

Newsletter Nr. 81 (EN)

**Income tax liability for in Hong Kong
employed persons rendering services
outside Hong Kong**

August 2011

I. General overview

1. Introduction

In Hong Kong, personal income tax is known as “salaries tax”, regulated by law in the “Inland Revenue Ordinance” (IRO). Salaries Tax is only levied on the annual income of an individual derived from employment.

Income, not generated through employment, such as accrued dividends or profits realised through the sale of shares, is not subject to taxation in Hong Kong.

Any employee’s income is subject to “salaries tax”, whereas income of a self-employed person is subject to “profit tax”.

2. Territoriality Principle

Which parts of the income actually are subject to “salaries tax” is determined by using the Territoriality Principle. As a result of the appliance of this principle, income is only subject to salaries tax if the income is generated through an employment in Hong Kong or such income is derived from such employment in Hong Kong.

(Section 8(1)):

(1) Salaries tax shall, subject to the provisions of this Ordinance, be charged for each year of assessment on every person in respect of his income arising in or derived from Hong Kong from the following sources-

(a) any office or employment of profit; and

(b) any pension.

The definition of income in this context includes remuneration, salary, allowances, bonuses and employer’s payments into pension funds. However, it does not include achievements from pension funds which are not established under the jurisdiction of

Hong Kong or compensations for the loss of employment.

3. Rate of taxation in Hong Kong

There are two different alternatives of computing “salaries tax”. It is the tax payer’s right to opt for the alternative leading to a lower tax burden:

- a flat tax rate of 15 % on the assessable income after all deductions (From 2008/09 onwards), or
- a progressive tax rate levied on the assessable income after the deductions of expenses and allowances.

The progressive rates for the assessment years 2009/10 are as follows:

HK\$ 0 to HK\$40,000	2%
HK\$40,000 to HK\$80,000	7%
HK\$80,000 to HK\$120,000	12%
HK\$120,000 and more	17%

Nevertheless, for the financial year 2010/2011, 75% of the salaries tax is waived, capped at HKD 6,0000.

II. Salaries tax for services rendered offshore

1. General view of Hong Kong’s Inland Revenue Department (IRD)

In connection with the Territoriality Principle, the following has to be taken into consideration:

When determining whether an employment is a “Hong Kong employment” (source of employment) the IRD in general regards the three following factors as relevant:

- a. where the contract of employment was negotiated and entered into, and is enforceable; and
- b. the place of residence of the employer; and
- c. the place of payment of the employee's remuneration.

Accordingly, if all three conditions are fulfilled, the IRD assumes a Hong Kong employment with the consequence that the income out of such employment is taxed in Hong Kong.

The Hong Kong tax authorities have the reputation to examine each individual case carefully. In case a tax payer objects to the assessed tax, it is likely that the IRD demands a substantial documentation supporting the view of the taxpayer.

The IRD will normally determine an employment as a Hong Kong employment, if the employer is a Hong Kong resident, even though the contract of employment might have been negotiated and signed in another country.

The Board of Review held the following view in a case with an employee from the US, where all details of the contract were negotiated and finalised in the United States:

“He (the employee) was not employed by any company in the United States and he was not subject to any master and servant relation with any United States company. His master and servant relation was clearly with the company in Hong Kong with whom he entered into an employment contract. In the circumstances of this case the fact that he was physically in the United States when he received the employment contract is not material.”¹

2. Services rendered offshore

However, Hong Kong's tax law provides clear regulations on taxation of income derived from services rendered outside Hong Kong:

(Inland Revenue Ordinance (Cap 112), Section 8(1A) (b)):

¹ Case No. D8/92, 7 IRBRD 107

(1A) for the purposes of this Part, income arising in or derived from Hong Kong from any employment:

- (a).....
- (b) excludes income derived from services rendered by a person who-
 - (i) is not employed by the Government or as master or member of the crew of a ship or as commander or member of the crew of an aircraft; and
 - (ii) renders outside Hong Kong all the services in connection with his employment; and
- (c) excludes income derived by a person from services rendered by him in any territory outside Hong Kong where-
 - (i) by the laws of the territory where the services are rendered, the income is chargeable to tax of substantially the same nature as salaries tax under this Ordinance; and
 - (ii) the Commissioner is satisfied that that person has, by deduction or otherwise, paid tax of that nature in that territory in respect of the income

Consequently, all salary paid in Hong Kong deriving from services rendered outside Hong Kong is exempted from “salaries tax”, however, only if the salary actually has been taxed in a foreign jurisdiction.

III. Deductions and allowances

Hong Kong's general tax rate is one of the lowest in the world. Therefore, tax deductions are limited. All together there are three types of tax deductions available:

- a. *Outgoings and Expenses;*
- b. *Concessionary deductions, and*
- c. *Allowances* (not applicable for tax-payers paying the flat tax rate).

Deductible expenses in the assessment period 2009/10:

- charitable donations up to 35% of the personal income;
- residential care expenses for parents and grandparents up to HK\$72,000 p.a.(the parents/ grandparents must be aged 60 or above);

- home loan interest up to HK\$100,000 p.a. limited to a maximum of ten years;
- mandatory contributions to recognized retirement schemes up to HK\$12,000 p.a.;
- depreciation on factories and machines, which are necessary for earning personal income;
- personal allowance in the amount of HK\$108,000 (singles) and HK\$216,000 (married persons);
- child allowance in the amount of HK\$60,000 for each child;
- dependant parent, dependant grandparent, dependant brothers and sisters allowance HK\$30,000 each person;
- disabled dependant allowance HK\$60,000;
- Expenses of self-education HK\$60,000.

IV. “Housing Benefits”

1. Introduction

The so called “Housing Benefits” are not deductible from tax and therefore have to be considered when calculating the taxable income.

This also applies, if the employer pays the rent for an apartment in Hong Kong and provides it to his employee rent-free during the term of the employment.

According to Section 9(1) (b) (c) the so called “rental value” is part of the employee’s taxable income:

- (1) *Income from any office or employment includes-*
- (a).....
- (b) the rental value of any place of residence provided rent-free by the employer or an associated corporation;

(c) where a place of residence is provided by an employer or an associated corporation at a rent less than the rental value, the excess of the rental value over such rent;.....

It is significant whether the employee’s residence is provided 100 % rent-free, or only for less than the normal rental value.

2. 100% rent-free

In case the residence is provided 100 % rent-free the surplus to be added to the taxable income is dependant on the type of accommodation.

Type of accommodation	Surplus in %
flat or serviced apartment	10%
two rooms in a Hotel, Hostel or Boarding House	8%
one room in a Hotel, Hostel or Boarding House	4%

Note: If the employer provided a flat which is shared by more than one employee, the computation of the rental value is the same as that for a hotel, hostel or boarding house.

3. Provision for less than the normal rental value

In the case the employer provides to the employee his residence for a rent less than the rental value, the excess of the rental value over such rent is a taxable income, according to *Inland Revenue Ordinance (Cap 112), section 9 (1)(c)*.



We hope that the information provided in this brochure was helpful for you. If you have any further questions please do not hesitate to contact us.

Lorenz & Partners (Hong Kong) Limited
Unit 1003, 10th Floor, Kinwick Centre, 32 Hollywood Road, Hong Kong SAR
Tel: +852(0) 252 814 33 Fax: +852 (0) 254 114 11
E-Mail: hongkong@lorenz-partners.com

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