



Risks of sale and purchase of properties by way of transfer of shares

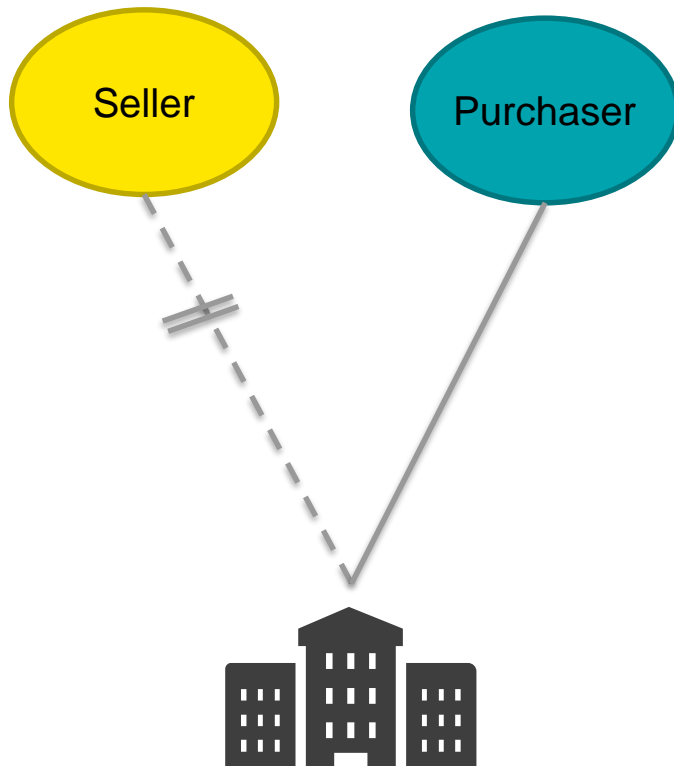
Wilson Cheng

Partner, Tax Leader, Hong Kong and Macau
Ernst & Young Tax Services Limited

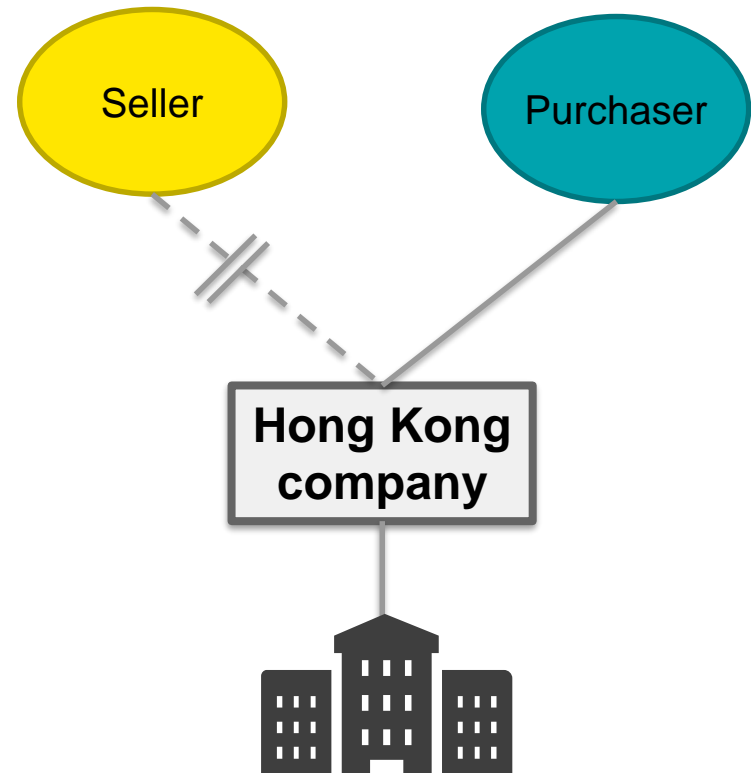
21 March 2023

Sale and purchase of properties: Direct transfer vs. Through the transfer of shares

Direct transfer



Share transfer



Content

- ▶ Tax implications and other considerations
- ▶ Potential tax risks and mitigation methods
- ▶ Latest update on S.45 intra-group stamp duty relief
- ▶ Q&A session

