

Comprehensive Double Taxation Agreement with India

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INTRODUCTION

On 19 March 2018, Hong Kong concluded a comprehensive double taxation agreement (“CDTA”) with India. This brings the total number of CDTA entered by Hong Kong with other jurisdictions to 39.

The CDTA will enter into force after both Hong Kong and India have completed their ratification procedures. This newsletter summarizes the key features of the CDTA that are applicable to Hong Kong residents.

KEY FEATURES

From the perspective of Hong Kong residents, the key features of the CDTA are as follows:

(1) Persons Covered

Individuals

Under the CDTA, an individual qualifies as a Hong Kong resident if:

- he ordinarily resides in Hong Kong; or
- he stays in Hong Kong for more than 180 days during a tax year or for more than 300 days in two consecutive tax years one of which is the relevant tax year.

Corporations

Companies incorporated in Hong Kong and companies incorporated outside Hong Kong but being normally managed or controlled in Hong Kong.

The protocol to the CDTA defines that a company is normally managed or controlled in Hong Kong if its executive officers and senior management employees make day-to-day key decisions in Hong Kong for the strategic, financial and operational policies for the company, and the staff of the company conduct in Hong Kong, the day-to-day activities necessary for making those decisions.

(2) Salaries Income

Income from employment

A Hong Kong individual is exempted from tax in India if he satisfies the following conditions:

- He is present in India for not more than 183 days in any 12-month period commencing or ending in the tax year;
- His remuneration is not paid by, or on behalf of, an employer who is a resident of India; and
- His remuneration is not borne by a permanent establishment or a fixed place which his employer has in India.

Directors' fees

Directors' fees derived by a Hong Kong resident in the capacity as a member of the board of directors of a company in India may be taxed in India.

(3) Business Income

Active business profits

Under the business profits article, only profits attributable to the permanent establishment maintained by a Hong Kong company in India will be subject to income tax in India.

Associated enterprises (Transfer pricing)

The CDTA contains an associated enterprises article which allows Hong Kong or India to make transfer pricing adjustments for transactions between associated enterprises. Such adjustments may give rise to potential double taxation. In such case, the article also provides that the tax

authorities are obliged to make an appropriate adjustment in order to relieve the double taxation.

(4) Capital Gains

Gains derived from the disposal of the following capital assets will be taxed in India:

- Immovable properties situated in India.
- Movable properties of a permanent establishment maintained by the Hong Kong enterprise in India.
- Shares of a company deriving more than 50% of its asset value directly or indirectly from immovable property situated in India.
- Shares in a company which is a resident in India.

Gains derived from the disposal of capital assets other than the above-mentioned may be taxed in each Hong Kong and India in accordance with the provisions of their respective domestic tax laws.

In other words, the CDTA does not provide any exemption to Hong Kong residents deriving disposal gains of capital assets which are taxable under the Indian domestic tax laws.

(5) Withholding tax on passive income

The relevant withholding tax rates for dividends, royalties, interest and fees for technical services under the CDTA are summarized as follows:

	<u>Dividend</u>	<u>Royalty</u>	<u>Interest</u>	<u>Technical fee</u>
HK non-treaty	0%	4.5% / 4.95% (Note 1)	0%	0%
India non-treaty	0%	10%	20% (Note 2)	10%
CDTA rate	5%	10%	10%	10%

Note 1 – 4.5% if received by an unincorporated business; 4.95% if received by a corporation.

Note 2 – The 20% rate applies in general whereas a lower rate applies for certain specified types of interest.

The CDTA only offers favorable withholding tax treatment on interest income paid out of India to Hong Kong.

(6) Income from international shipping transport

Under the CDTA, a Hong Kong enterprise derived in India from the operation of ships in international traffic may be taxed in India, but the tax imposed in India shall be reduced by 50 percent.

This differs from the provisions contained in most of the tax treaties concluded by Hong Kong with other jurisdictions where the profits derived from the operation of ships in international traffic is only taxed in the state of residence.

(7) Beneficial owner test and limitation on benefits

It should be noted that when claiming preferential withholding tax rates under the CDTA, the recipient has to satisfy the beneficial owner test, i.e. the recipient must



be the beneficial owner of the passive income.

The CDTA also contain provisions to counteract treaty shopping activities. If the main purpose or one of the main purposes of any person involved in the arrangement is to take advantage of the treaty benefits applicable to passive income, capital gain or other income, the treaty benefits will be denied.

(8) Exchange of information (“EOI”)

The EOI article provides that the competent authorities of Hong Kong and India shall exchange information that is foreseeably relevant for carrying out the provisions of the CDTA or to the administration or enforcement of the domestic laws of Hong Kong or India.

CONCLUSION

In 2017, India was Hong Kong's seventh largest trading partner and the total value of bilateral trade reached HK\$266 billion. Following the conclusion of the CDTA with India, 13 out of Hong Kong's top 20 major trading partners are CDTA partners, accounting for about 73% of Hong Kong's world trade. They are China, Japan, Korea, Thailand, Vietnam, Malaysia, United Kingdom, United Arab Emirates, Switzerland, Netherlands, France and Italy.



The content of this newsletter is only for general guidance on matters of interest and is not meant to be comprehensive. The application and impact of laws can vary widely based on the specific facts involved. Readers are advised to consult their tax advisors before making any business decisions.

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