

Hong Kong Taxation System

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This summary will present an introduction to the Hong Kong taxation system. The legal basis and practice of the Hong Kong tax regime will be explained with a description of the relevant sources in Hong Kong tax law. Four case studies will be discussed with reference to the Hong Kong Inland Revenue Ordinance (IRO) and Inland Revenue Rules, and Departmental Interpretation and Practice Notes (DIPN). Other relevant decisions by the Board of Review and related court cases will be referenced as well.

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Definition of Tax

According to the Inland Revenue Ordinance Section 2, tax is defined as “any tax imposed by the Inland Revenue Ordinance”. There are three types of tax, namely, direct tax, indirect tax and Ad Valorem duty. Direct tax refers to the tax a person directly pays to the Inland Revenue Department (IRD), whereas indirect tax means the tax that will be indemnified at the expense of another person. Ad Valorem duty is the tax based on a value. The purpose of taxation is to finance the government and the implementation of its policies. Taxation is part of the fiscal policy that facilitates the re-distribution of income.

Source of Hong Kong Tax Law

The sources of Hong Kong tax law can be divided into three parts: statutory law, case law, and other sources. For **statutory law**, major tax legislations are passed by the Legislative Council, which include Inland Revenue Ordinance (Chapter 112), Inland Revenue (Amendment) Ordinance, Inland Revenue Rules (IRR), Stamp Duty Ordinance (SDO) (Chapter 117), and Estate Duty Ordinance (EDO) which was abolished in 2006. The second source, **case law**, includes decisions in precedent cases in Hong Kong courts which are binding for future cases with similar circumstances. Under the common law system, tax cases in the United Kingdom and Commonwealth countries are also a source for Hong Kong tax law. However, a court case decision can be overruled by a new amendment to existing tax legislation. Cases decided by the Board of Review (BoR) are also included as a source for Hong Kong tax law. BoR is an independent statutory body constituted under IRO Section 65 to determine tax appeals regarding decisions made by the Commissioner of Inland Revenue (CIR) and tax assessment under IRO Section 82A. However, BoR decisions are not legally binding. Lastly, other sources for Hong Kong tax law come from the DIPN provided by IRD, which is a booklet containing interpretations of legislations and is for reference only with no binding effect. Despite the above laws, there exist exemptions under specific circumstances. For example, according to IRO Section 87, the Chief Executive has the authority “*to exempt any person, office or institution from payment of the whole or any portion of any tax chargeable under the IRO.*”, and IRO Section 88 provides that the CIR has the authority to exempt charitable institutions from any tax chargeable under the IRO.

Features of the Hong Kong Taxation System

The IRD is the government body responsible for taxation in Hong Kong. It administers different ordinances including IRO (Cap 112), SDO (Cap 117), Betting Duty Ordinance (Cap 108), Estate Duty Ordinance (Cap 111), and Hotel Accommodation Tax Ordinance (Cap 348), among others.

There is a **schedular tax system** in Hong Kong. Tax is imposed under three headings, namely property tax, salaries tax, and profits tax. Interest tax was abolished in 1989. Income that does not fall into any of the categories is not subject to Hong Kong tax. With the exception of personal assessment, which aggregates all income sources of the taxpayer, the schedular tax system in Hong Kong can be deemed to represent a no total income concept.

There is a **territorial source concept** under this taxation system. Income will only be taxed if it arises in or is derived from Hong Kong. Thus, the nationality and residence of a person will be irrelevant in determining whether the income is taxable or not (i.e. no residence concept). To illustrate this point, for salaries tax, only income from [employment or office][*What does “office” mean here? How is it different from employment?*] in Hong Kong will be taxable; for profits tax, only income from trading, business or profession in Hong Kong will be taxable.

There is no capital gains tax in Hong Kong. However, gains from disposal and sale of capital assets may be subject to profits tax if the transaction constitutes a trade, which is determined by facts and circumstances. Furthermore, there is no dividend or interest income tax either.

Lastly, there is a provisional tax assessment system (IRO Section 63B to 63P). It refers to the payment of income tax in instalments during the year of assessment.

Property Tax

The scope of property tax in Hong Kong is provided in IRO s5(1). The owner of any land and/or buildings situated in Hong Kong will be subject to property tax at standard rates on the net assessable value. This means that the citizenship of the owner is irrelevant in determining the imposition of property tax. If the owner does not rent out the property and use it residential purposes, no property tax is charged. The assessable value of the property includes rent, premium, payment for the right to use furniture, and management fee paid to the owner. These are taken into consideration together with money received by the owner in respect of the right to use the land/buildings.

