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# *Strengthen your resilience to Inland Revenue Department's (IRD) review on charitable organisations*





## Preventing from being targeted by IRD, and handling tax disputes effectively

Charitable organisations have recently been under the media’s spotlight. Reported irregularities have sparked public concern over the governance of charities and have attracted the attention from Government departments.

In this regard, the Inland Revenue Department (“IRD”) has tightened its grip on charitable organisations and commenced reviewing their tax exemption status.

Resolving tax disputes divert an organization’s resources which would otherwise be applied on charitable work,

unresolved disputes may even result in unnecessary litigation.

In view of the above, charities should take extra care in ensuring that their mode of operations and any activities carried on comply with the IRD’s latest practice on administering charities.



## Changing regulatory requirements faced by charities

### Charities in media spotlight

- Media coverage on certain charities’ non-compliance incidents
- Public’s increased expectations on charity governance

- Report issued in December 2013 recommending 18 changes in regulations governing charities
- Recommendations include increasing IRD’s resources on reviewing charities’ accounts

### Impact

- IRD increases its scrutiny on charities
- More serious consequences for non-compliance

### Recommendations from the Law Reform Commission

### Audit Commission’s review on the IRD

- Report issued in April 2017 suggested giving the IRD the authority to cancel non-compliant charities’ tax exemption status
- Suggested increasing IRD’s resources in reviewing charities

- From May to June 2017, the Commissioner of Inland Revenue was requested by the Legislative Council (LegCo) to explain the IRD’s procedures in handling non-compliant charities

### LegCo’s challenges on the IRD’s Commissioner



## Types of tax reviews on charities and common areas of dispute

- Focuses on reviewing tax exemption status of charities

**Charity Section 88 Review**

**Unit 1 Profits Tax**

- Processes profits tax filings and assesses tax liability of charities
- Reviews the nature of income and expenditure of charities

### Tax reviews on charities

- Charities' obligations as an employer
- Staff / Contractors' individual tax issues

**Unit 2 Individual Tax**

**Unit 4 Tax Audit**

- Reviews specific tax matters in charities' accounts
- Deals with voluntary disclosures



## Common areas of dispute

Business profits	Directors' remuneration	Expenses not meeting charitable objectives	Charitable activities outside Hong Kong
Property rental income and disposal gain	Staff salaries tax issues	Related party transactions	
Securities investment gain	Employer's obligations		
Donations in return for goods / services			



## Possible consequences if not handled properly

<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>
Profits partially or fully subject to tax	Directors requested to refund remunerations	Additional salaries tax for staff	Penalties and interests	Diversion of organisation's resources to deal with IRD	Reputation risks	Cancellation of S.88 tax exemption of status for serious cases



## *Possible actions*

**1**

### *Planning and ongoing health check*

- Review if organisation structure meets IRD requirements
- Defense files to prepare for documentary evidence required in IRD's review
- Annual and ongoing review / health check of activities and operations to identify and rectify any deficiencies
- Compliance check on employee remunerations

**2**

### *Handling IRD's review*

- Identify potential risks and key issues
- Formulate strategies against IRD review
- Follow up and provide documentary evidence
- Negotiate with IRD to resolve disputes

**3**

### *Remedial actions*

- Restructure to comply with IRD requirements
- Revise Articles of Association if necessary
- Review corporate governance and internal control policies
- Internal policies documentation and establish risk management framework
- Seek professional advice as necessary

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[www.pwchk.com/en/services/tax/hong-kong-tax-controversy-services.html](http://www.pwchk.com/en/services/tax/hong-kong-tax-controversy-services.html)