

# The Changing Landscape of Inbound and Outbound Investment to and from Hong Kong: Taxation Implications for Investors and Corporate Entities

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TAXATION LAW RESEARCH PROGRAM (TLRP)

THURSDAY, 25 AUGUST 2022, 3:00 – 4:00 PM  
HONG KONG TIME VIA ZOOM

# About the Presenter

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Dr Sarah Hinchliffe is an AIFL Honorary Fellow at the University of Hong Kong, and specializes in international and comparative taxation law and corporate strategy. Dr Hinchliffe is an Australian Lawyer as well as a Chartered Tax Advisor, an Associate member of the Law Institute of Victoria, and of the Taxation Institute of Australia. She has practical experience in taxation law having worked for the Australian Taxation Office and in private legal practice. Dr Hinchliffe is a co-founder of a boutique law firm based in Melbourne, Australia. She has held international academic appointments, including at Harvard Law School, the College of William and Mary, Boston University School of Law, the University of Akron, the University of Nevada William S. Boyd School of Law, the University of Hong Kong, the University of Melbourne, Monash University, Victoria University, and the Taxation Institute of Australia. Dr Hinchliffe has been an external editor for the Law Institute Journal, Editor in Chief of the Journal of Australian Taxation, and has been engaged by the Productivity Commission as a consultant.

# Overview

Businesses continue to look to expand beyond their domestic market into new markets. This creates novel business opportunities but navigating taxation implications can pose its own complexities. This presentation addresses current outbound and inbound entity structures, tax compliance issues, and comments on indirect tax planning and advice. Of interest to tax practitioners and accountants is the changing landscape of outbound and inbound investments concerning Hong Kong in the present economy, and ongoing strategies to better develop corporate structures for foreigner operations.

International activities are a 2-way street

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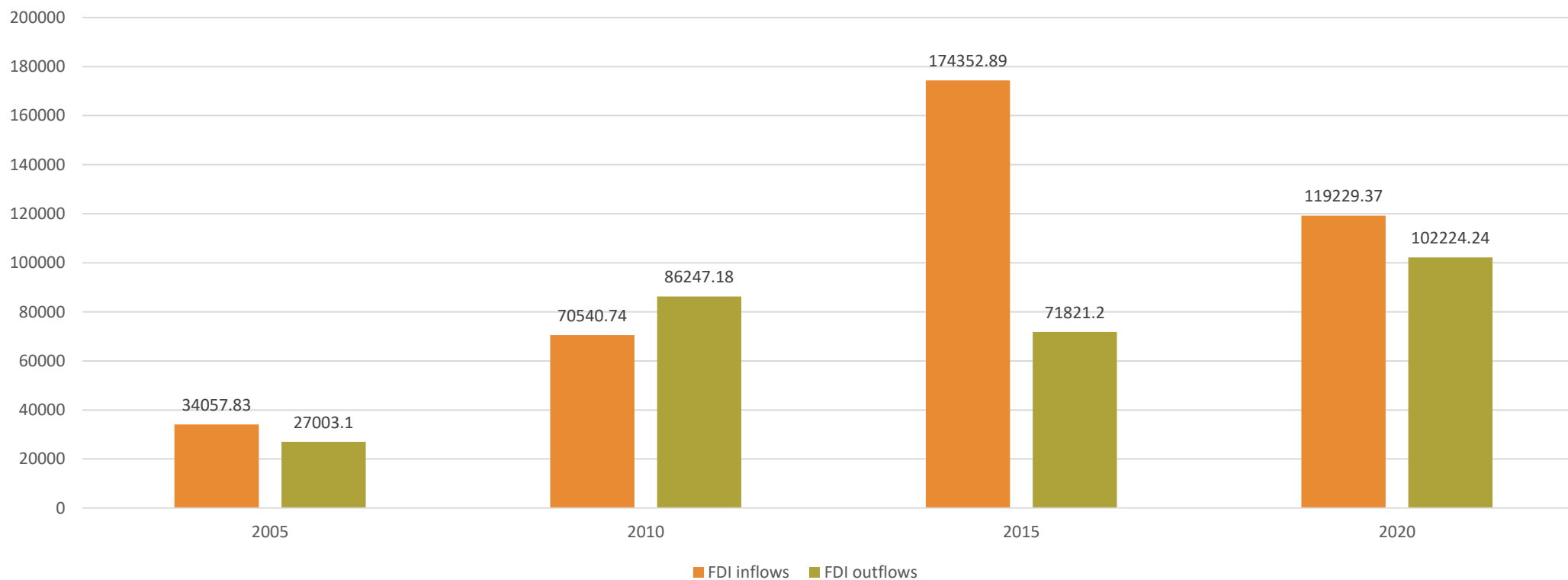
**MNEs → Corporate  
Sustainability**



