

**DOING
BUSINESS
IN**

HONG KONG



Hodgson Impey Cheng

Certified Public Accountants, Consultants and Business Advisers

*Doing Business
in Hong Kong*

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1. Foreword

This booklet has been prepared for the use of Clients, Partners and Staff of HLB International member firms, including HLB Hodgson Impey Cheng.

It is intended to be a general guide to doing business in Hong Kong and is written primarily for business people from abroad seeking an overall summary of the environment in which business is conducted and it is not intended to be a comprehensive document.

You should consult us, therefore, before taking further action.

HLB Hodgson Impey Cheng is the Hong Kong member firm of HLB International. The firm was formed in 1983 but can trace its origins back 50 years in Hong Kong and over 200 years in the United Kingdom.

We are a firm large enough to give clients a comprehensive range of business and financial advice, international enough to help our clients meet their needs throughout the Asian region and worldwide. Yet we make every effort to ensure we offer a truly personal service.

We look forward to welcoming new clients to the exciting commercial possibilities that Hong Kong and China have to offer in the 21st Century.

“OUR AIM IS QUALITY SERVICE.....meeting our client’s needs and exceeding their expectations.”

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2. Introduction

This booklet is designed to give some background information to overseas businessmen looking at China and the Asian region, and how Hong Kong in particular can act as a base for corporate activity.

Hong Kong was very much in the news when, on 1 July 1997, sovereignty reverted back to the People's Republic of China after 150 years as a British colony. As from that date it became the Hong Kong Special Administrative Region (SAR). Although now fully a part of China, the SAR retains an extraordinary degree of autonomy. This is guaranteed under the Basic Law, a sort of mini-constitution, originally hammered out between Britain and China. Although some (even within Hong Kong itself) were unsure just how much independence would be permitted time has shown that, in practice, doing business in Hong Kong is exactly the same after 1 July 1997 as it was before.

This fact is greatly welcomed by many who trusted the values and integrity of Hong Kong. What doubts there were have been largely dispelled and, today it really is a case of 'business as usual'.

Since the early 1990s the Hong Kong economy has become inextricably linked to that of southern China. This has been a significant factor in the SAR's continued prosperity. Even so, important as it is, Hong Kong remains also a centre for trade throughout the rest of Asia and for international companies doing business in the region.

At the end of March 2005, Hong Kong's stock market was the second largest in Asia (eighth largest in the world) in terms of capitalisation, and Asia's third largest foreign exchange market in terms of turnover (seventh in the world).

Hong Kong's stock market is highly internationalised with a large number of stocks. At the end of March 2005, there were over 1,000 companies listed on the stock exchange, including some 200 companies on the growth enterprise market (GEM), with a total market capitalisation of US\$843 billion. Currently, about 200 Chinese mainland enterprises are listed on the local stock market, either as H-share or 'red chips' companies.

Hong Kong has been long used by multinational companies as a regional base to manage their businesses in the Asia Pacific, particularly in the Chinese mainland. Based on a government survey in Hong Kong in June 2003, there were 5,414 regional operations of overseas companies in Hong Kong, an increase of 10% from a year previously. Of these regional operations, 92% have operations related to mainland China. Nowadays, Hong Kong also provides an international gateway for mainland companies wishing to explore financing opportunities, within or outside Asia.

There are many reasons for this success, but probably the main reasons are as follows:

- A stable government dedicated to the encouragement of free enterprise and opposed to regulation or intervention unless deemed absolutely essential.
- A respected, independent, legal system based on transparent Anglo-Saxon principles.
- A free press that is widely-owned, independent, and vocal.

- A good blend of entrepreneurial skills and a stable, talented, adaptable and hard-working labour force.
- A complete absence of foreign exchange controls and only minor import duties on a small number of items.
- Very low levels of taxation by international non-tax haven standards.
- No restrictions on foreign investment.
- Superb communications and banking facilities.
- A location at the geographical centre of Asia.
- The willingness of its businessmen to diversify according to international market demand and react quickly to changing trends.
- The complete range of high quality professional services available.



3. *About HLB International*

HLB International is a worldwide organisation of professional accounting firms, each providing clients with a comprehensive and personal service relating to auditing, taxation, accounting and general and financial management advice.

Formed in 1969, HLB can assist clients to do business in over 100 countries, with more than 1,600 partners and 10,440 staff in over 430 offices.

