How Will the IRD Review of NGOs Impact Me?

Asian Charity Services
10 August 2021
Our speakers

Kenneth Wong
Leader
— Hong Kong Tax Controversy Services
+852 2289 3130
philip.ft.hung@hk.pwc.com

Philip Hung
Director
— Hong Kong Tax Controversy Services
+852 2289 3130
philip.ft.hung@hk.pwc.com

Felix Tsang
Senior Manager
— Hong Kong Tax Controversy Services
+852 2289 3881
felix.wv.tsang@hk.pwc.com
Agenda

1. Developments in tax environments of charities
2. Current IRD reviews on NGOs and NGOs’ common misconceptions leading to tax problems
3. Way forward
4. Q&A
Developments in tax environment of charities
**Sequence of events – IRD’s review on charities**

<table>
<thead>
<tr>
<th>Time</th>
<th>Event</th>
</tr>
</thead>
</table>
| 2016 | • Court of Final Appeal decision in *Sheng Kung Hui* case  
• Audit Commission reviews IRD’s practice on administering charities |
| 2017 | • IRD commenced reviews on charities tax exemption status under S. 88 of the IRO  
• PwC TCS team set up a charity task force |
| 2019 | • PwC meeting with DCIR and IRD Charities team on draft guidelines and assessing practice  
• IRD issued new guideline on charities |
| 2020 | • PwC providing suggestions to DCIR on the revised guideline on charities  
• IRD issued revised guideline on charities  
• IRD’s letter specifying FSTB contact for future S.87 petition on other issues |
| 2021 | • Certain foundation cases and university cases referred to tax audit team |
Current IRD reviews on NGOs and NGOs’ common misconceptions leading to tax problems
**All profits used for charity = exempt?**

**IRD’s tax guide for charities:**
A charity carrying on a business is chargeable to profits tax unless all of the following conditions are satisfied:

<table>
<thead>
<tr>
<th>Expense side</th>
<th>Income side</th>
<th>Consequence if not meet</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entity level qualify for S.88 exemption?</td>
<td>If entity qualifies for S.88 exemption:</td>
<td>• Specific income not exempt:</td>
</tr>
<tr>
<td>• For public benefit?</td>
<td>Each activity is evaluated separately and profit exempt only if all 3 conditions are met:</td>
<td>• Tax on that income</td>
</tr>
<tr>
<td>• All funds used for charity?</td>
<td>Each activity evaluated separately:</td>
<td>• Penalty on tax undercharged?</td>
</tr>
<tr>
<td>• Active / dormant?</td>
<td>a. Profit solely used for charity AND b. Profit substantially used in HK AND c. (i) business is “carrying out” object; or (ii) Business is carried out by beneficiaries.</td>
<td>• Penalty on non-compliance?</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Which units within the IRD?</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Other points to note:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>≠ lose overall exemption?</td>
</tr>
<tr>
<td></td>
<td></td>
<td>≠ all other income taxable?</td>
</tr>
<tr>
<td></td>
<td></td>
<td>≠ affect donation deduction?</td>
</tr>
</tbody>
</table>
Case sharing 1: Activities exercised in “carrying out objects?” *

XYZ group

Charity XYZ (object: help under-privileged children)

Donation
Reimburse expenses

Shop A
Second hand books donated to XYZ

Shop B
New books and souvenirs

Property C
Spare office units for rental

Investment D
Discretionary a/cs HK listed shares

Investment E
Diversified investment fund

Restaurant F
Mainly staffed by part time students

Restaurant G
Mainly staffed by senior citizens

- Profits all used for charitable purposes in HK
- “Object” clause includes running shops, property rental, investments and restaurants
- Are the shops / property rental / investments / restaurants considered “carrying out objects”?
- Mitigation measures?

* The above examples are extracted from various real life cases
**Case sharing 2: Directors’ remuneration & dormant charity**

**Expense recharge? Director fee?**

**Listed group**

Donation

**Charity XYZ**

(object: help under-privileged children)

**Expense breakdown**
- Stationery
- Salaries
- Director fees
- Rental etc

**Shop A**
Second hand books donated to XYZ

**Shop B**
New books and souvenirs

**Property C**
Spare office units for rental

**Investment D**
Discretionary a/cs HK listed shares

**Investment E**
Diversified investment fund

**Restaurant F**
Mainly staffed by part time students

**Restaurant G**
Mainly staffed by senior citizens

**IRD’s tax guide for charities:**
Director remuneration only allowed in exceptional circumstances:

a. Special qualifications not otherwise available; AND

b. Number of remunerated directors must be less than majority of quorum; AND

c. Remunerated directors must be absent from discussions about their remunerations.

**Disallow donation deduction after 2015?**

**S.88 status granted in 2000**

**Ceased operation** since 2018

Reviewed by the IRD in 2018

S.88 status cancelled from 2015

**Expense recharge? Director fee?**

* The above examples are extracted from various real life cases
Way forward
Way forward

Stay alert to new developments

1. Restructure / segment accounts for taxable operations
2. Restructure HK / Non-HK charities
3. Explore Section 87 exemption or other alternatives within IRO
4. Health check
5. Prepare defence file
6. Voluntary disclosure
Q&A

Thank you!

This content is for general information purposes only, and should not be used as a substitute for consultation with professional advisors. PwC has no obligation to update the information as law and practices change. The application and impact of laws can vary widely based on the specific facts involved. Before taking any action, please ensure that advice specific to your circumstances is obtained.

© 2021 PricewaterhouseCoopers Limited. All rights reserved. PwC refers to the Hong Kong member firm, and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.