**Global trade and investment**

**Global  
Marketplace**

# FDI Financial Flows (millions of US\$) – Hong Kong



**PLEASE  
SIGN IN & OUT  
HERE**

# Inbound and Outbound FDI

## Inbound Activities – “IN”



Benefits attributed to FDIs	Measures to facilitate FDIs	Tax Incentives
<ul style="list-style-type: none"><li>• productivity gains;</li><li>• technology transfers;</li><li>• the introduction of new processes;</li><li>• managerial and technological expertise within the domestic market;</li><li>• employee training;</li><li>• international production networks; and</li><li>• market access.</li></ul>	<ul style="list-style-type: none"><li>• law reforms;</li><li>• providing guarantees for the repatriation of profits and investments; and</li><li>• creating mechanisms for the settlement of investment disputes and the provision of tax incentives.</li></ul>	<ul style="list-style-type: none"><li>• reduced tax rates on profits;</li><li>• tax holidays;</li><li>• accounting rules that permit accelerated depreciation;</li><li>• tariff reductions on imported equipment, raw materials and components; and</li><li>• increased tariffs to protect domestic markets in the event of import substitutions.</li></ul>

## Outbound Activities – “OUT”



# Inbound Incentives – Hong Kong

## Home country level factors that influence firm investment decisions

Policies	Specific elements	Relationship
Market size and per capita income	GDP level and per capita income	positive
Exchange rate	Exchange rate level or volatility	negative
Labour costs	Wages or Labour Units Costs	negative
Distance	Geographic distance, border adjacency, common language, colonial ties	negative
Inflation	Inflation level or volatility	negative
Agglomeration effects	Presence of other foreign-owned firms	positive
Taxation	Corporate tax levels, labour tax levels	negative
Trade Policy	Average tariffs, anti-dumping duties	positive/negative
Quality of institutions	Quality of domestic institutions, regulatory quality, the rule of law and judicial system, control of corruption, protection of intellectual property rights	positive/negative
Education and human capital	Quality of transport, communications, energy infrastructure	positive/negative
Infrastructure	Quality of transport, communications, energy infrastructure	positive
Investment policy	Lack of FDI restrictions; the ease of doing business; sectoral targeting or quality of investment promotion agencies	positive
International investment, trade and tax agreements	Bilateral investment agreements, preferential trade agreements, double taxation treaties	positive/negative

- *Stamp Duty (Amendment) Bill 2020* - abolishment of the Double Ad Volorem Stamp Duty.
- Taxation of the digital economy, e-commerce and digital assets. Transfer Pricing considerations since 2018.
- Sections 50AAF(1) or 50AAK(2) of the IRO (Cap. 112). See also section 82A.

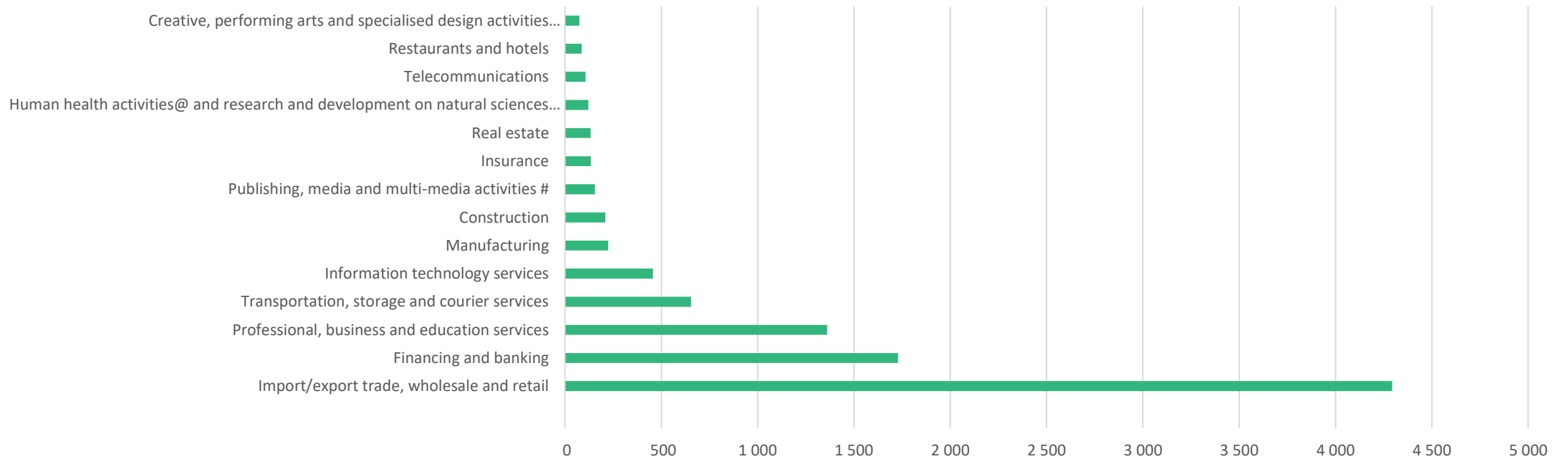
Ship leasing concession, enacted in June 2020. 0% profits tax rate; reduced tax rate 8.25% (concessionary profits tax rate)