Up-to-date information and general assistance on international matters can be obtained from any of the partners of HLB Hodgson Impey Cheng or from the HLB Executive Office in London:

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4. General Information

4.1 Geography and History

Hong Kong as a territory is a small outcrop of China, part island and part mainland, south of Guangzhou (formerly known as Canton). The total land area of Hong Kong is approximately 1,000 sq. Kilometres, of which around 10%, comprising Hong Kong Island itself, some of Kowloon and some outlying islands was ceded to the British Government in perpetuity under the Treaty of Nanking. The remaining land area, being the remainder of Kowloon, the New Territories and the other islands, was leased from the Chinese Government. For 150 years it was officially a British Crown Colony but in reality had independent government as far as day-to-day administration was concerned.

The leases expired on 1 July 1997 and it was agreed between the British and Chinese Governments that the ceded territory would be returned to China at the same time. From that date on the territory has been administered by the people of Hong Kong themselves as a Special Administrative Region (SAR) of China. Under the terms of the Sino-British Joint Declaration the Hong Kong SAR will continue to enjoy essentially the same system of law, government, and ways of doing business as operated at the time of the return of sovereignty. This will continue at least until 2047 - or 50 years after the reintegration of the SAR with the mainland.

Today, Hong Kong has a population of 6.84 million, generating GDP of some US160 billion, and projected to grow at a real rate of 9.5%. Unemployment rate is around 6.8%. The official language is Cantonese but English is widely spoken and is the main form of business communication.

Hong Kong enjoys a sub-tropical climate. Summer season is rather warm and humid from June to September, while in the winter, the temperature can drop to as low as around 10 degrees celsius.

4.2 Gateway to China

Due to its physical proximity to the mainland of the People's Republic of China, Hong Kong has developed into the main base for China operations over the years. Most major banks, law firms and ourselves, as a leading accounting firm, have expertise available to assist clients wishing to invest in or trade with China. It is very common for Hong Kong companies to be incorporated as the vehicle for such trade.

Over 50% of the total external investment in China goes through Hong Kong. The financial ties between Hong Kong and the southern Chinese mainland province of Guangdong, which abuts Hong Kong, are especially strong. As many as six million people in Guangdong province alone are employed either directly (through joint-venture operations) or indirectly (in the form of outward processing arrangements) by Hong Kong companies. Forty percent of the mainland's foreign trade is handled via Hong Kong. Three of China's four Special Economic Zones are in Guangdong province, while the best known of these, Shenzhen, a large thriving city in its own right, actually lies immediately across the border.

4.3 China Now and in the Future

Today China enjoys one of the world's fastest growing economies. Some analysts argue that the mainland economy is already the third largest in the world, and estimate that during the 21st century it will be the largest. The rapid growth and industrialisation in the south, and along the eastern and northern coastline is beginning, albeit gradually, to spread out into the hinterland. The move towards an unfettered market economy has brought with it a requirement for modern technology and equipment, for up-to-date management and financial systems, for the latest in design and for consumer goods. These can really only be met from overseas at this stage of China's development. China's economic growth and opportunities for foreign businesses will accelerate rapidly during the years immediately following the admission of China into the World Trade Organisation (WTO).

On top of which there is the consideration of China's 1.3 billion population. The prospect of being in a position to reach such a huge consumer base, in the not too distant future, has led to many well known brand names entering the market - often using Hong Kong as a 'springboard'.

Our China Business Department is able to handle the rapidly growing demands of those wishing to do business with China.

4.4 Asian Centre

Hong Kong is often used as the base for the Asian operations of overseas companies. It is arguably the financial centre of Asia and it is possible to establish a company in Hong Kong which carries on trade with other Asian countries totally free of Hong Kong taxation. (See Section 7 on Hong Kong Tax Structure).

4.5 Government

In 1997, a newly created post, that of Chief Executive of the Hong Kong SAR, replaced the colonial Governor. This is an elected position and must be filled by a local Hong Kong person. In most other respects though the form, and practice, of government remains largely unchanged. The Chief Executive is assisted by an Executive Council and a Legislative Council: the former consisting of ex-official members and others from government and the general community, while the latter comprises an elected element. The Government is served by a professional Civil Service. The Government of the People's Republic of China retain power over matters relating to defence and foreign affairs. In virtually all other areas the SAR is fully 'self governing'.

4.6 Regulations

Regulation of business is kept to a minimum, the Government preferring to rely on market forces. Hong Kong has been fortunate in having a Government which not only advocates but also actively encourages the essential role of private enterprise in all spheres of activity.

