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Topic 1: Salaries Tax Allowances and Deductions

Allowable Deductions – s.12	
s.12(1)(a)	All outgoing and expenses, *other than expenses of a domestic or private nature and capital expenditure*, **wholly**, **exclusively** and **necessarily incurred in the production of assessable income** are allowable.
s.12(1)(b)	**Depreciation allowances** on machinery or plant essentially used by a taxpayer in the production of assessable income are allowable.
s.12(1)(e)	**Expenses of self-education** mean expenses paid by the taxpayer as: – fees, including tuition and examination fees, of a prescribed course organized by a course provider (e.g. university or college or institute registered under Education Ordinance); or – fees in respect of an examination set by education provider, or by a trade, professional or business association for its members, and undertaken by the taxpayer to gain or maintain qualifications for use in any employment, but does not include: – expenses which is allowable or has been allowed under other provision of the IRO; or – expenses to the extent to which they have been reimbursed or are reimbursable (unless the reimbursement has been or will be included in the assessable income). Maximum deduction for 2015/16 would be $80,000.
s.26C	**Approved charitable donations** made by the taxpayer or his/her spouse are allowable if: (1) the aggregate amount is not less than $100; and (2) the aggregate amount is not exceeding 35% (2015/16) of [assessable income minus allowable outgoings and expenses minus depreciation allowances]; and (3) not allowable as a deduction under profits tax. (4) the donated organizations must be charitable institutions approved by the IRD and exempt under s.88 of the IRO. (5) the payment must be a donation of money (6) the same donation cannot be granted to more than one person (7) the donation should be one that transferred voluntarily and no material advantages or benefits should have been received by the transferor.

Concessionary Deductions – s.26	
s.26D	Any **Elderly residential care expenses** paid by the taxpayer or his/her spouse in respect of a parent or a grandparent of the taxpayer or his/her spouse are allowable if: (1) parent or grandparent who at any time in that year of assessment is: • ≥ 60; or • eligible to claim an allowance under the Government's Disability Allowance Scheme. (2) The expenses should be paid to a residential care home licensed under the HK law. (3) The maximum allowable deduction for each parent or grandparent as specified in Schedule 3C of the IRO was $80,000 (2015/16) ***Note:*** *No more dependent parent/grandparent allowance in respect of the same parent or grandparent would be allowable.*
s.26E	Deduction of **home loan interest** paid by the taxpayer in respect of: (1) A dwelling in which the taxpayer is the owner (2) The dwelling is used exclusively or partly as his place of residence (if the taxpayer has more than property, only the interest in respect of his principal place of residence is allowed). (3) The dwelling must be situated in Hong Kong (4) A home loan must be applied wholly or partly for the acquisition of a dwelling. (5) The home loan must be secured by a mortgage or charge over that dwelling or any other property in Hong Kong. (6) Interest is paid to – the Government; – a financial institution; – a credit union registered under the Credit Unions Ordinance; – a money lender licensed under the Money Lenders Ordinance; – the Hong Kong Housing Society; – an employer of the person; or – any recognized organization or association. (7) Starting from the year of assessment 2012/13, the deduction period for home loan interest (whether continuous or not) is extended to 15 years. (8) The maximum amount allowable in each year of assessment is specified in Schedule 3D of the IRO ($100,000 for 2015/16). *If the taxpayer is not a sole owner of the dwelling, the maximum would reduce with regard to the person's share of ownership.* ***Note:*** Pursuant to s.26F, if the person entitled to the deduction has no income, property or profits chargeable to tax for that year of assessment, his/her spouse may be nominated to claim the deduction for that year of assessment.

