

Hong Kong Tax Alert

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IRD explains legislative bill for inward re-domiciliation for foreign incorporated or domiciled companies to redomicile to Hong Kong

On 20 December 2024, on the same day as the Companies (Amendment) (No. 2) Bill 2024 (the Bill) was gazetted, the Inland Revenue Department (IRD) posted on its website guidance¹ on the interpretation of the various tax provisions of the Bill.

The provisions relating to the re-domiciliation requirements under the proposed amendments to the Companies Ordinance (amended CO) and other related enactments are essentially the same as discussed in our previous alerts, to which please refer. For ease of reference, a flow chart outlining the re-domiciliation procedures under the amended CO is shown in Appendix I to this alert.

Adapted from the IRD's guidance, this alert focuses on the transitional tax rules for a redomiciled non-Hong Kong company that before re-domiciliation has not carried on a trade, profession or business in Hong Kong and has carried on the trade, profession or business or another trade, profession or business in Hong Kong after the re-domiciliation.

¹ The guidance can be retrieved from the link below:
[IRD : Company Re-domiciliation Regime](#)

Amendments to the Inland Revenue Ordinance (IRO) for re-domiciliation

To strengthen our position as a global business and financial hub, the Government proposed to introduce an inward company re-domiciliation regime (the Regime) which allows companies incorporated or domiciled elsewhere to transfer their domicile to Hong Kong.

Under the Regime, non-Hong Kong incorporated or domiciled companies that have successfully registered as re-domiciled companies under the amended CO are able to preserve their legal identity and maintain their business continuity.

Hong Kong does not impose tax on the basis of residence or domicile. Under section 14 of the IRO, any persons, including corporations, partnerships, trustees and bodies of persons, carrying on any trade, profession or business in Hong Kong are chargeable to tax on all profits (excluding profits arising from the sale of capital assets) arising in or derived from Hong Kong from such trade, profession or business.

If a non-Hong Kong domiciled company has never carried on any trade, profession or business in Hong Kong before it re-domiciles to Hong Kong, no profits tax will be charged on the company for the period before it commences business in Hong Kong.

The tax legislative amendments are only applicable to the situation where a re-domiciled company has carried on a trade, profession or business outside Hong Kong before re-domiciliation and commences to carry on the same or another trade, profession or business in Hong Kong after re-domiciliation. The main aspects covered by the legislative amendments to the IRO are as follows:

- (a) Adding general interpretation provisions under section 2 of the IRO to the effect that references therein to a company “incorporated in Hong Kong” include a re-domiciled company and references to a company “incorporated outside Hong Kong” exclude a re-domiciled company.

Generally speaking, under the comprehensive avoidance of double taxation agreements or arrangements (CDTAs) signed between the Hong Kong Special Administrative Region (HKSAR) and other jurisdictions, a resident of the HKSAR is defined for the purpose of the CDTA to mean, among others, a company incorporated in the HKSAR or, if the company is incorporated outside the HKSAR, being managed or controlled in the HKSAR. By adding the above general interpretation provisions to the IRO, the IRD considers that when construing the term “resident of the HKSAR” under the CDTA, a re-domiciled company will also be regarded as a company incorporated in Hong Kong and in turn a resident of the HKSAR.

- (b) Introducing section 40AZA and Schedule 17L to the IRO to address matters regarding transitional tax arrangements and elimination of double taxation.

Transitional tax arrangements

Prerequisite conditions for deduction of expenses or expenditures

Any expense or expenditure incurred in the production of the assessable profits of a re-domiciled company is to be allowed for deduction to the extent that no deduction:

- (i) is allowable in respect of the expense or expenditure for the purposes of profits tax under other provisions of the IRO; and
- (ii) has been allowed in respect of the expense or expenditure for a similar tax imposed under the law of a place outside Hong Kong.

Without limiting the deduction criteria imposed by other provisions under the IRO, the above prerequisite conditions apply to all expenses or expenditures incurred by re-domiciled companies before re-domiciliation which are deductible for the purposes of profits tax.

