

Hong Kong Tax Alert

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2018/19 profits tax filing season will commence soon

On 1 April 2019, the Inland Revenue Department (IRD) will issue bulk profits tax returns to taxpayers for the year of assessment 2018/19. This tax alert draws your attention to the filing due dates for the 2018/19 profits tax returns and the requirement to notify the IRD of chargeability.

In addition, we would also like to draw your attention that many taxpayers are also required to disclose additional detailed information by way of supplementary forms to be filed together with their 2018/19 profits tax returns. The requirement to provide this additional information is for the purpose of determining a taxpayer's eligibility for preferential tax benefits offered and to ensure their compliance with the transfer pricing regime of Hong Kong.

Furthermore, when filing the 2018/19 returns, you may need to consider whether the returns should be prepared on a mark-to-market or realization basis.

Should you have any questions regarding the filing of your tax returns and the supplementary forms, or the filing bases to be adopted, please contact your tax executives.

2018/19 tax filing deadlines

The tax filing season for the fiscal year ending 31 March 2019 (i.e., year of assessment 2018/19) will commence with the IRD's bulk issuance of the relevant profits tax returns (i.e., Form BIR 51 or Form BIR 52) on 1 April 2019. As a matter of practice, the IRD issues returns in bulk annually in early April to corporations or partnerships that are likely to be chargeable to tax or meet certain conditions.

Returns are normally due for filing within one month of their date of issue. However, the IRD has for many years operated a block extension scheme whereby the filing deadline can be extended in instances where a taxpayer is professionally represented. Under the 2018/19 block extension scheme, the filing dates for the bulk returns issued on 1 April 2019 can be extended as follows:

For taxpayers with accounting dates falling between	Extended due date
1 April 2018 - 30 November 2018 (Accounting date code "N")	No extension, return due on the normal due date of 2 May 2019 (Thursday)
1 December 2018 - 31 December 2018 (Accounting date code "D")	15 August 2019 (Thursday)
1 January 2019 - 31 March 2019 - with taxable profits for the year (Accounting date code "M")	15 November 2019 (Friday)
1 January 2019 - 31 March 2019 - with tax losses for the year	31 January 2020 (Friday)

Notification of chargeability where no tax return has been issued

Taxpayers who are not issued with a tax return but nonetheless have profits chargeable to tax for any year of assessment (before the set-off of losses brought forward) are required to notify the IRD of their chargeability. The notification is required to be in writing, addressed to the Commissioner of Inland Revenue (CIR) and submitted within four months after the end of the basis period for the year of assessment concerned.

It should be noted that a taxpayer's basis period for a year of assessment depends on their accounting year-end date. As a result, the time limit for taxpayers to inform the IRD of chargeability will vary. For example, Company A (with an accounting year ended on 30 June 2018) and Company B (with an accounting year ended on 30 September 2018) were required to inform the IRD of their chargeability for the year of assessment 2018/19 on or before 31 October 2018 and 31 January 2019 respectively (i.e., within four months of their respective year-end dates).

Failure to inform the IRD of chargeability within the stipulated time frame, without reasonable excuse, will render a taxpayer liable to a fixed fine of up to HK\$10,000 and potentially a penalty of up to three times the tax involved for each offence.

However, there is no need for a taxpayer to inform the IRD of chargeability if the taxpayer has been filing tax returns annually and could reasonably expect that in the normal course of events the IRD would issue a return in the current year. Conversely, if a chargeable taxpayer has previously been advised by the IRD that a profits tax return will no longer be issued on an annual basis, or the taxpayer has recently commenced business, the CIR must be notified of chargeability within the stipulated period.

New supplementary forms S1 to S10

In addition to completing the 2018/19 profits tax return, Form BIR51 or Form BIR52, certain categories of taxpayers are required to provide the IRD with additional detailed information, by way of completing and filing certain supplementary forms, numbering from S1 to S10. This requirement will apply to taxpayers who fall within any of the following situation(s):

1. Have elected to be taxed under the two-tiered profits tax rates regime where, not belonging to a Hong Kong listed group, they had connected entities carrying on business in Hong Kong for the year;
2. Belong to an international group which has Country-by-Country (CbC) Report filing obligation in Hong Kong or elsewhere;
3. Have concluded an advance pricing arrangement with the IRD;
4. Have transactions with non-resident associated persons;
5. Have claimed deduction for R&D expenditure under section 16B of the Inland Revenue Ordinance (IRO);
6. Have claimed deduction for expenditure on energy efficient building installation under section 16I of the IRO;
7. Fall within the scope of the preferential tax regimes of Hong Kong listed below as:
 - a. a ship owner;
 - b. a professional reinsurer;
 - c. an authorized captive reinsurer;
 - d. a qualifying corporate treasury center;
 - e. a qualifying aircraft lessor;
 - f. a qualifying aircraft leasing manager.