Concessionary Deductions – s.26	
s.26G	Deductions on **Contributions to a recognized retirement scheme** shall be the smallest of the following three amounts: 1. The amount specified in Schedule 3B of the IRO (i.e. $18,000 for 2015/16); or 2. The amount of contributions by the taxpayer as an employee to the scheme; or 3. The amount of the mandatory contributions that the taxpayer would have been required to pay as an employee if at all times while an employee during the year of assessment in question he had contributed as a participant in a MPF scheme. ***Note:*** From 12/2000 to 05/2012: MC = 5% (max $1,000 per month) From 06/2012 to 05/2014: MC = 5% (max $1,250 per month) From 06/2014 : MC = 5% (max $1,500 per month)

<table>
<tr><th colspan="3">Personal Allowances (2015/16)</th></tr>
<tr><td><u>Basic allowance</u></td><td>– Granted to all taxpayers.
– No person may be granted a basic allowance if a MPA is granted to him/her or his/her spouse.</td><td>$120,000</td></tr>
<tr><td><u>Married Person's allowance</u></td><td>– Granted to a person if, at any time during that year of assessment, married and
(a) The spouse did not have assessable income;
(b) Joint assessment is elected under s10(2) or
(c) Personal assessment is elected.

<u>Where husband and wife are living apart</u>, a MPA can only be granted to the spouse maintaining and supporting the other spouse (for single income case). Such claim may be revoked within the year of claim or within 6 years thereafter.</td><td>$240,000</td></tr>
<tr><td><u>Dependent Parent/Grandparent allowance</u></td><td>– Granted to a single person in respect of each parent or grandparent
– Granted to a married person (not being a person with the spouse living apart), in respect of each parent or grandparent including the spouse's parents or grandparents.
<u>Granting conditions</u>
– The parent/grandparent must be an ordinary resident in HK, and
– Maintain** the parents/grandparents by the taxpayer or his/her spouse; and
– <u>[case 1]</u>
aged 60 or more (if aged under 60, must be eligible to claim an allowance under the government's Disability Allowance Scheme), or
– <u>[case 2]</u>
aged 55 or more but under 60 and not eligible to claim an allowance under the Government's disability Allowance Scheme

**Maintain means:
✓ The parent/grandparent resides, otherwise than for full valuable consideration, with that person and his/her spouse for a continuous period of not less than 6 months in the year of assessment); or
✓ The person or his/her spouse contributes not less than $12,000 in money toward the maintenance of that parent/grandparent.</td><td>[Case 1]
@$40,000

[Case 2]
@$20,000</td></tr>
</table>

Personal Allowances (2015/16)		
<u>Additional Dependent Parent / Grandparent allowance</u>	– Granted (on top of basic DPA / DGA) in respect of each dependent who has resided with the person or his/her spouse, otherwise than for full valuable consideration, ***continuously throughout the year of assessment***.	**[Case 1]** @$40,000 **[Case 2]** @$20,000
<u>Child allowance</u>	– Granted to a taxpayer maintained a child during that year of assessment who is: – Unmarried, and – Under the age of 18, or – aged 18 – 25 receiving full time education, or aged over 18, physically or mentally disable, incapacitated for work. *For husband and wife not living apart:* – The child allowances in respect of **<u>all children</u>** shall be granted to **<u>one spouse</u>** (to be nominated between the two spouses), and – No apportionment is available. *For husband and wife living apart:* The allowance can be apportioned having regard to the contributions made by each individual to the maintenance and education of the child.	@$100,000 (max: 9)
<u>Additional Child Allowance</u>	From 2007/08 onwards, for each child born during the year, additional Child Allowance will available for taxpayers.	@$100,000
<u>Dependent brother or dependent sister allowance</u>	– Granted to a taxpayer or their spouse maintained a brother or sister during that year of assessment who is: – Unmarried, and – Under the age of 18, or aged 18 – 25 receiving full time education, or aged over 18, physically or mentally disable, incapacitated for work A brother or sister is only treated as maintained if any time during the year, the person or the spouse had **<u>sole or predominant care</u>** of the brother or sister or of the brother or sister of the spouse. No child allowance has been claimed by any person in respect of the brother or sister in the same year of assessment.	@$33,000