- Hong Kong has now concluded 45 tax treaties.
- OECD Code of Liberalization of Capital Movements?

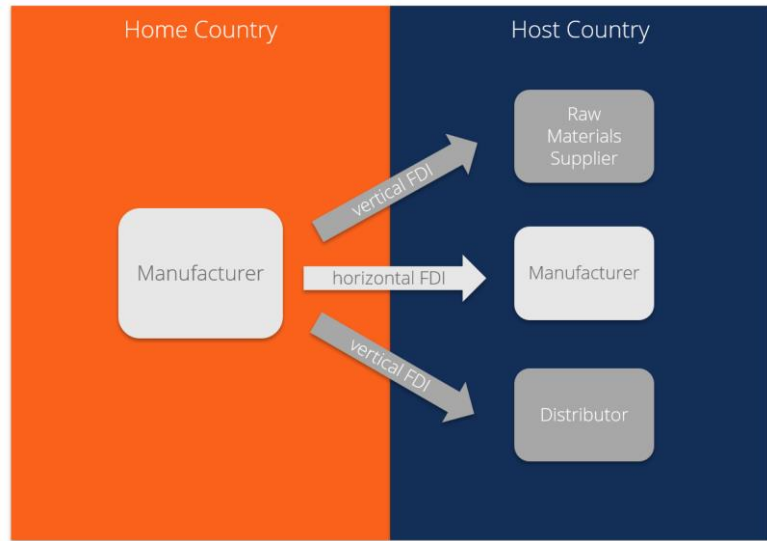
# 2021年有香港境外母公司的駐港公司按年統計調查報告

## Report on 2021 Annual Survey of Companies in Hong Kong with Parent Companies Located outside Hong Kong

Total number of regional headquarters/regional offices/local offices by major line of business in Hong Kong, 2021



Source: Censtatd.gov.hk



- Acquiring voting stock in a foreign company
- Mergers and acquisitions
- Joint ventures with foreign corporations
- Starting a subsidiary of a domestic firm in a foreign country

# Foreign Direct Investment

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# Inbound Incentives – Hong Kong