4.7 Availability of Staff

Although Hong Kong is generally blessed with near full employment most of the time, the work force is extremely fluid right up to the highest levels. Consequently, a supply of properly qualified staff is always available, although locating them can sometimes prove more difficult. Shortages of labour can occur from time to time in certain sectors.

Our Executive Search and Recruitment Division would be pleased to assist with the recruitment or search assignments, or advise on executive remuneration packages.

4.8 Communications

Excellent communication facilities of all types exist both internally and externally. In general, it is possible to have all forms of electronic communications and international telephone services rapidly connected. Telecommunications facilities are reckoned to be among the best in the world; there is a wide choice of Internet Service Providers (ISP), and rates are highly competitive. Hong Kong's port and airport facilities are of international standard and serve all major carriers. The vast new Chep Lap Kok airport opened in 1998. Hong Kong is on the international route network of most major airlines and acts as an Asian interchange point for many of them. The container port is one of the largest and most efficient in the world. Public transport facilities within Hong Kong are of high quality, readily available, and are relatively inexpensive by international standards.

4.9 Availability of Office Space

Prime property in the central business/financial district can generally be secured quite quickly at rental levels commensurate with facilities and location. Hong Kong has a constant ample supply of office space, which helps to maintain rental costs at reasonable levels. The main commercial areas are Central District and Admiralty. More recently erected buildings usually provide good facilities including those that cater for the increasing "IT" needs.

4.10 Availability of Accommodation

Private accommodation can easily be secured on either a short or long term lease basis and varying in both size and level of luxury according to the desires of the occupant or corporate policy. Again, rental levels are rarely cheap, but they vary enormously depending upon location and reasonably priced accommodation is always available.

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5. *Trade, Monetary and Financial System*

5.1 Trade

For many years Hong Kong relied on its excellent harbour and proximity to China. Although there was some local manufacturing the mainstay of Hong Kong's business was acting as a conduit for goods flowing in and out of China. In the 1950's many factors combined to cause a fundamental change. Based on its free port laissez-faire business atmosphere and entrepreneurial skills, Hong Kong changed into a large manufacturing centre. Utilising its large and relatively cheap work force Hong Kong initially specialised in labour-intensive industries such as textiles and plastics. Since then, the emphasis has changed towards high quality, high value manufacturing, with most of the actual production process being carried out in southern China, but with the 'value-added' element executed in Hong Kong. It is said that the 'brains' of many enterprises - the head office, design, sales and financial functions are still located in Hong Kong, while the 'brawn', the manufacturing itself, is done north of the border. Nowadays the service industries, especially financial services, are both Hong Kong's largest revenue earners and its major employer.

5.2 Monetary System

The local currency is the Hong Kong dollar which has been linked to the US Dollar and fixed at the rate HK\$7.8 to one US Dollar since 1983. Otherwise the currency floats freely on the international money markets. The Hong Kong dollar is the universally accepted unofficial currency in the Special Economic Zone of Shenzhen, across the border from Hong Kong, and in the nearby former Portuguese enclave of Macau.

5.3 Exchange Control

No form of exchange control exists; nor does any requirement of reporting or obtaining approval for international transactions. As a result, capital and profit can be freely remitted in and out of Hong Kong.

5.4 Banking System

Hong Kong has a three-tier system for financial institutions. They are divided into licensed banks, licensed deposit taking companies and registered deposit taking companies. Of the world's 100 largest banks some 80% operate in the SAR. There are 214 banks and 92 representative offices operating in Hong Kong. At the end of October 2003, total loans to financial international trade amounted to US\$12.6 billions, and other loans for use outside Hong Kong totaled US\$27 billion. Financial services are of a high level and all the sophisticated banking services are available that one may expect in an environment that claims to be the world's third major financial centre. Statutory requirements are laid down in the Banking Ordinance whilst the Monetary Authority ("HKMA") is entrusted with the supervision of the industry.

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6. *Legal System*

The legal system of Hong Kong remains based upon that of England and Wales. Legislation is by locally enacted Ordinance and, in practice, especially as the law applies to ordinary citizens or business people from overseas, little has changed since 1 July 1997. The local Court of Final Appeal has replaced the role previously exercised by the Privy Council in Britain. Courts in the People's Republic of China have no authority within the SAR and there are no plans to bring Hong Kong's legal system or its laws into line with those operating on the mainland. The fundamental principles upon which the law operates are to remain because they have been incorporated into the Basic Law of the Hong Kong Special Administrative Region and are thus protected. All sections of Hong Kong society, including government, business, the entire political spectrum and trade unions have expressed support for continuing the present system as all agree it is an essential ingredient for Hong Kong's continued prosperity.