Personal Allowances (2015/16)		
Single parent allowance	– Granted to a person if at any time during the year of assessment the person had the sole or predominant care of a child of whom the person was entitled to be granted a child allowance for the year of assessment. A person shall not be entitled to SPA:- (a) If at any time during the year of assessment the person was married and not living apart from the spouse; (b) Only made contribution to the maintenance and education of the child; or (c) In respect of any second or subsequent child SPA can be apportioned by reference to the periods of the sole or predominant care of the child.	$120,000
Disabled dependant allowance	– This is granted to an individual in respect of every dependent of his or hers or is eligible to claim an allowance under the Government's Disability Allowance Scheme. A dependent means: (a) A spouse in respect of whom the individual is entitled to be granted a married person's allowance; (b) A parent, or parent of the individual's spouse, in respect of whom the individual is entitled to be granted a dependent parent allowance; (c) A grandparent or grandparent of the individual's spouse, in respect of whom the individual is entitled to be granted a dependent grandparent allowance. (d) A child in respect of whom the individual is entitled to be granted a child allowance. (e) A brother or sister, or a brother or sister of the person's spouse, for whom the person is entitled to be granted a dependent brother or dependent sister allowance.	@$66,000

Topic 2: Stamp Duty (AVD, BSD, SSD and exemptions/reliefs)

Ad Valorem Duty (AVD)

Unless specifically exempted or otherwise provided, AVD is payable at Scale 1 on an agreement for sales (AFS) for the acquisition of **any residential property or non-residential property**, if the agreement is executed on or after 23 February 2013. Scale 1 also applies to a conveyance on sale of such a property executed on or after that date (unless the related agreement for sale was executed before 23 February 2013).

However, lower rates (Scale 2) will apply to any agreement/conveyance for a residential property where the purchaser is a Hong Kong permanent resident (HKPR) acting on his own behalf and he does not own any other residential property in Hong Kong at the time of acquisition of the subject property.

A limited company, regardless the residency status of its shareholders and directors, AVD would be based on Scale 1 if it acquires the property is acquired on or after 23 February 2013.

Sale or Transfer of Immovable Property

For immovable property in Hong Kong, stamp duty is calculated at rates which vary with the amount/value of the consideration or value of the property as follows:-

Higher Rates of Ad Valorem Stamp Duty Rate (Scale 1)

Amount or value of the consideration or Value of the Property		Rate (with effect from 23 February 2013)
Exceeds	Does not exceed	
	$2,000,000	1.5%
$2,000,000	$2,176,470	$30,000 + 20% of excess over $2,000,000
$2,176,470	$3,000,000	3.00%
$3,000,000	$3,290,330	$90,000 + 20% of excess over $3,000,000
$3,290,330	$4,000,000	4.5%
$4,000,000	$4,428,580	$180,000 + 20% of excess over $4,000,000
$4,428,580	$6,000,000	6.00%
$6,000,000	$6,720,000	$360,000 + 20% of excess over $6,000,000
$6,720,000	$20,000,000	7.5%
$20,000,000	$21,739,130	$1,500,000 + 20% of excess over $20,000,000
$21,739,130		8.5%

Lower Rate of Ad Valorem Stamp Duty (Scale 2)

Amount or value of the consideration or Value of the Property		Rate (with effect from 1 April 2010)
Exceeds	Does not exceed	
	$2,000,000	$100
$2,000,000	$2,351,760	$100 + 10% of excess over $2,000,000
$2,351,760	$3,000,000	1.5%
$3,000,000	$3,290,320	$45,000 + 10% of excess over $3,000,000
$3,290,320	$4,000,000	2.25%
$4,000,000	$4,428,570	$90,000 + 10% of excess over $4,000,000
$4,428,570	$6,000,000	3.00%
$6,000,000	$6,720,000	$180,000 + 10% of excess over $6,000,000
$6,720,000	$20,000,000	3.75%
$20,000,000	$21,739,120	$750,000 + 10% of excess over $20,000,000
$21,739,120		4.25%

If a conveyance on sale of residential property is executed in ***conformity*** with a chargeable AFS, the conveyance is chargeable with Stamp Duty of $100 only.

All parties to the transaction and all other persons executing the conveyance are jointly and severally liable to pay Stamp Duty.

Stamp Duty normally payable within 30 days after the relevant date (i.e. Date of original AFS).