Other specific conditions for deduction of specified types of expenses or expenditures

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| Trading stocks | Deduction of trading stock, which was acquired by a re-domiciled company before re-domiciliation and is used for a trade or business in Hong Kong after re-domiciliation, is based on the lower of the cost or net realizable value on the re-domiciliation date (i.e. the date on which a certificate of re-domiciliation is issued to the re-domiciled company under the amended CO). |
| Expenditures on registration of intellectual property rights, building refurbishment or research and development (R&D) | <p>The following expenditures which were incurred by a re-domiciled company before re-domiciliation -</p> <ul style="list-style-type: none"> (i) sum expended for the registration of a trade mark or design, the registration or grant of a patent or plant variety right under section 16(1)(g) of the IRO; (ii) expenditure on the renovation or refurbishment of a building or structure within the meaning of section 16F of the IRO; or (iii) R&D expenditure related to an R&D activity for the purposes of section 16B of the IRO, <p>are taken to have been incurred by the re-domiciled company in the basis period of the year of assessment in which the re-domiciled company begins to use the respective asset or right for any trade, profession or business in Hong Kong (Hong Kong business), or the relevant activity becomes an R&D activity related to the Hong Kong business.</p> |
| Expenditures on purchase of intellectual property rights or on provision of prescribed fixed assets or environmental protection facilities (the specified asset or right) | <p>The following expenditures which were incurred by a re-domiciled company before re-domiciliation -</p> <ul style="list-style-type: none"> (i) expenditure on the purchase of any patent rights or rights to any know-how within the meaning of section 16E(4) of the IRO; or (ii) specified capital expenditure within the meaning of section 16EA, 16G or 16H of the IRO, <p>are taken to have been incurred by the re-domiciled company in the basis period of the year of assessment in which the re-domiciled company begins to use the specified asset or right for the Hong Kong business, and the deductible amount is (A) or (B) below, whichever is the lower -</p> <ul style="list-style-type: none"> (A) the aggregate of the actual amount of specified expenditure minus the accumulated amortization and impairment losses in respect of the specified asset or right up to the re-domiciliation date; (B) the market value of the specified asset or right as at the re-domiciliation date. |

Depreciation allowance for machinery or plant

A re-domiciled company is entitled to claim depreciation allowances in respect of the machinery or plant if it -

- (i) has incurred capital expenditure on the provision of machinery or plant in relation to a trade, profession or business carried on outside Hong Kong before the re-domiciliation date; and
- (ii) uses the machinery or plant for any Hong Kong business on or after the re-domiciliation date.

The capital expenditure on the provision of machinery or plant incurred by the re-domiciled company before the re-domiciliation date is taken to have been incurred for producing profits chargeable to tax under Part 4 of the IRO by the re-domiciled company in the basis period for the year of assessment in which the re-domiciled company begins to use the machinery or plant for the Hong Kong business.



The amount of the capital expenditure for calculating depreciation allowances is determined as follows -

| Is the machinery or plant acquired under a hire purchase agreement? | Amount of the capital expenditure |
|---|---|
| No | <p>(C) or (D) below, whichever is the lower -</p> <p>(C) the actual cost of the machinery or plant minus the notional amount of the annual allowance which would have been made under section 37(2) or 39B(2) if the machinery or plant had been used by the re-domiciled company for producing profits chargeable to tax after its acquisition;</p> <p>(D) the market value of the machinery or plant as at the re-domiciliation date.</p> |
| Yes | <p>For the year of assessment of the re-domiciliation year (i.e., the year of assessment in which the re-domiciliation date falls):</p> $E / F \times G$ <p>where:</p> <p>(E) means the capital portion of the instalment payments made by the re-domiciled company up to the end of the basis period for the re-domiciliation year</p> <p>(F) means the capital portion of all the instalment payments required to be made by the re-domiciled company under the hire purchase agreement</p> <p>(G) means the lower of the above (C) or (D)</p> <p>For any year of assessment after the re-domiciliation year:</p> $H / I \times J$ <p>where:</p> <p>(H) means the capital portion of the instalment payments made by the re-domiciled company in the basis period for the year of assessment</p> <p>(I) means the capital portion of all the instalment payments required to be made by the re-domiciled company under the hire purchase agreement</p> <p>(J) means the lower of the above (C) or (D)</p> |

Insurance business

The supplementary provisions for section 23 (life insurance business) or section 23AAA (non-life long term insurance business) of the IRO under Schedule 17L to the IRO are applicable to the company as mentioned below that is a re-domiciled insurer within the meaning of section 3BA or 3BB of the Insurance Ordinance if the following conditions are satisfied

