
**The Establishment of
Operations in Hong Kong**

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1. INTRODUCTION

Hong Kong is generally perceived by the international business community as one of the major financial and commercial centres of the world.

This note provides an outline of matters to be considered for a corporation based outside Hong Kong (the “**non-Hong Kong company**”) which intends to establish operations in Hong Kong.

This note describes the general features of the *Companies Ordinance* (“**CO**”), which is the principal legislation governing the establishment of business operations in Hong Kong.

2. COMMON METHODS OF ESTABLISHING BUSINESS OPERATIONS IN HONG KONG

The main consideration for a non-Hong Kong company is how their business operations in Hong Kong should be carried out. Common methods are:

- incorporating a limited liability private company in Hong Kong as a wholly-owned subsidiary of the non-Hong Kong company (“**Subsidiary**”); or
- setting up a branch office of the non-Hong Kong company; or
- setting up a branch office of another overseas subsidiary of the non-Hong Kong company.

While there are other ways of setting up operations in Hong Kong (such as under joint venture arrangements, through a partnership or by way of the acquisition of an existing business), this brochure focuses on the methods above.

3. INCORPORATING A SUBSIDIARY

Generally, if the Subsidiary incorporated in Hong Kong by the non-Hong Kong company is not established primarily for the raising of equity, it will often be incorporated as a private company limited by shares (cf. public limited company) as private companies have less onerous disclosure obligations than public companies.

Under the CO of Hong Kong, a private company in Hong Kong, is defined as a company which by its articles¹:

- (i) restricts the shareholders’ right to transfer shares;
- (ii) limits the number of its shareholders to 50 (which does not include (a) persons currently employed by the company and (b) former employees of the company who were members of the company while they were employed) and who continue to be members of the company; and
- (iii) prohibits the making of any invitation to the public to subscribe for any shares or debentures of the company.

In addition, a private company must not be a company limited by guarantee.

¹ Section 11 CO

3.1 Incorporation

To incorporate the Subsidiary, the non-Hong Kong company must prepare the following incorporation documents:

- (a) Articles of association of the company;
- (b) Form NNC1 – Incorporation Form (Company Limited by Shares)²; and
- (c) Form IRBR1 - Notice to Business Registration Office.

These documents must be submitted to the Registrar of Companies together with a registration fee and business registration fee.³

When the Subsidiary is registered, the Companies Registrar will issue a certificate of incorporation that certifies its incorporation and limited liability status. The certificate is also conclusive evidence that⁴:

- (a) all requirements of the CO in respect of registration have been complied with; and
- (b) that the association is a company authorised to be registered and is duly registered under the CO.

Typically, the incorporation process takes four to five working days from the date of submission of the relevant documents to the Companies Registry. However, it is also possible to incorporate a subsidiary within a day or two by purchasing a “shelf company”. A “shelf company” is a company which has already been incorporated with a standard form of articles of association. The constitution and name of the “shelf company” can be amended as desired at a later stage. The fee for changing the company name is HK\$295.⁵

3.2 Constitution

The constitution of the Subsidiary is set out in the articles of association.

The articles of association is a document fundamental to the formation of a registered company. The CO provides that the following companies are required to have an objects clause (i.e. a clause specifying the proposed business scope or activities and the powers of the company) in their articles of association.⁶

- (i) Companies intending to apply for a licence to dispense with the word “Limited” in their names; or
- (ii) Companies whose articles of association are subject to the requirements of other Hong Kong legislation.

² section 67 to 70 and schedule 2 CO

³ section 67 CO

⁴ sections 69, 70 (1), (2) and 72 CO

⁵ section 26 Companies (Fees) Regulation

⁶ section 82 CO

3.3 Share Capital

The CO provides that shares in a Hong Kong company have no nominal value. The CO has not prescribed any requirement for the number of shares to be issued. The articles of association of a Hong Kong company with a share capital can state the maximum number of shares that the company may issue.

Under the CO, Hong Kong companies must have at least one member (i.e. shareholder) and that one member may be a nominee of the beneficial owner. The member need not be resident in Hong Kong and can be an individual or a corporation.

3.4 Name

The name of the Subsidiary must, except in very limited cases (such as charitable companies), end with the word “Limited” and must not be the same as that of a company already registered with the Registrar of Companies, or that of a body corporate established under any ordinances in Hong Kong.⁷

A company may now be registered with its name expressed either in English or in Chinese or with names in both languages. Where Chinese characters are used for the Subsidiary’s name, four prescribed Chinese characters (“you xian gong si”, translated as “limited company”) must appear at the end of that name. Sensitive words including “Government”, “Department” or “Commission” or other names that may give the impression that the company is connected in any way with the Central People’s Government or the Government of Hong Kong or any governmental department can only be used with the permission of the Registrar of Companies.⁸ When choosing a company name, companies should be aware of the common law tort of “passing off” which involves using a business name which is deceptively similar to the name of another business so that actual damage has been, or is likely to be, caused to the owner of that other business.

If the Subsidiary is registered under a name which is identical or too similar to that of another company that is already registered, the Registrar may direct the Subsidiary, within 12 months of registration, to change its name.

