

tax notes

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Hong Kong signs first comprehensive Double Tax Agreement with Belgium

On 10 December 2003 the Government of the Hong Kong Special Administrative Region (HKSAR) and the Government of the Kingdom of Belgium signed an Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital. Once approved the Agreement will be effective from 1 January 2004 in Belgium and 1 April 2004 in Hong Kong.

Although the Government of the HKSAR and the Central Government of the People's Republic of China entered into a Memorandum of Understanding for the avoidance of double taxation on income in February 1998 the Agreement with Belgium is the first comprehensive agreement for the avoidance of double taxation (DTA) which Hong Kong has signed with another country.

This represents the start of the realisation of the HKSAR's government policy over the last few years which was to establish a network of comprehensive DTAs with countries both in the Asia Pacific Region and Europe.

The DTA applies to the following taxes imposed by the Kingdom of Belgium:

Individual Income Tax, Corporate Income Tax, Income Tax on legal entities, Income Tax on non residents and Supplementary crisis contributions.

In the HKSAR it applies to the following taxes:

Profits Tax, Property Tax and Salaries Tax

The DTA applies to persons who are residents in either or both of Hong Kong and Belgium. For Hong Kong this means that it applies to any person who is resident in Hong

Kong for the purpose of Hong Kong taxation. A "person" for this purpose includes a company. The importance of residence in the DTA is that it adds a new dimension to Hong Kong taxation as the concept of residence has in the past played very little part in determining tax liabilities in Hong Kong due to Hong Kong's territorial or source system of taxation. The Inland Revenue Ordinance does not contain any definition of residence and the question of the residence of a person and a company has previously been derived from case law.

The protocol section of the DTA contains the following definitions of a Hong Kong resident.

Individual – (a) any individual who ordinarily resides in the HKSAR in any year of assessment; or (b) any individual who stays in the HKSAR for more than 180 days in a year of assessment or more than 300 days in two consecutive years of assessment, one of which is the relevant year of assessment.

Company – a company incorporated in the HKSAR or, if incorporated outside the HKSAR, having its central management and control in the HKSAR.



The main provisions regarding the taxation of income under the DTA are as follows.

- **Income from immoveable property** will be taxed in the country in which the property is situated.
- **Business profits.** A Hong Kong company which derives profits in Belgium will be subject to tax only in Hong Kong unless it carries on business in Belgium through a permanent establishment in Belgium, in which case it may be subject to tax in Belgium on the profits attributable to the permanent establishment.
- **Dividends** will be taxed in the country in which they are received. However, Hong Kong does not impose tax on dividends received from Belgium (or in fact from any other country). The advantage of the DTA for Hong Kong residents is that the rate of withholding tax on dividends will be reduced from a maximum of 25% to a maximum of 15% with no withholding tax if a Hong Kong resident company holds at least 25% of the Belgian company paying the dividend.
- **Interest income** will be taxable in the country in which it is received. Under Hong Kong's territorial system interest income with a Belgian source will not be subject to tax in Hong Kong. However such income will suffer Belgian withholding tax on the payment by the Belgian payer. Under the DTA this withholding tax will be reduced from 15% to 10%.
- **Royalties** are taxed in the recipient country.

Royalties with a Belgium source are not subject to tax in Hong Kong in the hands of the recipient. Under the DTA the rate of Belgian withholding tax on such royalties will be reduced from an effective rate of 12.75% of gross royalties to 5%.

Royalties paid by a Hong Kong company to a Belgian company are currently subject to withholding tax at the rate of 5.25% or 17.5% depending upon the category. Under the DTA the rate is reduced to 5% for all categories.

Please see our Tax Notes Issue 9 on the withholding taxes on royalties in Hong Kong.

- **Personal services** will be taxed in the jurisdictions on which the services are rendered. However there are exceptions to this which include payments to artistes and sportsmen.
- **Director's fees** – these will be taxed in the country in which the company paying the director's fees is resident. It should be noted that income received by directors which does not fall within the definition of director's fees will be considered to be for personal services and will be taxed accordingly.
- **Elimination of Double Taxation** – where income is subject to tax in both Belgium and the HKSAR, the DTA provides for relief to reduce or eliminate the double taxation. Hong Kong residents may use any Belgian tax paid on income as a credit to offset their Hong Kong tax liabilities on the same income. However the tax credit may not exceed the Hong Kong tax on that same income.

The DTA contains exchange of information provisions and Hong Kong has undertaken to exchange information with Belgium on taxpayers under Article 25 of the DTA. However whilst this exchange of information is a departure from Hong Kong's secrecy provisions, the DTA states that any information provided to the Authorities in Belgium can only be used by the Belgian Authorities and cannot be disclosed to any other jurisdiction without the prior approval of the HKSAR Authorities.

The DTA will now be subject to "negative vetting" by the Legislative Council in Hong Kong. If it passes this hurdle (which it is expected to do) then the agreement will become effective in Hong Kong from 1 April 2004.

The DTA offers a number of tax savings as well as a greater degree of certainty for Hong Kong residents doing business in Belgium. This treaty and its interpretation will therefore be an important factor in considering investments in Belgium by Hong Kong residents.

Should you have any queries regarding this DTA please contact David Southwood, Gary James or your normal Grant Thornton contact partner.

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