

Latest Development of Hong Kong's Refined Foreign Source Income Exemption Regime

Highlight

- The Refined Foreign Source Income Exemption ("FSIE") Regime was gazetted on 28 October 2022.
- Applications for Commissioner of Inland Revenue's opinion on taxpayers' relevant tax position are now open until the enactment of the new FSIE legislation (i.e. 1 January 2023).



Introduction

Subsequent to the consultation stage for the proposed refined foreign source income exemption (“FSIE”) regime, the Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Bill 2022 (“the Amendment Bill”) was gazetted on 28 October 2022 and was introduced into the Legislative Council on 2 November 2022 proposing that starting from 1 January 2023, certain foreign-sourced income derived by a member of a multinational enterprise (“MNE”) group carrying on a trade, profession or business in Hong Kong is to be regarded as arising in or derived from Hong Kong and chargeable to profits tax when such income is received in Hong Kong.

Snapshot of the refined FSIE regime

Covered taxpayers:

- A constituent entity (including a permanent establishment) of an MNE group which is carrying on a trade or business in Hong Kong which receives In-Scope Offshore Passive Income in Hong Kong.
- An MNE group means any group that includes at least one entity or permanent establishment that is not located in the jurisdiction of the ultimate parent entity (i.e. involving two or more jurisdictions).

Covered offshore-sourced income:

- The In-Scope Offshore Passive Income generally includes interest income, dividend income, disposal gains and IP income arising in or derived from a jurisdiction outside Hong Kong.

Definition of “received in Hong Kong”

- According to the Amendment Bill, a sum is regarded as received in Hong Kong in the following circumstances (not an exhaustive list):
 - The sum is remitted to, or is transmitted or brought into, Hong Kong;
 - The sum is used to satisfy any debt incurred in respect of a trade, profession or business carried on in Hong Kong; or
 - The sum is used to buy movable property, and the property is brought into Hong Kong.

Regarding the details of the refined FSIE regime including how to satisfy the requirements to enjoy the offshore tax exemption for the above In-Scope Offshore Passive Income, please refer to our previous newsletter released in August 2022.

Application for Commissioner's opinion to confirm the tax position

To alleviate the compliance burden of taxpayers and to provide them with tax certainty, the IRD encourages taxpayers to seek Commissioner's Opinion ("the Opinion") on compliance with the Economic Substance Requirement ("ESR") as a transitional arrangement before the passage of the Amendment Bill.

The application for the Opinion is not compulsory and the Opinion is not an advance ruling made pursuant to section 88A of the Inland Revenue Ordinance (Cap. 112). The Commissioner will, however, apply the enacted ESR in accordance with the Opinion provided that the arrangements and parameters stated in the Opinion are adhered to, and the enacted ESR is substantially the same as that proposed in the Amendment Bill. Taxpayers can rely on the Opinion to report their compliance with the enacted ESR in their profits tax returns.

A taxpayer can apply for the Opinion if it is an MNE entity carrying on a trade, profession or business in Hong Kong and accrues or receives In-Scope Offshore Passive Income on or after 1 January 2023. The application can be made either on an individual application basis or on a group application basis (including other Hong Kong entities of the same MNE group).

Upon the passage of the Amendment Bill and the enactment of the amendment ordinance, the transitional measure on the application for the Opinion will cease, and taxpayers will then be able to apply for advance rulings on how the enacted ESR applies to their circumstances or arrangements. Certain fees will be charged by the Inland Revenue Department ("IRD") for making the advanced rulings subject to relevant rules and conditions.