3.5 Directors And Company Secretary

The Subsidiary must have at least one director and one company secretary but the director cannot also be the secretary if the company has only one director.⁹

A director of the Subsidiary:

- (i) can be of any nationality and can be an individual or corporation (the CO requires every private company to have at least one director who is a natural person);
- (ii) must have attained the age of 18; and

⁷ It is advisable to check the Registrar of Company’s index of company names and the Trademark Register maintained by the Government of the Hong Kong Special Administrative Region Intellectual Property Department (<http://ipsearch.ipd.gov.hk/index.html>)

⁸ section 100(2) CO

⁹ sections 454 to 455 and section 474 CO

- (iii) must not have been disqualified from acting as a director (for example, due to bankruptcy¹⁰, conviction of fraud or other indictable offence involving dishonesty or persistent defaults in relation to the CO).

The company secretary is responsible for performing duties such as keeping the books and records of the Subsidiary, keeping custody of the company seal and making sure that all necessary documents are filed with the Registrar of Companies. The company secretary can be an individual or a corporation. If the company secretary is an individual, he/she must be resident in Hong Kong. However, if the company secretary is a corporation, it must have its registered office or place of business in Hong Kong.¹¹

3.6 Registered Office

The intended address of the Subsidiary's registered office is required to be stated in the incorporation form registered. Any change in the registered office address after the date of incorporation must be notified to the Registrar. The Subsidiary must have a registered office in Hong Kong to which any legal documents, notices or communications can be served on the company.¹² Such notices or communications are properly served if left at or sent by post to that office.¹³ If the address of the Subsidiary's registered office is changed, a notice of the change in the specified form (Form NR1) must be sent to the Registrar within 15 days after the date of the change.

The registered office does not need to be the address from which the company operates and could for example be the address of its auditor. Various statutory registers and documents of a company are required to be kept at its registered office.¹⁴ These include registers of debenture holders, shareholders, charges, directors and company secretaries, copies of every instrument creating a charge, copies of permitted indemnity provisions or written memoranda setting out the terms of such provisions, copies of management contracts or written memoranda setting out the terms of such contracts, copies of shareholders' resolutions, minutes of proceedings of general meetings and written records of decisions of a sole member, and a register of particulars referred to in section 384 CO.

If these registers and documents are kept at an address other than the company's registered office, the Registrar of Companies must be notified of their location.¹⁵

3.7 Auditor

Pursuant to the *Professional Accountants Ordinance*, the Subsidiary must appoint an auditor who is either an accountant or firm of accountants registered in Hong Kong and having recognised qualifications.¹⁶

3.8 Business Registration

Under the *Business Registration Ordinance*, at the time an incorporation application is made, the applicant must pay to the Commissioner the prescribed business registration fee and levy and deliver a notice in a form specified by the Commissioner (Form IRBR1) together with the

¹⁰ section 480(1) CO

¹¹ section 474 CO

¹² section 658(1) CO

¹³ section 827 CO

¹⁴ sections 309(1)(a), 351(1), 352(1)(a), 385(1)(a), 471(2), 543(3), 619(1)(a), 628(1)(a), 641(3)(a) and 648(3)(a) CO

¹⁵ section 309(2), 351(4), 354(1), 385(2), 471(4), 543(5), 619(2), 628(2), 641(4), and 648(4) CO

¹⁶ section 393(1) CO

other incorporation documents to the Registrar. On the incorporation of the Subsidiary, the Subsidiary is deemed to have made a business registration application.

A business registration certificate will then be issued together with the certificate of incorporation on the incorporation of the company. The business registration certificate must be displayed by the Subsidiary. A business registration certificate can be obtained for:

- (a) one year; or
- (b) three years.

4. SETTING UP A BRANCH

For commercial reasons, a non-Hong Kong company may prefer to establish a branch office (the “**Branch**”) in Hong Kong, or establish a branch office via an overseas subsidiary of the non-Hong Kong company. The following describes the procedures for setting up a branch office of a non-Hong Kong company in Hong Kong (similar rules apply to the establishment of a branch of an overseas subsidiary).

4.1 Formalities

A Branch exists where a place of business of the non-Hong Kong company has been established in Hong Kong.

For the purposes of Part 16 of the CO, a “**place of business**” includes a share transfer or share registration office,³ but it does not include a local representative office established with the approval of the Hong Kong Monetary Authority by a Hong Kong licensed bank. A place of business will normally exist if premises are occupied in Hong Kong on a relatively permanent basis from which officers or employees carry on business for the non-Hong Kong company. A non-Hong Kong company which appoints an agent in Hong Kong,³ but has no office or other place of business of its own in Hong Kong,³ will not generally be deemed to have an established place of business in Hong Kong.

4.2 Registration Requirements

Any non-Hong Kong company that establishes a place of business in Hong Kong must apply for registration as a “**non-Hong Kong company**” under Part 16 of the CO.

For registration purposes, the following documents and information must be delivered to the Registrar of Companies within one month of the establishment of the place of business in Hong Kong:¹⁷

- (a) certified copy of the non-Hong Kong company’s constitutional documents (charter, statutes or memorandum and articles of the company or other instrument constituting or defining the company);
- (b) certified copy of the non-Hong Kong company’s certificate of incorporation (where it is not the practice under the law of the place where the non-Hong Kong company purports to be incorporated to issue a certificate of incorporation, the non-Hong Kong company may tender other evidence of incorporation that the Registrar of Companies deems sufficient);