Direct transfer vs. Through the transfer of shares: Stamp duty considerations



Ad valorem stamp duty (AVD) on properties

Currently enacted rates				Current rates pursuant to Stamp Duty (Amendment) Bill 2023	
Value of the property (HK\$) ¹	Flat rate ²	Rates at Scale 1 ^{3,4}	Rates at Scale 2 ^{3,5}	Value of the property (HK\$) ¹	Rates at Scale 2 ^{3,6}
Below \$2M	15%	1.50%	\$100	Below \$3M	\$100
\$2M – \$2.2M (Scale 1) \$2M – \$2.4M (Scale 2)		\$30,000 + 20% of excess over \$2M	\$100 + 10% of excess over \$2M	\$3M – \$3.5M (Scale 2)	\$100 + 10% of excess over \$3M
\$2.2M - \$3M (Scale 1) \$2.4M - \$3M (Scale 2)		3%	1.5%	\$3.5M - \$4.5M (Scale 2)	1.5%
\$3M – \$3.3M		\$90,000 + 20% of excess over \$3M	\$45,000 + 10% of excess over \$3M	\$4.5M – \$4.9M	\$67,500 + 10% of excess over \$4.5M
\$3.3M – \$4M		4.5%	2.25%	\$4.9M – \$6M	2.25%
\$4M – \$4.4M		\$180,000 + 20% of excess over \$4M	\$90,000 + 10% of excess over \$4M	\$6M – \$6.6M	\$135,000 + 10% of excess over \$6M
\$4.4M – \$6M		6%	3%	\$6.6M – \$9M	3%
\$6M – \$6.7M		\$360,000 + 20% of excess over \$6M	\$180,000 + 10% of excess over \$6M	\$9M – \$10M	\$270,000 + 10% of excess over \$9M
\$6.7M – \$20M		7.5%	3.75%	\$10M – \$20M	3.75%
\$20M – \$22M		\$1,500,000 + 20% of excess over \$20M	\$750,000 + 10% of excess over \$20M	\$20M – \$22M	\$750,000 + 10% of excess over \$20M
Over \$22M		8.5%	4.25%	Over \$22M	4.25%

Note:

1. The value of property is rounded to the nearest hundred thousands.
2. Applicable to agreements for sale and purchase of **residential** property signed on or after 5 November 2016.
3. Marginal relief is available.
4. Applicable to agreements for sale and purchase of **non-residential** property signed on or after 23 February 2013 but before 26 November 2020.
5. Applicable to agreements for sale and purchase or transfer of **non-residential** property executed on or after 26 November 2020 but before 11am on 22 February 2023. Applicable to agreements for sale and purchase of **residential** property signed on or after 23 February 2013 but before 11am on 22 February 2023 if specific conditions are fulfilled.
6. Applicable to agreements for sale and purchase or transfer of property executed on or after 11am on 22 February 2023 if specific conditions are fulfilled.

Other stamp duty on residential property transactions

Special Stamp Duty

Payable when it is:

- a) A residential property transaction; and
- b) Disposed within 36 months

SD rate depends on holding period:

- <7 months: 20%
- 7-12 months: 15%
- 13-36 months: 10%

Buyer's Stamp Duty (BSD)

Payable when it is:

- a) A residential property transaction; and
- b) Purchased by a non-HK resident or corporation

SD rates:

15%

Note: Applicable to residential property acquired on or after 27 October 2012 (Source: [https://www.gov.hk/en/residents/taxes/docs/IRSD123\(E\).pdf](https://www.gov.hk/en/residents/taxes/docs/IRSD123(E).pdf))

Agreements on or after 19 October 2022:

If eligible incoming talents become HK permanent residents, they may apply for refund of extra AVD and BSD paid for purchasing their first residential properties in HK, which are still held by them at the time of application

Stamp duty on sale and purchase of HK stock

Hong Kong stock

Stock transfer is required to be registered in HK (e.g., listed on HKEX, incorporated in HK)