## Home country level factors that influence firm divestment decisions

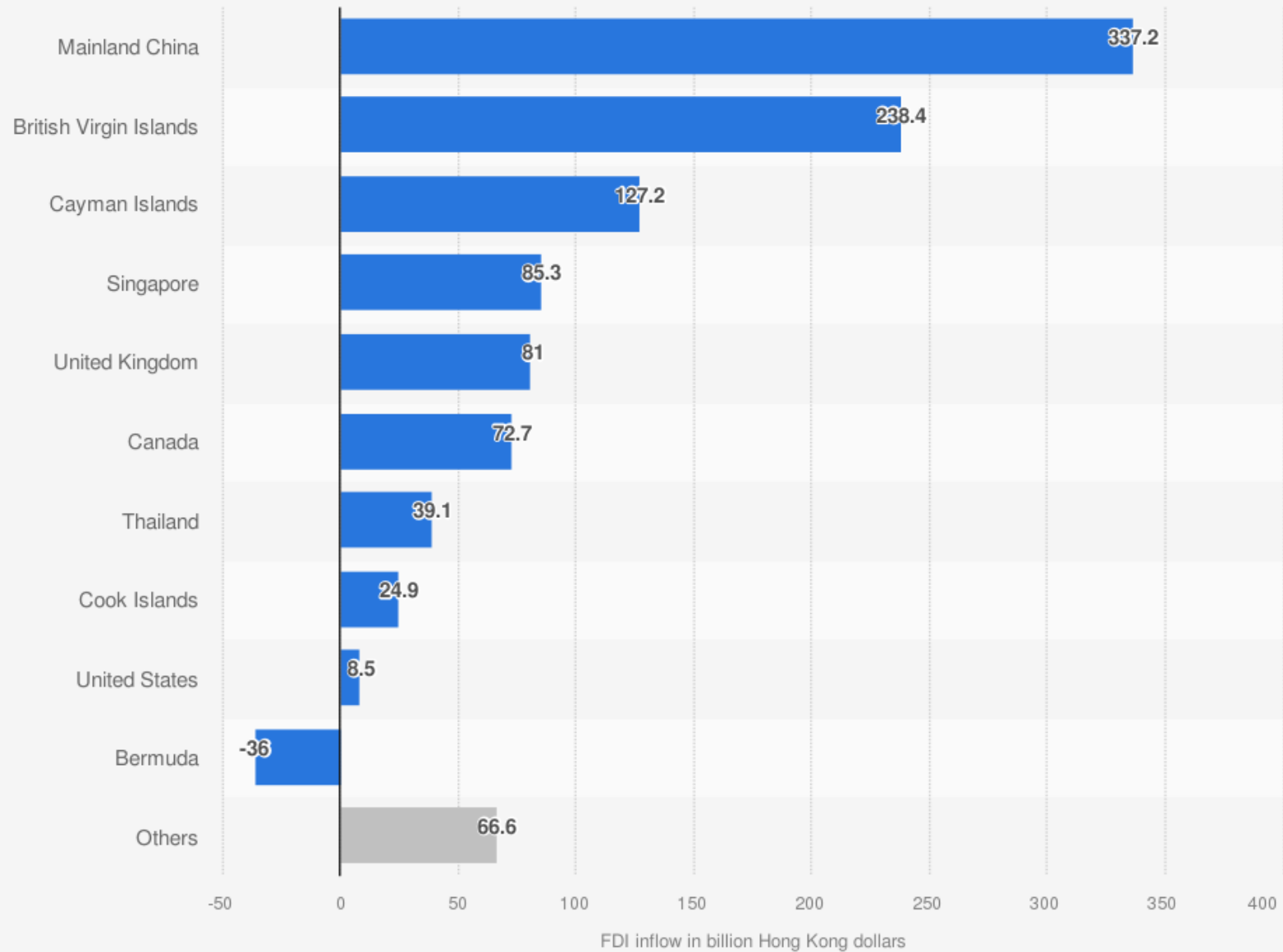
Firm-level or business unit-level factors	
Factors considered	Relationship
Size (of the affiliate or the parent)	positive
Parent's performance	negative
Affiliate's performance	postive/negative
Business relatedness	positive
Business diversification	positive
Internationalisation / the geographic scope of the economic group	postive/negative
Existence of other affiliates	positive
Other divestments/acquisitions	postive/negative
Strong parent firm governance	positive
Sector-level factors	
Factors considered	Relationship
Growth	postive/negative
Concentration	postive/negative
Technologic change	positive
Changes to regulation and institut	positive
Level of internationalisation	postive/negative
Sunk costs	postive/negative

Host-Country Level Factors	
Factors considered	Relationship
GDP	negative
Real eschange rate volatility	positive
Capital-to-labour ratio	negative
Wages	positive
Trade openness	positive
Skills	positive
Policy stability	negative
Disputis against the host	positive

Shares?

Assets?

## Inward foreign direct investment (FDI) flows to Hong Kong in 2020, by country or region of origin (in billion Hong Kong dollars)