¹⁷ section 776 CO and Companies (Non-Hong Kong Companies) Regulation

- (c) Form NN1 (Application for Registration as Registered Non-Hong Kong Company) disclosing the following information:
- name of the non-Hong Kong company;
 - place of incorporation of the non-Hong Kong company;
 - date of establishment of the place of business in Hong Kong;
 - address of the principal place of business in Hong Kong and in the place of incorporation, if any
 - address of the registered office in the place of incorporation;
 - particulars of its directors and secretary (if any) including their names or alias, any former names, residential addresses, nationality and identity card/passport numbers (if the director or secretary is a company, the name and registered/principal office of that company) and their date of appointment; and
 - the name and address of at least one person (a natural person resident in Hong Kong or a firm of practising solicitors or professional accountants) who is authorised to accept on behalf of the company service of process and any notices required to be served on the non-Hong Kong company.
- (d) certified copy of the non-Hong Kong company's latest published accounts in the form required by the law of the place of incorporation of the non-Hong Kong company or, if there is no such requirement, in the form in which they are submitted to its members. The non-Hong Kong company would not need to comply with this requirement if:
- (i) The company is not required to publish its accounts or to deliver copies of its accounts to any person in whose office they may be inspected as of right by members of the public by:
 - the law of the place of its incorporation;
 - the law of any other jurisdictions where the company is registered as a company; or
 - the rules of any stock exchange or similar regulatory bodies in any of those jurisdictions.
 - (ii) The company has been incorporated for less than 18 months prior to the date of delivery of the Form NN1 and the accounts of the company that are required to be published have not been made up;
- (e) Form NM1 (Mortgage or charge details) together with a certified copy of the instrument by which the charge is created or evidenced if the company has created a charge on its property situated in Hong Kong or acquired a property situated in Hong Kong subject to an existing charge. (a registration fee of HK\$340 is required); and
- (f) Form IRBR2 (Notice to Business Registration Office).

A registration fee is payable to the Companies Registry and a business registration fee is payable to the Inland Revenue Department.

A certificate of registration of a non-Hong Kong company will be issued by the Registrar of Companies and a business registration certificate will be issued by the Inland Revenue Department when the registration requirements have been satisfied. Normally the certificate of registration will be issued within 14 working days.¹⁸

4.3 Name

There are restrictions on the registration of the name of a non-Hong Kong company which establishes a Branch in Hong Kong which are similar to those applying to a Subsidiary (see paragraph 3.4 above).

4.4 Business Registration

The provisions of the *Business Registration Ordinance* apply to the establishment of a Branch as they do to a Subsidiary (see paragraph 3.8 above).

5. CONTINUING OBLIGATIONS

A Subsidiary

5.1 Registers

A number of registers must be maintained by the Subsidiary. These include registers of debenture holders, shareholders, charges, directors and company secretaries.

5.2 Books of Account

The Subsidiary must keep proper accounting records which are sufficient to show and explain its transactions, to disclose with reasonable accuracy, at any time, the Subsidiary's financial position and financial performance; and to enable the directors to ensure that the financial statements comply with the CO.¹⁹

The books of account must be kept at the registered office of the Subsidiary or at such other place as the directors of the Subsidiary think fit. Unlike other records required by the CO, for example, the register of shareholders and the register of charges, the books of accounts need not be kept in Hong Kong. If they are kept overseas, the accounts and returns which are sufficient to disclose the financial position of the Subsidiary with reasonable accuracy must be sent and kept at a place in Hong Kong at intervals of not more than 6 months. They must also be sufficiently detailed to enable the Subsidiary's accounts to be prepared.

5.3 Annual General Meeting

The Subsidiary must, in respect of each financial year, hold its annual general meeting ("AGM") (which is a meeting of its shareholders) 9 months after the end of its accounting reference period. The accounting reference period is the period by reference to which the financial year is to be determined.

¹⁸ <http://www.cr.gov.hk/en/publications/docs/14-e.pdf>

¹⁹ section 373(2) CO

If the accounting reference period is the first accounting reference period of the Subsidiary and is longer than 12 months, the Subsidiary must hold its AGM within 9 months after the anniversary of the Subsidiary's incorporation or 3 months after the end of that accounting reference period, whichever is the later.

The AGM provides an opportunity for shareholders to question the directors on any matter, but in particular, accounts and reports which are usually presented at the meeting. Other business of the AGM may include declaring a dividend (if it is proposed that one be declared), electing directors in place of those directors retiring, and appointing auditors.

5.4 Annual Return

Each year within 42 days of the anniversary of its incorporation, the Subsidiary must file with the Registrar of Companies an annual return – Form NAR1 (giving details of various matters, including its share capital and its directors). The annual return must be manually signed by a director or the company secretary of the company.

If the return is not filed within the prescribed time limit, the Subsidiary and every officer of the Subsidiary are liable to face prosecution and, if convicted, default fines.²⁰ In addition, a substantially higher registration fee shall become payable for the late filing of an annual return. The Companies Registry may strike-off companies from the register of companies which have consistently failed to file their annual returns.²¹

5.5 Annual Accounts

The directors (in practice the auditor) are required to prepare and put before the AGM of the Subsidiary the financial statements made up to a date not more than 9 months before the meeting.²² The financial statements must show a true and fair view of the financial position and the financial performance of the Subsidiary for that financial year.²³

Various other matters which must be specified in the accounts are detailed in Schedule 4 to the CO, including details of directors' emoluments, compensation for loss of office and loans to directors. In general, the Subsidiary would also need to disclose the name and place of incorporation of its ultimate holding company in its annual accounts.

A director who fails to lay the financial statements before the company in a general annual meeting commits an offence.

