim measures.

## Litigation

Court litigation is the traditional legal dispute resolution method, commonly adopted in Hong Kong. Generally, people have no preference between litigation and arbitration, rather, they choose the best dispute resolution method based on a particular scenario. For example, litigation is usually preferred in insolvent related cases, intra-company dispute, debt enforcement, as well as cases where the enforcement is anticipated to be problematic because the counterparty is not located in an arbitration-friendly jurisdiction.

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With a legal system that is based on common law, the litigation process in Hong Kong is generally an adversarial one, during which opposing parties act as adversaries seeking to convince the court or tribunal that their version of events or their legal submissions should prevail over those of the other side. This provides international parties with the familiarity of a legal system.

Civil procedures are mostly governed by legislation, including the High Court Ordinance and Rules of the High Court, the District Court Ordinance, and Rules of the District Court.

To commence litigation in Hong Kong, the party has first to identify the appropriate court, based on the nature and amount of the claim. For commercial disputes, it would often be the District Court or the Court of First Instance of the High Court, in which a party would commence an action. In addition to the above, complicated commercial cases (e.g., construction of mercantile documents, export or import of the merchandise, insurance, banking, etc.) will be directed by the court to the Commercial List, which is developed by the Chief Justice to facilitate the disposal of actions involving commercial matters. The matters are heard before a Commercial List judge, most of whom have expertise in commercial disputes and are bilingual so that they can understand the complexity of the case in both Chinese and English. Corporate insolvency and shareholder disputes are generally handled in an informal 'companies' list headed by a judge experienced in such matters.

The courts follow the doctrine of precedents, by which a lower court is bound to follow the *ratio decidendi* (i.e. the legal precept applied by the Court in resolving the issues before the Court) of a judgment by a superior court. Court decisions are generally made public and accessible online via the Judiciary's website at [https://www.judiciary.hk/en/judgments\\_legal\\_reference/judgments.html](https://www.judiciary.hk/en/judgments_legal_reference/judgments.html).

If an applicant succeeds in his application for judicial review, the Court has the discretionary power to grant a form of final relief appropriate to the circumstances, including an order of *mandamus* (to perform an act), prohibition, or *certiorari* (to bring up and quash a decision), an injunction, a declaration (as to legal rights), or an award of damages, as the case may be.

Subject to relevant law and procedures, appeals from decisions of the Court of First Instance in civil proceedings can be brought to the Court of Appeal and the Court of Final Appeal, which is the apex of the Court system. The Court of Final Appeal is vested with the "power of final adjudication" by the Basic Law.

As for enforcement outside Hong Kong, the Supreme People's Court of China and the Department of Justice at Hong Kong SAR have signed the Arrangement between Mainland and the HKSAR on Reciprocal Recognition and Enforcement of the Decisions of Civil and Commercial Cases under Consensual Jurisdiction (the Arrangement) on January 18, 2019. The Arrangement makes provisions about the scope, procedures, and means of reciprocal recognition and enforcement of court decisions on civil and commercial cases. At the time of writing, the Arrangement has yet to become effective.

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# Tax, Audit, and Accounting

- ◆ What are the major taxes in Hong Kong?
- ◆ What are the key compliance requirements?
- ◆ International taxation

# What are the major taxes in Hong Kong?



**JENNIFER LU**  
Director  
Hong Kong Office

According to the Basic Law of Hong Kong, the taxation system of the Chinese Mainland is not applicable to Hong Kong, which essentially means that Hong Kong enjoys an independent taxation system. Because the city only imposes three direct taxes, Hong Kong has one of the simplest tax systems 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 various business activities. In this part of the guide, we first introduce the unique features of Hong Kong'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 (IRD). The tax assessment year usually runs from April 1 to March 31 each year. A company may also choose its fiscal year at its own discretion.

*“Hong Kong doesn't have any turnover taxes, including sales tax or value added tax, making it a favorable location for various business activities.”*

## Key features of Hong Kong's taxation system

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. That said, some foreign source income could be regarded as arising or derived from Hong Kong, under the 2022 amendment of the Inland Revenue Ordinance in relation to the foreign source income exemption (FSIE) standard.

Besides, there is no comprehensive system of income taxation in Hong Kong. Instead, a taxpayer is liable for 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

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 the tax reduction, subject to a maximum.

NET CHARGEABLE INCOME = TOTAL INCOME - DEDUCTIONS - ALLOWANCES

NET INCOME = TOTAL INCOME - DEDUCTIONS

<b>Tax Rates</b>		
<b>Progressive rates (Year of Assessment 2018/19 onwards)</b>		
<b>Net chargeable income (HK\$)</b>	<b>Rate</b>	<b>Tax (HK\$)</b>
On the first 50,000	2%	1000
On the next 50,000	6%	3,000
On the next 50,000	10%	5,000
On the next 50,000	14%	7,000
Remainder	17%	

<b>Standard rate of tax (year of assessment 2017/18 onwards)</b>
15%

<b>Allowance</b>	
<b>Year of assessment 2023/24 onwards, in HK\$</b>	
Basic allowance	132,000
Married person's allowance	264,000
Child allowance (For each of the 1 <sup>st</sup> to 9 <sup>th</sup> child)	130,000
For each child born during the year, the child allowance will be increased by	130,000
Dependent brother or sister allowance (for each dependent)	37,500
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	50,000
» Parent/grandparent between the age of 55 to 60	25,000
<b>Additional dependent and dependent grandparent allowance</b>	
» Parent/grandparent aged 60 or above or is eligible to claim an allowance under the Government's Disability Allowance Scheme	50,000
» Parent/grandparent between the age of 55 to 60	25,000
Single parent allowance	132,000
Disabled dependent allowance (for each dependent)	75,000
Personal disability allowance	75,000

<b>Deductions (Maximum Limits)</b>	
<b>Year of assessment 2023/24 onwards, in HK\$</b>	
Expenses of self-education	100,000
Elderly residential care expense	100,000
Home loan interest	100,000
Mandatory contribution to recognized retirement schemes	18,000
Approved charitable donations (income - allowable expenses - depreciation allowance) x percentage	35%
Qualifying premiums paid under Voluntary Health Insurance Scheme (VHIS) policy (for each insured person)	8,000
Qualifying annuity premiums and tax deductible MPF voluntary contributions	60,000
Domestic rent deduction*	100,000

## Maximum tax reductions

Salaries tax for the year of assessment 2022/23\* is further reduced by a one-off tax reduction of 100 percent, subject to a ceiling of HK\$6,000 per case. For single taxpayers, the ceiling is applied to each individual; for couples jointly assessed, the ceiling is applied to each married couple (that is, capped at HK\$6,000 in total). Married persons may elect personal assessment separately to reduce tax liability.

The tax reduction will only be applicable to the final tax for the year of assessment 2022/23, but not to the provisional tax of the same year. Therefore, taxpayers are still required to pay their provisional tax on time despite the reduction measure.

## Provisional salaries tax

Salaries tax is chargeable on the assessable income for each year of assessment. As the assessable income for any particular year cannot be known until after the end of the year concerned, a provisional tax charge has to be raised. When the assessable income for the year of assessment is subsequently ascertained, an assessment will be made and the provisional salaries tax paid will be utilized to offset the tax liability under the assessment.

The tax payer can apply in writing for holding over of the whole or part of the provisional salaries tax on the grounds as specified in the Inland Revenue Ordinance (Cap. 112).

\*Legislative amendments are required for implementing the tax measures as proposed by the Financial Secretary in the 2023-24 Budget.

## Profits 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 arising in or derived from Hong Kong (excluding profits arising from the sale of capital assets). Profits tax is levied based on assessable profits, which is determined by excluding deductions and tax-exempt incomes. It is further reduced by the tax reduction, subject to a maximum.

### Profits tax rate

#### Normal rate

Generally, profits earned by a corporation are taxed at a standard rate of 16.5 percent, while profits earned by unincorporated businesses are taxed at a standard rate of 15 percent.

Starting from the year of assessment 2018/19, the two-tiered profits tax regime has been introduced, which lowers the tax rate for the first HK\$2 million of assessable profits.

Two-Tiered Profits Tax Rates in Hong Kong		
Assessable profits	Corporations	Unincorporated businesses
First HK\$2 million	8.25%	7.5%
Over HK\$2 million	16.5%	15%

Under the two-tiered tax regime, the first HK\$2 million of profits earned by a corporation will be taxed at 8.25 percent. The remaining profits will continue to be taxed at the existing 16.5 percent tax rate. For unincorporated businesses, the first HK\$2 million of profits earned will be taxed at 7.5 percent. The remaining profits thereafter will be taxed at the existing 15 percent tax rate.

However, for two or more connected entities, only one of them may elect the two-tiered profits tax rates. The rest of the entities shall still be taxed at 16.5 percent for corporations and 15 percent for incorporated businesses.

In order to avoid double benefits, enterprises that already benefit from preferential tax regimes, such as the corporate treasury center regime, aircraft leasing regime, etc. shall be excluded from the two-tiered profits tax regime.