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|---|--|
| Non-HK insurer that was not a designated insurer immediately before the date on which it becomes a re-domiciled insurer (the critical date) | <ul style="list-style-type: none"> it has elected to have its assessable profits to be calculated in the manner provided in section 23(1)(b) of the IRO; it carries on any life or non-life long term insurance business in Hong Kong on or after the critical date; and |
| Non-Hong Kong incorporated company that was not an authorized insurer before the critical date | <ul style="list-style-type: none"> it has carried on any life or non-life long term insurance business outside Hong Kong before the critical date and continues to carry on, or carries on, that business outside Hong Kong on or after the critical date. |

The deficit or surplus as at the date immediately before the critical date that is attributable to the life or non-life long term insurance business carried on by the re-domiciled insurer outside Hong Kong ("specified deficit" or "specified surplus") has to be taken into account in ascertaining the adjusted surplus of the re-domiciled insurer deemed to arise in the critical basis period (i.e., the basis period in which the critical date falls) as follows -

- if a report is made under section 23(2) in respect of a period ending immediately before the critical basis period - the specified deficit is to be added to the deficit mentioned in section 23(4B)(a)(i); or the specified surplus is to be added to the surplus mentioned in section 23(4B)(b)(i).
- if no report has been made - the specified deficit is to be the deficit mentioned in section 23(4B)(a)(i); or the specified surplus is to be the surplus mentioned in section 23(4B)(b)(i).

Elimination of double taxation

If a re-domiciled company has paid tax in its place of incorporation which is of substantially the same nature as profits tax (specified tax) in respect of its unrealised income or profit (specified income) because of company re-domiciliation, and after re-domiciliation, profits tax under the IRO is also payable on the actual income or profit derived by the re-domiciled company, unilateral tax credits are available to the company for elimination of double taxation in the re-domiciliation year or any subsequent year of assessment.

The amount of the actual income or profit for a particular year of assessment must not exceed the specified income (relevant income). In addition, the amount of the tax credit for a particular year of assessment is capped at the lower of the specified tax paid or the profits tax payable on the relevant income.

Any excess amount of the specified tax paid over the cap of the tax credit will be allowed for deduction in ascertaining the assessable profits of the re-domiciled company for the particular year of assessment.

Commentary

We welcome the introduction of the proposed Regime in Hong Kong, which enables a company incorporated or domiciled elsewhere to redomicile to Hong Kong, thereby preserving its legal identity and maintaining its business continuity.

Upon its de-registration overseas, the Regime would relieve the redomiciled company from having to comply with the regulatory requirements such as the economic substance requirement of its place of incorporation or original domicile.

The fact that under the global minimum tax initiative, large multinational enterprises (MNEs) will be required to pay tax of at least 15% in every jurisdiction in which they have operations would further reduce the appeal to such MNEs locating their operating companies in traditional no or low tax jurisdictions.

This may also create the demand for such MNEs redomiciling some of their non-Hong Kong investment holding or operating companies to Hong Kong, which is a leading destination for business and investment, renowned for ease of doing business with the underpinning of a strong tradition of rule of law.

The availability of a unilateral tax credit for unrealized profits of a redomiciled company that are taxed overseas upon its exit from its original place of incorporation or domicile when the profits are taxed again in Hong Kong upon realization is also welcome and is in line with similar provisions contained in the Singapore re-domiciliation regime.