5.6 Annual Reports

An auditors' report and a director's report must be attached to the Subsidiary's annual accounts before the same are presented at the Subsidiary's AGM for consideration by its members. The auditors' report must state (subject to exceptions) whether the financial statements exhibit a true and fair view of the Subsidiary's financial position and financial performance. Detailed information about the Subsidiary and its business, in particular the Subsidiary's profit and loss for the financial year and the state of affairs of the Subsidiary as at the end of the financial year, must be dealt with in the directors' report.

²⁰ section 662(6) CO

²¹ The Company Registry has expressed that it may consider taking strike-off action in appropriate cases. Please refer to http://www.cr.gov.hk/en/faq/faq05_a.htm

²² section 431(1) CO

²³ section 380(1) CO

5.7 Registration Of Charges

Particulars of certain charges or other security created by the Subsidiary must be delivered to the Registrar of Companies together with a certified copy of the instrument (if any) creating or evidencing the charge within one month of their creation. Charge documents delivered beyond the prescribed time period will not be accepted unless an order extending the time for registration is granted by the court.²⁴ For charges created outside of Hong Kong over property situated outside Hong Kong, the registration period is one month after the date on which a certified copy of the instrument creating or evidencing that charge could, if despatched with due diligence, have been received in Hong Kong in due course of post .²⁵

Similarly, when the Subsidiary acquires a property subject to an existing charge, such a charge must be registered within one month after the date on which the acquisition is completed. Failure to register the charge results in the charge being void against any liquidator and any creditor of the Subsidiary. Although the charge is void, the “chargee” has the right to claim as an unsecured creditor for the repayment of any debts secured by the charge and this amount may become immediately payable by the Subsidiary.²⁶

5.8 Registered Particulars

The Registrar of Companies must be notified when there are any changes in the details and particulars registered. These include but are not limited to:

- (a) any change of registered office;²⁷
- (b) allotment of shares by the Subsidiary²⁸;
- (c) any change of director and company secretary of the Subsidiary and any change of their particulars;²⁹
- (d) special resolutions passed by the shareholders of the Subsidiary, for example, amending its articles of association.

5.9 Public Inspection

All documents filed with the Registrar of Companies are open to public inspection and any person, upon payment of fees, can obtain copies of such documents.³⁰

5.10 Disclosure

The Subsidiary must exhibit its full and correct name outside every office or place in which it carries on business in Hong Kong in a conspicuous position in legible characters and must state the same on, among other things, all of its business letters, notices and other official publications.³¹

²⁴ section 346 CO

²⁵ section 335(5) CO

²⁶ section 337(4) CO

²⁷ section 658 CO

²⁸ section 142 CO

²⁹ sections 645(1) and (4), 652 (1) and (2) CO

³⁰ section 45(1) CO

³¹ section 659 CO, Companies (Disclosure of Company Name and Liability Status) Regulation

The Subsidiary may possess a common seal containing the full name of the Subsidiary and must be made of metal.³²

A Branch

5.11 Annual Return

Each year within 42 days of the date of registration of the company in Hong Kong, the non-Hong Kong company must file with the Registrar of Companies an annual return – Form NN3. The annual return must be manually signed by a director, the company secretary, or the Hong Kong authorised representative of the non-Hong company.

If the return is not filed within the prescribed time limit, a substantially higher registration fee shall become payable for the late filing of an annual return.

5.12 Accounts

The non-Hong Kong company need not deliver its accounts to the Registrar of Companies if it is a company of the type described in paragraph 4.2(d) above. Otherwise, the non-Hong Kong company must submit its accounts together with an annual return to the Registrar of Companies within 42 days after each anniversary of the date of registration of the company in Hong Kong.³³ The accounts must be duly certified by a director, the company secretary, or the Hong Kong authorised representative of the non-Hong Kong company.

In any event, the Branch should prepare branch accounts for tax return purposes.

5.13 Registration Of Charges

Under Section 336, only charges on Hong Kong property created or acquired by non-Hong Kong companies which are registered under Part 16 will be required to be registered with the Registrar of Companies. Accordingly, charges created by non-Hong Kong companies which are not registered under Part 16 will not need to be registered.

Section 333(2) specifies that ships and aircraft that are registered in Hong Kong will be treated as property in Hong Kong irrespective of their physical location. Likewise, ships and aircraft registered outside Hong Kong will be treated as property outside Hong Kong.

The non-Hong Kong company is required to register with the Companies Registry particulars of any mortgages and charges created by it over property situated in Hong Kong within 1 month of their creation.³⁴ Further, it is also required to register an existing charge on acquired property situated in Hong Kong.

5.14 Registered Particulars

The Registrar of Companies must be notified of any change in certain registered documents or particulars of the non-Hong Kong company. These include:

³² section 124 CO

³³ section 789 CO, Companies (Disclosure of Company Name and Liability Status) Regulation

³⁴ section 336(6) CO

- (a) any change of directors, company secretary or authorised representatives of the non-Hong Kong company and of their particulars (to be filed within 1 month from the date of change)³⁵;
- (b) any change of address of the principal place of business in Hong Kong and in the place of incorporation and the address of the registered address in the place of incorporation (to be filed within 1 month of change)³⁶;
- (c) any alteration in the constitution, charter, statutes or memorandum of articles (to be filed with supporting documents within 1 month of such alteration)³⁷; and
- (d) change in the corporate name of the non-Hong Kong company (to be filed with supporting documents issued by the relevant government authority within 1 month of such change)³⁸.

