KPMG

HONG KONG TAX ALERT

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New transfer pricing legislation introduces changes to Salaries Tax relief for double taxation

Summary

Amendments to the existing double taxation relief mechanism for Hong Kong Salaries Tax, introduced as part of the new transfer pricing regime, may have an impact on mobile employees who are subject to Salaries Tax and who render services and pay tax abroad.

On 4 July 2018, the Legislative Council enacted Hong Kong's new transfer pricing regime. Included in the legislation were a number of amendments relating to the existing double taxation relief mechanisms for Salaries Tax. The amendments potentially impact employees based in Hong Kong who work partly in other territories and pay tax in those territories.

In particular, an amendment was made to the exemption under section 8(1A)(c) of the Inland Revenue Ordinance. This exempts from Salaries Tax income for services rendered in another territory which is also subject to tax in that other territory. Going forward, if the double taxation arises in a territory with which Hong Kong has a tax treaty[1], and the taxpayer can claim tax credit relief under that tax treaty, the outright exemption under this section will no longer be available. Instead, the income will be subject to Salaries Tax and foreign tax credit relief will have to be claimed.

Although this may not appear to be a significant change, in some cases, this change will result in a higher effective tax rate than was previously the case. This is because the method used to calculate the tax credit relief often means that some Salaries Tax will remain payable. Some taxpayers will be subject to actual double taxation – that is, they will pay tax in Hong Kong and in the other territory on the same income.

[1] Currently, Hong Kong has entered a comprehensive double taxation agreement ("CDTA") with 40 territories with the most recent being with Finland. Hong Kong has concluded CDTAs with: Austria, Belarus, Belgium, Brunei, Canada, Czech, Finland, France, Guernsey, Hungary, India, Indonesia, Ireland, Italy, Japan, Jersey, Korea, Kuwait, Latvia, Liechtenstein, Luxembourg, Mainland of China, Malaysia, Malta, Mexico, Netherlands, New Zealand, Pakistan, Portugal, Qatar, Romania, Russia, Saudi Arabia, South Africa, Spain, Switzerland, Thailand, UAE, United Kingdom and Vietnam.

The new legislation also introduced a number of "enhancements" to the current tax credit system:

- Extended period for claiming tax credit relief from two years to six years;
- Requiring taxpayers to minimise their foreign tax liability by making full use of all other available relief under any tax treaty and local legislation in the foreign territory before resorting to tax credit relief; and
- Mandating that taxpayers notify the Inland Revenue Department (IRD) of amendments to their foreign tax payments.

The amendments to the double taxation relief mechanisms for Salaries Tax apply in relation to tax payable for a year of assessment beginning on or after 1 April 2018. Therefore the new regime will have effect for the year of assessment 2018/19.

KPMG observations

The removal of the ability to claim unilateral relief will result in some taxpayers in Hong Kong paying more tax. Throughout the consultation process and in the paper prepared by the House Committee for the Legislative Council, the suggestion was that the changes were necessary to align domestic relief with the expectations of Hong Kong's tax treaty partners.

If these issues could impact you or your employees, please contact one of our Global Mobility Services contacts below.

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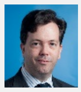

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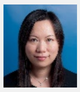

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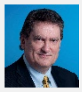

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