Additionally, the assessable profits for sums received by or accrued to holders of qualifying debt instruments as interest, gains, or profits shall be excluded, as these should already be taxed at half the rate (8.25 percent or 7.5 percent, as the case may be).



## Concessionary rate

A tax rate at 50 percent of the normal profits tax rate will be applied to:

- trading profits and interest income received or derived from “short / medium term debt instruments” (issued before 1 April 2018);
- qualifying profits of a qualifying corporate treasury centre (for the year of assessment 2016/17 onwards);
- qualifying profits of a qualifying aircraft lessor or a qualifying aircraft leasing manager (for the year of assessment 2017/18 onwards);
- qualifying profits of a professional reinsurer or authorized captive insurer (for the year of assessment 2018/19 onwards);
- qualifying profits of a specified insurer or licensed insurance broker company (for the year of assessment 2020/21 onwards); and
- qualifying profits of a qualifying ship lessor or a qualifying ship leasing manager (for the year of assessment 2020/21 onwards).

A profits tax rate at 0 percent or 50 percent of the normal profits tax rate will be applied to:

- qualifying profits of a qualifying ship lessor or a qualifying ship leasing manager (for the year of assessment 2020/21 onwards); and
- qualifying profits of a qualifying ship agent, a qualifying ship manager, or a qualifying ship broker (for the year of assessment 2021/22 onwards).

Moreover, the concessionary profits tax rate for the assessable profits of (a) eligible family-owned investment holding vehicles managed by eligible single family offices in Hong Kong and (b) family-owned special purpose entities earned from the qualifying transactions and incidental transactions for a year of assessment commencing on or after April 1, 2022 is 0 percent.

## 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;
- Interest, profits or gains from qualifying debt instruments (issued on or after April 1, 2018) exempted from payment of profits tax; 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.

A person is exempt from payment of profits tax in respect of the following sums:

- Interest (accrued on or after 22 June 1998) that is derived from any deposit placed in Hong Kong with an authorized institution, excluding interest received by or accrued to a financial institution; and
- Starting from the year of assessment 2009/10, interest on and any profit made in respect of Renminbi sovereign bonds.

## 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. 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.

- Non-deductible items

- » Domestic or private expenses and any sums not expended for the purpose of producing the profits;
- » 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 Inland Revenue Ordinance (Cap. 112), except salaries tax paid in respect of employees' remuneration; and
- » 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.



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- 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 consecutive years commencing from the year in which the expenditure is incurred; with effect from the year of assessment 2018/19, a full deduction is allowed during the basis period (instead of over five years) in which the expenditure is incurred for procuring environmental protection installations, including any part of expenditure on environmental protection installation that remains to be deducted (and is to be fully deducted) in the year of assessment 2018/19.
    - » 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 SAR, amounting in aggregate not less than HK\$100 but not exceeding 35 percent (Year of Assessment 2008/09 onwards) of the adjusted assessable profits before deduction of donations, are allowable for deduction in computing the assessable profits.

## Maximum tax reductions

Profits tax for the year of assessment 2022/23\* is further reduced by the tax reduction of 100 percent, subject to a ceiling of HK\$6,000 per case.

The reduction will be reflected in the final tax payable for the year of assessment 2022/23, but not to the provisional tax of the same year. Therefore, taxpayers are still required to pay their provisional tax on time despite the reduction measure.

## Provisional profits tax

Profits tax is chargeable on the assessable profits for each year of assessment. As the assessable profits for any particular year cannot be known until after the end of the year concerned, a provisional tax charge has to be raised. When the assessable profits for the year of assessment are subsequently ascertained, an assessment will be made and the provisional profits tax paid will be utilized to offset the tax liability under the assessment.

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\*Legislative amendments are required for implementing the tax measures as proposed by the Financial Secretary in the 2023-24 Budget.

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The tax payer can apply in writing for holding over of the whole or part of the provisional tax on the grounds as specified in the Inland Revenue Ordinance (Cap. 112).

If the provisional tax is payable by two installments and the first installment has been settled by the due date, an application for holding over of the whole or part of the second installment may be made subject to the prescribed time limit and grounds for application.

## Property tax

Property tax is levied on income arising from the letting of immovable property in Hong Kong, which is payable by the owner(s) at the standard rate of the year of assessment on “net assessable value” (NAV). Under the provisions of the Inland Revenue Ordinance (Cap. 112), 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 NAV:

- If the tenant pays rates, the NAV is equal to AV less than a standard allowance of 20 percent for repairs and outgoings; and
- If the owner is responsible for paying rates, rates paid can be deducted before allowing for the 20 percent deduction.

## Provisional property tax

Property tax is chargeable on NAV for each year of assessment. As the NAV for any particular year cannot be known until after the end of the year concerned, a provisional tax charge has to be raised. When the NAV for the year of assessment are subsequently ascertained, an assessment will be made and the provisional property tax paid will be utilized to offset the tax liability under the assessment.

The tax payer can apply in writing for holding over of the whole or part of the provisional property tax on the grounds as specified in the Inland Revenue Ordinance (Cap. 112).



### RELATED SERVICES

For assistance navigating Hong Kong's various tax compliance requirements, please contact our tax experts at [hongkong@dezshira.com](mailto:hongkong@dezshira.com)

## Hong Kong's principle of taxation based on territorial source

Hong Kong adopts a territorial source principle of taxation. Only profits derived from a trade, profession, or business carried on in Hong Kong are taxable here. Profits sourced elsewhere are not subject to Hong Kong profits tax. The principle itself is very clear but its application in particular cases can be contentious.

Over the years, the following principles have emerged from authoritative court decisions:

- **Matter of fact** – the question of locality of profits is a hard, practical matter of fact. No universal rule can apply to every scenario. Whether profits arise in or are derived from Hong Kong depends on the nature of the profits and of the transactions which give rise to such profits.
- **The operations test** – identifying the operations that generated the profits in question and determining where they were carried out. The guiding principle is to examine what the taxpayer has done to earn the profits and where they were earned. The source of profits must be attributed to the operations of the taxpayer responsible for generating them, rather than to those of other entities within the taxpayer's group.
- **Antecedent or incidental activities** – the relevant operations do not comprise the whole of the taxpayer's activities. The focus is on establishing the geographical location of the taxpayer's profit-producing transactions as distinct from activities antecedent or incidental to those transactions.
- **Place where decision is made** – the place where the day-to-day investment and business decisions take place is only one factor which must be considered in determining the source of profits. It is not usually the deciding factor.
- **Gross profits from transactions** – the distinction between Hong Kong profits and offshore profits is made by reference to the gross profits arising from individual transactions.
- **Business presence overseas** – while a company may have operations outside of Hong Kong that generate profits, the lack of such a presence does not automatically mean that all profits arise in or derive from Hong Kong. However, if the company's main operations are in Hong Kong and there is no presence overseas, it is highly likely that any profits earned will be subject to profits tax in Hong Kong.

In trading companies, the location of profits from goods and commodities is typically determined by the place where contracts for their purchase and sale are "effected." This includes not only the legal execution of the contracts, but also the negotiation, finalization, and fulfillment of their terms.

In manufacturing businesses, the source of profits is determined by the location where the goods are produced. Profits derived from the sale of goods manufactured in Hong Kong are subject to full taxation here. If the goods are produced both inside and outside of Hong Kong, the portion of profits related to the production outside of Hong Kong will not be considered to arise in Hong Kong. The location where the goods are sold does not factor into this determination.

If a business earns commission by securing buyers for products or by securing suppliers of products needed by customers, the source of commission income is the location where the agent performs these activities. The income arises from the arrangement of transactions between the parties. Therefore, if these activities take place in Hong Kong, the commission income is sourced in Hong Kong.

To provide certainty and clarity in the operation of the territorial source principle, the IRD provides advance rulings on the source of profits of a business for profits tax purposes. The service is subject to the payment of a fee.

## New rules on foreign source income exemption


In 2022, Hong Kong amended the provisions of the Inland Revenue Ordinance in relation to the foreign source income exemption (FSIE), in a move to comply with international tax standards, to avoid being added to the European Union (EU)'s grey list of non-cooperative tax jurisdictions. The FSIE amendments came into effect on January 1, 2023.

Under the new FSIE regime, certain foreign-sourced income accrued to a member of a multinational entity (MNE) group carrying on a trade, profession, or business in Hong Kong is to be regarded as arising in or derived from Hong Kong and chargeable to profits tax when it is received in Hong Kong, unless certain additional conditions can be satisfied. Previously, these incomes were not subject to profits tax at all if they were foreign-sourced.

The in-scope foreign source income include interest, dividend, disposal gain from the sales of equity interests in an entity (disposal gain), and IP income. Nevertheless, any interest, dividend, or disposal gain derived by certain entities, such as a regulated financial entity, do not fall into the scope.