5.15 Authorised Representative

The non-Hong Kong company must have an “authorised representative” in Hong Kong (see section 4.2(e) above) until at least 1 year after it has ceased to have a place of business in Hong Kong.³⁹

5.16 Issues Of Shares

The non-Hong Kong company must not offer shares or debentures to the public in Hong Kong unless it adheres to a number of disclosure and registration requirements mainly imposed by the CO and the *Securities and Futures Ordinance*.

5.17 Disclosure

A non-Hong Kong company which carries on business in Hong Kong must state its name, country of incorporation and (if so) the fact that it is incorporated with limited liability in legible characters in all bill-heads and letterheads, notices and other official publications of the corporation, and, if the corporation is in liquidation, in all advertisements of the corporation with the words “in liquidation” added after its name.⁴⁰

6. SPECIAL PROVISIONS

Depending on the type of business that is being operated, the business may be subject to the operation of other additional legislation and subject to the supervision and control of various regulatory bodies. The following is a non-exhaustive list of business types that are subject to other legislative provisions in Hong Kong:

- Banking and the taking of deposits
- Insurance business
- Investment management and advice

³⁵ section 791(2)(b) & (c) CO

³⁶ section 791(2)(d) CO

³⁷ section 791(2)(a) CO

³⁸ sections 778 and 779 CO

³⁹ section 786 CO

⁴⁰ section 337 CO

- Dealing in foreign exchange, derivatives, securities and commodities
- Textiles import-export business
- Employment and travel agencies
- Food and liquor business
- Money changing business
- Media business (including cinema, newspapers, theatres, telecommunications and television)
- Shipping, aviation and transport services
- Professionals (including lawyers and accountants)

Specialist advice should be obtained if the intended business falls within these categories.

7. TAXATION ASPECTS OF SUBSIDIARIES AND BRANCHES IN HONG KONG

7.1 Introduction

The Hong Kong system of taxation is based on the principle of territoriality (i.e. only profits which are derived from Hong Kong are taxable in Hong Kong). There are no payroll, turnover, sales, value added, gift or capital gains taxes in Hong Kong. There is also no tax on dividends paid by Hong Kong companies. In Hong Kong, the principal tax likely to be payable by either the Subsidiary or the Branch which has established business operations in Hong Kong is profits tax.

7.2 Profits Tax

Profits tax is charged on every person carrying on a trade, profession or business in Hong Kong in respect of assessable profits which arise in or are derived from Hong Kong from such trade, profession or business. In certain circumstances, profits tax may be charged in respect of profits deemed to arise in or be derived from Hong Kong.⁴¹ No distinction is made between residents and non-residents.

The source of profits is therefore crucial in determining whether or not they are taxable. The question of whether a business is carried on in Hong Kong and whether profits are derived from Hong Kong is largely a question of fact. The courts determine whether assessable profits of a trade, profession or business have arisen in Hong Kong by examining what has been done to earn the profits and then seek to establish where these profits were derived.

The source of profits may not be immediately apparent and it may be necessary to consider this question at length. Specialist advice should be sought if necessary.

7.3 Determination of Profits

Tax is charged on the assessable profits for a year of assessment. The assessable profits are the net profits (or loss) arising in or derived from Hong Kong during the year of assessment,⁴² calculated in accordance with the provisions of the *Inland Revenue Ordinance* (“IRO”)

⁴¹ section 14 and 18 IRO

⁴² section 18 and 18B IRO

The Subsidiary or Branch must include its accounts when submitting profit tax returns issued to it. If the Inland Revenue is satisfied that the Branch accounts show the Branch's true profits, they are adopted and the tax payable is calculated under profits tax principles. If not, the non-Hong Kong company's worldwide profits are adjusted to conform with profits tax principles and apportioned on the basis of the ratio of Branch turnover to worldwide turnover. If, in the Inland Revenue's opinion, this would be impracticable or unfair, it has the power to assess what it considers to be a "fair" percentage of the turnover of the Branch to profits tax.

7.4 Rates of Profits Tax And Assessments

Corporations are charged profits tax at the current rate of 16.5%. A concession of half the normal profits tax payable is provided for trading profits and interest income received or derived from qualifying debt instruments in Hong Kong. The amount of profits tax payable is assessed on receipt of tax returns submitted to the Inland Revenue by the taxpayer. This tax return must be submitted within 4 months from the end of a tax year (on or before 31 July in each year).⁴³

As the profits of any particular year cannot be ascertained until after the tax year ends, a provisional profits tax is payable at the standard rate by reference to the agreed assessable profits of the year preceding the year of assessment.⁴⁴ The provisional assessment is payable in two instalments, 75% in the final quarter of the current tax year and the balance within three months of the first instalment. Any provisional profits tax that is not applied to the payment of the actual profits tax payable when a profits tax assessment is made shall be refunded.⁴⁵ The amount of provisional profits tax payable in the following year shall be adjusted accordingly.

7.5 Double Taxation

Hong Kong has reached an understanding with the relevant tax authorities in the Central People's Government, PRC for the avoidance of double taxation between the Mainland and Hong Kong. The arrangement covers airline and shipping operations as well as other business activities. In addition, double taxation relief arrangements in shipping and airline income with other countries have also been concluded.⁴⁶

7.6 Treatment of Losses And Deductions

Loss relief may be available to the Branch or Subsidiary. In general, where a loss is incurred in any year of assessment, the amount of such loss attributable to activities in Hong Kong shall be set off against assessable profits in that year of assessment. Where an amount of loss cannot be wholly set off for the year of assessment in which the loss occurred, the amount not set off shall be carried forward to future years.⁴⁷ A corporation carrying on more than one trade can have losses in one trade offset against profits of the other trade.