These supplementary forms will not however be enclosed together with the hard-copy Form BIR 51 or Form BIR52 sent to taxpayers by the IRD.

Instead, whenever any of the supplementary forms S1 to S10 are applicable, taxpayers will have to go to the IRD's webpage¹ to access and complete the relevant supplementary form(s) electronically. After completing the relevant supplementary form(s) in their electronic format, taxpayers will then have to print, hand-sign and then file the relevant form(s) together with the Form BIR 51 or Form BIR 52, all in hard-copy format, with the IRD².

Clients may also refer to our Hong Kong Tax alert issued on 1 February 2019 (2019 Issue No. 3) for details of these supplementary forms.

Filing basis can be mark-to market or realization

Background

Many financial instruments are required to be accounted for on a mark-to-market fair value basis under Hong Kong Financial Reporting Standard No. 9 (HKFRS 9). Such a basis of accounting involves recognizing profits or losses in respect of financial instruments which is then regarded as unrealized or anticipated for tax purposes.

In November 2013, the Court of Final Appeal held in the case of *Nice Cheer*³ that such unrealized profits or losses should not be taxable or deductible. As such, taxpayers who prepare their accounts under HKFRS 9 will need to make tax adjustments to their accounts when they file their tax returns.

Despite the decision in *Nice Cheer*, many taxpayers have expressed a desire to file their tax returns on a fair value basis. In so doing, these taxpayers hope to avoid the trouble of tracking transactions on a realization basis for tax reporting purposes.

In response to requests made by such taxpayers, as an interim administrative measure, the IRD has since 2013/14 accepted tax returns in which taxpayers have chosen to file on a fair value basis.

To provide more clarity and certainty, a new law effective from the year of assessment 2018/19 has now been passed to codify the interim administrative measure into the IRO.

Election required under the new law - specific provisions for transition and exit arrangements

Tax assessment on a realization basis will be the default position for all taxpayers. Those who prepare financial statements in accordance with HKFRS 9, and wish to align the tax treatment with the accounting treatment, can make an election in writing pursuant to the new law.

Upon election, the alignment of the tax treatment with the accounting treatment will apply to the year of assessment for which the election is made and all subsequent years of assessment. In other words, subject to the amounts involved being Hong Kong sourced and are revenue in nature, the profits or losses as reflected in such accounts, regardless of whether the same are realized or unrealized, will generally be taxable or deductible as the case may be.

Furthermore, upon election, all unrealized profits or losses which have been excluded from taxation or deduction in the tax returns of the previous years on the basis of the *Nice Cheer* case will become taxable or deductible in the year of assessment for which the election is made.

The election will cease to have effect (i) when the taxpayer ceases to prepare their financial statements under HKFRS 9; or (ii) the CIR approves an application in writing by the taxpayer to revoke the election. The CIR may approve such an application where he is satisfied that there are good commercial reasons for the revocation and that avoidance of tax is not the main purpose, or one of the main purposes, of the revocation. Such a revocation will apply from the year of assessment as specified by the CIR.

In the case of either (i) or (ii) above, every financial instrument held by the taxpayer at the end of the basis period for the year of assessment immediately preceding the cessation year is taken to have been disposed of and reacquired, or released and reassumed, at its fair value on the first day of the basis period for the cessation year.

Please also refer to our Hong Kong Tax alerts issued on 15 November 2018 (2018 Issue No. 15) and 20 February 2019 (2019 Issue No. 4) in which we explained in detail the provisions of the new law.

Clients who have any questions regarding the filing of their tax returns and the supplementary forms, or the filing bases to be adopted, should contact their tax executives.

1. Samples of the 2018/19 profits tax return and supplementary forms can be accessed from the following link: www.ird.gov.hk/eng/tax/taxrep.htm
E-fillable supplementary forms will be available for downloading with effective from 1 April 2019 from the below link: www.ird.gov.hk/e_pfr

2. Those qualifying as a small corporation and opting to file their profits tax returns electronically will not be required to complete and file Forms S1 to S10.

3. *Nice Cheer Investment Limited v CIR* FACV 23/2012

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