Meanwhile, the in-scope foreign-sourced income received in Hong Kong will not be brought into charge if the MNE entity meets the exception requirements specifically for the particular types of incomes. The exception requirements are as follows:

Exception Requirements for Specified Foreign-Sourced Income under the New FSIE Regime				
Exceptions	Specified foreign-sourced income			
	Interest	Dividend	Disposal gain	IP income
Economic substance requirement	✓	✓	✓	
Nexus requirement				✓
Participation requirement		✓	✓	



In general, the economic substance requirement will be tested in terms of the number of qualified employees in Hong Kong and the amount of operating expenditure incurred in Hong Kong. The participation requirement is an alternative to the economic substance requirement for the foreign-sourced dividend or disposal gain. It requires certain conditions to be met, such as the MNE entity must continuously hold not less than five percent of equity interests in the investee entity concerned for a period of not less than 12 months immediately before the foreign-sourced dividend or disposal gain accrues. The nexus requirement will be tested in reference to the research and development activities concerning the IP.

To further mitigate the impact of the new FSIE regime, Hong Kong introduced a unilateral foreign tax credit system for the in-scope income. If an MNE entity has specified foreign-sourced income chargeable to profits tax and has paid similar tax in a territory outside Hong Kong, double taxation relief will be available regardless of whether that territory has entered a comprehensive avoidance of double taxation arrangement with Hong Kong or not. The amount of tax credit is capped at the lower of foreign tax paid and the profits tax that would have been payable on the same income. If an MNE entity has paid tax for its in-scope income in a foreign jurisdiction, it will only need to pay a reduced or even no tax in Hong Kong in most cases, given Hong Kong's relatively low tax rate.

To be noted, relevant taxpayers will be subject to some additional obligations under the new FSIE regime. An MNE entity must do the following:

- Report its specified foreign-sourced income in the profits tax return and submit relevant form (IR1478) for the year of assessment in which the income accrues;
- Report the amount of chargeable specified foreign-sourced income in the profits tax return and designated form for the year of assessment in which the income is received in Hong Kong;
- Notify the Commissioner in writing that it is chargeable to profits tax within four months after the end of the basis period of the year of assessment during which the income is received in Hong Kong in case no profits tax return has been issued to it for the year of assessment concerned;
- Notify the Commissioner in writing of the withdrawal, abandonment, or refusal of a patent application made under Cap. 514 or under the law of any place outside Hong Kong, for which an excepted portion of qualifying IP income was regarded as not chargeable to profits tax in a previous year of assessment, within four months after the end of the basis period of the year of assessment in which the withdrawal, abandonment or refusal takes place; and
- Retain records of transactions, acts, or operations relating to the specified foreign-sourced income at least until the expiry of seven years after the completion of those transactions, acts or operations, or the expiry of seven years after the income is received, or to be regarded as received, in Hong Kong, whichever is later.



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In conclusion, the amendments to the FSIE regime have made Hong Kong's territorial source principle of taxation more advanced than before. Taxpayers with foreign sourced income that falls under the scope of the new rules should review their business structure, understand the updated compliance requirements, and make any necessary arrangements to optimize their tax status. However, the impact of the new regime will mainly be felt by shell companies of multinational enterprises. The tax impact on most companies with existing operations in Hong Kong is expected to be minimal. With Hong Kong committed to maintaining its competitiveness, businesses can continue to benefit from the territory's relatively low tax rates and straightforward tax system, particularly smaller companies.

#### **Interaction with the Territorial Source Principle of Taxation**

With the new FSIE regime coming into effect, the territorial source principle of taxation is no longer as simple as it used to be. But as clarified by the IRD, the determination of source of profits is not affected by the introduction of the economic substance requirement. The source of profits and the economic substance requirement will be considered in separate contexts, with the former continuing to be determined based on the prevailing requirements of the Inland Revenue Ordinance (Cap. 112) and the broad guiding principle as established by judicial precedents.



#### **RELATED SERVICES**

To evaluate how Hong Kong's new foreign source income exemption (FSIE) regime will affect the tax burden of your business, please contact our tax experts at [hongkong@dezshira.com](mailto:hongkong@dezshira.com).

# What are the key compliance requirements?

## Accounting standards

As one of the two SARs of China, Hong Kong enjoys the rights to develop its own accounting standards, rather than applying the relative standards of the Chinese Mainland. 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. 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 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 Companies Ordinance (Cap. 622) and highlighted in Paragraphs 22-43 of this standard.

## Bookkeeping requirements

According to Part 9 of the Hong Kong Companies Ordinance (Cap. 622), companies incorporated in Hong Kong must maintain proper books of accounts and must also satisfy statutory audit requirements on an annual basis.

To be more detailed, the bookkeeping requirements in Hong Kong are as follows:

- **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 Companies Ordinance (Cap. 622).

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\* Section 51C of the Inland Revenue Ordinance (Cap. 112) provides a more specific list of the records to be kept

- » 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.
  
- **Where to keep the accounting records:**
  - » A company's accounting records must be kept at its registered office or any other place that the directors think fit, and must be open to inspection by the directors at all times without charge; and
  - » 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 six 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 or matter recorded in the records, or the accounts and returns, relates.
  
- **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 Companies 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 Companies 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:

<b>Documents to be Maintained for Financial Statements by Type of Transaction</b>	
<b>Type</b>	<b>Record to be maintained</b>
Sales	Sales invoice
	Goods return note
	Receipt slip
	Daily receipt record
Purchases	Purchases invoice
	Petty cash voucher
	Payment slip
	Check stub
General expenses	Statement
	Expenses invoice
	Payment receipt
	Check stub
Bank transaction	Salary record
	Bank statements
	Bank paid-in slip and related receipt details
Tangible assets	Check stub and copy
	Purchase and sale agreement
	Invoice and receipt
Inventory	Check stub and copy
	Purchase and sale agreement
	Invoice and receipt
	Check stub and copy
Investment	Inventory list (including quantity and unit cost on every item)
	Obsolete or slowing-moving inventory
	Security ask/bid confirmation slip
	Purchase and sale agreement
	Capital inspection report (apply for PRC investment)

# International taxation



**ALBERTO VETTORETTI**

Managing Partner  
Hong Kong Office

## Hong Kong's transfer pricing regime

The Inland Revenue (Amendment) (No.6) Ordinance 2018 (“the Amendment Ordinance”), which was gazette on July 13, 2018, established a more comprehensive transfer pricing regime in Hong Kong. It codified the transfer pricing principles, implemented certain measures under the Base Erosion and Profit Shifting (BEPS) Package, and aligned the provisions in the Inland Revenue Ordinance (Cap. 112) with international tax requirements.

### Fundamental transfer pricing rule

On the basis of the arm's length principle, the Amendment Ordinance introduced fundamental transfer pricing rules (FTPR) that further empower the IRD. This includes the ability to adjust the profits or losses of an enterprise where the actual provision made or imposed between two associated persons departs from the provision that would have been made between independent persons and has created a tax advantage.

The Amendment Ordinance does not contain any safe harbor rules in respect to the FTPR. What this means is that taxpayers of all sizes, engaged in either domestic and/or cross border intercompany transactions of any size, will be required to ensure that the prices are at arm's length.

### Transfer pricing documentation

The Amendment Ordinance further introduced mandatory documentation requirements based on the three-tiered approach of Country-by-Country (CbC) Reporting, Master File, and Local File.

- Requirements and exemption thresholds for Master File and Local File

Hong Kong entity of a group will be required to prepare a Master File and a Local File for each accounting period beginning on or after April 1, 2018. The Master File and Local File must be prepared within nine months after the end of the entity's accounting period, and be retained for a period of no less than seven years after the end of the accounting period of the entity. The Hong Kong entity has to declare in the profits tax return and supplementary form S2 whether a master file and a local file have to be prepared. The master file and the local file should be ready for submission upon request by the Assessor. The information items to be included within the Master File and the Local File are largely in-line with the Organization for Economic Co-operation and Development (OECD) guidance.

*“ In light of the IRD's focus on related party transactions, it is imperative that companies ensure they have a reasonable charging mechanism in place and that any related party payments made in Hong Kong are arm's length in nature. ”*

Taxpayers will not be required to prepare Master and Local Files if they meet either of the following two sets of exemptions:

<b>1) Based on size of business (any two of the three criteria)</b>	<b>Threshold per financial year</b>
Total revenue	≤HK\$400 million
Total assets	≤HK\$300 million
Employees	≤100

If the amount of a category of related party transactions for the relevant accounting period is below the respective threshold, the entity will not be required to prepare a Local File for that category of transactions.

<b>2) Based on controlled transactions (for that particular category of transactions)</b>	<b>Threshold per financial year</b>
Transfer of properties (excluding financial assets/intangibles)	≤HK\$220 million
Transactions in financial assets	≤HK\$110 million
Transfer of intangibles	≤HK\$110 million
Any other transactions (e.g. service income/royalty)	≤HK\$44 million

If all of an entity's controlled transactions are exempted by the above related party transaction criteria, the entity is not required to prepare both the Master File and the Local File.

