BoardRoom
Smart Business Solutions

Asia Tax Insights – Hong Kong

Pillar Two of BEPS 2.0 Implementation: Hong Kong's Proactive Approach

20 February 2024

Asia Tax Insights – Hong Kong
Pillar Two of BEPS 2.0 Implementation: Hong Kong's Proactive Approach

Candice Ng & Eunice Hooi

Base Erosion and Profit Shifting (BEPS) 2.0 – Pillar Two

In July 2021, the Organisation for Economic Co-operation and Development (OECD) introduced BEPS 2.0, a strategic move to address the challenges of base erosion and profit shifting.

Pillar Two of BEPS 2.0 specifically targets multinational enterprise (MNE) groups with consolidated annual revenue of EUR 750 million or more, ensuring that these MNEs pay a minimum tax rate of 15% on their profits across all jurisdictions in which they operate in. This objective is achieved through two interconnected rules - i.e. *the Income Inclusion Rule (IIR)* and *the Undertaxed Profits Rule (UTPR)*, collectively known as the global anti-base erosion (GloBE) rules. To further reinforce its taxing authority, a jurisdiction may choose to implement a domestic minimum top-up tax (DMTT).

Hong Kong's Proactive Approach

Hong Kong, a key player in the international business arena, is proactively working towards the implementation of Pillar Two of BEPS 2.0 framework. The government aims to safeguard its taxing rights while minimising compliance burdens for MNE groups. To achieve this, Hong Kong plans to adopt the global minimum tax and introduce the DMTT in Hong Kong (HKMTT) starting from 2025.

On 21 December 2023, the government released a consultation paper regarding the implementation of the global minimum tax and the HKMTT. The consultation period will last for three months, closing on 20 March 2024.

This consultation aims to explain the policy rationale and design features of the GloBE rules relevant to Hong Kong. It also seeks feedback on various aspects, including the administration framework of GloBE rules, as well as the design and administration of HKMTT. Hong Kong's approach aligns closely with OECD model rules, with room for limited local adaptations.

Legislative amendments, incorporating feedback received during the consultation, are expected to be introduced in the second half of 2024.

Outlined below are some key features of the proposed rules:

1. Implementation of the global minimum tax in Hong Kong

Scope of Global Anti-Base Erosion (GloBE) rules and Hong Kong's Minimum Taxation on Multinational Enterprises (HKMTT)
The GloBE rules and HKMTT will be applicable to MNE groups that meet specific criteria, with consolidated annual revenue of EUR 750 million or more in at least two of the previous four fiscal years.

The proposal recommends a pragmatic approach by allowing the use of local financial accounting standards for calculating the HKMTT.A minimum effective tax rate of 15% will be applied and the Undertaxed Profits Rule (UTPR) will be imposed as an additional tax using the equivalent adjustment approach.

To strike a balance between promoting tax fairness and avoiding undue compliance burdens, the proposal includes provisions for a de minimis exclusion, substance-based income exclusion, as well as relief for MNE groups in their initial phase of international activity.

Legislative approach
Hong Kong will adopt a hybrid legislative approach, directly incorporating the Model Rules into the Inland Revenue Ordinance (IRO) with limited adaptations. The enacted GloBE rules will be interpreted and applied in alignment with the Commentary and Administrative Guidance in force before the enactment.

To streamline the tax framework, the top-up tax under the GloBE or HKMTT regime will be treated as profits tax, integrating related provisions under the IRO instead of a separate Ordinance.

Specific provisions may be included to address the interaction between the enacted GloBE rules and the existing IRO provisions.

Effective fiscal year
The global minimum tax (IIR and UTPR) and HKMTT will become effective for fiscal years starting from 1 January 2025.

Residence
For the purposes of the GloBE rules and HKMTT, an entity is considered a Hong Kong resident entity if it meets one of the following conditions:

a) It is a company incorporated in Hong Kong or, if incorporated outside Hong Kong, is normally managed or controlled in Hong Kong; or
b) In other cases, it is an entity constituted under the laws of Hong Kong or, if otherwise constituted, is normally managed or controlled in Hong Kong.

2. **Safe Harbours**
   To provide businesses with tax certainty, the government is proposing two key safe harbour measures.

   The proposed transitional Country-by-Country Reporting (CbCR) safe harbour under the GloBE rules aims to ensure smooth transition, whilst the proposed inclusion of a permanent Qualified Domestic Minimum Top-up Tax (QDMTT) safe harbour in the legislation adds a long-term foundation.

3. **Tax compliance and administrative framework**
   In accordance with the tax framework, an in-scope MNE group is mandated to submit both an annual top-up tax notification and a top-up tax return through a dedicated electronic platform. The top-up tax notification must be filed within six months from the fiscal year-end, while the top-up tax return must be filed within 15 months (extended to 18 months for the transition year).

   To streamline the process, the MNE group has the option to designate a Hong Kong constituent entity to manage the tax filings and payment process on its behalf.

   No provisional top-up tax will be imposed, and upon receiving the Notice of Assessment, there is a two-week grace period for the payment of the top-up tax.

4. **Mandatory electronic filing of profits tax returns for in-scope MNE groups**
   The IRD proposes the introduction of mandatory e-filing of profits tax returns, which will specifically apply to in-scope MNE groups at the initial stage.

   To enforce this requirement, the IRD intends to issue a gazette notice, making it mandatory for all Hong Kong constituent entities of in-scope MNE groups to electronically file their profits tax returns starting from the year of assessment 2025/26 and subsequent years.

Key Takeaway
As the implementation of GloBE rules and HKMTT draws near, it is crucial for MNE groups to assess the potential impact on their business operations and proactively plan their strategies.

We strongly recommend a thorough review of the Hong Kong Government's Consultation Paper, which outlines the key considerations.

References
The Consultation Paper can be accessed via this link:
https://www.fstb.gov.hk/tb/tc/others/Consultation%20paper_Global%20minimum%20tax%20and%20HKMTT%20(Eng).pdf

How we can help

Embracing a client-centric approach, our Regional Tax Team is committed to delivering strategic tax and transfer pricing solutions, ensuring compliance and maximising opportunities for our clients across diverse tax jurisdictions.

Contact us! We look forward to assisting you in navigating the complexities of taxation in today's dynamic business landscape, driving financial success and building lasting partnerships.

Meet our Regional Tax Team:

Eunice Hooi
Managing Director Asia

Ade Teo
BoardRoom Singapore

Cheong Woon Chee
BoardRoom Malaysia

Candice Ng
BoardRoom Hong Kong

Ellen Zhuang
BoardRoom China

About BoardRoom

BoardRoom is Asia Pacific's leader in Corporate and Advisory Services with a strong and reputable 50-year track record. Headquartered in Singapore we are ranked amongst Forbes Asia's Top 200 Companies under a Billion. With our strong presence in the region, and a direct office presence in Singapore, Malaysia, Hong Kong, China and Australia, we are well positioned to support you.

Our smart business solution suite comprises of the following services:

- Global Tax & Accounting
- Regional Payroll
- Corporate Secretarial
- ESG Services
- Share Registry
- Employee Share Plans

Get in touch with us today to take your business further, faster.

Scan to learn more about our services.