<u>Section 45/29H exemption</u>

The following transactions between associated corporations are exempt from AVD:

- Conveyance of immovable property
- Transfer of beneficial interest in Hong Kong stock
- AFS of residential immovable property

Associated Corporations means two corporations where:

- one is directly or indirectly the beneficial owner of not less than 90 per cent of the other; or
- a third corporate is owner of not less than 90% of the issued share capital of each corporation

The following anti-avoidance provisions stated that relief is not applicable if:

(1) any part of the consideration for the transfer of immovable property or Hong Kong stock between associated companies was provided by an unrelated non-associated person (s.45(4)(a)).

(2) the said interest was previously conveyed, transferred, purchased or sold, directly or indirectly, by such a person (s.45(4)(b)).

(3) the transferor and transferee cease to be associated within the two-year period **by reason of a change in the percentage of the issued share capital of the transferee** (s.45(4)(c)).

Where a transferor and transferee cease to be associated within 2 years after the date of execution of the instrument and relief from stamp duty has been claimed:

- the transferor and transferee shall notify the Collector the cessation within 30 days after the date of the cessation;
- the transferor and transferee are jointly and severally liable to pay within 30 days after the date of the cessation by way of stamp duty an amount equal to the stamp duty which would have been chargeable on the instrument had relief not been granted.

If the amount is not paid within the 30 days, penalty may be imposed.

Special Stamp Duty (SSD)

The liability to SSD will arise if all of the following 3 conditions are met -

(a) The transaction involves the sale and purchase or transfer of a residential property;

(b) The property is acquired by the vendor or transferor on or after 20 November 2010; and

(c) The property is disposed of by the vendor or transferor within 24 months from the date of acquisition (if acquired on or after 20 Nov 2010 and before 27 Oct 2012) or within 36 months from the date of acquisition (if acquired on or after 27 Oct 2012).

The amount of SSD payable is calculated by reference to the stated consideration or the market value of the residential property, whichever is the higher, at the following regressive rates for different holding periods by the vendor or transferor before the disposal –

Holding Period	The property was acquired on or after 20 November 2010and before 27 October 2012	The property was acquired on or after 27 October 2012
6 months or less	15%	20%
More than 6 months but for 12 months or less	10%	15%
More than 12 months but for 24 months or less	5%	10%
More than 24 months but for 36 months or less	-	10%

For the purposes of SSD, the counting of the holding period of a residential property is based on calendar months. The period from a certain day in a month to the preceding day in the following calendar month is counted as 1 month.

All parties to the transaction and all other persons executing the AFS / Conveyance are jointly and severally liable to pay Stamp Duty.

Chargeable agreement for sale or conveyance on sales is to be stamped with SSD at the same time as that for the ad valorem stamp duty.

SSD is exempted if:

(a) Nomination of the spouse, parents, children, brothers or sisters to take up the assignment of the residential property, and sale or transfer of the residential property to the spouse, parents, children, brothers or sisters.

(b) Addition / deletion of name(s) to / from a chargeable agreement for sale or a conveyance on sale in respect of the residential property if the person(s) is the spouse, parents, children, brothers or sisters of the original purchaser(s).

(c) Sale or transfer of residential properties by a court order or pursuant to a court order (including a compulsory sale of residential or a foreclosure order).

(d) Sale of the estate of a deceased person, which involves residential property, by the executor or personal representative and sale or transfer of a residential property by a person whose property is inherited from a deceased person's estate or passed to that person under the right of survivorship.

(e) The residential property sold relates solely to a bankrupt's estate or the property of a company which is being wound up by the court by reason of its inability to pay debts.

(f) Sale of mortgaged residential properties in various forms by a mortgagee which is a financial institution within the meaning of section 2 of the IRO, or by a receiver appointed by such a mortgagee.

(g) Sale or transfer of residential properties to the Government; and

(h) Sale or transfer of residential properties between associated bodies corporate.

Buyer Stamp Duty (BSD)

BSD is payable on an agreement for sale or a conveyance on sale for the acquisition of any residential property if the residential property is acquired by any person on or after 27 October 2012, except a Hong Kong permanent resident (HKPR) acquiring the property on his/her own behalf (i.e. the person is both the legal and beneficial owner).

