



HONG KONG TAX ALERT

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The European Union has decided to put Hong Kong on its “grey list” for tax purposes



Summary

Effective from 5 October 2021, Hong Kong will be added to the European Union's “grey list” on non-cooperative jurisdictions for tax purposes

Changes to Hong Kong's territorial system of taxation will be one of the most significant changes to Hong Kong Profits Tax which will have a significant impact to the tax profiles of many companies.

Following a review of Foreign-Source Income Exemption Regimes, the European Union has decided to add Hong Kong to Annex II of its list on non-cooperative jurisdictions for tax purposes effective 5 October 2021. This means that the European Union considers aspects of Hong Kong's territorial tax system may facilitate tax avoidance or other tax practices they regard as harmful. It also means that Hong Kong has agreed to make changes to the relevant legislation. The European Union has granted the affected jurisdictions until 31 December 2022 to make the necessary changes.

Annex II is effectively a watchlist. It means that the European Union will further monitor the situation and consider moving Hong Kong to a blacklist if the identified harmful aspect of its tax system does not change. Punitive measures against blacklisted jurisdictions include denial of deduction of payments made, increased withholding taxes, application of controlled foreign company rules, taxation of dividends and administrative measures.

Changes to the territorial system in Hong Kong will be one of the most significant changes to Hong Kong Profits Tax for many years and will have a fundamental impact on the tax profiles of many companies operating. While Hong Kong is still considering how to effect the changes, businesses should keep abreast of developments and work with their tax advisors to understand the implications.

Contact us



Lewis Y. Lu
Head of Tax, China
Tel: +86 21 2212 3421
lewis.lu@kpmg.com



John Timpany
Head of Tax, Hong Kong
Tel: +852 2143 8790
john.timpany@kpmg.com



Ivor Morris
Partner, Hong Kong
Tel: +852 2847 5092
ivor.morris@kpmg.com



Anita Tsang
Director, Hong Kong
Tel: +852 2143 8540
anita.tsang@kpmg.com



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