

Hong Kong clarifies certain profits tax issues

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In its 2019 annual meeting, the Hong Kong Tax Authority (HKTA) clarified the following matters:

Timing of tax deductions for operating leases

If there is a rent-free period under an operating lease for real estate, the accounting expense recognized in a financial year would be different from the contractual rental payments made during the year.

The HKTA stated that the tax deductible amount for this lease arrangement should be equal to the accounting expense.

Nonresident enterprise with a Hong Kong promotional agent might be exposed to tax in Hong Kong

Under the tax law, a non-treaty jurisdiction resident enterprise is considered to have a permanent establishment (PE) in Hong Kong if a person (1) habitually concludes contracts in Hong Kong on behalf of the enterprise or (2) habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise.

The HKTA's view is if a person regularly and actively solicits potential customers in Hong Kong to convince them to conclude contracts containing standard terms with the nonresident enterprise, such person in Hong Kong would be regarded as "playing the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise."

Timing of payment of tax withheld

The HKTA's position is that a Hong Kong payer is required to pay the tax withheld to satisfy the liability of a nonresident person¹ when the Hong Kong payer records the accounting liability to pay the amount to the nonresident person. This may be earlier than the Hong Kong payer is contractually required to pay the amount to the nonresident person.

Endnote

1. Subject to tax pursuant to section 20B(2) of the Inland Revenue Ordinance.

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