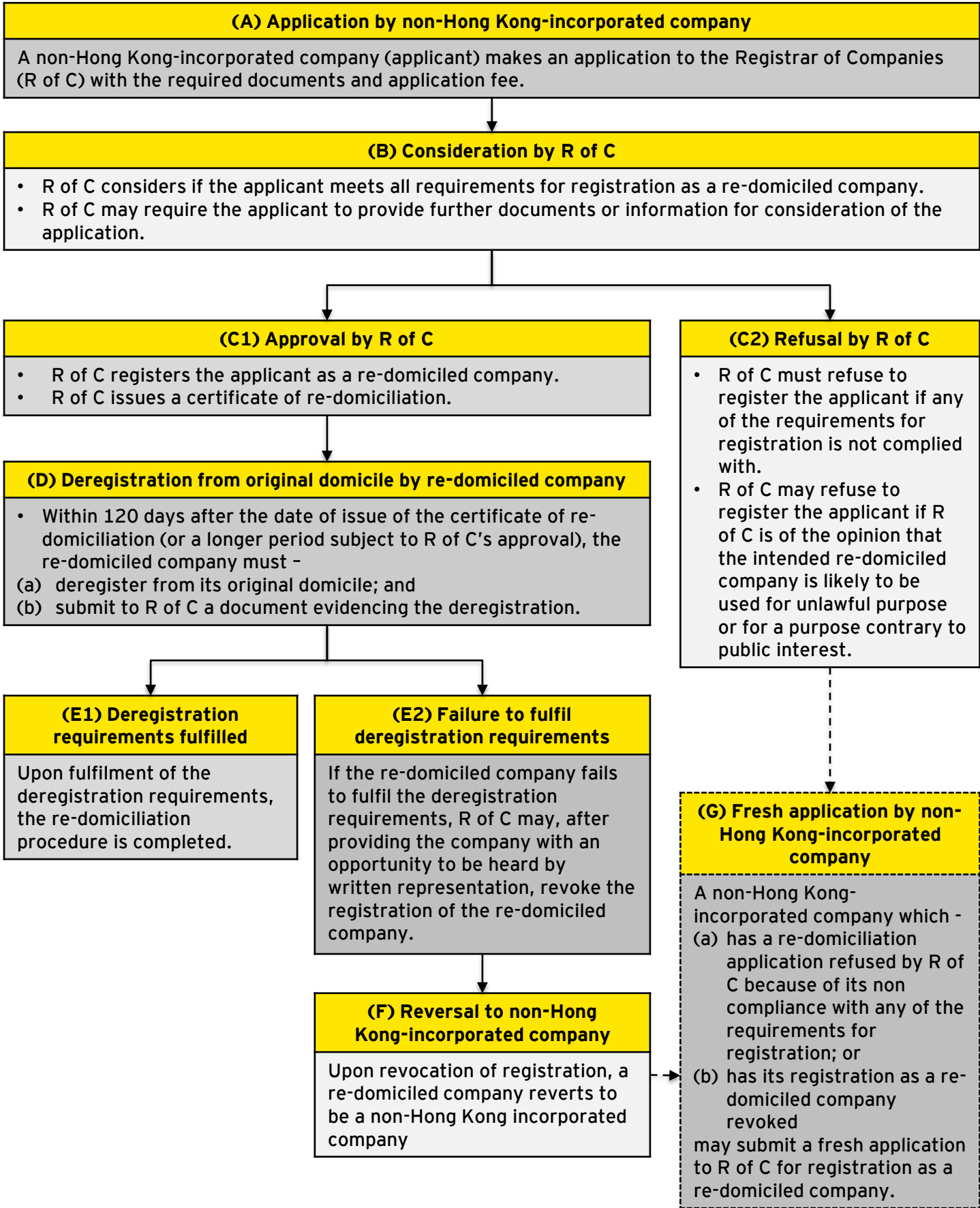
The IRD's explanation that a redomiciled company could be regarded as a company incorporated in Hong Kong, and therefore a Hong Kong resident for most Hong Kong's CDTAs also seems persuasive.

It however seems that transfer of shares in a redomiciled company would be liable to stamp duty in Hong Kong given that a re-domiciled company is essentially treated as a Hong Kong incorporated company and is required to comply with all the applicable provisions of the amended CO, there being no provision in the Bill exempting or remitting the stamp duty.

Clients who have any views on the Regime can contact their tax executives so that we can convey the same to the Government in an appropriate manner.



Appendix I - Flow chart of the application procedures of company re-domiciliation²



² The flowchart was extracted from Annex B of the Legislative Council Brief of Companies (Amendment) (No. 2) Bill 2024