Source  
Census and Statistics Department Hong Kong  
© Statista 2022

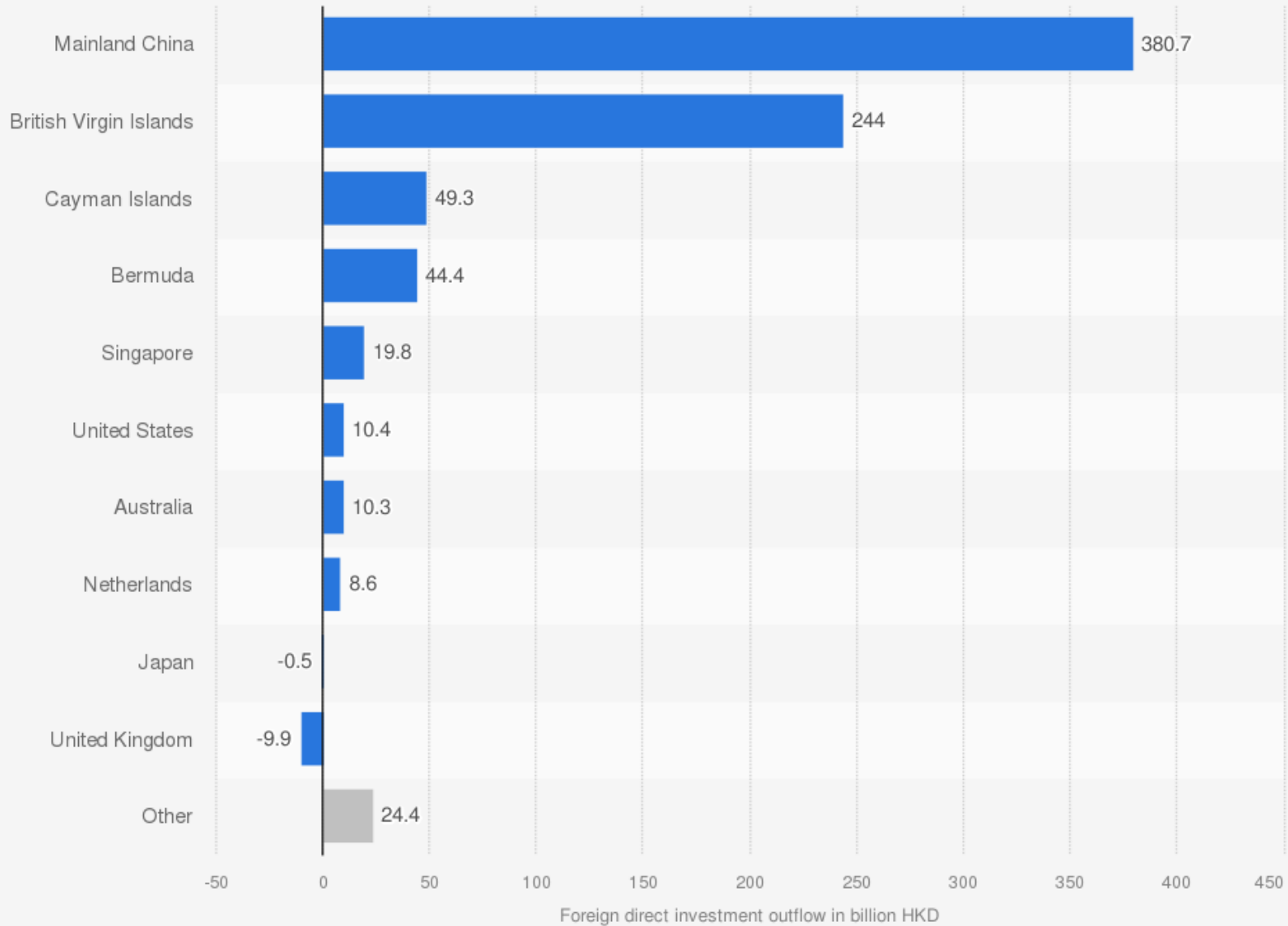
Additional Information:  
Worldwide; Hong Kong; 2020

# Inward FDI by region of origin

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## Outward foreign direct investment (FI) flows from Hong Kong in 2020, by recipient (in billion Hong Kong dollars)