7. *Hong Kong Tax Structure*

As a general rule, taxation is only levied on income or transactions having a direct connection with Hong Kong. The concepts of residence, domicile or citizenship have little, if any, relevance. Taxation is based on the 'territorial' concept.

Direct Taxation

There are three distinct taxes designed to tax income derived from Hong Kong:

- Profits Tax (See Section 7.1)
- Salaries Tax (See Section 7.2)
- Property Tax (See Section 7.3)

There is no taxation of capital gains on transfer or on gifts, save where they fall within the limited gift provisions relating to Estate Duty (See Section 7.5) which is a death duty charged upon the net value of the Hong Kong assets of the deceased.

Indirect Taxation

There are a few indirect taxes and a Stamp Duty (See Section 7.6.1) on transfers of shares in Hong Kong companies and of interests in land and buildings located in Hong Kong.

Tax Treaties

Hong Kong has signed the only Double Tax Treaty with Belgium to eliminate double taxation instances encountered by Hong Kong and Belgium investors through the allocation of taxing rights and the provision of tax relief. In addition, Hong Kong has reached an understanding with the PRC Government to prevent double taxation of airline, shipping and other business income in the SAR and PRC. The Government has recently raised the possibility of negotiating double tax treaties with major trading partners at some future date. However, the existing position greatly assists in maintaining confidentiality in the ownership and use of a Hong Kong company. Many countries give unilateral relief for Hong Kong taxation paid when instances of double taxation arise.

7.1 Profits Tax

Profits Tax is levied at the rate of 17.5% on corporations, and 16% on unincorporated entities on business profits which satisfy both of the following criteria:

- The company must be carrying on business in Hong Kong.
- The relevant profits must be earned in or derived from Hong Kong.

7.1.1 Source

The source of income is generally regarded as a “practical hard matter of fact”. In the context of international operations, this typically means that the person ultimately deriving the income may have some tax planning opportunities. Rates of Hong Kong taxation are low and with care effective rates can be made even lower. Hong Kong does not have any form of dividend taxation or withholding taxes and hence profits accumulated in a Hong Kong company can be distributed without tax deduction in Hong Kong.

7.1.2 Deemed Income

Certain types of incomes are deemed taxable. These are mainly rents or royalties received in connection with the use of equipment, patents, and copyrights etc. in Hong Kong. Due to the method by which expenses are allowed, the effective rate of tax for royalties, copyright fees etc., can be lower than the normal rate.

7.1.3 Withholding Taxes

There are withholding taxes on royalties paid to non-residents. The payer is required to withhold tax on the royalty payment as agent for the non-resident recipient.

7.1.4 Interest

Deposit interest accruing to individuals and Hong Kong companies, from deposits placed in Hong Kong, is exempt from Profits Tax unless the bank deposits secure a borrowing. Deposit interest accruing to Hong Kong companies from deposits placed in offshore accounts is exempt from Profits Tax. It is extremely easy for Hong Kong companies to place deposits in offshore accounts.

7.1.5 Tax Returns

Any company potentially liable to Profits Tax will be issued with a tax return for completion at the end of each tax year. This should be submitted within one month of issue (although in practice longer periods may be granted upon application) together with audited financial statements covering the company's accounting year ending in the relevant tax year.

This return forms the basis for a final tax assessment on respect of the relevant tax year payable for the current years. For example, a company with a 31 December year-end would report its results for that year-end in its return for the tax year ending the following 31 March.

7.1.6 Anti-Avoidance Measures

If a transaction is entered into for the 'sole or dominant purpose' of enabling a tax benefit to be conferred, the Inland Revenue Department has the power to assess tax liabilities as if the transaction had not taken place, or otherwise counteract the tax benefit.

Provided care and advice are taken, there is no reason for these measures to significantly affect Hong Kong's appeal as a low or zero tax jurisdiction.

Our Tax Department would be pleased to advise clients about the Hong Kong and international taxation consequences of proposed transactions.

7.2 Salaries Tax

Although many salary and wage earners pay no tax due to levels of income below the threshold, employment income with a Hong Kong source is strictly subject to Salaries Tax. In most circumstances where tax is payable a flat rate of tax at (2004/05: 16%) applies, but in the case of annual income levels below US\$98,718 (for a single person) or US\$162,820 (for a married couple) lower effective rates can apply. These lower rates are applicable irrespective of whether or not the salary earner is a resident of Hong Kong.

