

A decorative graphic consisting of two overlapping orange parallelogram shapes. The top shape is positioned to the right of the bottom shape, creating a stepped effect.

Hong Kong clarifies determination of individual tax residence under tax arrangement with Chinese Mainland

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Issue 1

In brief

The Hong Kong Inland Revenue Department (IRD) has recently updated the frequently asked questions (FAQs) on the comprehensive double taxation arrangement between Hong Kong Special Administrative Region (Hong Kong) and the Chinese Mainland (HK / Chinese Mainland CDTA)¹. The updates clarify the determination of tax residence status in cases where an individual qualifies as a resident of both sides at the same time (i.e. tie-breaker rules). Specifically, the IRD uses individuals who hold domiciliary registration (also known as household registration or 'hukou') in the Chinese Mainland and who have been admitted to work in Hong Kong under a talent admission scheme as examples to illustrate how the rules apply in practice.

This news flash summarises the updated FAQs and our observations thereon. Determining tax residence is complex from both technical and practical perspectives. Even if an individual is regarded as a tax resident of one side under the HK / Chinese Mainland CDTA, this does not necessarily mean that they are not subject to tax in the other side. It is important to conduct a detailed, case-by-case analysis of the tax implications and compliance requirements for different types of income, taking into account the respective tax laws of Hong Kong and the Chinese Mainland, as well as the HK / Chinese Mainland CDTA. If you have any questions about the matters covered in this news flash, please seek professional advice tailored to your specific circumstances.

In detail

Background

‘Residence’ is an important concept under the HK / Chinese Mainland CDTA. Its determination directly decides which side has the right to tax a particular income, and affects whether an individual is entitled to the CDTA benefits (such as entitlement to tax exemptions or tax credits in one side), thereby effectively avoiding double taxation.

According to the relevant clauses, in the Chinese Mainland, a resident individual refers to a person who, under the laws of the Chinese Mainland, is liable to tax therein by reason of their domicile, residence or other similar criterion, but excludes any person who is liable to tax in the Chinese Mainland only in respect of income from sources within the Chinese Mainland. The Individual Income Tax Law provides that an individual that fulfils the following criteria is regarded as a Chinese Mainland tax resident:

- (i) An individual who is domiciled in the Chinese Mainland; or
- (ii) An individual who is not domiciled in the Chinese Mainland but has resided in the Chinese Mainland for an aggregate of 183 days or more within a tax year.

Having a ‘domicile’ in the Chinese Mainland means habitually residing in the Chinese Mainland due to domiciliary registration, family or economic interests. Those who reside in the Chinese Mainland for study, work, visiting relatives, travel, etc., but do not habitually reside in the Chinese Mainland, are considered as not having a ‘domicile’.

In Hong Kong, a resident individual refers to:

- (i) an individual who ordinarily resides in Hong Kong; or
- (ii) an individual who stays in Hong Kong for more than 180 days during a year of assessment or for more than 300 days in two consecutive years of assessment, one of which is the relevant year of assessment.

‘Ordinarily resides in Hong Kong’ is not statutorily defined. According to the Departmental Interpretation and Practice Notes published by the IRD, in general, an individual is regarded as ‘ordinarily residing in Hong Kong’ if they have a permanent home in Hong Kong where they or their family live. Other relevant factors include the duration of their stay in Hong Kong, whether they have a permanent place of residence in Hong Kong, whether they own any property overseas for residential purposes, and whether they are primarily resident in Hong Kong or overseas.

As the two sides adopt different definitions of ‘resident’, an individual may be treated as a resident of both sides at the same time (i.e. dual residence status). For example, this may occur where a person holds domiciliary registration in the Chinese Mainland but frequently travels between the two sides for work. To resolve this issue, the individual’s residence status is determined under the tie-breaker rules in the HK / Chinese Mainland CDTA, which apply the following criteria in order of priority:

- (1) Where they have a permanent home;
- (2) If they have a permanent home in both sides, where they have a closer personal and economic relationship (i.e. centre of vital interests);
- (3) In either of the following situations, where they have a habitual abode:
 - (i) They have a permanent home in both sides but the side in which their centre of vital interests lies cannot be determined; or
 - (ii) They do not have a permanent home in either side; and

- (4) If the residence status still cannot be determined after applying the above criteria in order of priority, it will be determined by mutual agreement between the competent authorities of both sides.

