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RSM Tax Advisory (Hong Kong) Limited

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TAX CONCESSIONS FOR FAMILY-OWNED INVESTMENT HOLDING VEHICLES

The Inland Revenue (Amendment) (Tax Concessions for Family-owned Investment Holding Vehicles) Ordinance 2023 (“the Amendment Ordinance”) was gazetted and came into operation on 19 May 2023. It introduces profits tax concessions to (a) eligible Family-owned Investment Holding Vehicles (“FIHVs”) managed by eligible Single Family Offices (“SFOs”) in Hong Kong; and (b) Family-owned Special Purpose Entities (“FSPEs”), of which the assessable profits of an FIHV or an FSPE earned from the qualifying transactions and incidental transactions (the latter being subject to a 5% threshold) would be taxed at a concessionary profits tax rate of 0%. Such concessions would apply retrospectively to any year of assessment commencing on or after 1 April 2022.

1. FAMILY-OWNED INVESTMENT HOLDING VEHICLES (“FIHV”)

To enjoy the profits tax concession, the FIHV must satisfy the following conditions:

- It must be an entity ^(Note 1) that is not a business undertaking for general commercial or industrial purposes
- At all times during the basis period for the year of assessment:
 - Unrelated parties (excluding tax-exempt charities under Section 88 of the Inland Revenue Ordinance (“IRO”)) can hold not more than 5% (in aggregate) of the beneficial interest (direct or indirect) in the FIHV;
 - Members of the family ^(Note 2) must have (i) at least 95% (in aggregate) of the beneficial interest (direct or indirect) in the FIHV (in case no tax-exempt charities are involved); or (ii) at least 75% (in aggregate) of the beneficial interest (direct or indirect) in the FIHV (in case tax-exempt charities are involved); and
 - The FIHV must be “normally managed or controlled in Hong Kong”

- The FIHV is managed by an eligible Single Family Office and meets the minimum asset threshold; and
- The FIHV’s core income-generating activities (“CIGAs”) are carried out in Hong Kong and meet the substantial activities requirements of qualified full-time employees and operating expenditures.

The minimum asset threshold and the substantial activities requirements are as follows:

Minimum Asset Threshold	<ul style="list-style-type: none"> • The aggregate amount of the net asset value (“NAV”) of the assets (“specified assets”) specified under Schedule 16C to the Inland Revenue Ordinance (“IRO”) <i>(Note 3)</i> managed by an eligible Single Family Office for the FIHV (or multiple FIHVs) at the end of the basis period for the year of assessment (“subject year”) must be at least HK\$240 million. • In case the Aggregate NAV for the subject year falls below HK\$240 million, the minimum asset threshold is considered to be met if the Aggregate NAV during the period listed below is at least HK\$240 million: <ul style="list-style-type: none"> – At the end of the FIHV’s basis period for the year of assessment immediately preceding the subject year (1st preceding year), or – At the end of the FIHV’s basis period for the year of assessment immediately preceding the 1st preceding year.
Substantial Activities Requirement	<ul style="list-style-type: none"> • The number of qualified full-time employees employed and the amount of operating expenditure incurred by the FIHV, or by the eligible SFO on behalf of the FIHV if the CIGAs are outsourced, must be commensurate with the level of the CIGAs carried out in Hong Kong. • At a minimum, the FIHV is required to have: <ul style="list-style-type: none"> – at least two qualified full-time employees in Hong Kong who carry out the CIGAs; and – at least HK\$2 million operating expenditure incurred in Hong Kong for carrying out the CIGAs.

In addition, profits tax concessions will also be provided at the Family-owned Special Purpose Entities (“FSPE”) level to the extent which corresponds to the percentage of beneficial interest of the FIHV in the FSPE.

2. SINGLE FAMILY OFFICE (“SFO”)

On the other hand, an eligible SFO should:

- be a private company (incorporated in or outside Hong Kong) that is “normally managed or controlled in Hong Kong”;
- Unrelated parties (other than tax-exempt charities) can hold not more than 5% (in aggregate) of the beneficial interest (direct or indirect) in the SFO;
- Members of the family must have (i) at least 95% (in aggregate) of the beneficial interest (direct or indirect) in the SFO (in case no tax-exempt charities are involved); or (ii) at least 75% (in aggregate) of the beneficial interest (direct or indirect) in the SFO (in case tax-exempt charities are involved);
- provides investment services ^(Note 3) to specified persons of the family ^(Note 4) during the basis period for the year of assessment and the fees for the provision of those services are chargeable to tax; and
- fulfils the safe harbour rule (i.e. at least 75% of the SFO’s assessable profits is derived from services provided to specified persons in the current year of assessment (“YOA”) or the current YOA and up to 2 preceding YOAs on average).