## Country-by-country reporting

Country-by-Country (CbC) Reporting is a minimum standard formulated by OECD under Action 13 of the BEPS Package. In Hong Kong, the requirements for filing a CbC Return, which includes a CbC Report, only apply to a MNE group whose annual consolidated group revenue reaches the specified threshold amount, i.e. HK\$6.8 billion (Reportable Group).

In respect of a Reportable Group, the primary obligation of filing a CbC Return is on the ultimate parent entity (UPE) resident in Hong Kong and not on any other constituent entities resident in Hong Kong (Hong Kong Entities). The Hong Kong UPE is required to file a CbC Return for each accounting period beginning on or after January 1, 2018.

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A Hong Kong Entity of a Reportable Group whose UPE is not resident in Hong Kong is subject to a secondary obligation of filing a CbC Return under certain conditions. Each Hong Kong entity of a Reportable Group must file a written notification informing within three months after the end of the accounting period.

The deadline for filing a CbC Return is 12 months after the end of the relevant accounting period or the date specified in the assessor's notice, whichever is the earlier. A service provider (SP) may be engaged to file a CbC Return or the related notification.

## **AEOI reporting**

In September 2014, Hong Kong indicated its support for implementing automatic exchange of financial account information (AEOI) on a reciprocal basis with appropriate partners. In 2016, Hong Kong introduced an amendment bill regarding the implementation of AEOI, which commenced operation on June 30, 2016.

Under the AEOI standard, financial institutions are required to identify financial accounts held by tax residents of reportable jurisdictions or held by passive non-financial entities whose controlling persons are tax residents of reportable jurisdictions in accordance with due diligence procedures. Required information of these accounts has to be collected and furnished to the IRD on an annual basis.

“Tax residents of reportable jurisdictions” refer to those who are liable to tax by reason of residence in the jurisdictions. In general, whether or not an individual is a tax resident of a jurisdiction is determined by having regard to the person's physical presence or stay in a place (e.g. whether over 183 days within a tax year) or, in the case of a company, the place of incorporation or the place where the central management and control of the entity is exercised. Account holders may be requested to provide self-certifications on their personal information including tax residence, so as to enable financial institutions to identify the reportable accounts.

Hong Kong has expanded the number of reportable jurisdiction from 75 to 126 (effective from January 1, 2020) for the more effective implementation of the arrangement relating to AEOI. These jurisdictions include all EU member states, all of Hong Kong's tax treaty partners that have committed to Common Reporting Standard (CRS), and other jurisdictions that have expressed an interest to the OECD in exchanging CRS information with Hong Kong.

Hong Kong will only conduct AEOI with a reportable jurisdiction when an arrangement is in place with the reportable jurisdiction concerned to provide the basis for exchange.



## BEPS 2.0

In 2021, Hong Kong, together with more than 130 jurisdictions across the globe, pledged to implement the international tax reform proposals drawn up by the OECD to address base erosion and profit shifting (abbreviated as BEPS 2.0). In the 2023-24 Budget Plan speech, the Financial Secretary said that Hong Kong will implement the global minimum effective tax rate in accordance with international consensus so as to safeguard the Hong Kong's taxing rights and maintain the competitiveness of the city's tax regime.

As to the new tax rules for the adoption of the BEPS 2.0, the Financial Secretary mentioned that Hong Kong plans to apply the global minimum effective tax rate on large MNE groups and implement the domestic minimum top-up tax starting from 2025 onwards. He also promised that Hong Kong will launch a consultation exercise to allow MNE groups to make early preparation.


## Hong Kong's double taxation agreement network

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 SAR government 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. As of April 2023, Hong Kong has signed comprehensive DTAs with 46 countries or regions. In addition, Hong Kong is in the process of negotiating comprehensive DTAs with 14 countries or regions such as Germany, Norway, Cyprus, and Türkiye.

Due to the international nature of aircraft operations, airline operators are more susceptible to double taxation than other taxpayers. As negotiation of a DTA may take a long time, it has been Hong Kong's policy to include double taxation relief arrangements for airline income in the bilateral Air Services Agreements negotiated between Hong Kong and its aviation partners.





Shipping income is another area of concern. Hong Kong is currently negotiating double taxation relief for shipping income with jurisdictions that either do not provide reciprocal tax exemption themselves or, even when reciprocal exemption provisions exist, prefer to employ bilateral agreements. There are also agreements that cover both airline and shipping income.

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 IRD in recent years. Consequently, the Advance Pricing Arrangement (APA) program\* 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.

## Certificate of Resident Status

A Certificate of Resident Status is a document issued by the Hong Kong competent authority to a Hong Kong resident who requires proof of resident status for the purposes of claiming tax benefits under the DTA.

The Certificate of Resident Status should constitute as a sufficient proof of the resident status of a Hong Kong resident. The Hong Kong competent authority will issue a Certificate of Resident Status after the DTA between Hong Kong and the relevant jurisdiction has become effective. Generally, only one Certificate of Resident Status will be issued to you in respect of each DTA for each year.

The following persons can apply for a Certificate of Resident Status:

- Individual who ordinarily resides in Hong Kong;
- Individual who 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;
- Company/partnership/trust/body of persons incorporated or constituted in Hong Kong; and
- Company/partnership/trust/body of persons incorporated or constituted outside Hong Kong but managed or controlled in Hong Kong.

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\* 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.

Below we listed countries and regions with existing DTAs with Hong Kong, or with DTAs under negotiation with Hong Kong.

Countries and Regions with Existing Comprehensive DTAs with Hong Kong		
A-I	J-N	O-Z
Austria	Japan	Pakistan
Belarus	Jersey	Portugal
Belgium	Korea	Qatar
Brunei	Kuwait	Romania
Cambodia	Latvia	Russia
Canada	Liechtenstein	Saudi Arabia
Czech	Luxembourg	Serbia
Estonia	Macao SAR	South Africa
Finland	Mainland of China	Spain
France	Malaysia	Switzerland
Georgia	Malta	Thailand
Guernsey	Mauritius*	United Arab Emirates
Hungary	Mexico	United Kingdom
India	Netherlands	Vietnam
Indonesia	New Zealand	
Ireland		
Italy		

\* Signed but yet to take effect.

Countries and Regions with DTAs Under Negotiation with Hong Kong		
Bahrain	Israel	North Macedonia
Bangladesh	Kyrgyz Republic	Norway
Croatia	Lithuania	Türkiye
Cyprus	Maldives	Ukraine
Germany	Nigeria	

## Tax rates for dividends, interest, royalties, and technical fees under DTAs

The following table shows the maximum rates of tax those countries / regions with Comprehensive DTAs with Hong Kong can charge a Hong Kong resident on payments of dividends, interest, royalties, and technical fees.

Tax Rates for Dividends, Interest, Royalties, and Technical Fees Under DTAs						
Country / region	Effective from	Dividends		Interest (%)	Royalties (%)	Technical fees (%)
		Qualifying companies (%)	Others (%)			
Austria	Year of assessment 2012/2013	0	10	-	3	NA
Belarus	Year of assessment 2018/2019	5	5	5	3/5	NA
Belgium	Year of assessment 2004/2005	0/5	15	10	5	NA
Brunei	Year of assessment 2011/2012	-	-	5/10	5	15
Cambodia	Year of assessment 2020/2021	10	10	10	10	10
Canada	Year of assessment 2014/2015	5	15	10	10	NA
Czech	Year of assessment 2013/2014	5	5	-	10	NA
Estonia	Year of assessment 2020/2021	0	10	0/10	5	NA
Finland	Year of assessment 2019/2020	5	10	-	3	NA
France	Year of assessment 2012/2013	10	10	10	10	NA
Georgia	Year of assessment 2022/2023	5	5	5	5	NA
Guernsey	Year of assessment 2014/2015	-	-	-	4	NA
Hungary	Year of assessment 2012/2013	5	10	5	5	NA
India	Year of assessment 2019/2020	5	5	10	10	10

Tax Rates for Dividends, Interest, Royalties, and Technical Fees Under DTAs						
Country / region	Effective from	Dividends		Interest (%)	Royalties (%)	Technical fees (%)
		Qualifying companies (%)	Others (%)			
Indonesia	Year of assessment 2013/2014	5	10	10	5	NA
Ireland	Year of assessment 2012/2013	-	-	10	3	NA
Italy	Year of assessment 2016/2017	10	10	12.5	15	NA
Japan	Year of assessment 2012/2013	5	10	10	5	NA
Jersey	Year of assessment 2014/2015	-	-	-	4	NA
Korea	Year of assessment 2017/2018	10	15	10	10	NA
Kuwait	Year of assessment 2014/2015	5	5	5	5	NA
Latvia	Year of assessment 2018/2019	0	10	0/10	0/3	NA
Liechtenstein	Year of assessment 2012/2013	-	-	-	3	NA
Luxembourg	Year of assessment 2008/2009	0	10	-	3	NA
Macao SAR	Year of assessment 2021/2022	5	5	5	3	NA
Mainland China	Year of assessment 2007/2008	5	10	7	5/7	NA
Malaysia	Year of assessment 2013/2014	5	10	10	8	5
Malta	Year of assessment 2013/2014	-	-	-	3	NA
Mauritius	pending	0	5	5	5	NA
Mexico	Year of assessment 2014/2015	-	-	4.9/10	10	NA
Netherlands	Year of assessment 2012/2013	0	10	-	3	NA
New Zealand	Year of assessment 2012/2013	0/5	15	10	5	NA

