

# Hong Kong Tax Alert

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## “Commissioner’s Opinion” as an interim measure to confirm compliance with the economic substance requirements under the revised FSIE regime

### Summary



The Inland Revenue Department (IRD) will introduce a mechanism that allows taxpayers to seek an opinion from the Commissioner of Inland Revenue (CIR) on their compliance with the economic substance (ES) requirements under the revised foreign-sourced income exemption (FSIE) regime. This serves as an interim measure during the period between the draft tax legislation on the regime is gazetted and before the legislation becomes effective, with an aim to provide greater tax certainty to taxpayers.

As a response to the European Union’s concerns about Hong Kong’s existing offshore regime for passive income, the HKSAR Government will introduce a revised FSIE regime effective from 1 January 2023. The relevant tax bill is expected to be gazetted in late October or early November of 2022 and has to be enacted into law by the end of 2022.

To help businesses in Hong Kong better prepare for the changes brought by the revised FSIE regime before it becomes effective, the IRD is going to introduce an interim arrangement under which taxpayers can seek the CIR’s opinion (Commissioner’s Opinion) on whether they are in compliance with the ES requirements under the FSIE regime according to the draft legislation once the tax bill is gazetted.

### The key features of the “Commissioner’s Opinion” mechanism

The key features of the “Commissioner’s Opinion” mechanism are set out as follows:

1. The IRD would request certain information from the taxpayer to process the application, such as (1) the details of specified economic activities carried out in Hong Kong, (2) the number of qualified employees, (3) the amount of operating expenditures incurred, (4) the amounts of turnover and profits and (5) the details of any outsourcing arrangements.
2. The CIR will give an opinion on the taxpayer’s compliance with the ES requirements based on the draft legislation in the tax bill and the information provided, normally within one month after the application and complete information are received.
3. The Commissioner’s Opinion is not an advance ruling made under Section 88A of the Inland Revenue Ordinance. The CIR will, however, apply the enacted ES requirements according to the Commissioner’s Opinion provided that the arrangements and parameters stated in the opinion are adhered to and the enacted ES requirements are substantially the same as those proposed in the tax bill. The taxpayer can rely on the opinion to report on its compliance with the enacted ES requirements in its tax return.

4. The application can be made to the IRD during the period between the gazettal of the tax bill and the coming into operation of the corresponding ordinance. After the ordinance comes into operation, the interim arrangement will no longer be available and taxpayers can apply for an advance ruling on their compliance with the enacted ES requirements if necessary.
5. The application procedures and the detailed information required will be announced on the IRD's website when the tax bill of the revised FSIE regime is gazetted.
6. Taxpayers can contact the IRD at 2594 1600 for any questions about this new interim mechanism.

### **KPMG observations**

We applaud the introduction of the above interim measure for the revised FSIE regime, which is a novel and unprecedented mechanism offered by the HKSAR Government for providing greater tax certainty to taxpayers. The interim measure illustrates the HKSAR Government's commitment to promoting tax certainty in Hong Kong and facilitating businesses in Hong Kong to cope with the revised FSIE regime.

MNE groups in Hong Kong currently relying on an offshore claim for non-taxation of offshore passive income should make good use of this interim measure if they are seeking certainty on their compliance with the ES requirements under the FSIE regime. Before submitting an application, these groups should perform a self-assessment on their current level of ES in Hong Kong and consider whether any changes to their holding structures or operating models are necessary to minimise the chance of getting an adverse opinion from the CIR. They should also consider how to best present the information requested in their applications to the IRD.

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