A limited company, regardless the residency status of its shareholders and directors will be liable to BSD if it acquires a residential property on or after 27 October 2012.

BSD is charged at 15% on the stated consideration or the market value of the property (whichever is the higher). The buyer or the transferee is liable to pay the BSD.

BSD has to be paid within 30 days after the execution of the chargeable document.

BSD is exempted if:

(a) acquisition of a residential property by a HKPR jointly with a close relative or close relatives (i.e. spouse, parents, children, brothers and sisters) who is/are not HKPR and each of the purchaser is acting on his/her own behalf;

(b) transfer of a residential property to a close relative who is not a HKPR, or to close relative(s) jointly one or more of whom not being HKPR and each of the transferee is acting on his/her own behalf;

(c) nomination of a close relative(s) who is/are not HKPR to take up the assignment of a residential property and each of the nominee is acting on his/her own behalf;

(d) addition/deletion of name(s) of a person(s) who is/are not HKPR to/from a chargeable agreement for sale or a conveyance on sale in respect of a residential property if the person(s) is/are a close relative(s) of the original purchaser(s) and each of the person is acting on his/her own behalf;

(e) acquisition or transfer of a residential property by a court order or pursuant to a court order, which includes a foreclosure order obtained by a mortgagee whether or not it falls under the definition of a financial institution within the meaning of section 2 of the Inland Revenue Ordinance;

(f) acquisition or transfer of a mortgaged residential property under a conveyance by or to a mortgagee which is a financial institution within the meaning of section 2 of the Inland Revenue Ordinance (Cap.112), or by a receiver appointed by such a mortgagee;

(g) acquisition or transfer of residential properties by or to the Government; and

(h) acquisition or transfer of a residential property by or to a body corporate from an associated body corporate;

(i) acquisition of a residential property by a person to replace another residential property which was owned by that person and that has been purchased or acquired pursuant to redevelopment projects pursued by the Urban Renewal Authority, or is resumed under the Lands Resumption Ordinance (Cap. 124) or purchased under section 4A of that Ordinance, or is sold pursuant to an order for sale made by the Lands Tribunal under the Land (Compulsory Sale for Redevelopment) Ordinance (Cap.545) and the person is acting on his/her own behalf;

(j) gift of residential properties to charitable institutions exempted from tax under section 88 of the Inland Revenue Ordinance.

Topic 3: Transfer pricing

Transfer Pricing is concerned with prices charged between associated enterprises for the transfer of goods, services and intangible property. In determining the transfer price, one should observe the arm's length principle.

The **arm's length principle** uses the transactions of independent enterprises as a benchmark to determine how profits and expenses should be allocated for the transactions between associated enterprises.

If transfer pricing does not follow the arm's length principle, the tax liabilities of associated enterprises will be distorted. IRD could adjust the profits tax charged or payable to reflect the position which would have existed if the arm's length principle had been applied instead of the actual price transacted between the enterprises.

Generally, the Commissioner would seek to apply the principles in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (the OECD Transfer Pricing Guidelines), except where they are incompatible with the express provisions of the IRO.

The OECD Transfer Pricing Guidelines place emphasis on the importance of comparability analysis and provide detailed descriptions of various transfer pricing methods. These comprise the traditional transaction methods:

- the comparable uncontrolled price method (CUP);
- the resale price method; and
- the cost plus method.

The OECD Transfer Pricing Guidelines also discuss the following transactional profit methods be considered to satisfy the arm's length principle:

- the profit-split method and
- the transactional net margin method.

As a general rule, if the enterprise is covered by a particular DTA, where the primary adjustment arose (arrived at that adjustment based on OECD principles), the Commissioner would give the relief on double taxation.

Topic 4: Arrangement between the Mainland of China and the HKSAR

Double tax agreements (DTAs) provide certainty to investors on the taxing rights of the contracting parties and the potential tax liabilities on their economic activities. They encourage trade by giving an added incentive for overseas companies to do business in Hong Kong, and likewise, for Hong Kong companies to do business overseas. As of 1 June 2016, Hong Kong has concluded comprehensive DTAs with 35 jurisdictions.