Tax Rates for Dividends, Interest, Royalties, and Technical Fees Under DTAs						
Country / region	Effective from	Dividends		Interest (%)	Royalties (%)	Technical fees (%)
		Qualifying companies (%)	Others (%)			
Pakistan	Year of assessment 2018/2019	10	10	10	10	12.5
Portugal	Year of assessment 2013/2014	5	10	10	5	NA
Qatar	Year of assessment 2014/2015	-	-	-	5	NA
Romania	Income derived on or after 01.01.2017	3	5	3	3	NA
Russia	Year of assessment 2017/2018	0/5	10	-	3	NA
Saudi Arabia	Year of assessment 2019/2020	5	5	-	5/8	NA
Serbia	Year of assessment 2021/2022	5	10	10	5/10	NA
South Africa	Year of assessment 2016/2017	5	10	10	5	NA
Spain	Year of assessment 2013/2014	0	10	5	5	NA
Switzerland	Year of assessment 2013/2014	0	10	-	3	NA
Thailand	Year of assessment 2006/2007	10		10/15	5/10/15	NA
United Arab Emirates	Year of assessment 2016/2017	5	5	5	5	NA
United Kingdom	Year of assessment 2011/2012	0/15	0/15	Domestic rate	3	NA
Vietnam	Year of assessment 2010/2011	10	10	10	7/10	NA



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## Human Resources and Payroll

- ◆ What obligations do I have as an employer?
- ◆ Salaries tax in Hong Kong
- ◆ Visa requirements and procedures in Hong Kong
- ◆ Employee leaves and vacations
- ◆ Terminating an employee

# What obligations do I have as an employer?

Generally, the main areas of an employer's obligation in the workplace include:

- Complying with obligations under the Occupational Safety and Health Ordinance (Cap. 398) and common law duty of care;
- Complying with obligations under the Employment Ordinance (Cap. 57) and the contract of employment;
- Complying with the Disability Discrimination Ordinance (Cap. 487); and
- Complying with the Employees' Compensation Ordinance (Cap. 282).

Below we list out some obligations that employers should pay special attention to.

## Employer's mandatory obligations

### Mandatory Provident Fund

Mandatory Provident Fund (MPF) is a retirement scheme introduced on December 1, 2000. Under the MPF scheme, an employer must comply with all MPF-related obligations under the law. These include enrolling all qualifying employees in MPF schemes, making MPF contributions for them, and records keeping and notifications.

The mandatory contribution rate for both employers and employees is five percent of the employee's relevant income to the MPF, subject to the minimum and maximum relevant income levels. Both employer and employee can make voluntary contributions in addition to mandatory contributions.

For a monthly-paid employee, the current minimum and maximum relevant income levels are HK\$7,100 and HK\$30,000 respectively. Please note that the figures may vary from year to year according to the government policy.

#### Mandatory Contributions Payable by Employer and Employee by Monthly Relevant Income

Monthly relevant income	Amount of mandatory contributions payable by employer	Amount of mandatory contributions payable by employee
Less than HK\$7,100	Relevant income x 5%	No contributions required
HK\$7,100 to HK\$30,000	Relevant income x 5%	Relevant income x 5%
More than HK\$30,000	HK\$1,500	HK\$1,500

“Relevant income” refers to all monetary payments paid or payable by an employer to an employee, including wages, salary, leave pay, fees, commissions, bonuses, gratuities, perquisites, or allowances, but excluding severance payments or long service payments under the Employment Ordinance (Cap. 57).

An employee can claim tax deduction for the mandatory contributions made to an MPF scheme, subject to the maximum amount of HS\$18,000 for the year of assessment 2015/16 onwards. For the voluntary contributions, an employee can only claim tax deductions when satisfying certain requirements, such as the employee has to be a member of MPF exempted ORSO schemes (introduced later), subject to the maximum deduction amount of HK\$60,000 for the year of assessment 2022/23 onwards.

Employers can claim tax deductions for the mandatory and voluntary contributions made for their employees, capping at 15 percent of the total emoluments of the employee. Besides, the Hong Kong Budget Plan proposes to increase the tax deduction for voluntary contributions made by employers to the MPF for employees aged 65 or above from the current 100 percent to 200 percent.

In addition to MPF, there is another pension scheme under Occupational Retirement Schemes Ordinance (Cap. 426) (ORSO), which operates on a voluntary basis. However, if an employer offers both ORSO scheme and MPF scheme, it must provide a one-time option to existing members and new eligible staff (if applicable) to choose between the two schemes.

## Employee’s Compensation Insurance (EC)

Under the Employee’s Compensation Ordinance (Cap. 282), employers in Hong Kong are obliged to hold an employee’s compensation insurance policy to cover their liability to compensate employees for “injury by accident” or “death” arising during the normal course of their work, irrespective of the length of employment contract or working hours, full time or part time employment.

The amount of the liability which must be insured is determined by reference to the total number of the employer’s employees:

<b>Number of employees</b>	<b>Amount of the liability which must be insured per event</b>
Not more than 200	Not less than HK\$100 million
More than 200	Nott less than HK\$200 million

The minimum amount of insurance cover is not the maximum liability that the party concerned is required to bear. The employer should therefore carefully assess the possible risk and consult insurers for professional advice on whether an insurance policy for an amount more than the minimum should be taken out. An employer shall not make any deduction from the earnings of an employee in order to defray the cost of insuring against their liability to pay compensation.





**SANDY ZHANG**  
Senior Manager  
Shenzhen Office

## Other payroll obligations

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.

### Keeping payroll records

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

- Personal details;
- Nature of employment: full time or part time;
- Position;
- Amount of cash remuneration, non-cash remuneration and other fringe benefits;
- Contributions to the Mandatory Provident Fund or its equivalent;
- Amendments to the terms of the employment contract; and
- Period 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; and
- The Hong Kong Identity Card No. of the employee.

### Reporting remuneration paid to an employee

On April 1 every year, the IRD will issue a document called the Annual Employee's Return (Form BIR56A) to companies. Within one month of receiving the Employer's Return, the company needs to complete it and lodge with the IRD even if it does not hire any employee, the business has not commenced, or the business has ceased. If a company has employed persons who meet the conditions for such a return to be filed but the company has not received the Employer's Return by mid April, it should request the IRD to issue a return.

Companies are required to report the below employees on the Employer's Return:

- Unmarried individuals that are paid an annual income of HK\$132,000 or more for the year of assessment 2022/23;
- Married individuals (regardless of amount);
- Part time staff (regardless of amount); and
- Directors (regardless of amount).

*“ 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. ”*

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; and
- Employees assigned or seconded to a Hong Kong company by its overseas holding company

When the company hires a new employee, it needs to inform the IRD by filing the Employer's Return (Form IR56E) within three months if the company anticipates that the employee is likely to be chargeable to salaries tax.

When an employee is terminated, the company needs to file the Employer's Return one month before the date of termination.

When an employee leaves Hong Kong permanently or for a substantial period of time, the employer needs to:

- Ascertain from the employee their expected date of departure;
- File two copies of the Employer's Return one month before the expected date of departure; and
- Withhold all amounts due to be paid to the employee (including salaries, commission, bonus, reimbursement of rent/expense, money or money's worth included) from the date of filing the Employer's Return until the employee has made tax clearance and can produce to the employer a "letter of release" issued by the IRD.

Below we listed some tax forms that are required by the IRD under specific situation for your easy reference:

<b>Statutory Obligation of an Employer to Report Remuneration Paid to an Employee</b>			
<b>Employment condition</b>	<b>Tax form to complete</b>	<b>Statutory period for notification</b>	<b>Notes</b>
Commencement of employment	IR56E	Within 3 months	Both IR56E & IR56B are required for the commencement year
Still under employment as of March 31	IR56B	Within 1 month	Must be submitted annually together with a BIR56A
Cessation of employment	IR56F	Not later than 1 month before cessation	IR56B for the cessation year is not required
Departure from Hong Kong	IR56G	Not later than 1 month before departure and withhold money from tax clearance	IR56B for the cessation year is not required

# Salaries tax in Hong Kong

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 the tax reduction, subject to a maximum.

$$\begin{array}{l} \text{NET CHARGABLE INCOME} = \text{TOTAL INCOME} - \text{DEDUCTIONS} - \text{ALLOWANCES} \\ \text{NET INCOME} = \text{TOTAL INCOME} - \text{DEDUCTIONS} \end{array}$$

For more details about the tax rates, deductions and allowances, please refer to Part two, Section one of this guide, titled “What are the major taxes in Hong Kong?”