7.2.1 Source of Income

Salaries Tax is charged on the basis of the principle of the "fundamental source of employment" being in Hong Kong. The Inland Revenue Ordinance does not give clear guidance

as to whether the fundamental source of a person's employment is in Hong Kong and it is necessary to rely on case law and Inland Revenue Department interpretations. The basic principle is that if a person's fundamental employment is in Hong Kong, his or her income is assessable in full to Salaries Tax unless all the services of the employment are rendered outside Hong Kong. The criteria to determine whether the fundamental source exists in Hong Kong includes: whether the employment contract was negotiated, concluded and is enforceable in Hong Kong; whether the employer is resident in Hong Kong; and where the remuneration is paid. A concession exists to exempt income derived from services rendered outside Hong Kong if a tax similar to Salaries Tax has been paid on the income. This exemption is principally to reduce the double taxation of those employees who are subject to China's Individual Income Tax, but has wider applications.

Separate rules apply to directors of Hong Kong companies, as their remuneration as directors is fully taxable in Hong Kong regardless of other factors, because it is considered that the office of director exists in Hong Kong.

If it can be established that the fundamental source of employment is outside Hong Kong, the employee is exempt from Salaries Tax provided he does not spend more than 60 days in Hong Kong in any tax year.

If you are in doubt as to whether you or your employees are or will be subject to Salaries Tax, our Tax Department would be pleased to advise.

7.2.2 Exemptions

Although Salaries Tax is levied irrespective of whether the salary earner is a Hong Kong resident, as long as an employee whose source of employment is outside Hong Kong and who spends less than 60 days in Hong Kong during a given tax year, he will be exempted from Salaries Tax on his income. This exemption does not apply to directors' fees however.

In addition, an employee who has a Hong Kong source employment and earns salary income for rendering services in places outside Hong Kong is exempt from Salaries Tax if he has paid tax in those places from which the income was derived.

Special rules apply to seamen and aircrew.

The Mandatory Provident Fund scheme (MPF) was implemented in 2000 with the aim of providing retirement benefits for the work force, and is calculated at 5% of an employee's income (capped at HK\$20,000). However, other than MPF, no other costs such as Social Security, National Insurance, etc. arise either to the employee or the employer. A tax deduction of up to HK\$12,000 per year will be available in respect of employees' contributions to MPF.

7.2.3 Benefits in Kind

Generous tax treatment of company supplied housing and other "benefits in kind" makes Hong Kong a competitive location for senior executives of international groups responsible for the Asian region. For example, the provision of accommodation, a company car, domestic furniture etc.

should, under suitable arrangements, attract no tax to the employee (whilst the cost should be fully deductible to his employer). Housing provided to an employee is taxed by way of increasing his taxable income by 10 percent. Only in exceptional circumstances does this have any direct relationship to the actual cost of the housing to the employer; the actual cost is usually significantly higher.

If you or your employees are in doubt as to the best way to structure possible benefits packages, our Tax Department would be pleased to advise.

7.3 Property Tax

This is charged on rents derived from land and buildings located in Hong Kong. Companies are exempt from the tax, being liable to pay Profits Tax on any such income.

7.4 Other Taxes

Rates on land and buildings are levied to support local services and infrastructure. Entertainment tax is levied on certain forms of entertainment e.g. cinema tickets. Hotel accommodation tax is levied on hotel bills. Airport departure tax is payable on departing through the International airport and a similar tax is payable on departing Macau. There are tolls payable on use of the cross-harbour tunnels. There are also duties charged on wines and spirits, tobacco, soft drinks and hydrocarbon oil.

7.5 Estate Duty

Estate Duty is based upon the legislation which existed in England prior to the introduction there of Capital Transfer Tax (now Inheritance Tax) and in most Australian States prior to abolition. Like all Hong Kong tax, the scope is limited by territoriality and consequently the charge is levied upon the net value of only the Hong Kong property of a deceased person, regardless of the residence or domicile of the deceased's estate. However there are complicated provisions, beyond the scope of this booklet, which can bring into charge the Hong Kong property of foreign corporations if the corporations were "controlled" by the deceased. In arriving at the net values of the estate, only Hong Kong liabilities are allowed as deductions from assets. At present no duty is charged on estates with a net value below HK\$7.5 million and above HK\$10.5 million, is 15%. Between the two amounts progressive rates apply starting at 5%.