Stamp duty rate

0.13% for each bought note and sold note

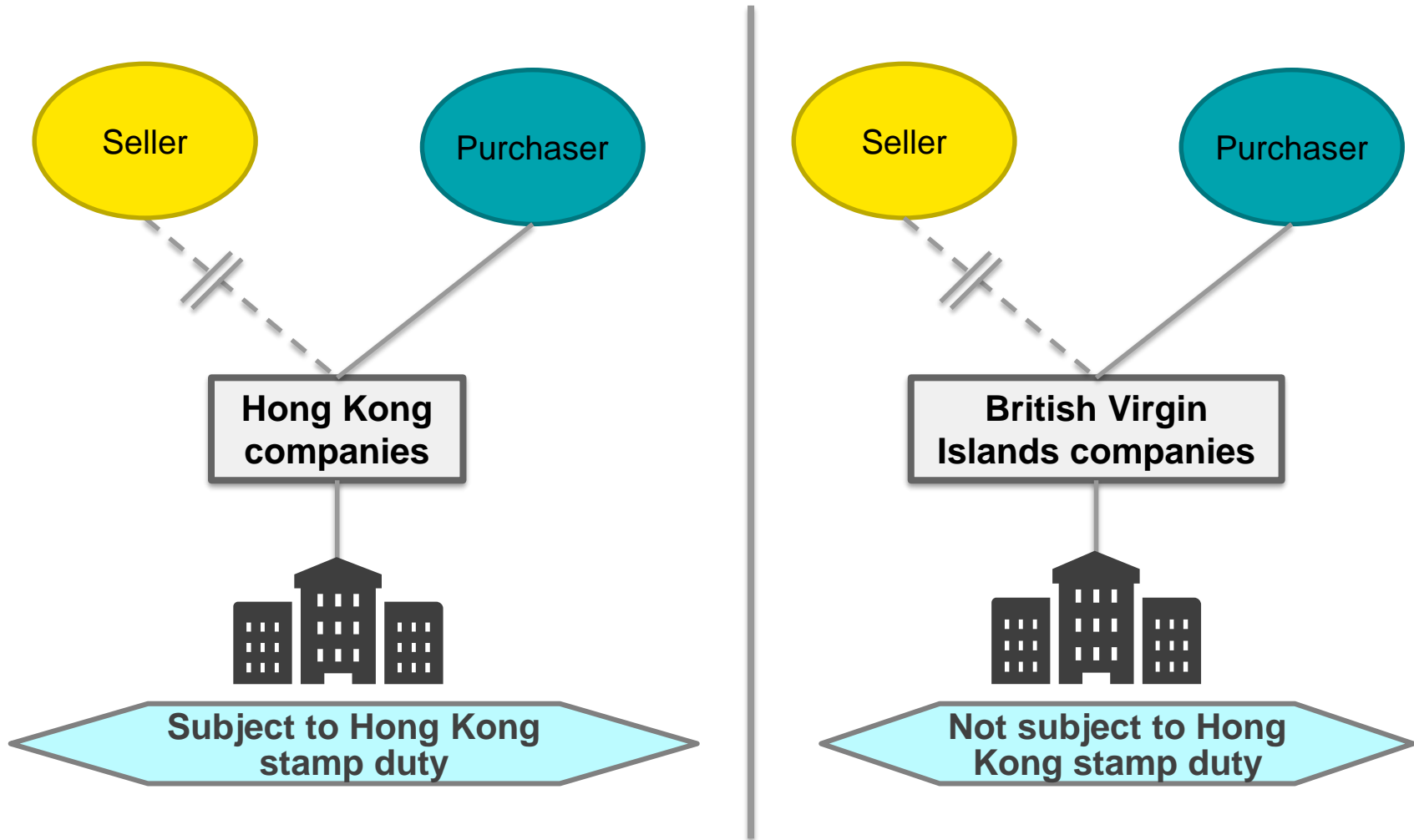
Liable person

Purchasers and sellers are jointly liable

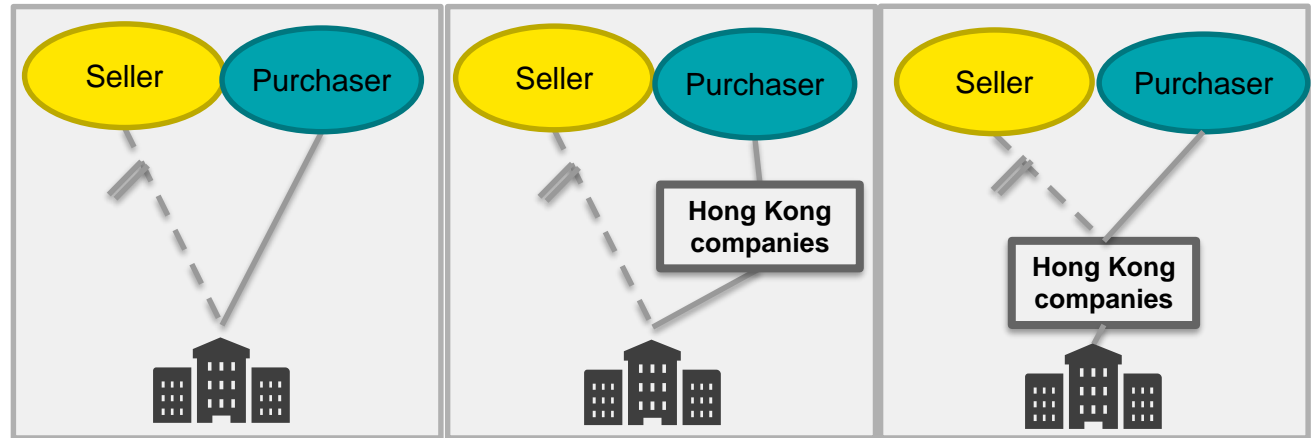
Time limit

- Within 2 days if effected in HK;
- Within 30 days if effected elsewhere

Hong Kong stock vs. Non-Hong Kong stock

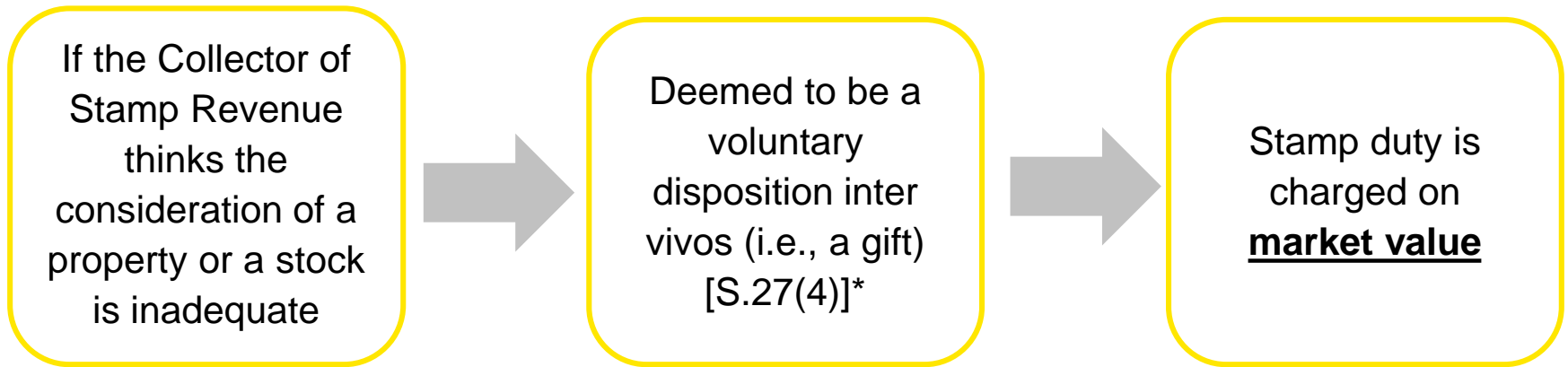


Comparison of Hong Kong stamp duty



	Purchased directly by an individual	Purchased directly by a company	Transfer of shares
Ad Valorem Stamp Duty on properties	Scale 2/15%	15%	-
Stamp Duty on Hong Kong stock	-	-	0.13% @ bought/sold note (0.26% total)
Buyer's Stamp Duty	0%/15%	15%	-
Special Stamp Duty	10%/15%/20%	10%/15%/20%	-

