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Tax Newsflash

Hong Kong Tax News:
HK-Korea tax treaty in force

The comprehensive double taxation agreement between Hong Kong and Korea ("the HK-Korea Treaty"), which was signed on July 8, 2014, was finally ratified by the Korean National Assembly on September 7, 2016 without any change from the original agreement. As a result, the HK-Korea Treaty became effective from September 27, 2016 after the ratification notice was exchanged among the two parties.

The provisions of HK-Korea Treaty will have effect on (i) Hong Kong taxes from the year of assessment 2017/18 and (ii) Korean taxes from January 1, 2017 (or April 1, 2017 for taxes withheld at source).

Details of the HK-Korea Treaty can be found in this link.

The HK-Korea Treaty will prevent double taxation and tax evasion by the resident of one jurisdiction earning an income in the other, and to be more specific, Hong Kong resident individuals and corporations will likely be enjoying treaty benefits and also be relieved from double taxation (note that Korea adopts a complicated tax system compared to Hong Kong and imposes withholding taxes on various Korean source income).

Key Features

The table below shows withholding rates for dividends, interest and royalties under the HK-Korea Treaty as compared to the rates under the Korean domestic laws (i.e., in the absence of the HK-Korea Treaty).

Income	Withholding tax rate under Korean domestic laws (including local income tax)	Reduced rate under the HK-Korea Treaty
Dividends	22%	15% or 10% if the recipient company is beneficial owner which holds directly at least 25% of the capital of the company paying dividends
Interest	22% (15.4% for the interests from bonds)	10%
Royalties	22%	10%

As summarized above, the HK-Korea Treaty significantly reduces the withholding tax rates on dividends, interest and royalties paid by a Korean company to Hong Kong residents. However, the HK-Korea Treaty does not provide for exemption of tax on capital gains, which is the lessor of (i) 11% of gross sales proceeds or (ii) 22% of capital gains realized under Korean domestic laws. In the absence of the HK-Korea Treaty, Hong Kong investors generally would be subject to a 22% withholding tax in Korea (including tax on capital gains derived from the sale of shares in a Korean company).

Other Notable Implications

Tax residency

One of the important implications of the HK-Korea Treaty being ratified is relatively reduced risk for Hong Kong residents that frequently travel to Korea for business being taxed as a Korean tax resident under the Korean domestic tax rules.

Under the new provisions of the Individual Income Tax Law of Korea which became effective from 2015, a non-Korean resident would be treated as a Korean tax resident if the individual resides in Korea for 183 days or more over 2 consecutive calendar years (unless stay by such individual is temporary and for non-business purposes such as sightseeing or medical care).

Under the provisions of the HK-Korea Treaty, a Hong Kong tax resident who is also treated as a Korean tax resident under the Korean tax law may be able to avoid being taxed as a Korean tax resident under the “tie-breaker” provision in the HK-Korea Treaty. The "tie-breaker" provision is complicated. Readers are advised to seek professional advice.

Holding company jurisdiction

The HK-Korea Treaty may increase the attractiveness of Hong Kong as a holding company location for investments in Korea, especially as compared to Singapore, one of the favorite jurisdictions which multinational companies use to invest into Korea.

In the absence of the HK-Korea Treaty, Hong Kong investors generally would be subject to Korean taxes under the Korean tax laws. It should be noted that the HK-Korea Treaty,

provides similar or even better treaty benefits given under the Singapore-Korea Treaty*.

* The reduced rate on royalties under the HK-Korea Treaty (10%) is lower than that under the Singapore-Korea Treaty (15%).

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