Hong Kong to enhance existing tax concessions for maritime service industry and introduce a new half-rate tax concessionary regime for physical commodity traders

A recent briefing paper submitted by the Transport and Logistics Bureau to the Legislative Council Panel on Economic Development[1] indicates that legislation for the captioned initiatives is to be introduced.

Maritime service industry

The proposed enhancements to the existing tax concessions for maritime service industry include:

(i) Relaxing the definition for ship leasing to cover short-term leases;
(ii) Introducing an additional option of a 15% concessionary tax rate for enterprises that are subject to the tax reform package (commonly referred to as "BEPS 2.0") of the Organization for Economic Co-operation and Development (This option is aimed at easing their compliance costs for BEPS 2.0);
(iii) Introducing tax deduction for acquisition costs of ships held under operating lease; and
(iv) Relaxing deduction rules for interest incurred to finance acquisition of ships.

Physical commodity traders

The government proposes introducing a half-rate profits tax concession (i.e. 8.25%) for assessable profits derived by qualifying physical commodity traders from a qualifying physical commodity trading activity. In-scope enterprises for BEPS 2.0 would also have an option to be taxed at 15% rather than the 8.25% concessionary tax rate.

In addition to the general conditions for preferential tax regimes, the eligibility for the new tax regime is subject to specific terms including (i) the minimum annual business turnover requirement; (ii) minimum requirements on the use of Hong Kong maritime services; and (iii) economic substance requirements.

The above measures, applying to the year of assessment 2025/26 onwards so as to be in alignment with the implementation timetable of BEPS 2.0 when enacted, are expected to be introduced into the Legislative Council within the first half of 2026.

Clients who are interested to explore how they can benefit from these proposed measures can contact their tax executive.

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[1] The briefing paper can be accessed at the link below:
https://www.legco.gov.hk/yr2025/english/panels/edev/papers/edev20250708cb3-1045-5-e.pdf

Enhancements to existing tax concessions for maritime service industry

Several tax concessionary measures have been introduced by the government in recent years to encourage more maritime service enterprises to choose Hong Kong as their base of operations, including:

(i) a zero-rate profits tax concession to qualifying ship lessors from the year of assessment 2020/21;
(ii) a half-rate (8.25%) profits tax concession to qualifying ship leasing managers from the year of assessment 2020/21; and
(iii) a half-rate (8.25%) profits tax concession to qualifying shipping commercial principals (i.e., ship agents, ship managers and ship brokers) from the year of assessment 2022/23.

In view of the implementation of BEPS 2.0, the above tax concessions are proposed to be enhanced to ensure compliance with international tax rules and to maintain Hong Kong's competitiveness.

Relaxing the definition for ship leasing

Currently, the Inland Revenue Ordinance (IRO) prescribes that the qualifying term of "operating lease" and "finance lease" in respect of a qualifying ship leasing activity shall be over one year, and that the lessee of the qualifying ship leasing activity and ship leasing management activity shall be "a ship lessor, ship leasing manager or ship operator".

To provide for greater flexibility for business operation, the government proposes (i) removing the one-year term restriction on "operating lease" and "finance lease" and (ii) extending the scope of lessees to be "any other persons". Such enhancements are largely modelled on the aircraft leasing tax concession effective from the year of assessment 2023/24.

Introducing an additional option of a 15% concessionary tax rate

Upon the implementation of BEPS 2.0 in Hong Kong, entities of an in-scope multinational enterprise (MNE) group will be subject to a global minimum tax at the effective tax rate (ETR) of 15% in each tax jurisdiction they operate. In-scope MNE entities whose ETRs are below the minimum will be subject to the top-up tax.

To facilitate the compliance of in-scope MNE groups with the BEPS 2.0 requirement, the government proposes introducing a 15% concessionary tax rate as an additional option for the relevant enterprises.

While retaining their eligibility for the original concessionary tax rate, this additional option, to be elected on an annual basis, is aimed at reducing the BEPS 2.0 compliance costs for the relevant enterprises. If so opted, a lower threshold of economic substance requirement will be imposed.

Introducing tax deduction for acquisition costs of ships held under operating lease

Under the current legislation, a qualifying ship lessor would not be entitled to claim tax deduction for the acquisition costs of ships held under operating lease. Instead, they are allowed to calculate their assessable profits based on 20% of their lease income (i.e., the 20% tax base concession). As the current tax rate applicable to qualifying ship lessors is 0% (i.e., not required to pay any tax), the 20% tax base concession does not have any impact.