Inadequate consideration



*This Ordinance applies to non-related transactions – *Lap Shun Textiles Industrial Co Ltd v Collector of Stamp Duty 1 HKTC 880*

Deemed consideration under S.24

Anti-avoidance measure to tackle transactions with disguised consideration

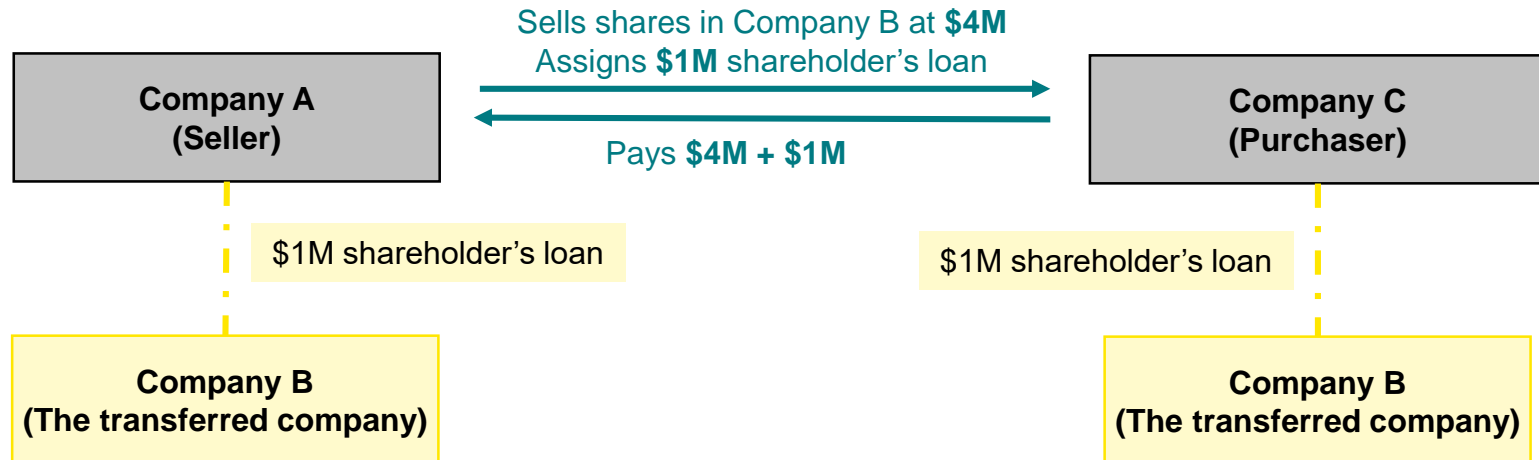
- ▶ Examples:
 - ▶ Discharge of a debt due to the purchaser
 - ▶ Payment of vendor's debt by purchaser to a third party
 - ▶ Payment by the purchaser to a third party (specified by the vendor)

Limitation

- ▶ Payment is independent of the subject sales and purchase transaction
- ▶ Disregard liabilities inherent in the property or stock (e.g., rent payable under a lease)

