

7th IMF-Japan High Level Tax Conference


Tax Reform to Improve Tax Compliance

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Deputy Commissioner
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Inland Revenue Department
Hong Kong Special Administrative Region

Legal Framework of Tax Compliance



Taxpayers' Obligations



Tax Authority's Powers



Anti Avoidance Rules

Taxpayer's Obligations

Registration

Register business within 1 month from commencement

Companies applying for incorporation are required to apply for business registration simultaneously

Record Keeping

Business records to be kept for not less than 7 years

Property owners to keep rental records for not less than 7 years

4 Major Categories

Payment

Payment of tax assessed on time

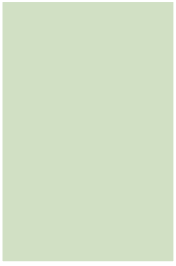
Reporting

Inform chargeability to tax within 4 months after the relevant basis period

File accurate tax returns on time

Provide information required by tax authority

Tax Authority's Powers



Information Seeking



Assessment

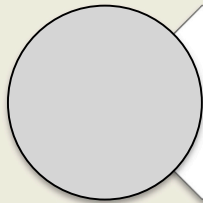


Penalties

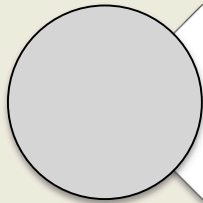


Tax Recovery

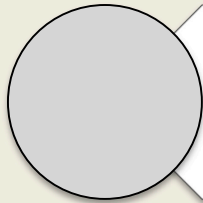
Information Seeking Powers



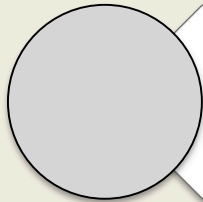
Require taxpayers and third parties (including banks) to provide information



Require taxpayers and other persons to attend interview and answer questions



Apply to the court for a search warrant



Invoke EoI mechanism in tax treaties

Assessment Powers

**Estimate
assessable
profits or
income if**

Taxpayer fails to
file return

Assessor does not
accept the return
filed

**Time
limits**

General cases -
raise assessments
and additional
assessments within
6 years after the
relevant year

Cases of fraud or
wilful evasion -
within 10 years

Penalties

Maximum monetary penalties for failure to inform chargeability, late return, incorrect returns, etc.

- 300% of the tax undercharged

Maximum penalty on criminal conviction for wilful evasion

- 3 years imprisonment; and
- fine of HK\$50,000; and
- further fine of 300% of the tax undercharged