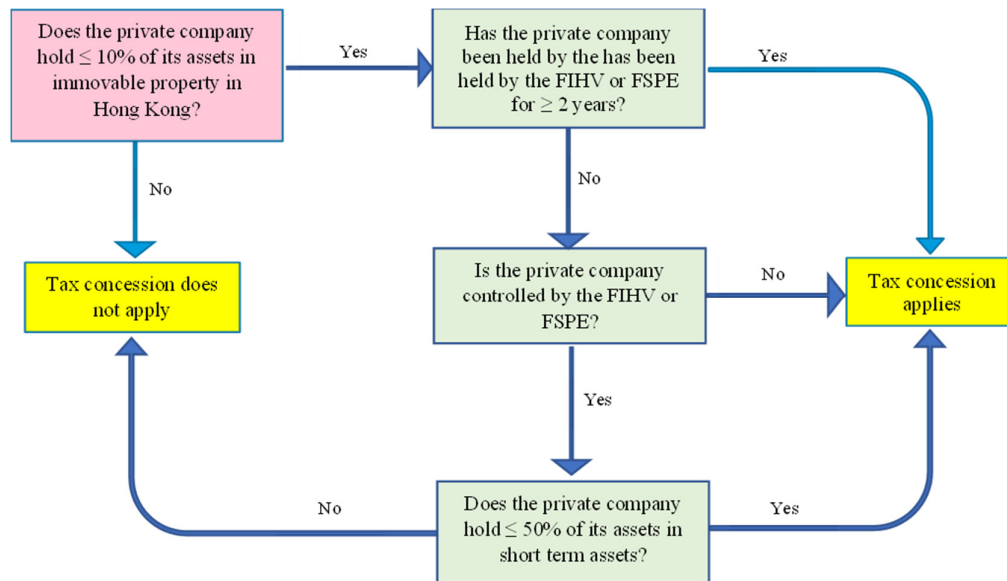
Not more than 50 FIHVs managed by the same eligible SFO may benefit from the profits tax concession.

3. INVESTMENT IN PRIVATE COMPANIES

To reduce the risk of tax avoidance, FIHV/FSPE will be taxed on its profits from the investment in private companies that do not meet the following three tests (same as the existing tests under the Unified Fund Exemption regime):

1.	Immovable property test	If FIHV/FSPE invests in a private company that holds, whether directly or indirectly, more than 10% of its assets in immovable property (excluding infrastructure) in Hong Kong, the FIHV/FSPE will be taxed on the profits arising from such an investment in the private company.
2.	Holding period test:	If the immovable property test is satisfied and the investment in the private company has been held by FIHV/FSPE for less than two years, FIHV/FSPE will be taxed on the profits arising from the transaction of the private company.
3.	Control test and short-term asset test	If the immovable property test is satisfied but the holding period test is not satisfied, profits tax concession would not apply if: <ul style="list-style-type: none">• FIHV/FSPE has control over the private company; or• FIHV/FSPE does not have control over the private company, but the latter holds more than 50% of the value of its assets in short-term assets ^(Note 4).

Diagram 1: Investment in Private Company



If any transaction in a private company fails to pass the tests above, the profits tax concession will not apply to the profits earned from that non-qualifying transaction only. The profits earned from other qualifying transactions of the FIHV or FSPE will not be affected.

4. ANTI-ROUND TRIPPING PROVISIONS

To prevent abuse of the profits tax exemption, the tax-exempt profits of the FIHV or FSPE are deemed as assessable profits of the resident person if the resident person: (1) has, either alone or jointly with its associate(s), not less than 30% beneficial interest in the FIHV or (2) has any beneficial interest in the FIHV and the FIHV is an associate of the resident person.

Given the special features of family offices and diverse holding structures of FIHV, a family may hold FIHV directly or indirectly through resident companies, and such companies are likely to be associated with the FIHV. In this connection, the anti-round tripping provisions would not apply to the following:

- resident individuals; and
- certain resident non-individual entities (i.e. an eligible SFO of the relevant family and a specified entity).