## Employer

As mentioned earlier, the employer needs to inform the IRD within three months if it anticipates that the employee is likely to be chargeable to salaries tax. The employer also needs to file the Employer’s Return one month before the date of termination when an employee is terminated, and file the Employer’s Return one month before the expected date of departure for employees leaving Hong Kong permanently or for a substantial period of time.

In addition, any post departure payments (e.g., bonuses, option gain, share awards, tax equalization settlements) that are paid to an employee after his/her departure in respect of the employee’s employment/assignment/secondment in Hong Kong shall be subject to Hong Kong’s salaries tax. As such, the employer is required to report the relevant post departure payments (if any) to the IRD accordingly.

## Employee

Employees are also legally responsible for the Annual Tax Return to the IRD.

If the employee receives an Individual Tax Return from the IRD, s/he must complete and submit it by the due date for filing even if they have no income that can be charged to salaries tax. The reporting should include total income, allowance, deductions, etc.

If the employee doesn’t receive a tax return, s/he should notify the IRD that the income could be chargeable to tax.

The IRD will evaluate the employee’s situation and decide on a tax rate which the employee needs to pay for the past tax period (from April 1 each year to March 31 of next year).

## Case study

From October 1, 2020, the subject's monthly salary is HK\$45,000 and MPF contribution is HK\$1,500. The financial year is April 1 to March 31 of the following year. Tax is filed and paid on annual base. No pre-deductions were required. Then how do we calculate the subject's salary tax for the year of assessment 2022/23 under the progressive rate and standard rate?

### 1. Under progressive tax rate

Year of assessment 2022/23	HK\$
Income: 6 months	$45,000 \times 6 = 270,000$
First deduction: MPF contribution	$1,500 \times 6 = 9,000$
Second deduction: Basic allowance	132,000
Net chargeable Income	$270,000 - 9,000 - 132,000 = 129,000$
Tax payable (before reduction) *:	$50,000 \times 2\% + 50,000 \times 6\% + 29,000 \times 10\% = 6,900$
Tax reduction for 2022/23: 100% tax exempt (Max.6,000)	6,000
Tax payable(after reduction):	$6,900 - 6,000 = 900$

\*For year of assessment 2022/23, the first HK\$50,000 net chargeable income is subject to tax rate of 2%, the second HK\$50,000 is subject to tax rate of 6%, and the third HK\$50,000 is subject to tax rate of 10%.

### 2. Under standard tax rate

Year of assessment 2022/23	HK\$
Income: 6 months	$45,000 \times 6 = 270,000$
First Deduction: MPF contribution	$1,500 \times 6 = 9,000$
Net income:	$270,000 - 9,000 = 261,000$
Tax payable (before reduction)	$261,000 \times 15\% = 39,150$
Tax reduction for 2022/23: 100% tax exempt (Max.6,000)	$39,150 \times 100\% = 39,150 > 6,000$
Tax payable (after reduction):	$39,150 - 6,000 = 33,150$

Through the comparison, the employee should better use progressive tax rate to calculate the annual tax, and the tax amount is shown in above table.

Also, in practice, there's some other deductible related considerations:

- Family status (spouse income status, children or dependents);
- Residential status;
- foreign staff (no need to pay MPF in the first 12 months);
- Home loan interests;
- Loss from other personal business; and
- Double tax treaties.

### **Hong Kong Minimum Wage**

Hong Kong has increased the minimum hourly wage rate from HK\$37.5 to HK\$40, with effect from May 1, 2023.

Following the rise in the minimum wage rate, from May 1, the Employment Ordinance (Cap. 57) has also been amended to come in effect from May 1, 2023.

Hong Kong employers must record the total number of hours worked by an employee in a wage period if:

- a. the employee is paid the minimum wage; and
- b. the wages payable to the employee for the wage period are less than the monetary cap specified in the Ninth Schedule to the Employment Ordinance (or a proportionate amount if the wage period is less than a month).

Accordingly, the monetary cap in the Ninth Schedule has been increased from HK\$15,300 per month to HK\$16,300 per month.



#### **RELATED SERVICES**

For assistance on employee payroll management, please contact our HR & payroll experts at [hongkong@dezshira.com](mailto:hongkong@dezshira.com)

# Visa requirements and procedures in Hong Kong

Generally, a visa or entry permit is required to work, study, establish, or join in any business or to take up residence in the HKSAR. Otherwise, there is high risk of being refused admission on arrival.

However, if an individual holds any of the following travel documents, no visa or entry permit shall be required for any purpose:

- Hong Kong Special Administrative Region Passport;
- British National (Overseas) Passport;
- Hong Kong Certificate of Identity;
- Hong Kong Re-entry permit (for entry from mainland of China and the Macao SAR only);
- Hong Kong Seaman's Identity Book;
- Hong Kong Document of Identity for Visa Purposes, provided that the document is valid or the holder's limit of stay in Hong Kong has not expired;
- Travel documents bearing one of the following endorsements:
  - » Holder's eligibility for Hong Kong permanent identity card verified
  - » The holder of this travel document has the right to land in Hong Kong
- Hong Kong Permanent Identity Card.

## Visitor's visa

Hong Kong grants a visa free period for citizens of most countries, usually for a length of 7, 14, 30, or 90 days depending on the country in question. Exceptions are for British nationals, who may stay in Hong Kong without visa for up to 180 days. To stay longer than the visa free period allowed, visitors must apply for a visa or entry permit before travelling to the HKSAR.

Visitors are required to have adequate funds to cover the duration of their stay without working and to hold onward or return tickets unless they are in transit to the mainland of China or the Macao SAR.

Visitors are not allowed to take up employment (paid or unpaid), to establish or join in any business or to enter school as a student, where other types of visa or entry permit might be applied.

## Employment visa

Hong Kong has several different types of visa for employment and investment, including visa under the General Employment Policy (GEP), visa under the Admission Scheme for Mainland Talents and Professionals (ASMTP), visa under Immigration Arrangements for Non-local

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Graduates (IANG), visa under Admission Scheme for the Second Generation of Chinese Hong Kong Permanent Residents, and visa under Capital Investment Entrant Scheme (CIES).

Generally, the type of visa that is most applicable to foreign investors is the employment visa under the GEP. 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.

**To apply for the employment visa, the following requirements must be fulfilled:**

- 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; and
- Remuneration is broadly in line with market levels.

**Apart from the application form, the following documents need to be submitted:**

- From the employee:
  - » Passport;
  - » Copy of academic qualifications and relevant work experience; and
  - » Recent photo.
- From the employer:
  - » 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; and
  - » Detailed business plan.

These documents need to be collected and delivered to the Immigration Department of Hong Kong SAR. Foreigners residing in the Chinese Mainland 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 two to three 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 and work in Hong Kong.



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# Employee leaves and vacations

## Statutory holidays

All employees are entitled to leave on statutory holidays, irrespective of length of services. Hong Kong's statutory holidays in 2023 are as follows:

- New Year's Day (January 1): 1 day;
- First three days of Lunar New Year (February 1, 2, and 3): 3 days;
- Ching Ming Festival (April 5): 1 day;
- Labor Day (May 1): 1 day;
- The Birthday of the Buddha (May 8): 1 day;
- Tuen Ng Festival (June 3): 1 day;
- Establishment of the Hong Kong SAR (July 1): 1 day;
- The day following Chinese Mid-autumn Festival (September 12): 1 day;
- Chinese National Day (October 1): 1 day;
- Chung Yeung Festival (October 4): 1 day; and
- Chinese Winter Solstice Festival or Christmas (December 22 or December 25, at the option of the employer): 1 day.

### Statutory holidays increased in Hong Kong from 2022

According to the Employment (Amendment) Ordinance 2021, which came into operation on January 1, 2022, the number of statutory holidays in Hong Kong shall be raised to 17 days progressively. The first addition is the Birthday of the Buddha on May 8, 2022. After that, a new holiday will be added every two years, including the first weekday after Christmas Day (in 2024), the Easter Monday (in 2026), the Good Friday (in 2028), and the day following Good Friday (2030).

All employees are entitled to the above statutory holidays. If the statutory holiday falls on a rest day, a holiday should be granted on the day following the rest day which is not a statutory holiday or an alternative holiday or a substituted holiday or a rest day. An employee having been employed under a continuous contract (i.e., being employed continuously by the same employer for four weeks or more, with at least 18 hours worked in each week) for not less than three months is entitled to pay on statutory holidays. Holiday pay should be paid to the employee not later than the day on which he is next paid his wages after that statutory holiday.

An employer can ask an employee to work on statutory holidays. But the employer is required to give their employee at least 48 hours' prior notice for work on a statutory holiday. The employer must then arrange an alternative holiday within 60 days before or after the statutory holiday. In this situation, an employer is advised to keep clear records of the alternative or substitute holiday taken by an employee. An employer must not make any form of payment to an employee in lieu of a statutory holiday.



