



HONG KONG TAX ALERT

March 2022 | Issue 2

The updated EU grey list - Bermuda and BVI are added to the list whereas Hong Kong will change its tax law to be delisted

Summary

In its latest round of review of the list of non-cooperative jurisdictions for tax purposes, the European Union (EU) decided to add, among other jurisdictions, Bermuda and the British Virgin Islands (BVI) to the grey list.

The Hong Kong SAR (Hong Kong) remains on the grey list. It will need to effect certain changes to its offshore regime in respect of passive income from 1 January 2023 in order to be removed from the grey list.

Businesses in Hong Kong should stay tuned of the tax law changes to be proposed by the HKSAR Government and be prepared to assess any potential impact of the proposed changes on their Hong Kong profits tax exposure.

On 24 February 2022, the EU announced the conclusion on the latest round of review of its list of non-cooperative jurisdictions for tax purposes¹. The EU decided to add, among other jurisdictions, Bermuda and the BVI to the grey list (i.e. Annex II of its list of non-cooperative jurisdictions for tax purposes). Hong Kong remains on the grey list². No jurisdictions were added to or removed from the blacklist (i.e. Annex I of its list of non-cooperative jurisdictions for tax purposes).

The updated grey list now contains 25 jurisdictions whereas the blacklist continues to include 9 jurisdictions³.

Based on the EU Code of Conduct Group report dated 2 February 2022⁴, Bermuda has been added to the grey list because it has yet to address the issues identified by the OECD Forum on Harmful Tax Practices (FHTP) with respect to the implementation of the economic substance regime. The BVI has been added to the grey list because it has yet to implement a recommendation made by the OECD Inclusive Framework on BEPS (IF) in relation to the implementation of the minimum standard for country-by-country reporting (CbCR) under Action 13 of the BEPS Action Plan. Both jurisdictions have made a high-level commitment to implement the recommendations of the EU and/or the OECD.

1 The EU's press release issued on 24 February 2022 can be accessed via this link: <https://www.consilium.europa.eu/en/press/pressreleases/2022/02/24/taxation-council-reviews-list-of-non-cooperative-countries-for-tax-purposes/>

2 For more details, please refer to our Hong Kong Tax Alert issued in September 2021 via this link: <https://home.kpmg/cn/en/home/insights/2021/09/tax-alert-10-hk-the-eu-has-decided-to-put-hong-kong-on-its-grey-list-for-tax-purposes.html>

3 For a complete list of listed jurisdictions, please refer to the EU's website via this link: [Taxation: EU list of non-cooperative jurisdictions - Consilium \(europa.eu\)](https://www.consilium.europa.eu/en/press/pressreleases/2022/02/24/taxation-council-reviews-list-of-non-cooperative-countries-for-tax-purposes/)

4 The EU Code of Conduct Group report dated 2 February 2022 can be accessed via this link: <https://data.consilium.europa.eu/doc/document/ST-5723-2022-IN/IT/en/pdf>

In addition, Thailand and Vietnam are also on the grey list as they have yet to implement the IF's recommendations on implementing the CbCR minimum standard and activate the CbCR exchange relationships with all EU Member States.

The next round of update of the EU tax lists is scheduled in October 2022.

KPMG observations

The EU will continue to monitor the progress of the grey-listed jurisdictions in implementing the recommendations of the EU and/or the OECD, and consider any necessary updates in the next round of review of the EU tax lists in October 2022. Businesses in Hong Kong with operations in or transactions with Bermuda or the BVI should closely monitor the future developments in this space and be prepared to assess the potential impact of any forthcoming changes to the tax regimes in these jurisdictions on their businesses.

As far as Hong Kong is concerned, the HKSAR Government has committed to amending the tax law to address the EU's concerns about the offshore regime in respect of passive income in Hong Kong. While the exact changes to the Hong Kong tax system required for Hong Kong to get off from the grey list are yet to be confirmed, the deadline of making such changes remains to be the end of 2022.

In its press release issued on 5 October 2021, the HKSAR Government has made it clear that Hong Kong will maintain the territorial source principle of taxation. In addition, the tax law changes will only target corporations involved in cross-border tax evasion, particularly those with no substantial economic activity in Hong Kong.

Some possible changes to the Hong Kong tax system to be effective from 1 January 2023 are: (1) taxation of offshore passive income remitted into Hong Kong, (2) introduction of a substance requirement and/or subject-to-tax condition for exempting offshore passive income remitted back to Hong Kong and (3) introduction of a participation exemption for dividends and gains from disposal of equity interest. If offshore passive income may be subject to tax in Hong Kong under certain circumstances in the future, consideration should also be given to whether Hong Kong should introduce a mechanism for unilateral tax credit in the absence of a tax treaty to provide relief for double taxation.

We will keep monitoring any future developments in this area and provide further update when more details become available.

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