Tax Recovery Powers

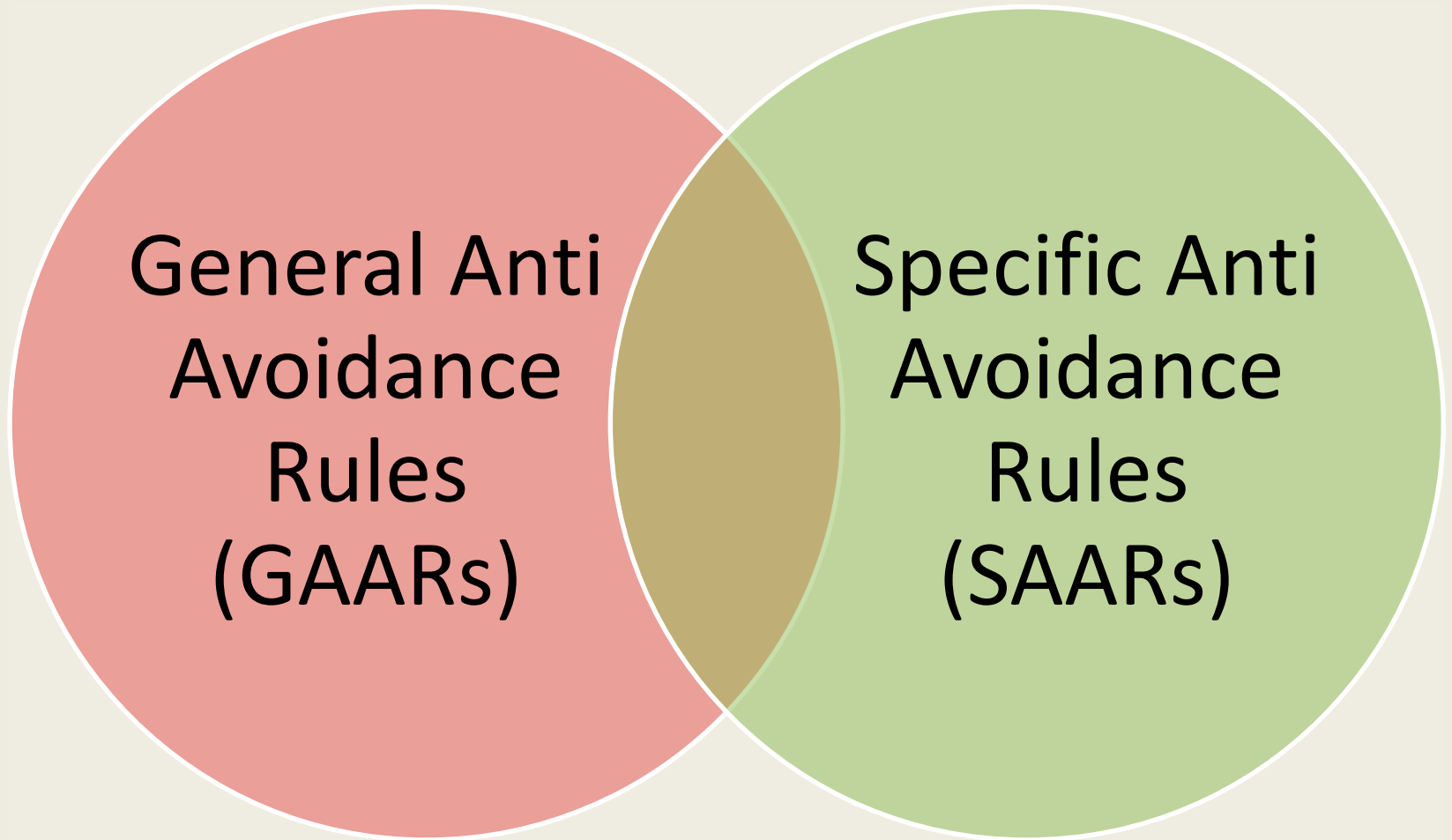
Impose surcharges for late payment

Recover tax in default from debtors of the taxpayers, including employers and bankers