Source  
Census and Statistics Department Hong Kong  
© Statista 2022

Additional Information:  
China; Hong Kong; 2020

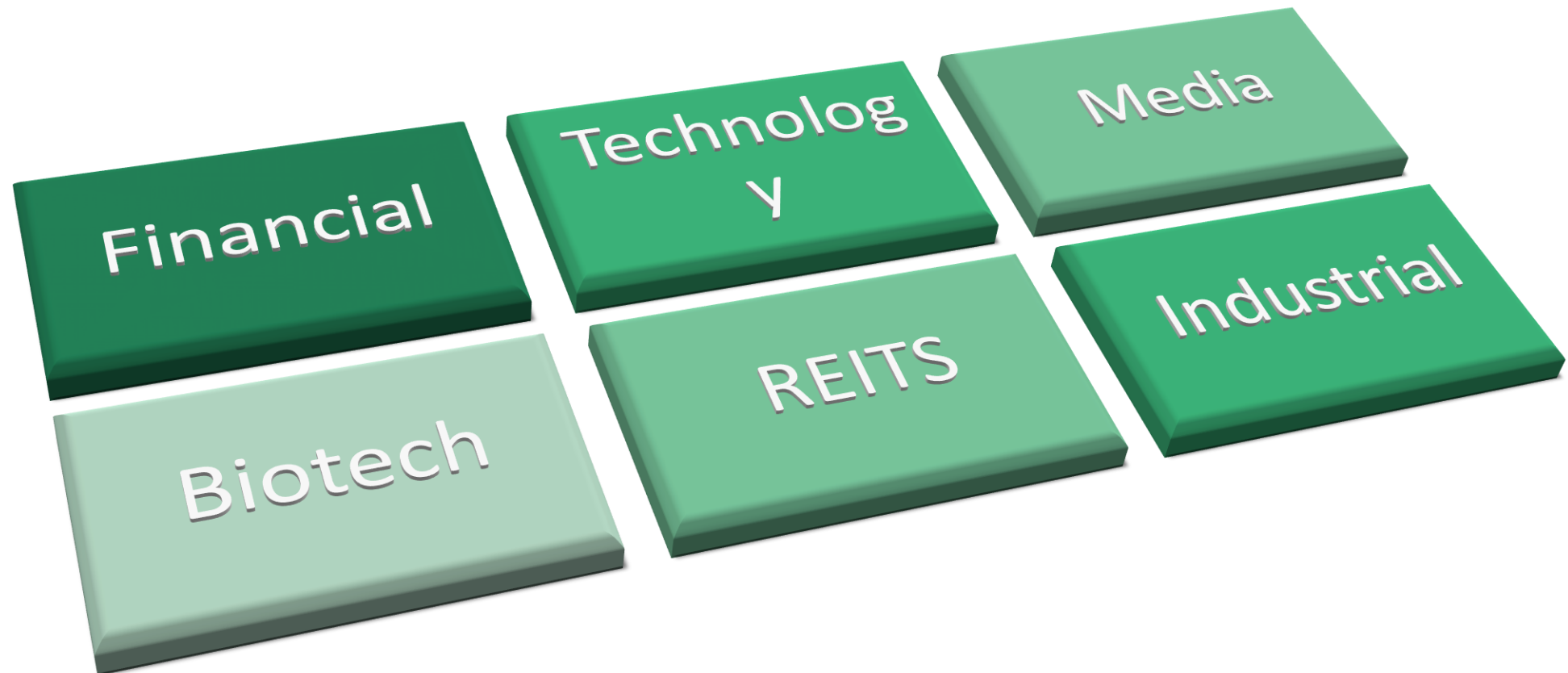
# Outward FDI by Recipient

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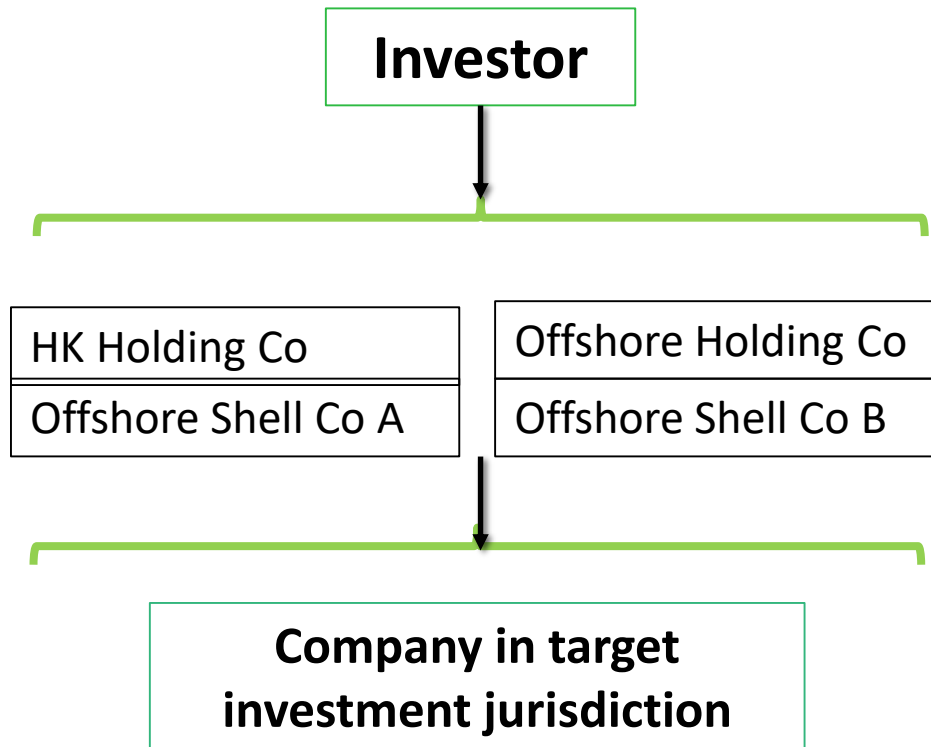
# Inbound and Outbound Investments – Hong Kong 2021 and 2022