## Annual leave

Employees are entitled by law to paid annual leave after having been employed under a continuous contract for every 12 months. An employee's entitlement to paid annual leave increases progressively from seven days to a maximum of 14 days according to the length of service with the company:

Entitlements of Paid Annual Leave									
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

Employers can determine when annual leave is to be taken after consultation with the employee or his representative and must give 14 days' written notice to the employee of the time that they have selected. Annual leave must, however, be granted within 12 months of the end of the leave year, although in practice, most employers allow annual leave to be taken as it accrues.

Paid annual leave should be granted for an unbroken period, unless the employee requires so. For leave entitlement not exceeding 10 days, up to three days can be granted separately and the balance should be granted consecutively. For leave entitlement exceeding 10 days, at least seven days should be granted consecutively. Any rest day or statutory holiday falling within a period of annual leave will be counted as annual leave and another rest day or holiday must be appointed.

### Can an employer make payment to an employee in lieu of annual leave?

An employer should not include in an employment contract a term to forgo all or any of the employee's annual leave entitlement, including payment of wages in lieu of any annual leave days. However, the law allows an employee to choose to accept payment in lieu of that part of the leave entitlement which exceeds 10 days. For example, if an employee is entitled to 12 days' annual leave, they can take 10 days' leave and accept payment of the equivalent wages for the 2 days' leave.

Employees are entitled to take a payment in lieu of any accrued and untaken statutory annual leave from the previous leave year that exceeds 10 days and are also entitled to payment in respect of any outstanding annual leave due upon cessation of employment on a pro-rata basis. The law also permits employees to carry forward all untaken annual leave for 12 months after the preceding leave year.

The daily rate of annual leave pay is a sum equivalent to the average daily wages earned by an employee in the preceding 12-month period. If an employee is employed for less than 12 months, the calculation shall be based on the shorter period.

## Sick leave

An employee employed under a continuous contract is entitled to sickness allowance if the following conditions are fulfilled:

- The sick leave taken is not less than four consecutive days with limited exceptions, such as pregnancy check-ups, post confinement medical treatment, or miscarriage;
- The sick leave is supported by an appropriate medical certificate; and
- The employee has accumulated sufficient number of 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, up to a maximum of 120 paid sickness days. 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; and
- Compensation is payable by law (Employees' Compensation Ordinance).

The daily rate of sickness allowance is a sum equivalent to 4/5 of the average daily wages earned by an employee in the past 12 months preceding the sickness day (or the first sickness day where the sick leave is longer than one consecutive day). If an employee is employed for less than 12 months, the calculation shall be based on the shorter period.

Day(s) of sickness day(s)	Specified dates
1 day	The sickness day
More than 1 consecutive day	The first sickness day

An employer is prohibited from terminating the contract of employment of an employee on his paid sick leave, except in cases of summary dismissal due to the employee's serious misconduct.

## Maternity leave

The Employment (Amendment) Ordinance 2020, which extends the statutory maternity leave from 10 weeks to 14 weeks, took effect on December 11, 2020. Since then, an employee who becomes pregnant is entitled to:

- A continuous period of 14 weeks' maternity leave;
- If child birth occurs later than expected, added leave until the child is born; and
- 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 worked under a continuous contract for 40 weeks and has given notice to the employer about the pregnancy with a qualified medical certificate provided. It should be noted, however, that any extended maternity leave due to late delivery and/or illness or disability will be unpaid.

The maternity leave pay is calculated at four-fifths of the employee's average daily wages earned in the 12-month period leading up to the first day of the maternity leave. If an employee is employed for less than 12 months, the calculation shall be based on the shorter period. The maternity leave pay for the additional maternity leave from the 11th to 14th week is capped at HK\$80,000 per employee.

After paying maternity leave pay to its employee, the employer can be 100 percent reimbursed by the government for the extra cost (i.e., maternity leave pay for the 11th to the 14th week), as long as the employee is eligible for 14 weeks' maternity leave pay under the Employment Ordinance.

The employee is also entitled to sickness allowance for any day on which the employee has attended a medical examination related to pregnancy, given that a certificate of attendance issued by professionals can be provided as proof.



## Paternalty leave

A male employee is entitled to 5 days' paternalty leave for each confinement of his spouse/partner if he:

- is the father of a new-born child or a father-to-be;
- has been employed under a continuous contract; and
- has given the required notification to the employer.

The employee may take paternalty leave at any time during the period from 4 weeks before the expected date of delivery of the child to 14 weeks beginning on the actual date of delivery of the child. The employee may take all five days of paternalty leave in one go or on separate days.

A male employee is entitled to paternalty leave pay if he has been employed under a continuous contract for not less than 40 weeks immediately before the day of paternalty leave, and has provided the birth certificate of his child, on which his name is entered as the child's father, to the employer within the stipulated period.

The daily rate of paternalty leave pay is a sum equivalent to four-fifths of the average daily wages earned by an employee in the 12-month period preceding the first day of paternalty leave. If an employee is employed for less than 12 months, the calculation shall be based on the shorter period.

## Other leave

There is no other employee leave defined in Hong Kong law, therefore, all other kinds of employee leave shall be mutual agreed by two parties and may be included in the employee's employment contract.

# 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; or
- Habitual neglect of duties.

Besides, no notice is required during the first month of a probation period – if one is agreed upon. The employee may terminate the contract without notice for:

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

To be noted, immediate termination is a serious disciplinary action. It only applies to cases where an employee has committed very serious misconduct or fails to improve himself after the employer's repeated warnings.

### Termination by notice or payment in lieu of notice

An employment contract may be terminated by either side by giving the other party notice, or by giving payment in lieu of notice. The default time within which to give notice is seven days during the probation period and one month after probation. Parties may contractually agree upon shorter notice, but no less than seven days. If termination happens in the first month of the probation period, then neither notice or payment are required.

The payment in lieu of notice is calculated by taking the employees average daily wages/month wages (depending on whether the notice period is expressed in days, weeks or months) as earned in the 12-month period preceding the day when a notice of termination is given, or the day when the contract is terminated in case a notice has not been given.

## 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; or
- An employee injured at work, without having first come to an agreement on compensation or before the issue of a certificate of assessment.

### Changes to the Employment Ordinance in light of the COVID-19 pandemic

On February 25, 2022, the Hong Kong government published in the gazette, the Employment (Amendment) Bill 2022 (the Bill). The Bill seeks to make certain amendments to the Employment Ordinance (Cap. 59) to address unique issues arising out of the COVID-19 pandemic. As of writing this guide, the Bill is expected to be introduced to the Legislative Council for scrutiny soon.

According to the Bill:

- **Employers can terminate employees for refusal to be vaccinated in certain circumstances:** If an employee fails to comply with a “legitimate vaccination request” made by his/her employer, he/she will be considered as being incapable of performing work for the purpose of his/her employment, which will constitute a “valid reason” for the employer to dismiss an employee or vary the terms of the contract of employment. Employees who are unfit for COVID-19 vaccination due to medical reasons, such as those with medical exemption certificates and those who are pregnant or breastfeeding, are not subject to this policy.
- **Certain employees are protected from termination for undergoing quarantine:** The Bill clarifies that an employee’s absence from work due to quarantine would be an invalid reason for dismissal or variation of the terms of the employment contract. However, this policy only applies to employees who have been employed under a continuous contract of two years or more.

## Termination payments

The items and amount of payments payable to an employee on termination of employment or expiry of the contract depend on a number of factors, such as the length of service, the terms of employment contract, and the reason for termination of contract. Termination payments usually include:

- Outstanding wages;
- Wages in lieu of notice, if applicable;
- Payment in lieu of untaken leave;
- Any outstanding sum of end of year payment, and pro rata end of year payment for the current payment period;
- Where appropriate, severance payment or long service payment; and
- Other payments under the employment contract, such as gratuity, provident fund, etc.

### Severance payment

Employee who has worked with a company for not less than 24 months under a continuous contract are eligible for severance payment. And severance payment 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 closes or intends to close the business, the employer has ceased or intends to cease 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.

The severance payment should be calculated according to the following formula:

- For monthly-paid employee

$$\text{SEVERANCE PAYMENT} = \frac{2/3 \text{ OF THE LAST FULL MONTH WAGES}^* \times \text{RECKONABLE YEARS OF SERVICE}}$$

- For daily-rated/piece-rated employee

$$\text{SEVERANCE PAYMENT} = \text{ANY 18 DAYS' WAGES CHOSEN BY THE EMPLOYEE OUT OF THEIR LAST 30 NORMAL WORKING DAYS}^* \times \text{RECKONABLE YEARS OF SERVICE}$$

\* The sum should not exceed 2/3 of HK\$22,500 (i.e. HK\$15,000)

Service of an incomplete year should be calculated on a pro rata basis. Any gratuity and/or employer's contribution together with interests/dividends in Provident Fund (PF) / MPF Schemes can be set off from the total amount of Severance Payment.

The total entitlement is subject to a maximum payment of HK\$390,000. Severance Payment shall be paid to the employee as soon as practicable and not later than two months from the receipt of a notice of claim made by the employee.