Recover tax in default as civil debts through court action

Apply to the court to prevent tax defaulters from leaving Hong Kong

Anti Avoidance Rules



GAARs

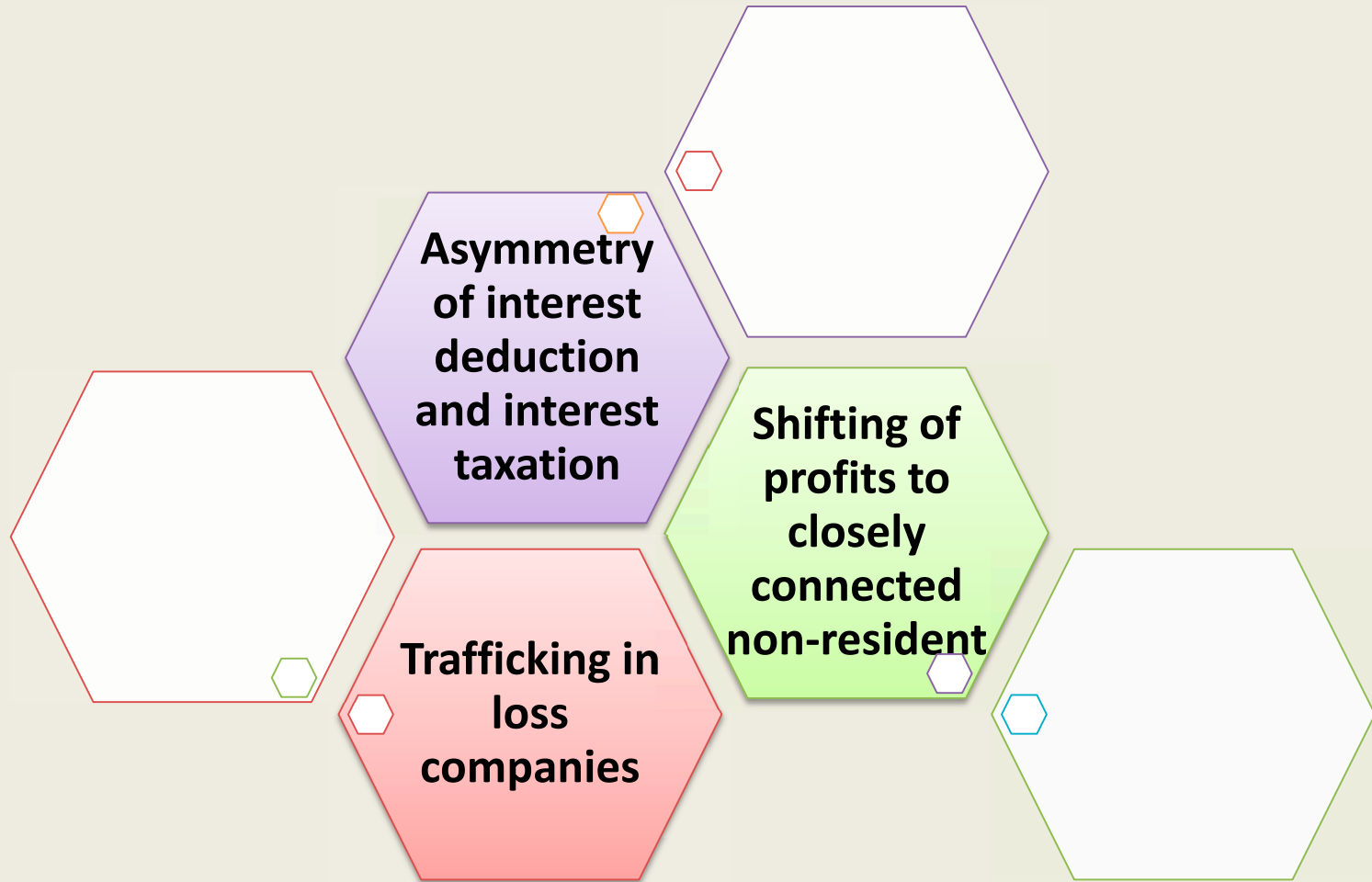
- Section 61 of the Inland Revenue Ordinance (IRO)
- In the law since 1947
- To disregard artificial or fictitious transactions
- The provision:

“Where an assessor is of the opinion that any transaction which reduces or would reduce the amount of tax payable by any person is artificial or fictitious or that any disposition is not in fact given effect to, he may disregard any such transaction or disposition and the person concerned shall be assessable accordingly.”

GAARs

- ❑ Section 61A of the IRO
- ❑ Enacted in 1986
- ❑ Consider 7 objective factors
- ❑ Conclude that a transaction is for the sole or dominant purpose of obtaining tax benefit
- ❑ Assess the relevant person by disregarding the transaction or in any way to counteract the tax benefit
- ❑ Successfully striking down a number of blatant and large scale avoidance schemes

Some SAARs



Interest deduction

The Mischief

- Sophisticated financing arrangements, particularly bank borrowings and issues of marketable instruments, in the absence of genuine need for finance
- Circular fund flows among group companies
- Generating interest deduction without interest taxation

Anti-avoidance rule

- Interest paid only deductible if it does not flow back directly or indirectly to the borrower, its associate or connected person tax free (section 16(2), (2A), (2B), (2C) of IRO)
- Prior to enactment of SAAR, had to rely on GAARs

Shifting Profits to Non-resident

Arrangement

- Resident person carries on business with a closely connected non-resident person, e.g. making purchases from the latter
- Resident person's profits reduced as a result, e.g. by inflated purchase prices

The Remedy

- Business done by the non-resident person pursuant to the arrangement deemed to be carrying on in HK
- Resident person assessed as if an agent of the non-resident person
- Section 20 of the IRO

Trafficking in Loss Companies

The Scheme

- Change in shareholding in a loss company
- Profits received by that company
- Sole or dominant purpose is to utilise the tax loss

The Remedy

- Disallow set off of loss
- Section 61B of the IRO

End

THANK YOU