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# One example of a Common Offshore Structure(s)

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Domestic

**What is the impact of impending tax changes?**

Overseas

Shareholding



# Tax Planning – Direct and Indirect Tax Considerations

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1. Hong Kong operates a **territorial system of taxation** (i.e., only income earned in Hong Kong is taxable). Corporate residency is not relevant in determining the taxability of an entity except in a tax treaty context.
2. The profits tax rules apply equally to Hong Kong incorporated companies carrying on a trade or business in Hong Kong and overseas incorporated companies carrying on a trade or business in Hong Kong through a branch.
3. The main types of investment vehicles used to carry on business in Hong Kong are a Hong Kong incorporated company, a branch of a foreign company, a partnership and an unincorporated joint venture.

Rates of tax	Where the two-tiered rates apply * (%)	Where the two-tiered rates do not apply (%)
Corporations:		
First HKD 2 million	8.25	16.50
On the remainder	16.50	
Unincorporated businesses:		
First HKD 2 million	7.50	15.00
On the remainder	15.00	

# Choice of Acquisition Vehicle

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## **Foreign parent company**

Dividends paid by a Hong Kong company to a non-resident shareholder are not subject to WHT in Hong Kong.

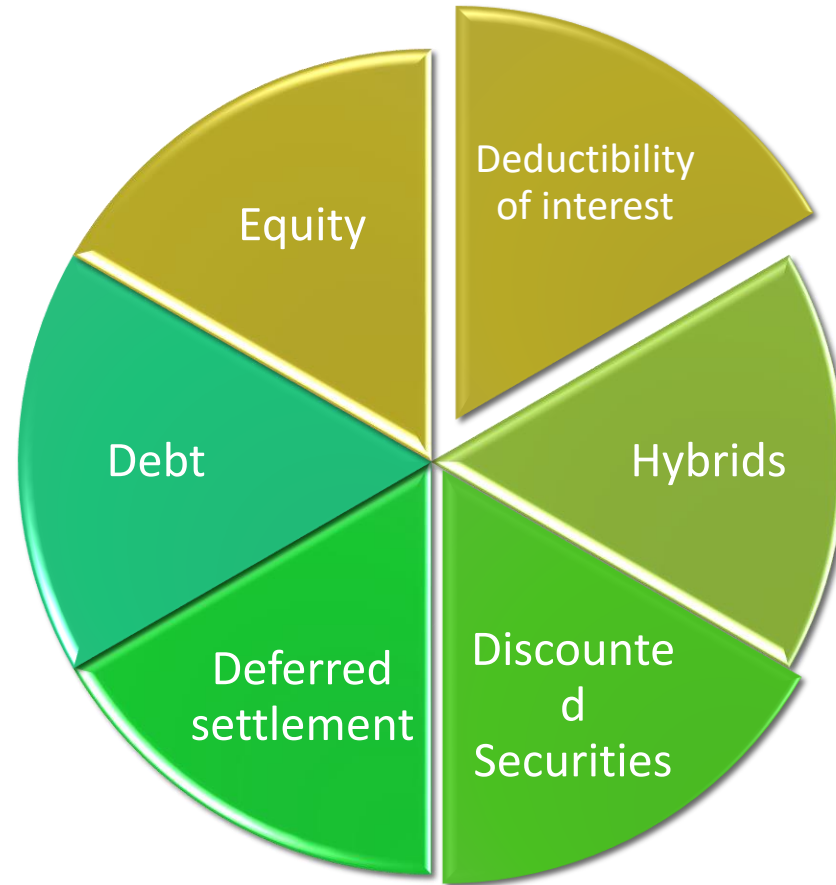
## **Non-resident intermediate holding company**

It may not be necessary (from a HK tax perspective) to set up a foreign intermediate holding company for inbound investments into Hong Kong.



# Choice of Acquisition Funding

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# Tax Planning – Foreign Sourced Income Exemption (FSIE) – Hong Kong

**Offshore corporations are tax-free, while companies formed in Hong Kong are tax-free on all foreign-sourced income.**

- Companies must be examined by the Hong Kong IRD to be eligible for Hong Kong offshore tax exemption.
- The IRD approval process for this letter is lengthy, taking at least 6 months.
- This is changing in January 2023.