Salaries Tax

The scope of salaries tax in Hong Kong is provided in IRO s.8(1). It states that salaries tax shall be imposed on every person in respect of his/her income arising in or derived from Hong Kong from [office, employment] or pension. The entire income is assessable. So, it is necessary to differentiate whether the income arises from employment, or profession. If it is employment, which means there is a contract of service, the entire income is assessable under salaries tax. However, if it is a profession (meaning the taxpayer is self-employed) and there is a contract for service, the income is subject to profits tax instead. The territorial concept is critical for determination of salaries tax which is dependent on whether Hong Kong is the source of income from employment. If the income is sourced outside Hong Kong, it is non-taxable for purposes of Hong Kong salaries tax. To identify whether the salaries are derived from services rendered in Hong Kong, Goepfert's principles from the court case *CIR v George Andrew Goepfert (1987)* can be referenced. In this case, three factors are considered when deciding the source of employment: (1) the place where the contract of employment is negotiated, entered into and enforceable; (2) whether the employer is resident in Hong Kong; and (3) whether the employee's remuneration is paid in Hong Kong. However, a totality of facts will be considered, which means looking into all facts and circumstances. It can be more complicated in a case where no service is rendered in Hong Kong but the source of employment is Hong Kong, or there is service rendered in Hong Kong but the source of employment is outside Hong Kong. In the first scenario, the income shall be 100% exempt from salaries tax whereas in the second scenario, the income shall be 100% taxable. Time basis apportionment of income shall be applied if the services are partly rendered in Hong Kong (under non-Hong Kong-sourced employment). Lastly, under the Double Taxation Agreements signed between Hong Kong and other countries, the person shall be exempt from Hong Kong salaries tax under several criteria relating to the length of stay and the nature of the remuneration.

Profits Tax

The scope of profits tax is provided in IRO Part 4 Section 14, "*profits tax shall be charged for each year of assessment ... on every person carrying on a trade, profession or business in Hong Kong in respect of his assessable profits arising in or derived from Hong Kong for that year from such trade, profession, or business (excluding profits arising from the sale of capital assets)...*". In other words, it means that there are three criteria to be fulfilled: (1) the person must engage in trade, business or profession, (2) in Hong Kong, and (3) the profit from that trade, business or profession is arisen or derived from Hong Kong. These indicate that the IRD will only consider the locality of profits instead of the residency of the taxpayer. The territorial source concept is important too because it determines if the trade, business or profession is in Hong Kong. A "Permanent Establishment" (IRR5) such as a branch, an agent,

and a subsidiary will be deemed as a trade. The next step is to determine whether the profit from that trade has arisen in or been derived from Hong Kong. Generally, there is a broad guiding principle including operations test, contract conclusion test, provision of credit test, and situs test. These are all from case law decisions.

Three Court Cases regarding Territorial Source Concept

In a landmark court case **CIR v Hong Kong Whampoa Dock Co. Ltd. (1960)**, a salvage ship was sent beyond Hong Kong waters. Upon inspection of the wrecked ship, it had to be pulled back to dock for repairment. Salvage price was negotiated with agreement at sea, and the ship was pulled back from public sea to Hong Kong. According to the final court decision, it was held that most of the obligations were performed outside Hong Kong, therefore the profits earned by the company arose from the salvage operation on the public sea was held as not arising in or derived from Hong Kong, despite the fact that the company was in Hong Kong. This case has set an important precedent for all subsequent cases regarding territorial source concept. The implication from this case is that it established a general rule that whether profit tax is applicable depends on where the operations from which the profit arose were performed.