Deemed consideration under S.24

Example 1

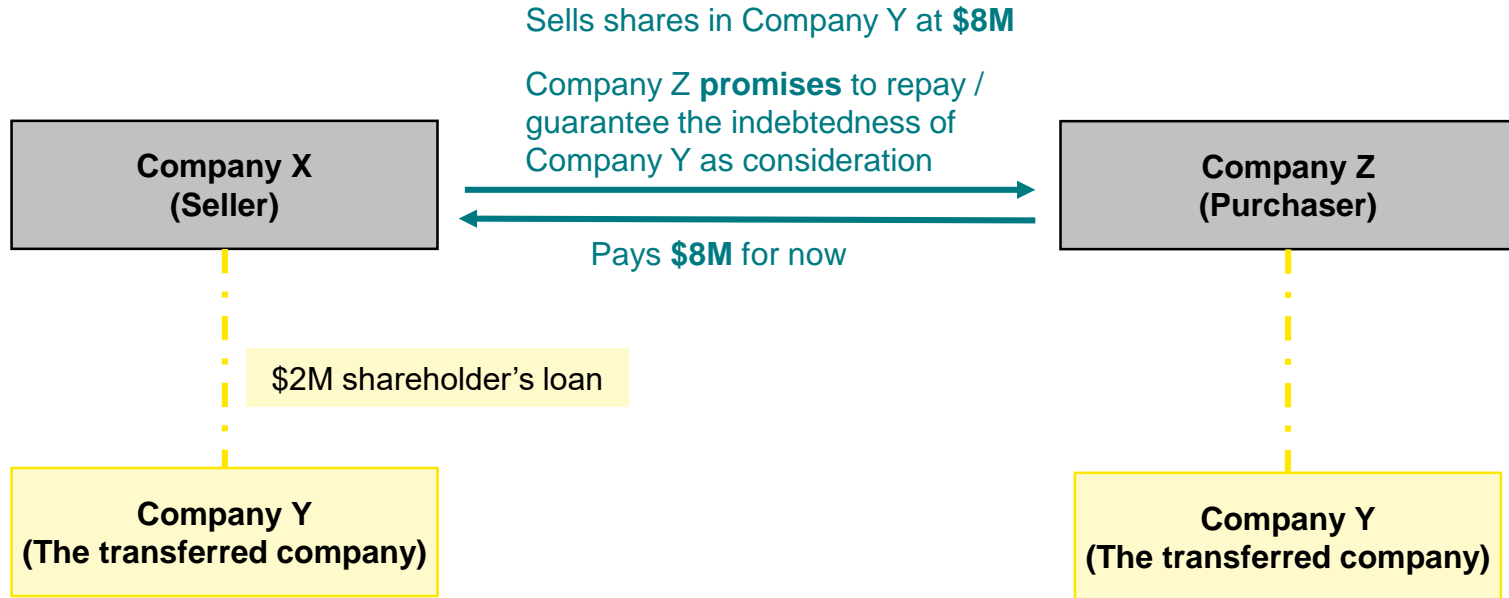


Chargeable consideration of stamp duty: **\$4 million + \$1 million**

Company C can only obtain the shares in Company B upon payment of the relevant sum.

Deemed consideration under S.24

Example 2



Chargeable consideration of stamp duty: **\$8 million + \$2 million**

As an integral part of the arrangement to purchase the shares, Company Z agrees to procure or guarantee that a loan due by Company Y to Company X will be repaid

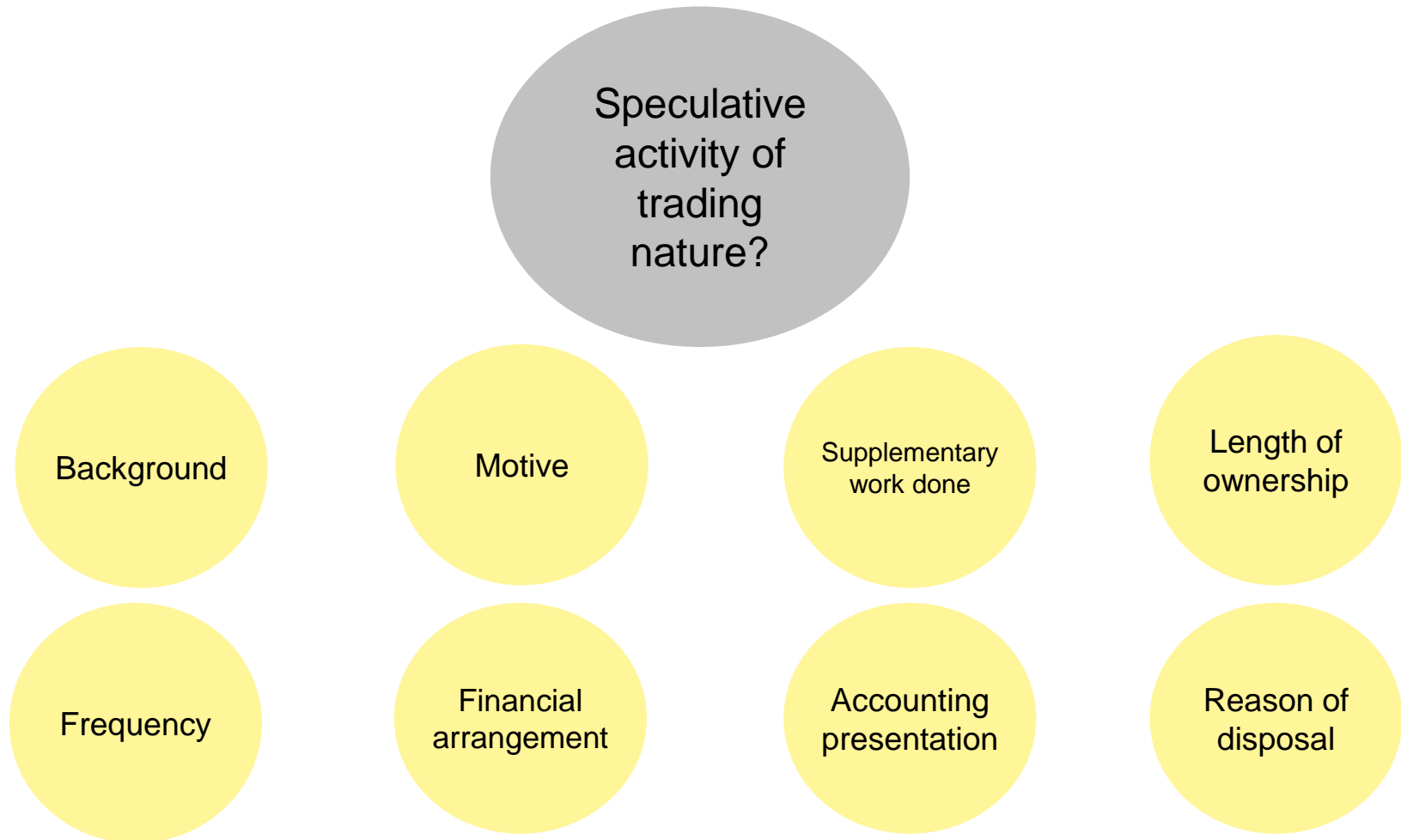
Direct transfer vs. Through the transfer of shares between companies (as seller and as purchaser) Profits tax considerations