**Refined FSIE regime applicable to:**

- (i) interest;
- (ii) income from intellectual properties;
- (iii) dividends; and
- (iv) disposal gains in relation to shares or equity interest.

**Foreign dividends and interest income (i.e. passive income) received by Hong Kong resident companies from overseas affiliates will qualify as offshore sourced income only provided that either:**

- the income has not been received in Hong Kong *or*
- the Hong Kong resident company satisfies the economic substance tests.

# Impending Tax Changes ...

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## Sale of Shares or Similar Equities in Foreign Companies

- A sale of shares or similar equity interests will no longer be eligible for the offshore source claim even if the sale would have been negotiated and concluded outside Hong Kong, unless the Hong Kong resident company meets the economic substance rules or if the new participation exemption rule applies

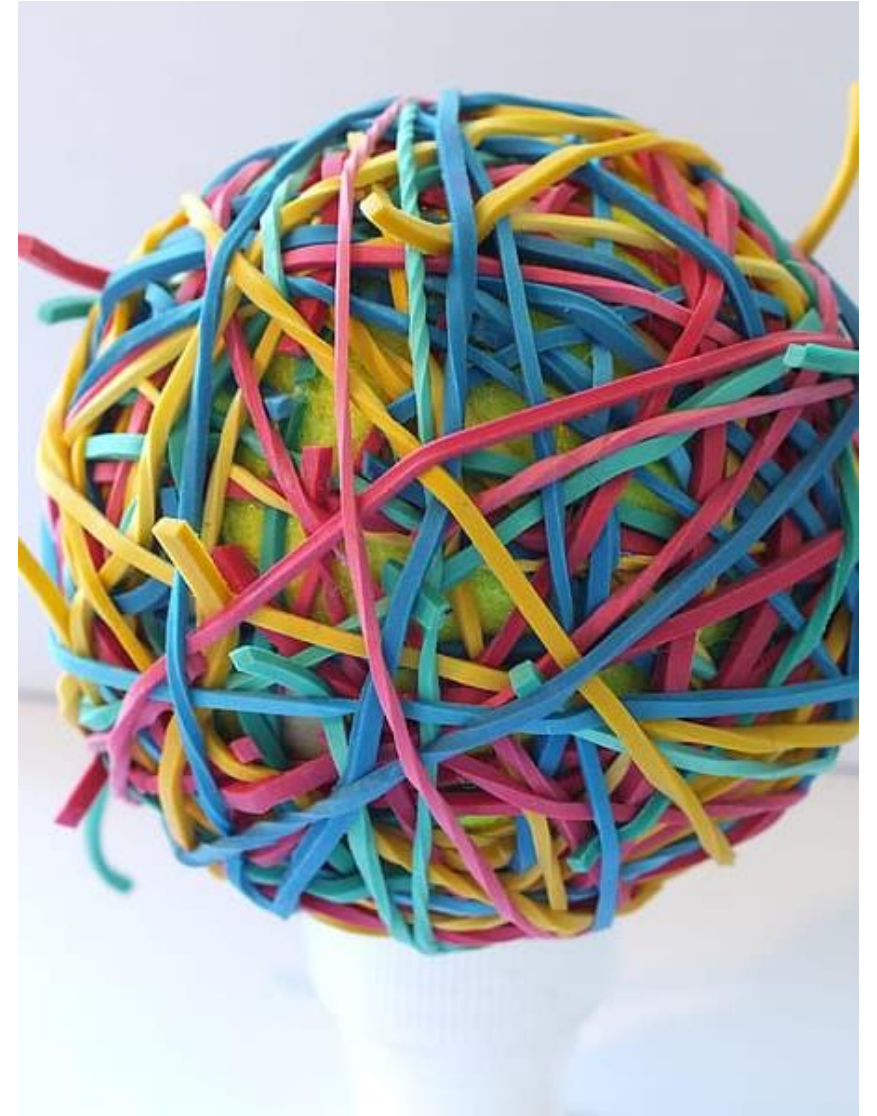
## Foreign Royalty Income

- Foreign royalty income will be exempt in respect of royalties which are paid for patents and similar rights developed in Hong Kong and computed in accordance with the modified nexus rules developed by the OECD.

# Summary and Take-Away Points

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- **Novel business opportunities on the horizon...**
  - Biotech, Tech and Telecommunications
- **Navigating tax implications can pose its own complexities**
  - Does this “attempt to level the playing field”?
- **Is there a changing landscape with respect to inbound and outbound investments with respect to Hong Kong?**
- **What are ongoing strategies to better develop corporate structures for foreign corporations and entities?**





Thank you

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Questions