Another well-known court case **CIR v Hang Seng Bank (1989)** will be referenced as well to show the circumstances under which profits are not taxable in Hong Kong. It was the first case regarding the territorial source concept that was decided by Privy Council. Hang Seng Bank was based in Hong Kong. It collected deposits, invested overseas and earned profits from trading certificates of deposits in London and Singapore through agents, who receive investment instructions from Hong Kong. The certificate of deposits was traded in markets out of Hong Kong and the bank earned profits from the trades. Here, the question is whether the profits arose in or were derived from Hong Kong. The CIR argued that the profits should be chargeable as the business was carried out in and the funds came from Hong Kong, the decisions were made in Hong Kong and the transactions were monitored there too. As according to IRO Section 15(1), deemed receipts on financial institution refer to the “*interest which arises through or from the carrying on by the financial institution of its business in Hong Kong, notwithstanding that the money’s in respect of which the interest is received or accrues are made available outside Hong Kong.*” However, Privy Council ruled that the activities from which the profits had arisen were the purchase and sale of the marketable securities in the overseas market, not Hong Kong. The profits in question were from buying and selling of the securities, not from the original acquisition of the money. The buying and selling could not happen without the original acquisition of deposits in Hong Kong, but it would be considered as a “*causa sine qua non*” (i.e., necessary) rather than a “*causa causans*” (i.e., primary cause) in other branches of the law. But this cannot alter the nature of the transaction, which is the buying and selling of the securities. Therefore, the profits in question were held to be not taxable, since they arose outside Hong Kong.

The implication from this case is that it reaffirms that a person carrying out business in Hong Kong can earn offshore profits not subject to taxation in Hong Kong. It proves that the focus should be on what the person has done to earn the profit in question. Some rules are derived from this case regarding whether certain income is taxable in Hong Kong. For rendering service, it depends on where services are rendered; for engaging activities, it depends on where activities are carried out; for securities, it depends on where the contracts are effected.

Following the Hang Seng Case, a rule of “one looks to see what the taxpayer has done to earn the profits in question and where he has done it” was used by TVB International. However despite the above Hang Seng case, another court case **CIR v HK-TVB International Ltd**

(1992) shows that the Hang Seng case was only an exception. In the TVB case the profits in question were held taxable. This case involves TVB International which earned its profits by sub

-licensing the rights to film to overseas independent TV stations and film distributors. This activity involved TVB international sending agents overseas to negotiate the business deal, and some agreements were entered into by both parties' agents signing the contract in that sub-licensing country, and some contracts were mailed to the overseas client for signing. TVB International was not the producer of the TV program, which was in fact TVB. TVB International acquired the intellectual property right in Hong Kong and sold the right to films to other countries. TVB International argued that TVB International provided a service overseas, and it exploited the assets by sub-licensing rights which were used overseas. In this case, the Privy Council had a guiding principle: "what were the transactions which produced the profit to TVBI". Here the relevant activities included the acquisition of the films and its exclusive rights to them, and granting sub-licenses to overseas customers. The business here of TVBI was the exploitation of film rights in Hong Kong. So, the profits were sourced in Hong Kong and thus taxable. This case shows that the Hang Seng Case was only a rare case in which the taxpayer with business in Hong Kong can earn profits offshore which are not subject to profits tax in Hong Kong. The judge mentioned that "*it is a mistake to try and find an analogy between the facts in this appeal and the example given by Lord Bridge in the Hang Seng Bank case.*".

Court Case regarding the Definition of Trade

With reference to the Royal Commission on the Taxation of Profits and Income 1955, there are six badges of trades established through court cases to consider whether a trade occurs: (1) subject matter of transaction; (2) length of ownership; (3) frequency and regularity of similar transactions; (4) supplementary work on the asset to increase its marketability; (5) circumstances that cause the asset disposal; (6) profit seeking motive. However, no one factor is conclusive. All circumstances must be reviewed as a whole. The most important factor is the original intention of the taxpayer when acquiring the asset. This rule derives from a court case ***Lionel Simmons Properties Ltd v CIR (1980)***. An implication from this case is that a trade requires an intention to trade. The question is whether this intention existed at the time of acquiring the asset. As it is hard to determine a person's original intention, objective evidence can be provided to infer the original motive. Evidence includes the person's ability to finance and hold the asset as a long-term investment, how the person acquired the asset, and any documents showing the intention, among others. If all the circumstances show that the person intended to invest in the asset rather than trade it at the time of acquisition, then the income is not taxable.

Court Case regarding the Intention to Trade (Property Trading or Investment)

Further from the above case regarding the original motive of trade, there is another case ***Church Body of the Hong Kong Sheng Kung Hui v CIR (2014)***, which illustrates the definition of property trading versus investment. The question in this case was whether there was a change in intention from capital holding to trading, and if so, the profits arising from the sale of the land should be chargeable for profits tax.

