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Structuring and Locating an IHQ in Hong Kong To Create a Tax Efficient Strategic Advantage in a Growth Plan

Source: JFU | Digital Tools
14 May 2025

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Hong Kong (HK) has long been an international business centre and has been able to form unique institutional advantages through learning from best practices adopted by the international business communities that HK serves over many decades.

This Note discusses HK's value proposition for setting up an international headquarters (IHQ) in Hong Kong to create a tax efficient strategic edge, capitalizing on HK's institutional advantages. It is written from the perspective of Chinese companies or entrepreneurs who can benefit from setting up an IHQ operation in the country's special administrative region. The discussion and intended benefits are also relevant to foreign companies and entrepreneurs.

It is important to emphasize that any tax planning must be integrated with genuine strategies designed to achieve business success. The IHQ should be considered as an integral part of a business' overall growth and enhancement strategy.

Valuable IHQ Functions

Here are the roles that an IHQ can effectively play in HK and contribute to the overall success of the business. These functions can be overlap, creating synergies within the organization.

- Strategic Planning & Corporate Governance (SPCG)

The IHQ serves as the central hub for developing and executing the organization's global strategy. This includes market analysis, identifying emerging opportunities, setting organizational goals and targets, and overseeing overall business performance.

Corporate governance functions, including development and compliance with international standards and best practices, can also be centralized in the IHQ.

- Finance & Treasury Management (FTM)

Managing the group's finances, including global cash flow, foreign exchange risk, and investment activities, is a critical function. This involves opening and managing multi-currency accounts, optimizing tax strategies, and ensuring compliance with relevant regulations. The IHQ can be empowered to manage relationships with international banks and financial institutions.

- Mergers & Acquisitions and Investment Management (M&A)

Identifying and executing strategic acquisitions, joint ventures, and other investments outside of Mainland China. This involves due diligence, negotiation, and post-acquisition integration. The IHQ manages investment portfolios and seeks out new investment opportunities aligned with the company's global strategy.

- Sales & Marketing (SM)

Developing and implementing global marketing strategies, managing international sales channels, and building brand awareness in target markets. This may include establishing regional sales offices or partnering with distributors.

- Innovation and Development (IND)

Establishing a development centre in HK to leverage the city's access to information on trends and technologies. This could involve developing new products and services tailored to the domestic and international markets or adapting existing products to meet evolving requirements.

- Supply Chain Management (SCM)

Coordinating global supply chains, sourcing materials and components from international suppliers, and managing logistics and distribution networks to optimize efficiency and delivery schedules.

- Human Resources (HR)

Managing international assignments, including recruitment, training, compensation, and benefits. Ensuring compliance with local labour laws and regulations in different countries. Facilitating the movement of personnel between different locations.

- Legal & Compliance (L&C)

Ensuring compliance with all relevant laws and regulations, including anti-corruption laws, trade regulations, and data privacy laws. Managing legal risks and disputes.

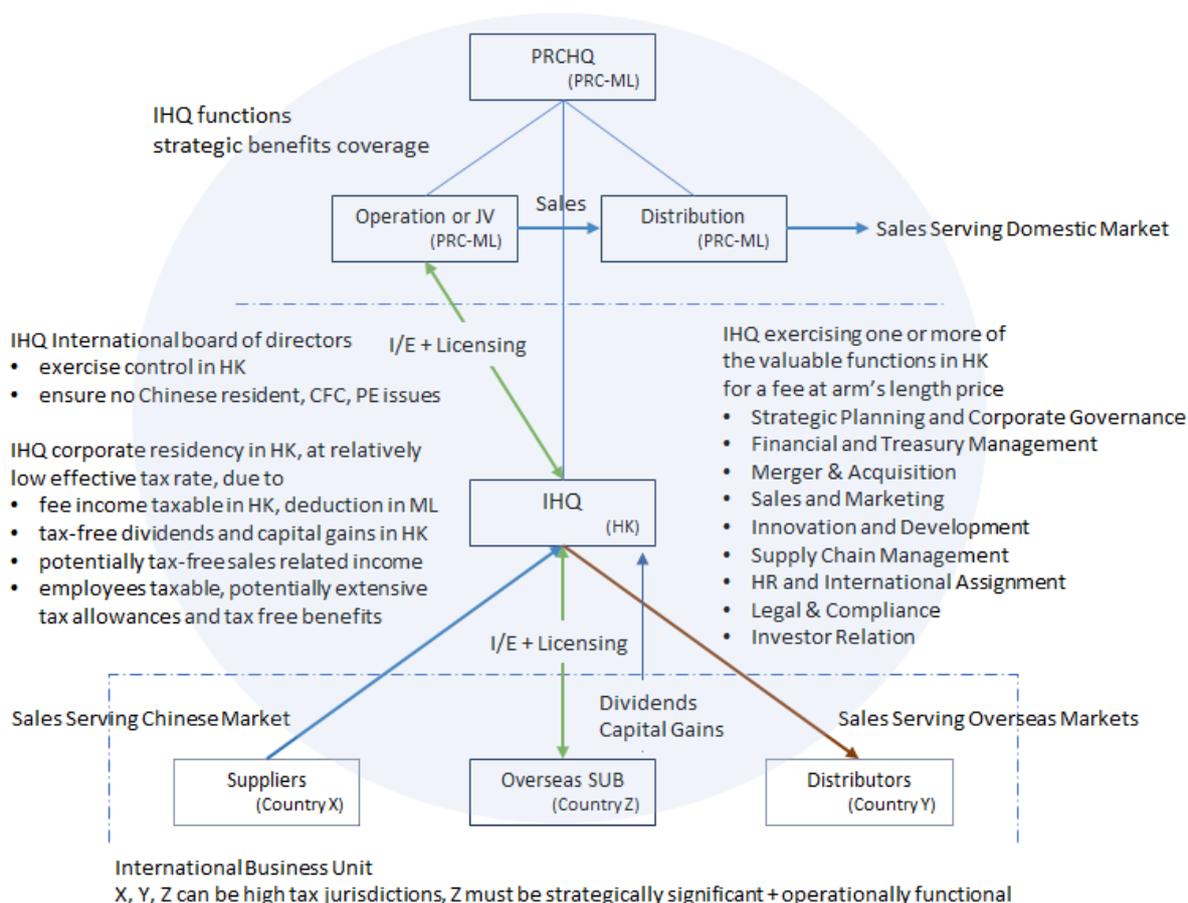
- Investor Relations (IR)

