

# HONG KONG TAX ALERT

ISSUE 12 | December 2019

## Hong Kong and Macau signed a comprehensive double taxation arrangement

### Summary

Hong Kong and Macau have recently signed a comprehensive avoidance of double taxation arrangement ("the Arrangement"), signifying enhanced tax co-operation between Hong Kong and Macau.

The Arrangement provides residents in Hong Kong and Macau more flexibility and greater tax certainty.

On 25 November 2019, Hong Kong signed a comprehensive double taxation arrangement ("Arrangement") with Macau ([click here](#)). The Arrangement will come into force upon completion of the formal ratification procedures by both sides.

### Permanent establishment ("PE") article

Prior to the Arrangement, a Hong Kong resident is subject to tax in Macau if it carries out business activities in Macau, even though the relevant activities may be limited (e.g., Hong Kong employees travelling to Macau to perform certain services for a short period of time). With the arrangement in place, a Hong Kong tax resident will not be subject to tax in Macau if its activities in Macau do not constitute a PE as defined in the Arrangement.

In addition to the standard definition of PE, the Arrangement also adopts the definition of dependent agent PE under the OECD BEPS Action 7. In simple terms, notwithstanding the absence of a fixed place of business, a Hong Kong enterprise could be regarded as having a PE in Macau if a Macau resident habitually concludes contracts in the name of the Hong Kong enterprise, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the Hong Kong enterprise. The Arrangement follows the latest standard of international tax rules to prevent the artificial avoidance of a PE.

### Business income article

Prior to the Arrangement, income earned by Macau residents in Hong Kong is subject to both Hong Kong and Macau income tax. Under the Arrangement, double taxation could be avoided by way of exempting the income taxed in Hong Kong from Macau tax, or by crediting the Hong Kong tax paid against the Macau tax payable in respect of the same income. The Arrangement also provides for a credit against the Hong Kong tax payable for any Macau tax paid.

### Capital gains article

Under the Arrangement, gains derived from the alienation of shares in a company, or comparable interest in other entities such as partnership and trusts, in which more than 50% of the assets comprised immovable property situated in one side at any time within the 365 days before the alienation of shares may be taxed in that side.

Under the current local tax laws of Hong Kong and Macau, both jurisdictions generally do not tax gains on disposal of shares in a company incorporated in their respective jurisdictions or companies holding immovable property situated in their respective jurisdictions, provided that the relevant shareholder does not carry out any business activities in their respective jurisdictions. This article may therefore have limited application.

### Employment income article

Short-term secondees and business travelers can now visit Macau for up to 183 days in any 12-month period, provided their costs are not borne by the employer's PE or fixed base in Macau. Further, a qualified teacher or researcher,

- i. who is employed by the qualified education or research institution in one side; and
- ii. engages in teaching or research activities for qualified education or research institution on the other side;

is exempt from tax on that other side in respect of the remuneration derived from the above activities for a period of three years. This is subject to the proviso that the relevant remuneration has been subjected to tax on the side where the person concerned is employed.

### Passive income withholding tax

The Hong Kong withholding tax on royalties is, under the Arrangement, reduced from the normal 4.95% in most cases to 3%.

Under the Arrangement, withholding tax on dividend and interest is reduced to 5%. However, given that Hong Kong and Macau currently do not levy withholding tax on dividend and interest, the reduced withholding tax rate should not be generally relevant.

### KPMG observations

The Arrangement offers additional incentives for the business sector of both sides to do business, invest, encourage exchange of talent and promote economic growth of the Guangdong-Hong Kong-Macau Greater Bay Area.

For more information and assistance, please contact your usual tax advisor or one of our tax advisors below.

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