Before we look into the case, we should look at a few of the six badges of trade that are relevant to it as mentioned. For the subject matter of transaction, it concerns whether the property or asset is acquired for the purpose of trading or for long-term investment. Generally, if the asset does not yield income or personal enjoyment through its ownership to the

taxpayer, it will be regarded as acquired for trading purpose rather than for long-term holding. If there is any evidence showing that the taxpayer is involved in both the acquisition and resale of the asset, it is likely that the transaction is in the nature of trade. For the length of ownership, it concerns how long the taxpayer holds the asset. The longer the period of ownership, the less likely the asset is for trade. For supplementary work on the asset, it concerns if the taxpayer has made the asset more marketable through improvements and repairs, or if the taxpayer has been actively looking for buyers through advertising, and in the latter case, the transaction is likely to be in the nature of trade. The important question is whether the taxpayer has enhanced the value of the asset. Lastly, to establish a profit-seeking motive, it depends on if the taxpayer, at the time of acquisition, acquired the asset with an intention of seeking profits by resale.

The background of this case is that the taxpayer owned a large estate in Tai Po since the 1930s. Then since the 1970s, the planned use of the land was partly for residential development and partly for institutional use. Since 1989, only residential development was involved in the plan. In order to redevelop that land, the taxpayer must receive approval and pay the difference in planned land use. Below is the timeline of the relevant key events in the case. In December 1990, the taxpayer applied for a surrender and regrant of the land, and in October 1992, the land premium was assessed at \$838,260,000, which was subsequently reduced to \$704,240,000 in May 1993. In July 1993, the taxpayer solicited tender offers from property developers, and Cheung Kong accepted tender. In December 1993, the taxpayer and Cheung Kong entered a joint venture for the residential development with 129 units and 94 parking spaces. These steps taken by the taxpayer eventually led to the redevelopment of the land with significant profits. An assessment of profits tax was sent to the taxpayer, who then appealed to the BoR, and then made further appeals to the Court of First Instance and the Court of Appeal.

The BoR assessed tax amounts of \$75.8 million and \$108.9 million. It argues that there was a change in intention from capital holding to trading since September 1989 even though the land was initially acquired as a capital asset. The first appeal to the CFI upheld the BoR decision, but the COA and CFA reversed it, stating that *“there must be evidence which establish the change of intention”*, and *“it is unhelpful to ask whether there is an enhancement for realization principle and I would not use that expression. I believe the expression...may provide a guide to the ultimate decision whether...the owner was engaged in trade”*. This means that the enhancement activities did not necessarily lead to the conclusion that the taxpayer was engaged in a trading activity. It is also stated that there is no “enhancement for realization principle” as set by precedent cases. Each case is judged on the totality of facts and the surrounding circumstances to infer the original intention of the taxpayer. Although the above-mentioned six badges of trade may act as a guideline, it is not conclusive and none of the single badges can be decisive. The CFA also stated that the BoR did not consider whether the taxpayer had spent substantial effort in selling the land that goes beyond what would generally be expected by a non-trader. In conclusion, the takeaway from this case is that there is room for a person to enhance his/her assets and this activity may not necessarily constitute trading, as long as upon selling the asset, the enhancement activity has not gone beyond what a non-trading owner would likely have done. It also underscores a rule that there is no single factor or a comprehensive principle which can perfectly determine whether a transaction is a trade. Each case is judged according to its circumstances and facts.

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Commissioner of Inland Revenue V. Hong Kong & Whampoa Dock Company Limited (1960) 1 HKTC 85.

Commissioner of Inland Revenue V. Mr. George Andrew Goepfert [1987] HKCFI 100; HCIA 5/1986 (10 April 1987). Retrieved from <https://www.hklii.hk/eng/hk/cases/hkcfi/1987/100.html>

Commissioner of Inland Revenue V. Hang Seng Bank Ltd. [1989] HKCA 356; HCIA 7/1988 (3 May 1989). Retrieved from [https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/1989/356.html?stem=&synonyms=&query=\(whampoa%20dock\)%20OR%20ncotherjcitationtitles\(whampoa%20dock\)](https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/1989/356.html?stem=&synonyms=&query=(whampoa%20dock)%20OR%20ncotherjcitationtitles(whampoa%20dock))