Direct transfer vs. Through the transfer of shares

From the seller's perspective

1. Whether gain from disposal of property or share is chargeable to Profits Tax



Direct transfer vs. Through the transfer of shares

From the seller's perspective

2. Basis for calculating depreciation allowances on assets if held by a company

Direct transfer

Balancing charges may arise upon disposal on which depreciation allowance was previously granted

Share transfer

No additional tax with regard to the depreciation allowances

Direct transfer vs. Through the transfer of shares

From the purchaser's perspective

1. Interest expense on loan for purchase

Direct transfer

Generally, deductible.
Because it is incurred in the production of the purchaser's chargeable profits.

Share transfer

Generally, not deductible
Because it is not incurred in the production of the purchaser's chargeable profits (only generate non-taxable dividend income).

Direct transfer vs. Through the transfer of shares

From the purchaser's perspective

2. Basis for calculating depreciation allowances on assets

Direct transfer

Calculation basis may vary (e.g., furniture).
Generous depreciation allowances of up to 72% of the capital expenditure incurred in the year of purchase.

Share transfer

Calculation basis remains unchanged regardless of the consideration for the share transfer.

Direct transfer vs. Through the transfer of shares

From the purchaser's perspective

3. Tax loss

Direct transfer

N/A

Share transfer

Retained and carried forward in the transferred company indefinitely
(Unless the sole or primary purpose is to exploit the losses in order to avoid tax liability / to reduce tax)

Direct transfer vs. Through the transfer of shares

From the purchaser's perspective

4. Tax computation of rental income

Direct transfer

Purchaser is subject to profits tax on rental income

(Actual income - All deductible business expenses) x 16.5%

Share transfer

The transferred company is liable to profits tax on rental income

What if the properties / shares are purchased by individuals instead?

4. Tax computation of rental income

Direct transfer

Individuals, who purchase and hold properties directly, are subject to property tax on rental income

Property Tax Computation

	HK\$	
Rental income*	240,000	A
Less: Irrecoverable rent	<u>(20,000)</u>	B
	220,000	C = A + B
Less: Rates paid by owner(s)	<u>(6,000)</u>	D
	214,000	E = C + D
Less: Statutory allowance for repairs and outgoings**	<u>(42,800)</u>	F = E x 20%
Net assessable value***	171,200	G = E + F
Property tax (@15%)	25,680	

*Includes:

- ▶ gross rent received or receivable;
- ▶ sums previously deducted as irrecoverable rent and now recovered; and
- ▶ lump sum premium