In order to better reflect their operating costs and align with the international tax rules under BEPS 2.0, it is proposed that, instead of granting the 20% tax base concession, tax deduction for the actual costs incurred by qualifying ship lessors for acquiring ships held under operating lease be granted.

This proposed deduction will be applicable to all ships regardless of the date of purchase. However, the acquisition costs will have to be suitably adjusted for depreciation for ships which have been purchased and used before the effective date of the legislative amendments.

Any proceeds received from the sale of a ship (limited to the total amount of the tax deductions previously allowed) will be deemed as taxable trading receipts for the year of disposal.

Compared to the 20% tax base concession which is a permanent difference, granting tax deductions based on the actual costs incurred, being a temporary difference, would allow deferred taxes to be included as covered taxes. This would avoid the ETRs of the relevant enterprises being unduly dragged down for BEPS 2.0 purposes.

Relaxing deduction rules on interest expenses incurred to finance acquisition of ships

Under the existing legislation, interest expenses incurred by ship lessors for the acquisition of ships would be tax deductible only if (i) the money is borrowed from a Hong Kong or overseas financial institution; or (ii) the financier is subject to tax in Hong Kong under the IRO in respect of the interest income.

Similar to the aircraft leasing tax concession regime, it is proposed that such interest expenses would also be tax deductible if (i) the financier, not a financial institution, is not associated with the borrower; or (ii) if associated, the financier is required to pay an overseas tax which is similar to profits tax in Hong Kong.

A summary of the above enhancement measures is contained in Appendix I to this alert.

New half-rate tax concessionary regime for physical commodity traders

Under the proposed new regime, assessable profits derived by qualifying physical commodity traders from a qualifying physical commodity trading activity would be taxed at 8.25%. In-scope enterprises for BEPS 2.0 would also have an option to be taxed at 15% rather than the 8.25% concessionary tax rate.

Similar to other preferential tax regimes, the eligibility for the new tax regime is subject to the following three general conditions:

(i) The central management and control of the qualifying physical commodity trader is exercised in Hong Kong;
(ii) The activities that produce the qualifying profits are carried out in Hong Kong by the qualifying physical commodity trader or arranged by it to be carried out in Hong Kong; and
(iii) The activities are not carried out by an overseas permanent establishment of the qualifying physical commodity trader.

Other eligibility conditions specific to the new tax regime include:

Minimum annual business turnover requirement	Minimum annual business turnover derived from the qualifying physical commodity trading activity is not less than HK$700 million
Minimum requirements on the use of Hong Kong maritime services	Expenditure to be incurred on services provided by "Hong Kong-based service providers": (a) 30% of the expenditure on any of the specified maritime services in aggregate; or (b) 50% of the expenditure on one of the specified maritime services. "Specified maritime service" means any service provided for, or in connection with the following: ship leasing activity, ship leasing management activity, ship agency activity, ship management activity, ship broking activity, freight booking, ship repairing, ship tug-and-tow, maritime legal services (provided that Hong Kong is specified as the place of arbitration of maritime-related disputes) and marine insurance.
Economic substance requirements	(a) For those electing for the profits tax rate of 8.25%: having not less than three full-time employees and incurring not less than HK$3 million annual operating expenditure; or (b) For those electing for the profits tax rate of 15%: having not less than one full-time employee and incurring not less than HK$1 million annual operating expenditure.

Qualifying physical commodity traders

A qualifying physical commodity trader refers to an enterprise fulfilling one of the three following criteria so as to ensure that it carries out qualifying physical commodity trading activities as its primary business in Hong Kong:

(i) It has carried out in Hong Kong one or more qualifying physical commodity trading activities and has not carried out in Hong Kong any activity other than a qualifying physical commodity trading activity;
(ii) It satisfies the safe harbor rule (i.e. the corporation should have not less than 75% of all its profits and assets being physical commodity trading profits and physical commodity trading assets); or
(iii) It has obtained the Commissioner of Inland Revenue's determination that the corporation is a qualifying physical commodity trader if the Commissioner is of the opinion that the relevant conditions specified in (i) and (ii) above would, in the ordinary course of business of the corporation, have been satisfied.

Qualifying physical commodity trading activity

A qualifying physical commodity trading activity refers to a physical commodity trading activity that fulfils the following conditions:

(i) The activity is carried out in the ordinary course of the corporation's business carried on in Hong Kong; and
(ii) The contract for buying and/or selling of a qualifying physical commodity item is effected in Hong Kong.