Commissioner of Inland Revenue v. HK- TVB International Ltd Co [1992] UKPC 21 (20 July 1992). Retrieved from [https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/ukpc/1992/21.html?stem=&synonyms=&query=\(tvb%20international\)%20OR%20ncotherjcitationtitles\(tvb%20international\)](https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/ukpc/1992/21.html?stem=&synonyms=&query=(tvb%20international)%20OR%20ncotherjcitationtitles(tvb%20international))

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Departmental Interpretation and Practice Notes. Inland Revenue Department, Hong Kong SAR Government. Retrieve from <https://www.ird.gov.hk/eng/ppr/dip.htm>

Halkyard, A. (2006). Source of Profits - its Time (for Change). Retrieved from [https://www.semanticscholar.org/paper/Source-of-Profits-its-Time-\(for-Change\)-Halkyard/e5620f5d7cbe33aed592acb5361adb0c1a884524](https://www.semanticscholar.org/paper/Source-of-Profits-its-Time-(for-Change)-Halkyard/e5620f5d7cbe33aed592acb5361adb0c1a884524)

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Inland Revenue Board of Review Decisions. (2000). Case No. D119/00. Retrieved from <https://www.info.gov.hk/bor/en/docs/d11900.pdf>

Inland Revenue Board of Review Decisions. (1989). Case No. D40/89. Retrieved from <https://www.info.gov.hk/bor/en/docs/d4089.pdf>

Inland Revenue Board of Review Decisions. (1993). Case No. D59/92. Retrieved from <https://www.info.gov.hk/bor/en/docs/d5992.pdf>

Kuan, L. (1991). Determining Sources of Income – A New Guiding Principle? Commissioner of Inland Revenue v. Hang Seng Bank Ltd. *Singapore Journal of Legal Studies*, 517-529. Retrieved December 15, 2020, from <http://www.jstor.org/stable/24865820>

Kuan, L. (1992). Income Tax - Source Principle Refined? Commissioner of Inland Revenue v. HK-TVB International Limited. Singapore Journal of Legal Studies, 566-578. Retrieved December 15, 2020, from <http://www.jstor.org/stable/24866195>

Lau Macpherson, A. (2015). *Hong Kong taxation: law and practice*. The Chinese University Press.

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Lionel Simmons Properties Ltd (In Liquidation) v CIR 53 TC 461.

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Stamp Duty Ordinance (Chapter 117), Hong Kong SAR Government. Retrieved from <https://www.elegislation.gov.hk/hk/cap117?p0=1&p1=1>

APPENDIX

Additional resources and readings

Deloitte. (2020). Hong Kong Tax Guide 2020. August 2020. Retrieved from <https://www2.deloitte.com/content/dam/Deloitte/cn/Documents/tax/ta-2020/deloitte-cn-tax-tap-0382020-en-200806.pdf>

- This reference is useful to quickly have an insight about the Hong Kong taxation system in brief. For example, it gives an overview of the system, particularly profits tax and salaries tax. From this source, it is noticed that the characteristics of the Hong Kong tax system include: simple tax system, territorial source concept, no interest income tax, no capital gain tax, no VAT, no real estate duty etc. This reference also gives guidelines on the compliance of the different types of tax. For example, the tax administration of profits tax starts from filing by the companies, then an assessment by IRD.
- Details regarding tax assessment which covers year of assessment (Y/A) and basis period are included with tax rates.

Departmental Interpretation and Practice Notes. Inland Revenue Department, Hong Kong SAR Government. Retrieve from <https://www.ird.gov.hk/eng/ppr/dip.htm>

- The source of Hong Kong tax law is from the IRO. However, DIPN is a guideline written by IRD to illustrate the laws under IRO. So, it is a critical reference to clarify some concepts about the sections. It is issued to explain the tax principles regarding computation of assessable amount. Its content also includes profits tax, property tax, salaries tax, Double Taxation Agreements, locality of profits etc. For my study, I have looked at DIPN No.1 about the scope of charge of salaries tax. I have also examined

DIPN No.13 to get a clear idea about the taxation of interest received under profits tax.