**Broad-brush deduction every year.

***If personal assessment is selected, deductions can be claimed for mortgage interest paid for purchase of property

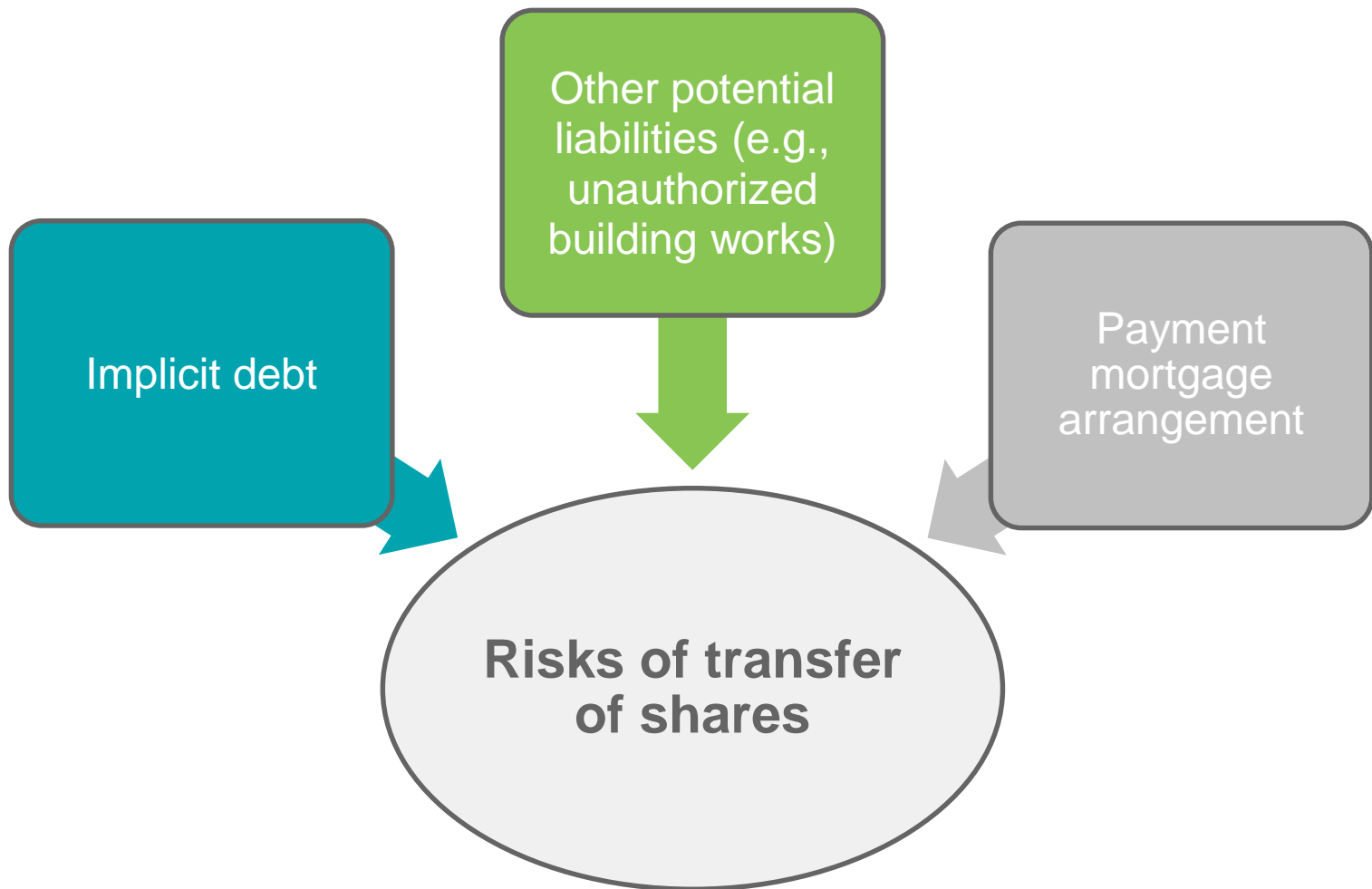
Share transfer

The transferred company is liable to profits tax on rental income

The potential tax risks and mitigation methods under the Property Transfer Arrangement



Risks of transfer of shares



Mitigation methods

▶ Engage professionals

- ▶ - Review the financial accounts
- ▶ - Conduct "due diligence" to ensure the companies have no implicit debt