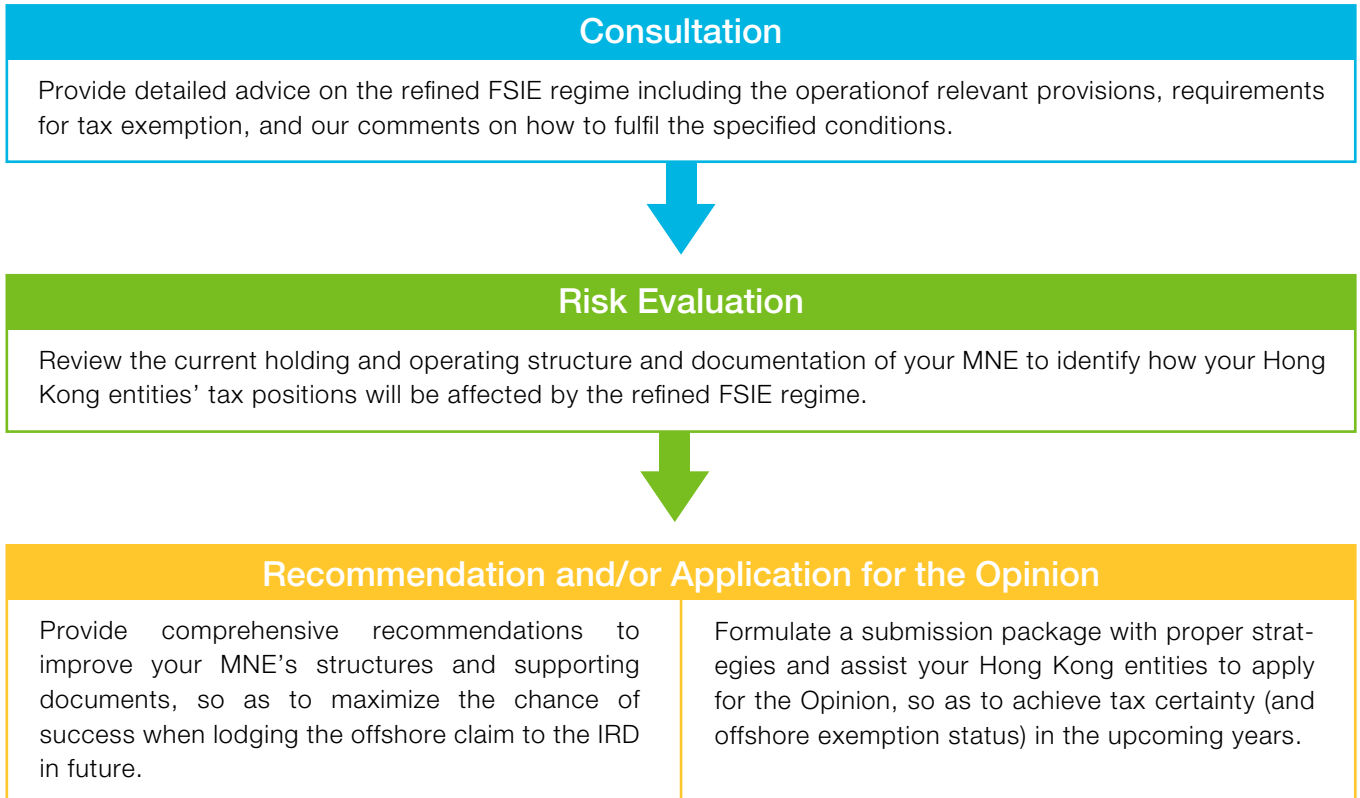
Processing time and covered period

To minimize the administrative burden, the application for the Opinion or an advanced ruling may cover a maximum of five years of assessment commencing from the years of assessment 2022/23 or 2023/24. In other words, once the Opinion or the ruling is granted, it can remain applicable for the subsequent five-year period.

The processing time of an application is normally around one month. Where the information available is not sufficient to form the Opinion, the IRD will request that taxpayers supply further particulars.

How PKF can help

Our tax professionals have assisted various clients in performing proper tax planning to increase their tax efficiency and successfully obtaining tax exemptions or preferential tax treatments in Hong Kong. We are well positioned to provide the following services to you in order to cope with the refined FSIE regime:-



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If you require assistance in any compliance or advisory matters, please feel free to contact our teams.



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