Halkyard, A. (2006). **Source of Profits - its Time (for Change)**. Retrieved from [https://www.semanticscholar.org/paper/Source-of-Profits-its-Time-\(for-Change\)-Halkyard/e5620f5d7cbe33aed592acb5361adb0c1a884524](https://www.semanticscholar.org/paper/Source-of-Profits-its-Time-(for-Change)-Halkyard/e5620f5d7cbe33aed592acb5361adb0c1a884524)

- This article discusses the law in Hong Kong which determines the source of profits. Several case laws and DIPN are included to show the controversy regarding the final decisions. Court cases such as CIR v Hang Seng Bank Ltd [1991] and CIR v HK-TVB International Ltd [1992] are included to demonstrate what the IRO means by "profits arising in or derived from Hong Kong". This research enables the reader to get an understanding of the rationale behind the judgments by the court, for example, by considering which factor is the most important in determining whether the income is assessable. It will be further discussed in the summary.

Ho, P. K.-W. (2019). **Hong Kong taxation and tax planning** (18th edition.). Hong Kong: Pilot Publishing Company Ltd.

- This reference is a study guide for Hong Kong taxation with reference to the law and legislation. Although much of its content is about tax computation, it gives a thorough idea of the concepts, for example, the source of employment, intention to trade etc. It provides a fundamental concept such as the current development of the tax law and the principles as set out by the precedent cases.

Inland Revenue Board of Review Decisions. (2000). Case No. D119/00. Retrieved from <https://www.info.gov.hk/bor/en/docs/d11900.pdf>

- This BoR decision referred to the case CIR v George Andrew Goepfert as a reference regarding the source of income under salaries tax. The three factors test were used in this case. It will be further discussed in the summary.

Inland Revenue Board of Review Decisions. (1989). Case No. D40/89. Retrieved from <https://www.info.gov.hk/bor/en/docs/d4089.pdf>

- This BoR decision referred to the case CIR v Hong Kong Whampoa Dock Co. Ltd. (1960) to come up with the final decision about the source of profits. A totality of facts is looked at to decide that the profits did arise in or derive from Hong Kong. It will be further discussed in the summary.

Inland Revenue Board of Review Decisions. (1993). Case No. D59/92. Retrieved from <https://www.info.gov.hk/bor/en/docs/d5992.pdf>

- This BoR decision referred to the case CIR v HK-TVB International Ltd (1992) with reference to other court cases such as CIR v Hang Seng Bank Ltd 3 HKTC 351 and CIR v The Hong Kong and Whampoa Dock Co Ltd 1 HKTC 85. The BoR compares the differences in those cases and finally allowed the appeal. It will be further discussed in the summary.

Kuan, L. (1991). **Determining Sources of Income – A New Guiding Principle?** **Commissioner of Inland Revenue v. Hang Seng Bank Ltd.** Singapore Journal of Legal Studies, 517-529. Retrieved December 15, 2020, from <http://www.jstor.org/stable/24865820>

- This journal discussed the case CIR v. Hang Seng Bank Ltd. in a professional manner.

It shows the confusing area of Hong Kong tax law even though there has already the IRO. It demonstrates how to effectively interpret tax statutes of the IRO and analyze the tax issues in the mentioned court cases. The writer has evaluated the legal arguments by CIR throughout the discussion which enables me to understand the controversy behind the Hang Seng Bank Case. It will be further discussed in the summary.

Kuan, L. (1992). **Income Tax - Source Principle Refined? Commissioner of Inland Revenue v. HK-TVB International Limited.** Singapore Journal of Legal Studies, 566-578. Retrieved December 15, 2020, from <http://www.jstor.org/stable/24866195>

- This journal offers a professional perspective on the court case CIR v. HK-TVB International Limited. It is said that it is impossible to formulate a definite test or guiding rules to determine the source of profits. Again, the writer evaluated the arguments of both parties which allow me to discover the case in great detail. It will be further discussed in the summary.

Lau Macpherson, A. (2015). **Hong Kong taxation: law and practice.** The Chinese University Press.

- This book is a study guide about the taxation system in Hong Kong. It gives reference to landmark court cases and DIPNs to demonstrate some important concepts such as territorial source concept and scheduler system. Besides, it interprets the laws in the IRO in a different way which is easier to understand with examples. Thus, I could easily apply it to the court case to understand the rationale behind the judgments.

Lee, D. (2016). **Advanced taxation in Hong Kong** (18th edition.). Hong Kong: Pearson Education Asia Limited.

- This book is another study guide about the taxation system in Hong Kong. Same as the two other study guides, it focuses more on the tax computation. But court cases are well illustrated in a reasoned manner to analyze the complicated and practical problems regarding the tax system in Hong Kong. In addition, the writer has discussed something on the current development of the tax system, for example, some new amendments on the IRO to prevent tax avoidance among taxpayers or avoid legal loopholes.