The specified entity must be a passive investment holding vehicle not carrying on any trade or business. At the same time, it must fulfil the following conditions:

- at least one member of the family to which the FIHV is related must have a direct or indirect beneficial interest in the entity;
- the entity is interposed between the family members and the FIHV; and

- regardless of the extent of the beneficial interest held by the family members in the entity, at least 95% of the beneficial interest in the FIHV must be held by family members.

5. POINTS TO NOTE

- An election for the profits tax concession must be made in writing. The election, once made, will apply to all subsequent years of assessment (i.e. no annual election is required) and is irrevocable.
- If the Commissioner is satisfied that:
 - the main purpose, or one of the main purposes of an FIHV or an FSPE in entering into an arrangement; or
 - the main purpose, or one of the main purposes of a person making a transfer of any asset or business to the FIHV or FSPE,

is to obtain a tax benefit, whether for the FIHV or FSPE or another person or entity, the profits tax concession will not apply to the FIHV or FSPE concerned.

However, for a transfer of asset or business to an FIHV or FSPE, the profits tax concession may still apply if the transfer is carried out on an arm's length basis and the transferor is chargeable to tax in respect of the assessable profits arising from the transfer.

- A responsible person for an FIHV and the eligible SFO should keep sufficient records to enable the identity and particulars of the beneficial owner(s) of the FIHV and the eligible SFO to be readily ascertained. Penalties will be imposed on the FIHV and the eligible SFO if they fail to comply with the record-keeping requirements without reasonable excuse.
- As the refined regime applies to any years of assessment commencing on or after 1 April 2022, taxpayers should closely monitor the developments and consult their tax advisors for assistance if necessary.

Note

1. *Entity means a body of persons (corporate or unincorporate) or a legal arrangement, including a corporation, partnership and trust (including a discretionary trust). It can be established or created in or outside Hong Kong.*
2. *Members of the family include a natural person (Person A) and all of the persons related to Person A (whether alive or deceased) mentioned below:*
 - *a spouse of Person A (Person B);*
 - *a lineal ancestor of Person A (Person C);*
 - *a lineal ancestor of Person B (Person D);*
 - *a lineal descendant of Person A (Person E);*
 - *a sibling of Person A, Person B, Person C or Person D (Person F);*
 - *a lineal descendant of Person F (Person G); and*
 - *a spouse of Person E, Person F and Person G.*

A lineal descendent includes adopted and stepchildren of the person's spouse (including a deceased spouse) or former spouse.

If a person ceases to be a spouse (i.e. other than being deceased) during a year of assessment that begins on or after 1 April 2022, the spouse and those persons who are connected to the spouse and considered as members of a family before the cessation would still be regarded as members of the family for the subject year of assessment and the following year of assessment (i.e. a total of two years).

3. *Specified assets specified under Schedule 16C to the IRO include the following:*
 - *Securities;*
 - *Shares, stocks, debentures, loan stocks, funds, bonds or notes of, or issued by, a private company;*
 - *Futures contracts;*
 - *Foreign exchange contracts under which the parties to the contracts agree to exchange different currencies on a particular date;*
 - *Deposits other than those made by way of a money-lending business;*
 - *Deposits (as defined by section 2(1) of the Banking Ordinance (Cap. 155)) made with a bank (as defined by Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571));*
 - *Certificates of deposit (as defined by Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571));*
 - *Exchange-traded commodities;*
 - *Foreign currencies;*
 - *OTC derivative products (as defined by Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571))*
4. *Investment activities include:*
 - *conducting research and advising on any potential investments to be made by the FIHV;*
 - *acquiring, holding, managing or disposing of property for the FIHV; and*
 - *establishing or administering an FSPE for holding and administering one or more underlying investments of the FIHV.*
5. *A specified person in relation to a family means:*
 - *an FIHV that is related to the family;*
 - *an FSPE in which the FIHV has a beneficial interest (whether direct or indirect);*
 - *an interposed FSPE of the FIHV; and*
 - *a member of the family.*
6. *Short-term assets are assets (excluding specified assets and immovable property in Hong Kong) held by the private company for less than three years before the date of disposal.*

RSM Tax Advisory (Hong Kong) Limited

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- Assist clients to discuss and clarify matters with tax officials, including transfer pricing and advance rulings
- Act as client representative in tax audits and tax investigations
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- Act as tax advisor on transfer pricing and tax compliance reviews for IPO applications
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