

International Taxation – Opportunities and Challenges

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Background of international taxation

- The power to make tax legislation, and to levy tax is deeply bound with the notion of sovereignty
- In an increasingly globalised economic context, different tax regimes may be incompatible, or produce un-commercial results, such as taxing the same income stream or capital gain twice or tax asymmetry
- 3. The solution is double tax treaties (DTTs) these are bilateral instruments governed by public international law that allocate taxing rights between jurisdictions
- 4. Hong Kong is not a sovereign state, but has delegated authority to make its own tax legislation (Article 106) and to negotiate international agreements in certain domains (Article 116) relevantly including taxation



How DTTs operate

- Bilateral arrangement and cannot bind third parties
- Hong Kong has a common law system, which is dualistic
- Important concepts include:
 - Treaty residence the DTT applies only to residents of one contracting party or the other
 - Permanent Establishment where a person resident in one contracting party has a taxable presence in the other contracting party
 - Transfer pricing arm' s length principle
 - Beneficial ownership of income and gains
 - ➤ Withholding tax (WHT) tax withheld by the payor at source
 - Dividends, royalties, and interest
 - Lower rates of WHT can be provided for in the DTT
 - Crucial aspect of tax planning through DTTs



Tax planning opportunities and challenges



International tax structuring

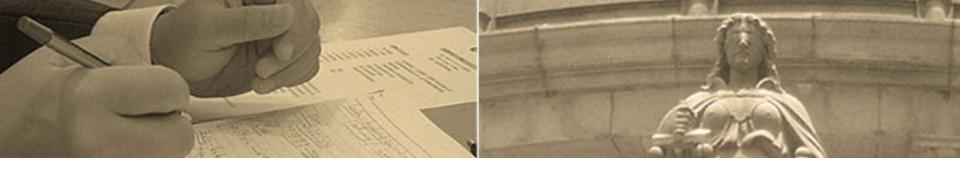
- DTTs are useful in tax planning:
 - Minimise taxation, and avoid double taxation
 - Provide legal certainty on the tax treatment of cross-border transactions
 - Dispute resolution mechanism in most DTTs by way of Mutual Agreement Procedure and Exchange of Information clauses
- Hong Kong is an advantageous structuring jurisdiction:
 - WHT of 4.95 (in general) on royalties and no WHT on interest and dividends
 - Dividends not tax on receipt
 - No capital gains tax
 - Light-touch tax compliance regime
 - Good double taxation agreement with China
- But there are challenges:
 - Need 'economic substance' to obtain certificate of resident status from Hong Kong Inland Revenue Department
 - > Treaty abuse and treaty shopping OECD measures to counter Base Erosion and Profit Shifting
 - Principal purpose test in art. 7 of the Multilateral Instrument



Current and future trends

- Multilateralism and the influence of the OECD
- From litigation to arbitration?
- Domestic and international anti-abuse and antiavoidance provisions
- Revenue authorities seeking to align tax with value creation
- Tax incentives discouraged can the territorial system of jurisdictions like Hong Kong, Singapore, and Malaysia survive?





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