Also, outgoing and expenses, to the extent to which they are incurred in the production of assessable profits during the year of assessment, may be deducted from tax chargeable to the Branch or Subsidiary.⁴⁸

⁴³ The tax year for corporation ends on 31 March each year for corporations.

⁴⁴ section 63G and section 63H IRO

⁴⁵ section 63K IRO

⁴⁶ Please refer to <http://www.ird.gov.hk/eng/tax/dta1.htm> for more information on which countries have double taxation agreements with Hong Kong.

⁴⁷ section 19 IRO

⁴⁸ section 16(1) IRO

Capital expenditure is not deductible but there is a system of capital allowances relating to buildings, plant and machinery (i.e. depreciation allowances for industrial and commercial buildings).⁴⁹

7.7 Dividends

There is no withholding tax on dividends payable by a Subsidiary or Branch.

7.8 Transfer Pricing

Due to Hong Kong's relatively low tax rates, it is uncommon for corporations to devise transnational arrangements for the purpose of tax avoidance. Nevertheless, the IRO contains anti-avoidance provisions to combat any such arrangements.

7.9 Keeping Business Records

All persons carrying on business in Hong Kong are required to keep sufficient records, in English or Chinese, of their income and expenditure to enable their assessable profits to be readily ascertained. There are also statutory requirements to record certain specified details of every transaction. Business records must be retained for at least seven years after the date of the transaction to which they relate.

7.10 Other Taxes

Property Tax is payable on rental income. There is no tax on capital gains or any form of sales tax in Hong Kong but there are special taxes on hotels, entertainment and betting and duties are payable on a number of products, such as alcohol and tobacco. There are also other duties (including stamp duty) and taxes chargeable in Hong Kong (see section 9.2 below).

8. INTELLECTUAL PROPERTY

This section outlines the main types of intellectual property protection available to all businesses in Hong Kong. The intellectual property laws of Hong Kong have changed dramatically since the handover of its sovereignty to China in July 1997.

8.1 Patents

Patents in Hong Kong are regulated by the Patents Registry of the Intellectual Property Department and governed primarily by the *Patents Ordinance* (“**PO**”). Under the PO, an application for a patent can be made to the Registrar by a proprietor of an invention.⁵⁰ An invention is patentable if it is susceptible to industrial application, is new and involves an inventive step (i.e. it is not obvious as part of the state of the art of a person skilled in the art). The proprietor of a “designated patent”(i.e. a patent granted by a designated patent office, normally the UK or China Patent Office) can also apply to the Registrar to record the patent without further examination.

8.2 Trademarks

The Subsidiary, or the non-Hong Kong company acting through its Branch, may sell goods or offer services by reference to a particular identifying mark. There is a Trade Marks Registry in

⁴⁹ section 33A and section 34 IRO

⁵⁰ section 12 PO

Hong Kong at which trade marks in respect of goods and services may be registered provided that they satisfy certain requirements.⁵¹ Civil and criminal remedies are available in respect of infringements of a registered trade mark.

8.3 Copyright

The *Copyright Ordinance* provides for the protection of original literary, drama, musical works, artistic works, sound recordings, films, broadcasts, cable programmes and published editions.⁵² Copyright works attract copyright protection under the Ordinance automatically upon creation and civil and criminal remedies are available in support of such rights.

8.4 Passing Off

The concept of “passing off” is based on English common law. It may be thought of as a form of unfair competition law and it seeks to protect established goods or services of traders from being imitated by others, thereby misleading the public and causing damage and loss to the trader’s business. Provided that all the necessary elements of the alleged passing off can be established, a trader is entitled to civil remedies.

8.5 Registered Designs

Any person claiming to be the owner of any article(s) can apply to Registrar of Designs to register the design in such article or articles(s).

In order to obtain a valid registration, the design must be novel, possess individual character and must be industrially applied to manufacture articles. Registering designs however protect only the shape, visual appearance, aesthetic appeal or ornamental characteristics of a new design and protection does not extend to any functional features, which are within the reign of technical patent for invention. Civil remedies are available in respect of any infringements of the rights of a proprietor of a registered design.

9. STAFF

It is common for a non-Hong Kong company to second/transfer staff from their overseas main office or recruit local or overseas expatriate staff to work in their Subsidiary or Branch in Hong Kong. These non-Hong Kong Companies should be mindful of Hong Kong immigration and taxation requirements when considering these alternatives.

9.1 Employment Visas

Generally, any person other than those having the right of abode, right to land or unconditional stay in Hong Kong must obtain an employment visa for their prospective employment from the Hong Kong Immigration Department prior to arriving in Hong Kong if they wish to take up employment in Hong Kong. It is immaterial whether the employment period is short or on a temporary basis. Spouse and children of the applicant for employment visa may apply for dependant relative visas.

The Hong Kong Immigration Department will invariably request to see a contract of employment executed between the Hong Kong company and the expatriate staff so they are satisfied that the employment terms are no less favourable than those which would be extended

⁵¹ section 47 of the Trademarks Ordinance (Cap 559)

⁵² section 2 Copyright Ordinance

to a local Hong Kong resident. The employment visa application would also require a local sponsor to guarantee the expatriate's stay in Hong Kong.