Hong Kong office

Jasmine Lee, Managing Partner, Hong Kong & Macau
27/F One Taikoo Place, 979 King's Road, Quarry Bay, Hong Kong
Tel: +852 2846 9888 Fax: +852 2868 4432

| Non-financial Services | | | Financial Services | |
|--|--|--|--|--|
| Wilson Cheng Tax Leader for Hong Kong and Macau +852 2846 9066 wilson.cheng@hk.ey.com | | | Paul Ho Tax Leader for Hong Kong +852 2849 9564 paul.ho@hk.ey.com | |
| Business Tax Services/Global Compliance and Reporting | | | Business Tax Services/Global Compliance and Reporting | |
| Hong Kong Tax Services | | | Hong Kong Tax Services | |
| Wilson Cheng +852 2846 9066 wilson.cheng@hk.ey.com | Jacqueline Chow +852 2629 3122 jacqueline.chow@hk.ey.com | Ryan Dhillon +852 3752 4703 ryan.dhillon@hk.ey.com | Paul Ho +852 2849 9564 paul.ho@hk.ey.com | Ming Lam +852 2849 9265 ming.lam@hk.ey.com |
| Tracy Ho +852 2846 9065 tracy.ho@hk.ey.com | Ada Ma +852 2849 9391 ada.ma@hk.ey.com | Jennifer Kam +852 2846 9755 jennifer.kam@hk.ey.com | Sunny Liu +852 2846 9883 sunny.liu@hk.ey.com | Helen Mok +852 2849 9279 helen.mok@hk.ey.com |
| May Leung +852 2629 3089 may.leung@hk.ey.com | Karina Wong +852 2849 9175 karina.wong@hk.ey.com | Leo Wong +852 2849 9165 leo.wong@hk.ey.com | | |
| Ricky Tam +852 2629 3752 ricky.tam@hk.ey.com | Susan Kwong +852 2629 3117 susan.tm.kwong@hk.ey.com | | | |
| China Tax Services | | | Customer Tax Operations and Reporting Services | |
| Ivan Chan +852 2629 3828 ivan.chan@hk.ey.com | Becky Lai +852 2629 3188 becky.lai@hk.ey.com | | Paul Ho +852 2849 9564 paul.ho@hk.ey.com | |
| | | | Francis Tang +852 2629 3618 francis-ks.tang@hk.ey.com | |
| Payroll Operate | | | US Tax Services | |
| Accounting Compliance and Reporting | | | Camelia Ho +852 2849 9150 camelia.ho@hk.ey.com | |
| Vincent Hu +852 3752 4885 vincent-wh.hu@hk.ey.com | Linda Liu +86 21 2228 2801 linda-sy.liu@cn.ey.com | Cecilia Feng +852 2846 9735 cecilia.feng@hk.ey.com | International Tax and Transaction Services | |
| International Tax and Transaction Services | | | International Tax Services | |
| Winnie Kwan +852 2629 3211 winnie.yw.kwan@ey.com | Sangeeth Aiyappa +852 2629 3989 sangeeth.aiyappa@hk.ey.com | Martin Richter +852 2629 3938 martin.richter@hk.ey.com | Sophie Lindsay +852 3189 4589 sophie.lindsay@hk.ey.com | Maggie Mang +852 3471 2759 maggie.mang@hk.ey.com |
| | Kenny Wei +852 2629 3941 kenny.wei@hk.ey.com | | Transfer Pricing Services | |
| Transaction Tax Services | | | Ka Lok Chu +852 2629 3044 kalok.chu@hk.ey.com | |
| Jane Hui +852 2629 3836 jane.hui@hk.ey.com | Jasmine Tian +852 2629 3738 jasmine.tian@ey.com | Emma Campbell +852 2629 1714 emma.ef.campbell@ey.com | Justin Kyte +852 2629 3880 justin.kyte@hk.ey.com | |
| People Advisory Services | | | Transaction Tax Services | |
| William Cheung +852 2629 3025 william.cheung@hk.ey.com | Christina Li +852 2629 3664 christina.li@hk.ey.com | Emily Chan +852 2629 3250 emily-my.chan@hk.ey.com | Sunny Liu +852 2846 9883 sunny.liu@hk.ey.com | |
| Winnie Walker +852 2629 3693 winnie.walker@hk.ey.com | Paul Wen +852 2629 3876 paul.wen@hk.ey.com | | Tax Technology and Transformation Services | |
| | | | Robert Hardesty +852 2629 3291 robert.hardesty@hk.ey.com | |
| Asia-Pacific Tax Center | | | | |
| Tax Technology and Transformation Services | | International Tax and Transaction Services | | |
| Albert Lee +852 2629 3318 albert.lee@hk.ey.com | US Tax Desk | | Operating Model Effectiveness | |
| | Jeremy Litton +852 3471 2783 jeremy.litton@hk.ey.com | | Edvard Rinck +852 9736 3038 edvard.rinck@hk.ey.com | |

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