Whilst good planning will usually reduce estate duty to nil, or an insignificant amount, many people fail to plan and incur unnecessary liabilities.

As announced in the 2005/2006 Budget Proposal, Estate Duty will be abolished as part of the measures to strengthen Hong Kong as an international financial centre.

If you need Estate Duty planning advice our Tax Department would be pleased to help.

7.6 Stamp and Capital Duty

7.6.1 Stamp Duty

Principally only two types of transactions are subject to Stamp Duty.

The transfer of shares in a Hong Kong company (whether private or publicly quoted) must be stamped. The rate of duty is 0.1% payable by each of the purchaser and seller involved in a transaction, giving an effective rate of 0.2%. Duty is charged on the sales consideration or the fair market value, whichever is the higher. In evaluating the fair market value, the Stamp Duty Office will normally accept the net asset value shown by the company's audited accounts, subject to an upward adjustment to reflect a higher value for land and buildings than that shown in the accounts, where appropriate. No Stamp Duty is charged in the case of transfers of shares within a group of companies, where both parties are under 90% common ownership.

Duty at the maximum rate of 3.75% is payable on the transfer of land and buildings located in Hong Kong and on agreements for sale. In order to dampen land speculation the government introduced Stamp Duty chargeable on agreements to purchase property. However, as a relief to a buyer of residential property, payment of Stamp Duty may be deferred until the assignment is executed according to the agreement on the date of re-sale of the property. The maximum period of deferral is three years after the execution of the agreement.

It is therefore advisable to take advice before committing to a transaction.

Stamp duty is also chargeable in relation to leases of immovable property, to units in unit trusts and to Hong Kong bearer instruments as well as duplicated of any chargeable instrument.

7.6.2 Capital Duty

A Capital Duty 0.1% must be paid on the nominal value of and on any increase in authorised share capital of Hong Kong companies and on the issue of shares at a premium. The capital duty is capped at HK\$30,000 in each case.



8. *Setting up Companies in Hong Kong*

8.1 Types of Business Organisations

Although the U.K. is no longer the sovereign power all the forms of business organisations found in systems based on English Law are available in Hong Kong, i.e.:-

- Hong Kong Companies (See Section 8.3)
- Branch operations of non-Hong Kong Companies (See Section 8.4)
- Sole Proprietorships (See Section 8.5)
- Partnerships (including Limited Partnerships) (See Section 8.6)

These are discussed in the following pages below.

8.2 Business Registration

Any person carrying on business in Hong Kong is required to obtain a Business Registration Certificate from the Inland Revenue Department. This is the primary source of information to the taxing authority in respect of new businesses.

8.3 Hong Kong Companies

Although it is quite possible to carry on business in Hong Kong via a branch of a non-Hong Kong company, it is normal for a business based in Hong Kong to be carried on by a company incorporated in Hong Kong. Reasons for this will vary, depending on the precise facts but would typically include:

- Greater convenience.
- High degree of flexibility associated with Hong Kong companies.
- Wider acceptance both in Hong Kong and in most "home" jurisdictions.
- Economic costs.

A Hong Kong company requires a minimum of one director, one shareholder, a company secretary and a registered office. The director(s) and shareholder(s) can be a corporation or an individual of any nationality while the company secretary must be a Hong Kong resident and the registered office must be in Hong Kong.

A Hong Kong company is required to prepare audited financial statements and submit it with a profits tax return with the Inland Revenue Department on an annual basis. The audited financial statements should also be presented in an annual general meeting for adoption by shareholders.

8.4 Branch Operations (Non-Hong Kong Companies)

In line with the laissez-faire business atmosphere in Hong Kong, no restrictions apply to the carrying on of a business through a company incorporated outside Hong Kong. All that is required is that the Hong Kong branch registers within one month of establishing a place of business in Hong Kong.

Under the Companies Ordinance, an overseas company must register by filing the following documents with the Companies Registry:

- A certified true copy, plus English translation where appropriate, of the company's constitution i.e., the company's Charter, Memorandum and Articles etc. and Certificate of Incorporation.
- Details of company officers, e.g. directors, secretary.
- The name and address of at least one individual, residing in Hong Kong, who is authorised to accept documents, notices, etc. served on the company and the company's authorisation in his favour (e.g. a power of attorney).

- For most companies, financial statements also must be filed with the Registrar upon registration and annually thereafter. These should be certified by a director of the company but need not be audited if this is not required by law in the place of the incorporation.