Documentation and information that is required to be submitted include the sponsor's constitutional documents as well as various specified forms (including forms that ascertain the sponsor's financial standing, detail the job to be performed by applicant, detail the education, academic and professional qualifications and work experience).

9.2 Salaries Tax

Salaries Tax is payable on income (including wages, salary, leave pay, fee, commission, bonus, gratuity, perquisite, or allowances derived from the employer or others⁵³) arising in or derived from Hong Kong from any office or employment of profit and any pension (voluntary or is capable of being discontinued).⁵⁴

(i) The source of income

Often, the most difficult matter to determine is the source of income. The relevant factors to consider include the place where the employment contract was negotiated and entered into and its governing law, the employer's place of residence, and, to a lesser degree, where and in what currency remuneration is paid.

If the source is found to be outside Hong Kong, only income derived from services rendered in Hong Kong will be subject to salaries tax. Therefore, the structure of an employee's employment should be carefully planned at the outset for maximum tax-efficiency. If the Inland Revenue Department considers that, in substance, the source of any employment, however structured, is really in Hong Kong then it may assess the employee on that basis.

If a person provides services in Hong Kong by visiting Hong Kong for no more than 60 days in any tax year, then usually no salaries tax is payable.⁵⁵ If double tax becomes payable on any income, limited relief is available.

(ii) Fringe benefits

Fringe Benefits provided to an employee which can be converted into money by the employee are chargeable as salaries tax.⁵⁶ Chargeable income also includes the rental value of accommodation provided rent-free⁵⁷ or subsidised⁵⁸ by the employer or associated corporation. Specific advice on the employee's proposed remuneration package should be obtained.

(iii) Rate

Net chargeable income (i.e. assessable income after deductions and allowances) is charged either at progressive rates of up to 17% or at the standard rate of 15% of net

⁵³ section 9(1) IRO

⁵⁴ section 8(1) and section 8(2) IRO

⁵⁵ section 8(1B) IRO

⁵⁶ section 9(2A)(ii) IRO

⁵⁷ section 9(1)(b) IRO

⁵⁸ section 9(1)(c) IRO

total income, whichever results in a lower tax bill. There is also a system of provisional salaries tax similar to the one mentioned in paragraph 8.4 for profits tax.

(iv) Employer's duties

An employer is not obliged to withhold any of his employee's tax except if the employee has given notice and intends to leave Hong Kong. An employer must file certain returns with the Inland Revenue Department and inform the Inland Revenue when an employee is due to leave Hong Kong.

9.3 Employment Protection

The *Employment Ordinance* (“*EO*”) and various other regulations contain employment protection provisions to protect employees.

(i) Termination of employment

Employment contracts are terminable upon the giving of one month's notice or on payment of one month's wages in lieu of notice, unless a different notice period (being not less than seven days) is agreed in writing.⁵⁹ There are legislative provisions (which may be supplemented in the contract) specifying circumstances that enable contract to be terminated by the employer without notice (for example, if the employee is guilty of fraud or dishonesty) in relation to his employment or by the employee without notice or payment in lieu of notice (for example, if the employee is subject to ill-treatment by the employer).⁶⁰

(ii) Anti-discrimination provisions and membership of trade unions

Special rules apply in relation to the employment of women, young persons and children. The *Sex Discrimination Ordinance*, the *Disability Discrimination Ordinance* and *Family Status Discrimination Ordinance* prevent discrimination by an employer against any person on the grounds of sex, disability or the family status of a person. Further, an employer is not allowed to prevent employees from belonging to or being active in trade unions registered under the *Trade Union Ordinance* or prevent them from taking part in their activities (although unions are not widespread outside the industrial sector).⁶¹

(iii) Rest days, holidays and leave

There are also special rules for the entitlement of employees to holidays and leave, including one rest day every seven days and statutory holidays. After the first year of employment, an employee is entitled to annual leave with pay, the length of which depends on the length of his service.⁶²

The EO provides that employees who have been employed under a continuous contract for a period of one month or more shall be entitled to receive sickness allowance in certain circumstances, at a rate of four-fifths of their wage for up to a maximum of 120 days accumulated on the basis of the length of service.⁶³

⁵⁹ section 6(2)(c) and 7(1A) EO

⁶⁰ section 9 and 10 EO

⁶¹ section 21B(1) and (2) EO

⁶² section 41AA EO

⁶³ section 33 and 35(2) EO

(iv) Long service and severance payments

An employee may be entitled to long service payment when he leaves his job. If an employee who is under a continuous contract for more than 5 years and retires at an age not less than 65 or dies, the employee shall be entitled to long service payment. In the event that the employee has died, the long service payment is payable to the employee's relatives or personal representatives. The amount of the long service payment that the employee is entitled to depends on the length of service together with any mandatory provident fund scheme or occupational retirement scheme benefit.⁶⁴

Severance payments are available to employees dismissed by the employer as a result of redundancy⁶⁵ or being laid off.⁶⁶ Employers are however, not permitted to dismiss employees with the intent to reduce or extinguish certain statutory benefits, rights or protection under the EO.

(v) Maternity leave

Women employed under continuous contracts for a period not less than 40 weeks are entitled to paid maternity leave⁶⁷. The rate of maternity leave pay payable is calculated at four-fifths of their normal wages immediately prior to her taking maternity leave.