A physical commodity trading activity refers to an activity of buying and/or selling of a qualifying physical commodity item that results in the physical delivery of that item, comprising one or more of the following actions:

(i) Solicitation of the qualifying physical commodity item to be bought/sold
(ii) Solicitation of the buyer and/or seller of the qualifying physical commodity item;
(iii) Setting and agreeing on the buying and/or selling terms of that qualifying physical commodity item;
(iv) Obtaining finance for the transaction of that qualifying physical commodity item;
(v) Executing the transaction of that qualifying physical commodity item;
(vi) Making arrangements for the transportation of that qualifying physical commodity item; or
(vii) Arranging insurance for the transportation of that qualifying physical commodity item.

Solicitation of commodity items for the purpose of self-consumption would not however be regarded as "physical commodity trading activity".

Qualifying physical commodity items

A full list of the proposed "qualifying physical commodity items" is reproduced as Appendix II.

The list has covered those commodity items that are actively traded physically and are commonly transported by sea so as to align with the policy intent of attracting physical commodity traders to Hong Kong to drive the further development of the maritime service industry. In addition, to promote trading of green maritime fuel in Hong Kong, the list has also included items such as biofuel and green methanol.

Commentary

We welcome the government's efforts to reinforce and enhance the tax concession regimes for the maritime service industry. Given that the industry is highly internationalized and its mode of operation inherently globalized with high mobility, such efforts are particularly important to maintaining Hong Kong as an international maritime center.

Another consideration may be whether Hong Kong should attract physical commodity traders to Hong Kong in their own right. For example, even if they may not use services provided by Hong Kong-based maritime service providers up to the "30% or 50%" requirement, Hong Kong may still consider granting them the tax concession if their level of local expenditures incurred is substantial enough to drive economic developments in other sectors.

Clients who are interested to explore how they can benefit from these proposed measures can contact their tax executive.

Appendix I – Summary of the proposed enhancement measures for maritime services industry

	Existing regime	Proposed enhanced regime
Ship acquisition cost	• No deduction of ship acquisition cost • Taxable amount of lease payments equal to 20% of the tax base, i.e., gross lease payments less deductible expenses (excluding depreciation allowance)	• Tax deduction will be allowed for ship acquisition costs, subject to adjustment if the ship is purchased and used before the effective date of the legislative amendments • The sales proceeds (limited to the total amount of tax deductions previously allowed) will be deemed as taxable trading receipts
Limitation on lease term	Not less than one year	No limitation
Covered leasing activities	Confined to leasing of ship to ship lessors, ship leasing managers or ship operators	Leasing of ship to any person
Interest payment to non-financial institution financiers outside Hong Kong	Generally non-deductible	• Deductible if the loan is wholly and exclusively used to finance the acquisition of a ship; and • Subject to paying a "similar tax" outside Hong Kong, if the financier is an associated person of the ship lessor (no additional condition if the financier is non-associated with the ship lessor)
Minimum threshold requirements	(1) Ship lessors: - Two full-time qualified employees - Annual operating expenditure HK$7.8 million (2) Ship leasing managers: - One full-time qualified employee - Annual operating expenditure HK$1 million (3) Shipping commercial principals: - One full-time qualified employee - Annual operating expenditure HK$1 million	Lower thresholds for taxpayers opting for the 15% concessionary tax rate: (1) Ship lessors: - One full-time qualified employee - Annual operating expenditure HK$3.9 million (2) Ship leasing managers: - One full-time qualified employee - Annual operating expenditure HK$0.5 million (3) Shipping commercial principals: - One full-time qualified employee - Annual operating expenditure HK$0.5 million

Appendix II – List of proposed qualifying physical commodity items

Energy and industrial commodities	Agricultural commodities	Metal mine commodities
- Crude oil	- Wheat	- Copper
- Natural gas	- Corn	- Aluminium
- Gasoline	- Soybeans	- Zinc
- Heating oil	- Coffee	- Nickel
- Liquefied petroleum gas	- Sugar	- Iron Ore
- Coal	- Cotton	- Lithium carbonate
- Bitumen	- Soybean oil	- Lithium hydroxide
- Diesel	- Lumber	- Cobalt hydroxide
- Fuel oil	- Oats	- Cobalt metal
- Naphtha	- Palm olein	- Bauxite
- Rubber	- Rough rice	- Aluminium metal
- Urea	- Cocoa	- Aluminium oxide
- Woodpulp	- Canola	- Gold ore and
- Metallurgical coke		- concentrates
- Petroleum coke		- Hot-rolled coils
- Hydrogen		- Lead
- Green methanol		- Molybdenum
- Biofuel		- Stainless steel
- Ammonia		- Steel
		- Tin
		- Titanium
		- Magnesium
		- Antimony
		- Silicon

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