Communicating with potential investors, providing financial updates, and promoting the company's investment profile.

Tax Efficient IHQ Structure

There are special tax concessions that HK offers to promote certain sectors or operations such as development and exploitation of patents, private equity firms and family offices. However, the primary tax advantages that HK offers lie in the tax system itself – limited indirect taxes, low direct tax rates, generous capital expenditure deductions, tax-free dividends, capital gains, and offshore profits from international operations.

The following diagram is a simplified tax efficient IHQ structure that entrepreneurs may use to build strategic and operational advantages, accumulate earnings, and reinvest for the future.



Basically, the IHQ bridges the gap, integrates the domestic and international markets, and creates a platform for running valuable functions vital for the success of the business. Its modus operandi and transactional formats are structured to capture earnings tax efficiently, leveraging HK's unique tax features.

The narratives in the diagram highlight and suggest ways (e.g. constitution of an international board) to address typical home-country tax issues – corporate residence, controlled foreign corporation (CFC),

permanent establishment (PE), pricing for related party transaction (TP). This requires more thorough treatment before the concept is finalized for detailed planning, programming, and documentation.

Risk Management

As with all business planning and decision making, the importance of risk management cannot be overemphasized.

Compliance Risks. International operation and associated tax planning require a sufficient degree of management sophistication. This means that the management must understand, respect, and comply with related technical rules as well as ethical standards including anti-corruption, fair trade, currency regulation, tax accounting requirements, and tax treaty rules on international issues. Documentation must be carefully compiled on a contemporaneous basis at all stages in the process of planning and execution. That can establish credibility and avoid disputes if good documentation can be readily available in dealing with any competent authorities.

Operational Risks. All business operations are inherently high-risk and there are added dimensions of complexity for international operations. This is the reason for which we highlight the importance of institutional advantages that HK can provide in support of IHQ operations.

HK's institutional advantages are embodied not only in the institutions but in the professionals who run the institutions – the lawyers, bankers, engineers, accountants, and many others, particularly the local entrepreneurs, business owners and professional managers who can provide valuable industry specific experiences, and who are also well-versed in international business practices.

Financial Risks. HK is a renowned financial centre that provides sophisticated banking and financial services for the IHQ to manage its foreign exchange, credit, and other financial risk exposure effectively.

Reputational Risks. One of HK's institutional advantages is the honour system, transparent and rule-based business practices. This is fundamentally important for companies to build and reinforce credibility, corporate brands, and reputation.

International Assignment and Migration Schemes

For international business operation to be successful, it is important to build a highly competent team of international assignees who can learn and execute their assignments proficiently.

Many assignees consider HK as one of the best places for hosting their international assignments. Effective tax rates are exceptionally low by international standards due to very generous tax treatments for employment benefits. Younger and outgoing assignees also find HK very electrifying and convenient to travel around. Thanks to recent economic adjustments, the cost of living and space of accommodation in HK have also been significantly improved.

There are several migration schemes promulgated to attract assignees coming and settling in HK with their dependents, including the merit-based Quality Migrant Admission Scheme (QMAS) and the Admission Scheme for Mainland Talents and Professionals (ASMTP).

Concluding remarks

HK has presented the world many amazing stories of economic success including its catalytic role in the rise of the Chinese economy. HK did well in that story because it brought together peoples' hearts and minds, building understanding and sharing common successes. HK has a lot of experiences in doing it again in a world now full of bizarre challenges.