Maternity leave shall be an aggregate of⁶⁸:

- (a) a continuous period of 10 weeks;
- (b) a further period beginning after the date of expected confinement up to and including the actual date of confinement; and
- (c) a further period, not exceeding 4 weeks, taken on the grounds of pregnancy-related illness or disability.

(vi) Mandatory Provident Fund

In the interests of funding benefits for employee's retirement, the Mandatory Provident Fund Schemes Ordinance ("MPFO") requires employers to take practical steps to ensure that their employees become a member of a registered mandatory provident fund scheme.⁶⁹ Both employers and employees must contribute to the fund, which is to be established in the form of trusts.

Compulsory contributions are required to be made by the employer to the employee's fund at the rate of 5% (unless otherwise prescribed by other regulations) of the relevant employee's income (i.e. all monetary remuneration except for housing allowance), subject to a maximum amount of HK\$1,500 per month.

10. PREMISES

⁶⁴ section 31V and 31Y EO

⁶⁵ section 31B(1) EO

⁶⁶ section 31E EO

⁶⁷ section 12(1) and 14(2) EO

⁶⁸ section 12(2) EO

⁶⁹ section 7 MPFO

Apart from considering the method of establishing business operations in Hong Kong, consideration must be given to the obtaining of commercial premises from which the business operations can be carried out. In addition, if staff are to be relocated from overseas, some thought must be given to the provision of housing to staff members and their families.

In all likelihood, purchasing either commercial or residential premises will not be a first option as Hong Kong property values are notoriously high and the property market can be volatile. Therefore, for the purposes of this brochure, only issues relating to the renting of premises will be addressed.

10.1 Commercial Premises

The terms and conditions of commercial tenancy agreements can vary greatly and market forces will dictate how negotiable these terms are.

As a general comment, market conditions usually favour Hong Kong landlords and usually landlords will only allow fairly cosmetic amendments to their “standard” documentation. Some larger commercial landlords reject changes altogether.

Nevertheless, professional assistance should always be sought for reviewing the terms of a proposed tenancy agreement and for advice in relation to pertinent commercial risks. A number of important commercial issues should be considered, including:

(i) Rent

Rent is often quoted as a dollar figure per square foot per month. It is important to determine whether the figure quoted includes such additional charges as management fees, air-conditioning charges, rates and utility charges (Usually the figure quoted for rent will exclude these extra charges and which the tenant is required to pay in addition to rent). In the current rental market it is possible to negotiate rent-free periods of one to two weeks prior to the commencement of the term.

(ii) Term

There are no standard terms for commercial tenancies in Hong Kong and the length of a tenancy is simply a matter for negotiation. Options to renew will not always be offered by landlords and Hong Kong legislation does not provide for security of tenure in the case of commercial premises.

(iii) Security Deposit

A security deposit will almost always be required and invariably it will be an amount equivalent to two or three months’ rent, management fees and other fees (such as air-conditioning charges). The security deposit will be refunded at the expiration of the term, but without interest, subject to forfeiture or deduction for breaches of the terms of the tenancy agreement. Hong Kong landlords are typically reluctant to accept bank guarantees in lieu of cash deposits.

(iv) Alienation Rights

Commercial tenancy agreements will seldom include unrestricted right for the tenant to alienate the tenancy. More often than not there will be no right to assign, sublet or otherwise part with possession of the premises, although it may be possible to negotiate the right to share the premises with an associated company.

10.2 Staff Housing

Unlike some countries where residential tenancy agreements are in a standard form endorsed by the local Law Society or real estate institute, Hong Kong has no standard form residential tenancy agreement. Accordingly, residential tenancies vary in terms just as widely as commercial tenancies.

Normally, residential tenancies are for a period of 2 years at a monthly rent fixed for the entire term. The tenant will bear the cost of rates, management fees and utility charges. Some landlords will grant the tenant a “break right” allowing the tenant to terminate the tenancy after, say, the first 12 months of the term upon the giving of 2 months’ notice. Options to renew are rarely included. However, the tenant will have some degree of security of tenure by virtue of the Landlord and Tenant (Consolidation) Ordinance. This Ordinance provides a mechanism for renewing a tenancy at the expiration of the term of the agreement at the then “prevailing market rent”, unless the landlord can show one of the statutory grounds on which to terminate the tenancy. As with commercial tenancies, a security deposit is almost always required.

11. ANCILLARY MATTERS

There are numerous other matters which need to be taken into consideration by the non-Hong Kong company when setting up operations in Hong Kong, including making suitable banking and financial arrangements, insurance arrangements (such as taking out compulsory Employees’ Compensation Insurance, fire, burglary and public liability insurance) and (if appropriate), employee pension or provident fund arrangements.

12. HOW WE CAN HELP YOU?

If you are considering establishing business operations in Hong Kong, whether by way of a Subsidiary or a Branch as outlined above, or any other means, we can assist by:

- providing advice on all aspects of commercial, company, property, intellectual property, tax, employment, immigration, pensions, insurance, banking and financial services law;
- advising on the structure of the proposed business;
- advising on the formalities to be observed when establishing the business;
- preparing necessary documents including submissions for any approvals and authorisations required to be obtained by the business, and liaise with the relevant authorities on your behalf; and
- providing practical advice on ancillary matters that need to be considered when setting up a business.

If you would like further information about establishing business operations in Hong Kong, please feel free to contact us on (852) 2905 7888 or write to us at 12th Floor, Dominion Centre, 43-59 Queen’s Road East, Hong Kong (Fax No. (852) 2854 9596).

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