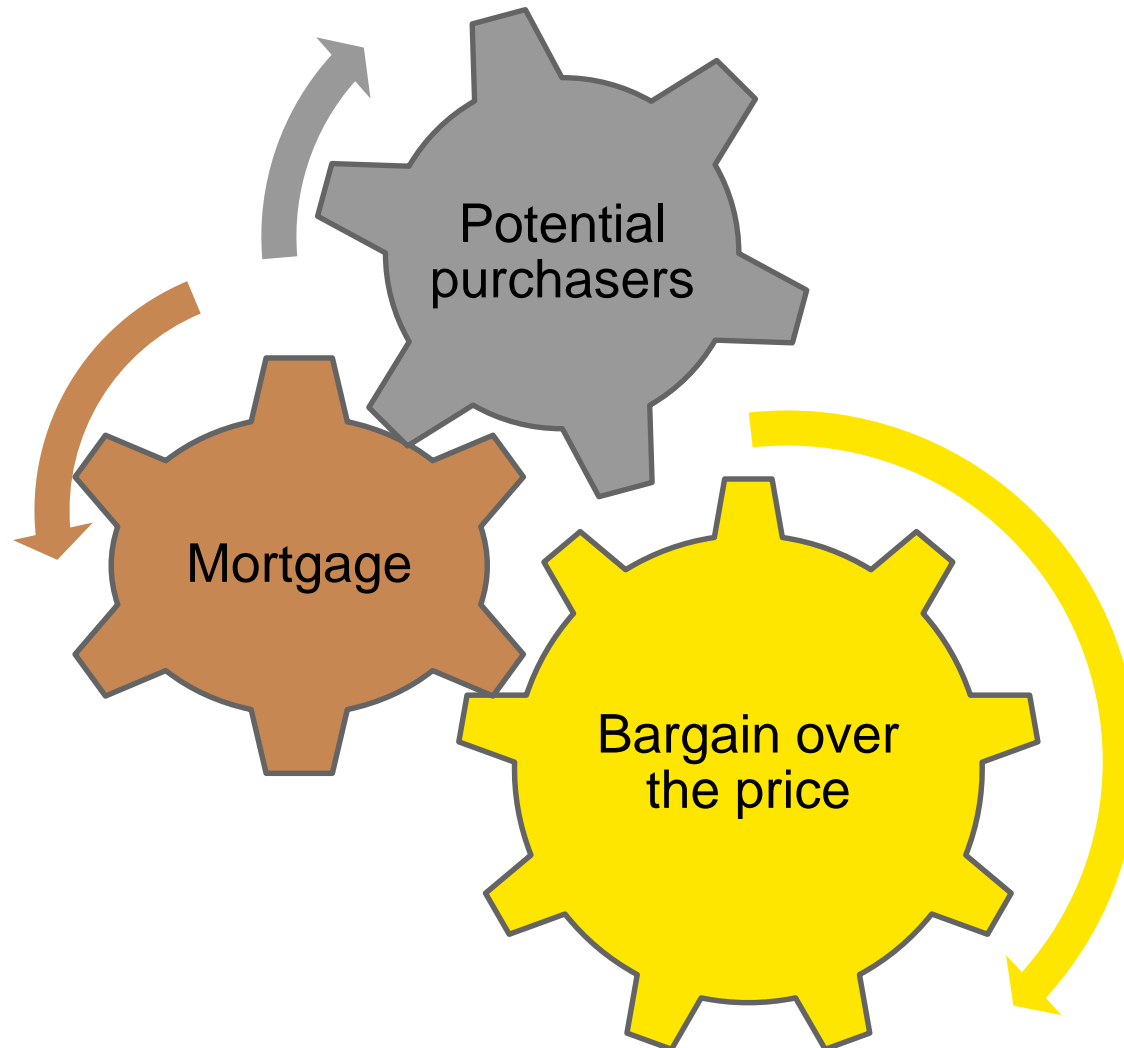
▶ Inclusion of a guarantee clause in agreement

- ▶ - Require sellers to guarantee the payment for any undiscovered liabilities

Inclusion of a cooling-off period in the agreement

During the period, the purchasers can terminate transactions and recover deposits if it is discovered that the property holding companies have implicit debts

Other considerations



S.45 intra-group stamp duty relief

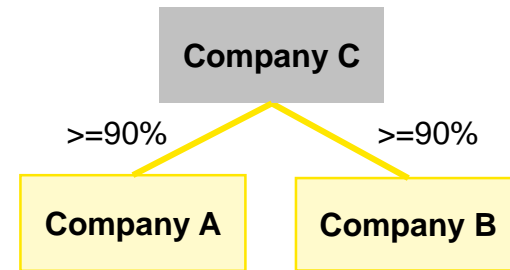
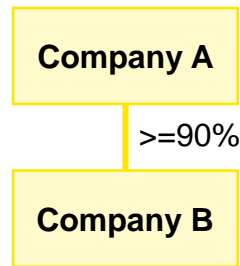


S.45 of the Stamp Duty Ordinance

Intra-group relief available for the transfer of immovable property or HK stock from one associated body corporate to another

Association is satisfied by either of the followings:

- ▶ (1) one is beneficial owner of not less than 90% of the issued share capital of the other
- ▶ (2) a third such body is beneficial owner of not less than 90% of the issued share capital of each Transferor and Transferee



Limited liability partnerships are also entitled to intra-group relief under S.45, pursuant to the decision in *John Wiley & Sons UK2 LLP and Wiley International LLC v Collector of Stamp Revenue DCSA 2/2021*.

Stamp Duty Group Relief - Misunderstanding

Disassociation Arrangement [S45(4)(c)]

- Relief **NOT** apply for arrangement under which the transferor and the transferee were to **cease to be associated** by reason of a **change** in the percentage of the **issued share capital of the transferee** in the beneficial **ownership of the transferor** or a **third body corporate**.

Deemed Relief Withdrawn [S45(5A)]

- Where a transferor and transferee cease to be associated **within two years** after the date of execution of the instrument, the relief is **deemed to be withdrawn**.

Q&A session



EY | Building a better working world

EY exists to build a better working world, helping create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients, nor does it own or control any member firm or act as the headquarters of any member firm. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. EY member firms do not practice law where prohibited by local laws. For more information about our organization, please visit ey.com.

© 2023 Ernst & Young Tax Services Ltd. All Rights Reserved.

APAC no. 03015694
ED None.

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, legal or other professional advice. Please refer to your advisors for specific advice.

ey.com/

Follow us on WeChat
Scan the QR code and stay up to date with the latest EY news.