PWC. (2014). **Enhancement of a capital asset for sale does not point to a trading intention, the court held in the Sheng Kung Hui case.** News Flash Hong Kong Tax. Retrieved from <https://www.pwccn.com/en/hk-tax-news/hktax-news-sep2014-11.pdf>

- This article helps the reader understand the lesson from the court case Church Body of the Hong Kong Sheng Kung Hui v CIR (2014) regarding how to determine the change of intention. It examines the message from the Sheng Kung Hui case. In this case, the key message is enhancement activities to increase the value of an asset may not necessarily lead to a change in intention from capital holding to trade. It really depends on whether the enhancement activities are realized. However, the writer also mentioned that the taxpayer needs to be careful in determining what is being considered as going beyond the safe zone of enhancement activities. Another lesson from the writer is that during the tax appeal process by the taxpayer, how the taxpayer words its activities between acquisition and the sale of the asset is important, and may eventually impact the court's decision in determining whether it is taxable or not. It will be further discussed in the summary.

PWC. (2016). **Sheng Kung Hui's enhancement activities do not constitute trading albeit there is no enhancement for realization principle.** News Flash Hong Kong Tax. Retrieved from <https://www.pwccn.com/en/hk-tax-news/hktax-news-mar2016-1.pdf>

- Same as the above reference, this article helps the reader understand the judgment from the court case Church Body of the Hong Kong Sheng Kung Hui v CIR (2014) on the concept of 'enhancement for realization principle'. The writer emphasizes the court's judgment that there is no single principle that can be applied to a case in determining the assessable value. All of the circumstances and questions of facts need to be taken into account. The taxpayer has to demonstrate its enhancement activities on the asset is within the safe zone. It will be further discussed in the summary.

Applicable case studies:

Church Body of The Hong Kong Sheng Kung Hui and Another V. Commissioner Of Inland Revenue [2014] HKCA 445; [2014] 5 HKLRD 384; [2015] 1 HKC 109; CACV 41/2010 (11 September 2014). Retrieved from [https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/2014/445.html?stem=&synonyms=&query=\(lionel simmons\) OR ncotherjcitationtitles\(lionel simmons\)](https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/2014/445.html?stem=&synonyms=&query=(lionel%20simmons)%20OR%20ncotherjcitationtitles(lionel%20simmons))

- This reference is one of the examples of the court case regarding the intention to trade under profits tax. The question in this case is whether there was a change in intention from capital holding to trading, and if so, the profits arising from the sale of the land should be chargeable to profits tax. It is further discussed in the summary.

Commissioner of Inland Revenue V. Hong Kong & Whampoa Dock Company Limited (1960) 1 HKTC 85.

- This reference is one of the examples of the court case regarding the territorial source concept under profits tax. This case is a landmark case which sets an important reference for all subsequent cases.
- In this case, a salvage ship was sent beyond Hong Kong waters. Under the inspection on the wrecked ship, the ship had to be pulled back to dock for repairment. Salvage price was negotiated with agreement at sea, and the ship was pulled back from public sea to Hong Kong.
- It was held that most of the operations were operated outside Hong Kong, therefore the profits earned by the company arose from the salvage operation on the public sea was held as not arising in or derived from Hong Kong.
- This case sets out a general rule on where the person performed those activities. Therefore, whether a profit is taxable depends on the operations involved in which the profit was realized. It is further discussed in the summary.

Commissioner of Inland Revenue V. Mr. George Andrew Goepfert [1987] HKCFI 100; HCIA 5/1986 (10 April 1987). Retrieved from <https://www.hklii.hk/eng/hk/cases/hkcfi/1987/100.html>

- This reference is one of the examples of the court case regarding the source of employment under salaries tax. This case is a historically important case which sets a broad guiding principle of the three factors which were mentioned in the summary.

- In this case, it is concluded that three factors are considered when deciding the source of employment: (1) the place where the contract of employment is negotiated, entered into, and enforceable; (2) whether the employer is resident in Hong Kong; and (3) whether the employee's remuneration is paid in Hong Kong.
- However, a totality of facts will be considered which look into all the facts and circumstances. It is further discussed in the summary.

