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# **HONG KONG TAX NEWS**

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## **Commissions, Rebates and Discounts**

The Hong Kong Inland Revenue Department ('IRD') recently revised an Interpretation & Practice Notes No. 12 ('DIPN') regarding the commissions, rebates and discounts payments.

### **Field Audit Findings**

In the course of IRD field audits, the irregularities in relation to commissions payments have been spotted including closely connected non-resident recipients not properly reflected in the profits tax return; commission payments were grouped with the purchase cost of goods; unsubstantiated commission payments were charged in financial statements.

### **Disclosure Rules**

In the new DIPN 12 (Revised 2001), the following disclosures are required when filing profits tax returns:

- (i) Instead of showing the income net of commissions, rebates and discounts, taxpayers should return the gross income and clearly distinguish the payment of commissions, rebates and discounts in the financial statements and tax computations submitted in support of profits tax returns.
- (ii) The following information should be disclosed for each payment:
  - full name, address and identity card number or business registration number of the recipient;
  - whether the recipient has any relationship with the taxpayer;
  - amount of the payment;
  - details of services rendered; and preferably
  - evidence of payment.

The only exceptions to the disclosure rules described in (i) above are:

- commissions, rebates and discounts paid in the ordinary course of trade on a principal to principal basis and it is expected that such commissions, rebates and discounts would be reflected in the financial statements of each party to the transaction;
- commissions, rebates and discounts will be disclosed in the payer's employer's return (BIR Form No. 56A).

## Compromised Arrangement

Where the taxpayer is unable or unwilling to disclose the names and addresses of the recipients, the amounts paid by way of commissions, rebates and discounts should be disallowed in the tax computations. This arrangement is accepted as a compromise to the business concerned and it does not relieve the recipient of these payments from his responsibility to return the amount for tax purposes.

However, the compromised arrangement is not acceptable to the IRD in the following circumstances:

- the payer suffers an overall operating loss in the basis period in which the commissions, etc., were incurred;
- the expenses were incurred in part of an accounting period which does not fall into a basis period and will consequently drop out for assessment purpose; or
- the expenses were incurred in respect of a capital transaction and would not have been allowable as a deduction in the first place.

Where the arrangement is not acceptable to the IRD, the payer has either to disclose the information as stated in (ii) above or, the payer will be assessed as agent of the recipients of the commissions, etc

## Concealed Commission, Rebate and Discount Payments

Taxpayers are advised to take advantage of voluntary disclosure to the IRD in case they have made commission, rebate and discount payments without proper disclosure and caused loss to the revenue. Taxpayers who do not would run a grave risk of prosecution under the Inland Revenue Ordinance when, as a result of Department enquiries, evidence of concealed commissions is obtained.

## Further information

For further information regarding the tax implications of commissions, rebates and discounts, please contact us at (852) 2351 4806 or send mail to [info@ajmcs.com.hk](mailto:info@ajmcs.com.hk) with questions.

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