Any changes to the particulars filed and any commencement of proceedings for liquidation must also be notified to the Registrar.

When such an overseas company ceases to have a place of business in Hong Kong, it must notify the Registrar and for the next three years, continue to have an authorised person in Hong Kong to accept service of documents on its behalf.

Place of business in Hong Kong for the purposes of registration is defined so as to exclude "place not used by the company to transact any business which creates legal obligations". Consequently certain representative offices do not need to register as above.

Our Corporate Services Department ("BMS") would be pleased to advise and assist overseas companies in registering a Hong Kong company and/or a branch.

8.5 Sole Proprietorships

It is open for any individual to engage in business in his own right. Apart from the need to satisfy certain qualification requirements in certain professions the main legal matter is the need to register the business name and obtain a Business Registration Certificate.

8.6 Partnerships

Partnerships are governed by the Partnership Ordinance and the Limited Partnership Ordinance both based upon the equivalent English Acts. Each type can have up to 20 partners, corporate or individual. Partnership assets are owned jointly by the partners who are also jointly and severally liable for partnership liabilities. If a Limited Partnership is formed the liability of some partners can be limited as long as they do not take part in the active management of the partnership.

8.7 Trusts

The trust is based on the concept of English law that property can be legally owned by one person but for the benefit of another person. Typically this takes the form of assets, such as shares in a company, being owned by a "trustee" in "trust" for the ultimate equitable owner, the "beneficiary". Full legal ownership is vested in the person holding the property ("the trustee") and he is therefore able to deal with it as if he owned it personally; however his actual ownership is limited in equity to holding and dealing with the property for the benefit of the beneficiary under the trust.

Although it is possible for trading operations to be carried out using a trust, in practice, such "trading trusts" are not common in Hong Kong. Trusts are mainly used in Hong Kong for the following purposes:

- Offshore tax planning
- Estate and emigration planning
- Indirect ownership of companies
- Asset protection
- Anonymity in investment
- Long-term family provision
- Continuity of ownership

Our Tax Department is able to advise on all matters relating to the establishment of a Trust in Hong Kong or overseas and is able to offer corporate trustees to administer the Trust.

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9. Typical Uses for Companies Based in Hong Kong

9.1 International Trading Companies

Acting as an intermediary in the sourcing of goods purchased by an international group or in the sale of a product. Typically the supplier or customer would be in the Asian region but this is not essential.

The extent to which such a company will be liable to Hong Kong taxation will depend on the factors of “source” and “carrying on business in Hong Kong” discussed earlier in Section 7.1. In this regard, the locations where the purchases and sales contracts were effected are the major criteria in determining the source of profits for international trading companies based in Hong Kong.

There may be considerable advantages in the “home” country for the profits to be taxed in the Hong Kong company which in turn either distributes by way of dividend or reinvestment.

In a similar context to companies buying and selling goods, it is common for Hong Kong companies to receive commissions either in connection with the sale of goods or by acting as a buying agent. Again, there may be considerable tax benefits to be gained by the payment of such commissions to the Hong Kong company.

9.2 Investment Holding Companies

Either because a company has accumulated its own profits from past transactions or because the owners of a company have injected funds into the company, it is not uncommon for Hong Kong companies to have substantial investment funds. These funds can be freely invested in Hong Kong or elsewhere. In line with the overall flexibility of the Hong Kong taxation system, most forms of the resultant investment income will suffer only the relatively low rates of Hong Kong taxation, if they are taxable at all; reference should be made to Section 7.1.2 on deemed income for Profits Tax purposes in this regard.

9.3 Specialist Uses

A Hong Kong company is also often used to ultimately hold overseas assets, perhaps in conjunction with trust arrangements. Other more specialised uses of Hong Kong companies are frequently encountered. For example, the tax system coupled with the absence of any foreign exchange control and Hong Kong's prominence as a financial centre make it an ideal location for intermediary companies in complex international financing arrangements, particularly for China ventures.

9.4 Hong Kong Companies for Doing Business in China

Hong Kong is an ideal base for many overseas companies seeking to do business in China - be it buying or selling - because Hong Kong's commercial foundations are based upon a clearly defined rule of law that closely resembles the UK-system. There are very few restrictions on setting up a company in Hong Kong; taxation rates are extremely low; the system operates in a totally transparent manner, and foreigners are on an equal footing with local people in all respects.

Added to which Hong Kong professional firms adhere to recognised international standards, and English is in common use both formally and informally.