The following is an extract of the Arrangement between the Mainland of China and the HKSAR for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income ('China–HK DTA') signed on 21 August 2006 together with the relevant protocols.

Article 4	**Resident** - Resident Individual - Resident Company Resident persons other than individuals and companies
Article 5	**Permanent Establishment** • space (a fixed place of business), • time (continuous or aggregate periods), and • function (activities of a preparatory or auxiliary character are excluded) **INCLUDING:** **1. Fixed Place PE** - a place of management; a branch; an office; a factory; a workshop; a mine, an oil or gas well, a quarry or any other place of extraction of natural resources - a building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only if such site, project or activities ***last more than 6 months*** **2. Service PE** - the furnishing of services by an enterprise of One Side in the Other Side, directly or through employees or other personnel engaged by the enterprise, but only if such services continue (for the same or a connected project) ***for a period or periods aggregating more than 183 days within any 12-month period*** **3. Agency PE** a dependent agent who regularly acts on behalf of that enterprise in the Other Side and has, and habitually exercises, an authority to conclude contracts in the name of that enterprise.

Article 7	**<u>Business Profits</u>** Profits of an enterprise of One Side shall be taxable only in that Side unless the enterprise carries on business in the Other Side through a PE situated therein, in which case its profits may be taxed in that Other Side, but only so much of them as is attributable to that PE.
Article 14	**<u>Income from Employment</u>** Salaries, wages and other similar remuneration derived by a resident of One Side in respect of an employment shall be taxable only in that Side unless the employment is exercised in the Other Side. Exemption Rule: 1. the recipient is present in the Other Side not exceeding in aggregate 183 days in any 12-month period commencing or ending in the taxable period concerned; AND 2. the remuneration is paid by, or on behalf of, an employer who is not a resident of the Other Side; AND 3. the remuneration is not borne by a PE which the employer has in the Other Side
Article 15	**<u>Directors' Fee</u>** Directors' fees and other similar payments derived by a resident of One Side in his capacity as a member of the board of directors which is a resident of the Other Side may be taxed in Other Side.
Article 21	**<u>Methods for Elimination of Double Taxation</u>** Both Sides eliminate double taxation by the allowance of a tax credit. In the case of a Hong Kong resident deriving income that is subject to tax in Hong Kong, any tax paid in the Mainland in respect of that income shall be allowed as a credit against the Hong Kong tax payable on that income. However, the amount of tax credit will not exceed the amount of tax payable in respect of that item of income, computed in accordance with the provisions of the Ordinance.
Article 24	**<u>Exchange of Information (EoI)</u>** The EoI Article requires the contracting parties, upon receiving a request for information, to exchange tax information foreseeably required for applying the Arrangement or the domestic law, even where the requested party does not need such information for its own tax purposes. Both parties are obliged to keep the information received confidential and can only disclose the information to persons involved in the assessment and determination of tax, including courts and state departments of administration.

Notes on Examination Technique:

1. ***Read the question carefully***
   It is important to identify the issue or issues that he question is referring to. Plan ahead before you start writing. A well structure answer would enable you to capture more relevant issues.

2. ***Be relevant***
   Use your time wisely. You won't score by rote-copying irrelevant materials. In an open book examination like QP, marks would be allocated to theoretical part but there must be more marks on the discussion part. So it is important to explain and apply the theory or rules that is relevant in the scenario given.

3. ***Time management***
   On top of the 1.8 minutes per mark guideline stated in the question, do plan your "productive" and "non-productive" time in advance and MUST attempt all the questions.

4. ***Avoid unnecessary panics***
   Questions in section B are usually independent to each other. A good strategy is to answer the questions in accordance with your confidence level.

5. ***Produce a marker-friendly answer script***
   Markers would not demand for some elegant English and/or handwriting, but something readable would suffice. Start a new page for every question and write in short paragraph with lines between paragraphs would facilitate the markers' marking. It is also good for yourself when you want to add something to your answer.