Commissioner of Inland Revenue V. Hang Seng Bank Ltd. [1989] HKCA 356; HCIA 7/1988 (3 May 1989). Retrieved from [https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/1989/356.html?stem=&synonyms=&query=\(whampoa dock\) OR ncotherjcitationtitles\(whampoa dock\)](https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/hkca/1989/356.html?stem=&synonyms=&query=(whampoa+dock)ORncotherjcitationtitles(whampoa+dock))

- This reference is another example of the court case regarding the territorial source concept under profits tax, about financial institutions trading securities and earning profits outside Hong Kong.
- It was the first case regarding the territorial source concept decided by Privy Council. Hang Seng Bank, based in Hong Kong invested overseas and earning profits from trading certificates of deposits. The question is whether the profits arose in or were derived from Hong Kong. The CIR argued that the profits should be chargeable as the business and the fund were carried out and came from Hong Kong, and the decisions were made in Hong Kong by such the transactions were monitored there too. It is further discussed in the summary.

Commissioner of Inland Revenue v. HK- TVB International Ltd Co [1992] UKPC 21 (20 July 1992). Retrieved from [https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/ukpc/1992/21.html?stem=&synonyms=&query=\(tvb international\) OR ncotherjcitationtitles\(tvb international\)](https://www.hklii.hk/cgi-bin/sinodisp/eng/hk/cases/ukpc/1992/21.html?stem=&synonyms=&query=(tvb+international)ORncotherjcitationtitles(tvb+international))

- This reference is another example of the court case regarding the territorial source concept under profits tax. This case is a landmark case which illustrates a different decision compared to the Hang Seng Bank case.
- In the TVB case the profits in question was held taxable. This case involves TVB International which earned its profits by sub-licensing the rights to film to overseas independent TV stations and film distributors. This activity was done by sending agents overseas to negotiate the trade, and some agreements were concluded by both parties' agents signing the contract in that sub-licensing country, and some contracts were mailed to the overseas client for signing. TVB International was not the producer of the video, which is in fact TVB. TVB International acquired the right of intellectual property in Hong Kong and sold the right to film to other countries. TVB International argued that TVB International produced a service overseas, and it exploited the assets by sub-licensing rights which were used overseas. In this case, the Privy Council had a guiding principle: "what were the transactions which produced the profit to TVBI". Here the activities involved include the acquisition of the films and its exclusive rights of film, and granting sub-licenses to overseas customers. The business here of TVBI was the exploitation of film rights in Hong Kong. So, the profits were sourced in Hong Kong and thus taxable. This case shows that the Hang Seng Case was only a rare case in which the taxpayer with business in Hong Kong can earn profits offshore which are not subject to profits tax. The judge mentioned that "it is a mistake to try and find an analogy between the facts in this appeal and the example given by Lord Bridge in the Hang Seng Bank case."
- In this case, the Privy Council had a guiding principle: "what were the transactions which produced the profit to TVBI". Here the activities involved include the

acquisition of the films and its exclusive rights of film, and granting sub-licenses to overseas customers. The business here of TVBI was the exploitation of film rights in Hong Kong. So, the profits were sourced in Hong Kong and thus taxable. It is further discussed in the summary.

Lionel Simmons Properties Ltd (In Liquidation) v CIR 53 TC 461.

https://library.cronerico.uk/cch_uk/btc/53-tc-461

- An implication from this case is a trade requires an intention to trade. The question is whether this intention existed at the time of acquiring the asset. As it is hard to determine a person's original intention, objective evidence can be provided to infer the original motive. It is further discussed in the summary.

Applicable laws

Inland Revenue Ordinance (Chapter 112) and Inland Revenue Rules, Hong Kong SAR Government. Retrieved from <https://www.elegislation.gov.hk/hk/cap112>

- The Hong Kong Inland Revenue Ordinance (Cap. 112) and Inland Revenue Rules provide insights about the laws of Hong Kong taxation. Divided into several parts, Part 2 focuses on Property Tax, Part 3 focuses on Salaries Tax, and Part 4 focuses on Profits Tax. There are different sections and schedules. Subsidiary legislation including Inland Revenue Rules and Double Taxation Relief Arrangements are included. In my summary, some sections are cited.

Inland Revenue Department. (2020). *Double Taxation Agreements*, Hong Kong SAR Government. Retrieved from https://www.ird.gov.hk/eng/tax/dta_inc.htm

- The Double Taxation Agreements (DTAs) are established between Hong Kong and a number of jurisdictions to prevent double taxation.

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