Which is why many overseas firms chose to locate initially in Hong Kong, and set up on the mainland only after they have gained more practical experience.

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10. Listing on the Stock Exchange of Hong Kong

Hong Kong is generally recognised as being the 'third leg', together with New York and London, that keep the global financial markets operating round the clock.

Although, in Asia, the Tokyo market is bigger in terms of capitalisation, Hong Kong remains predominant in terms of international business. Hong Kong is also welcoming PRC and foreign firms seeking to list on the local bourse. At March 2005 there were 1,096 companies listed on the stock exchange, including about 200 Chinese mainland enterprises, either as H-shares or 'red chips' companies. Capitalisation stood at US\$843 billion.

10.1 Main Board and GEM

Both the Main Board and the Growth Enterprise Market (GEM) Board are available to both local and overseas companies, as well as to those from the Chinese mainland (H-shares). Broadly, GEM is for smaller or newer companies, especially in emerging sectors, but are able to demonstrate good growth potential.

10.2 Main Board Entry Requirements

As one would expect from a major international bourse companies seeking to list on the Main Board need to satisfy quite rigorous standards showing established track record and growth. The main requirements being: i) a three year business track record with a minimum of HK\$30 million profit in the first and second year, and a minimum of HK\$20 million profit in the third year: ii) a minimum expected market capitalisation of HK\$200 million and the market capitalisation of securities in public hands must be at least HK\$50 million or 25% of the enlarged capital and iii) a requirement to engage qualified professional advisers - such as accountants, lawyers, sponsors and underwriters, etc. to assist in the listing process. Main Board listed companies must comply with the 'six month' interim and annual financial reporting requirements.

10.3 GEM Entry Requirements

GEM was launched in late 1999 to meet a need similar to that of NASDAQ in the USA and AIM in the UK. Listing requirements are generally not as stringent as on the Main Board. The main criteria are: i) a two year active business track record, though not necessarily with profit; ii) an ability to demonstrate growth potential, and iii) a market capitalisation of no less than HK\$46 million with at least 25% in the public float. However, quarterly reporting is a requirement on GEM.

10.4 Listing Rules and Corporate Governance

Listing Rules relating to both the Main Board and GEM are constantly changing. The last major amendments were made during 2004 which have incorporated new issues related to corporate governance, initial listing criteria and continuing listing obligations. It is imperative that those intended to list their business and those already listed issuers keep abreast of all these changes.

Our Corporate Finance Department is experienced in preparing companies for Initial Public Offerings (IPO) on both the Main Board and GEM listed companies.



11. Macau-Offshore Business Centre

The sovereignty of Macau reverted back to China in late 1999. It has a status of Special Administrative Region (SAR) broadly similar to that of Hong Kong. Macau, like Hong Kong, is an entry port for the Mainland and is situated at the western tip of the Pearl River Delta which serves the hinterland that includes major cities like Zhuhai and Zhongzhan.

Macau as a Tax Haven

The recent Macau Offshore Companies (MOC) legislation enables Macau to function as one of the newest tax havens in Asia. The Macau MOC Law has been in effect since 1 November 1999. The offshore finance business is regulated and supervised by the Macao Monetary Authority, while the offshore non-finance business is regulated and supervised by the Macao Trade and Investment Promotion Institute ("IPIM").

An investor has to submit a proposal on the planned offshore services and obtain approval from IPIM. Upon receipt of IPIM's approval, a MOC can carry out offshore service business, including commercial and service agents and overseas selling activities. For profits that are derived from offshore activities, the MOC can enjoy full exemption of all taxes in Macau. In addition, the managers and specialised technicians of a MOC authorised to work and reside in the Macau SAR are exempt from Macau salaries tax for the first three years of their employment with the MOC. A MOC is not required to file tax returns in Macau, but is required to submit an audit report to IPIM.

A MOC has to abide by the following rules in order to be fully exempt from Macau taxes:-

- (i) the transactions are carried out in non-Macau currency;
- (ii) the customers are non-Macau residents; and
- (iii) the market focus is non-Macau.

There can be considerable advantages in utilising a MOC especially to Hong Kong firms in certain lines of business such as manufacturing business, sales agencies, call services and back-office activities. The primary benefits include lower costs and a potential for considerable tax savings for the parent company.

We have long operated in Macau and are presently responsible for auditing and financial seminars there. We can advise on the suitability and help set up your office in Macau as a tax haven.



GROUP SERVICES STRUCTURE