To be noted, however, the Legislative Council passed the Employment and Retirement Schemes Legislation (Offsetting Arrangement) (Amendment) Bill 2022 on June 9, 2022, which abolishes the use of the accrued benefits of employers' mandatory contributions under the MPF System to offset severance payment and long service payment. The amendment will be effective in 2025.

## Long service payment

Employees who have been employed under a continuous contract for not less than five years are entitled to long service payment, if:

- The employee is terminated for reasons other than serious misconduct or redundancy;
- The contract expires and is not renewed\*;
- The employee dies (money goes to spouse, children or parents);
- The employee has been issued a certificate in a specified form by a registered medical practitioner or a registered Chinese medicine practitioner, certifying that he is permanently unfit for his present job and he resigns; or
- The employee is aged above 65 and resigns on ground of old age.

The amount of long service payment is calculated by reference to the same formula as for severance payment. The maximum entitlement shall not exceed HK\$390,000. The amount of any contractual gratuity based on length of service is deductible from the amount of long service entitlement. In addition, that part of a retirement scheme payment which is due to the employer's contributions may be deducted from the amount of long service payment. Long Service Payment shall also be paid to the employee as soon as possible but in any case not later than seven days after the day of termination.

*\*If not less than 7 days before the expiry of the fixed term contract in case of long service payment, the employer has offered in writing to renew the contract of employment or re-engage him under a new contract but the employee has unreasonably refused the offer, the employee is not eligible for the entitlements.*



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## Cybersecurity and Data Protection

- ◆ What are the major cybersecurity and data protection laws?
- ◆ What are some of the key compliance requirements?

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# What are the major cybersecurity and data protection laws?

Like other major economies, Hong Kong has been ramping up efforts on improving data privacy protection within its jurisdiction.

In Hong Kong, the *Personal Data (Privacy) Ordinance, Cap 486 of the Laws of Hong Kong (PDPO)* protects the privacy of individuals in relation to personal data, which was amended in 2021 to cope with new privacy challenges and address public concerns.

The PDPO is applicable to both the private and the public sectors. It is technology-neutral and principle-based. The Data Protection Principles (“DPPs” or “DPP”) in the PDPO outline how data users should collect, handle, and use personal data, complemented by other provisions imposing further compliance requirements.

When the PDPO was drafted, reference was made to the relevant requirements under the OECD Privacy Guidelines 1980 and the EU Directive 95/46/EC. Given that the European Union’s General Data Protection Regulation (GDPR), in effect from 2018, contains significant developments on personal data protection as compared to the EU Directive 95/46/EC, the GDPR includes several requirements that are not found under the EU Directive 95/46/EC and the PDPO.

One of the key developments introduced under the GDPR to the data protection landscape outside the EU is the explicit requirement of compliance by organizations established in non-EU jurisdictions in specified circumstances. The Personal Information Protection Law (PIPL) of the Chinese Mainland is also extraterritorial in its application. Given the diversified business scope and multiple types of transaction models (such as, several types of online transactions) in the current economic landscape, it is all the more important for enterprises in Hong Kong to ascertain if the GDPR or the PIPL is applicable to them to keep up with compliance requirements.

Hong Kong has not made a unified law regarding cybersecurity. Some provisions relevant to cybersecurity can be found in different laws including the Crimes Ordinance (Cap. 200), the Telecommunications Ordinance (Cap. 106), the Unsolicited Electronic Messages Ordinance (Cap. 593), and so on. There is no prescribed obligation imposed on cyber use or operators to adopt security measures, except those involving personal data as specified in the PDPO.

# What are some of the key compliance requirements?

Before going into the details of the compliance requirements, it is important to first get familiar with a few key definitions under the PDPO:

- **Personal data** means information that relates to a living individual and can be used to identify that individual. It must also exist in a form that is accessible or the processing of which is practicable.
- **Data subject** is the individual who is the subject of the personal data.
- **Data user** is a person who, either alone or jointly with other persons, controls the collection, holding, processing, or use of personal data.
- **Data processor** is a person who processes personal data on behalf of another person (a data user), instead of for their own purpose(s). Data processors are not directly regulated under the PDPO. Instead, data users are required to, by contractual or other means, ensure that their data processors meet the applicable requirements of the PDPO.

The collective objective of the Data Protection Principles is to ensure that personal data is collected on a fully informed basis and in a fair manner, with due consideration towards minimizing the amount of personal data collected. Once collected, the personal data should be processed in a secure manner and should only be kept for as long as necessary for the fulfillment of the purposes of using the data. Use of the data should be limited to or related to the original collection purpose. Data subjects are given the right to access and make correction to their data.

To be noted, the DPP do not regulate the conduct of data users in detail. It is when a data user fails to comply with the terms of an enforcement notice issued by the Privacy Commissioner for Personal Data after finding of a breach that the individual becomes liable to be punished under the PDPO. A data user will also commit an offence if they, having complied with an enforcement notice, intentionally performs the same act again or makes the same omission. Breach of a DPP can also form the basis of a civil suit against the data user by the aggrieved individual for compensation of damage suffered, regardless of whether an enforcement notice has been issued.

## Purpose and manner of collection

DPP1 (that is, the first Data Protection Principle prescribed in the PDPO) provides that personal data shall only be collected for a lawful purpose directly related to a function or activity of the data user. The data collected should be necessary and adequate but not excessive for such purpose. The means of collection should be lawful and fair.

If the data user collects personal data from data subjects directly, they should inform the data subjects whether it is obligatory or voluntary to supply the data, the purpose of using their data, and the classes of person to whom their data may be transferred. The data user should also inform the data subjects of the right and means to request access to and correction of their data.



## Accuracy and duration of retention

DPP2 requires data users to take all practicable steps to ensure that personal data is accurate and is not kept longer than is necessary for the fulfillment of the purpose for which the data is used. If data user engages a data processor for handling personal data of other persons, they should adopt contractual or other means to ensure that the data processor complies with the mentioned retention requirement.

Section 26 of the PDPO requires data users to take all practicable steps to erase personal data that is no longer required for the purpose for which the data is used, unless erasure is prohibited by law or is not in the public interest. A breach of Section 26 is an offence, punishable by a fine of up to HK\$10,000.

## Use of data

DPP3 prohibits the use of personal data for any new purpose which is not or is unrelated to the original purpose when collecting the data, unless with the data subject's express and voluntary consent. A data subject can withdraw their consent previously given by written notice.

Regarding restrictions on use of personal data, Part 6A of the PDPO further requires that data users must obtain informed consent before using a data subject's personal data for direct marketing or transferring the data to a third party for direct marketing. The consent must be an explicit indication by the data subject and broadly covers an indication of no objection. In other words, silence cannot constitute consent. Besides, the consent must be an informed one.

Failure to comply with the direct marketing requirements is an offence and can result in a fine of HK\$500,000 and imprisonment for three years, or up to a fine of HK\$1,000,000 and imprisonment for five years if data was provided to a third party for gain.

## Data security

DPP4 requires that data users take all practicable steps to protect the personal data they hold against unauthorized or accidental access, processing, erasure, loss, or use. Data users should have particular regard for the nature of the data, the potential harm if the abovementioned events happen, measures taken for ensuring the integrity, prudence and competence of persons having access to the data, etc. If the data user engages a data processor to process the personal data held, they must adopt contractual or other means to ensure that the data processor complies with the mentioned data security requirement.

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## Openness and transparency

DPP5 obliges data users to take all practicable steps to ensure openness of their personal data policies and practices, the kind of personal data held, and the main purposes for holding it.

## Access and correction

DPP6 provides data subjects with the right to request access to and correction of their own personal data. A data user should give reasons when refusing a data subject's request to access or correct their personal data.

DPP6 is supplemented by detailed provisions in Part 5 of the PDPO, which cover the manner and timeframe for compliance with data access requests and data correction requests, the circumstances in which a data user may refuse such requests, etc. Data users are also required to maintain a logbook to record all refusals made.

## Exemptions

While data privacy is an important right, the interests protected under PDPO have to be balanced against other important rights or public interest. PDPO provides a number of exemptions from some compliance requirements under particular circumstances.

Examples include crime prevention or prosecution, security and defense, statistics and research, news activity, protecting a data subject's health, etc. There is also an exemption if the use of personal data is required or authorized by law or court order or is required for exercising or defending legal rights in Hong Kong.

Nevertheless, data users are suggested not to routinely rely on exemptions. Instead, exemptions can only be considered on a case-by-case basis to defend a breach of the PDPO.



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## Our Offices in China

### Beijing

beijing@dezshira.com

### Guangzhou

guangzhou@dezshira.com

### Qingdao

qingdao@dezshira.com

### Suzhou

suzhou@dezshira.com

### Dalian

dalian@dezshira.com

### Hangzhou

hangzhou@dezshira.com

### Shanghai

shanghai@dezshira.com

### Tianjin

tianjin@dezshira.com

### Dongguan

dongguan@dezshira.com

### Ningbo

ningbo@dezshira.com

### Shenzhen

shenzhen@dezshira.com

### Zhongshan

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