Updated FAQs

- In response to the steadily increasing cross-border mobility between Hong Kong and the Chinese Mainland, as well as the growing number of individuals from the Chinese Mainland working in Hong Kong through various talent admission schemes in recent years, the IRD has updated the relevant FAQs to provide further guidance on determining individual residency under certain circumstances, particularly in cases where an individual may be considered a resident of both Hong Kong and the Chinese Mainland.

Question 8

Question: If an individual is at the same time both a resident of Hong Kong and of the Chinese Mainland under the definition set out in the HK / Chinese Mainland CDTA, how will the issue of dual residence status be resolved?

Answer highlights: The HK / Chinese Mainland CDTA has adopted the criteria set out in the model text of the Organisation for Economic Co-operation and Development (OECD), i.e. it applies the tie-breaker rules in order of priority using the four aforementioned criteria. Detailed interpretation on the tie-breaker rules can be referenced to the Circular of the Interpretation of the Provisions of the Agreement between the Government of the People's Republic of China and the Government of the Republic of Singapore for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and the Protocol Thereof (China/Singapore CDTA), i.e. Guoshuifa 2010 No. 75 (Circular 75). The interpretation on the tie-breaker rules under Circular 75 applies to the HK / Chinese Mainland CDTA².

Observation: *Circular 75 was issued by the State Taxation Administration earlier to set out its interpretation of the provisions of the China/Singapore CDTA. According to Circular 75, if the relevant provisions of a treaty concluded by China and any other jurisdiction accord with those of the China/Singapore CDTA, the interpretation in Circular 75 shall apply to the identical provisions of that treaty. Except for the use of 'nationality' as a criterion for determining an individual's residence status under the China/Singapore CDTA, the tie-breaker rules adopted under the HK / Chinese Mainland CDTA are the same as the corresponding rules in the China/Singapore CDTA. The update to Question 8 clarifies that the interpretation of the tie-breaker rules under Circular 75 also applies to the HK / Chinese Mainland CDTA, rather than introducing any change in interpretation.*

- The IRD has also added Questions 17 to 21 to illustrate how the tie-breaker rules are applied using the approach set out in Circular 75 to determine the final residence status of individuals with dual residence status under the HK / Chinese Mainland CDTA in certain situations. The new FAQs are summarised below:

Question 17

Question: Mr A holds a domiciliary registration in the Chinese Mainland. He successfully applied to work in Hong Kong through a talent admission scheme and is employed by a Hong Kong company. He owns or rents property in Hong Kong. His spouse and children have come to Hong Kong to live with him, and his children are studying in Hong Kong. Mr A spends most of his time living in Hong Kong and occasionally returns to the Chinese Mainland to visit his relatives or travel. Mr A stays in Hong Kong for more than 180 days during a year of assessment. Mr A is at the same time both a resident of Hong Kong and of the Chinese Mainland under the definition set out in the HK / Chinese Mainland CDTA. How should Mr A's residence status be determined?

Answer highlights: If Mr A's residence in Hong Kong is of a permanent nature and he does not have a permanent home in the Chinese Mainland, he will be regarded as a Hong Kong resident. Conversely, if he has a permanent home in the Chinese Mainland and his residence in Hong Kong is not of a permanent nature, he will be regarded as a Chinese Mainland resident.

Question 18

Question: Further to Question 17, if Mr A has permanent homes in both Hong Kong and the Chinese Mainland, how should his residence status be determined?

Answer highlights: One has to comprehensively consider his personal and economic relationship with both sides. Mr A will be regarded as a Hong Kong resident if he has closer relationship with Hong Kong, and vice versa.

Question 19

Question: Mr B holds a domiciliary registration in the Chinese Mainland. His situation is similar to that of Mr A as mentioned in Question 17, but due to his Hong Kong employer having business in the Chinese Mainland, Mr B is required to frequently work in the Chinese Mainland. Mr B stays in Hong Kong for more than 180 days during a year of assessment and spends most weekends in Hong Kong. In this situation, will there be any differences in applying the tie-breaker rules to resolve the issue of dual residence status?

Answer highlights: Mr B's frequent stay in the Chinese Mainland due to work increases the likelihood that he has a permanent home in the Chinese Mainland and has closer personal and economic relationship with the Chinese Mainland. Therefore, it is more probable that Mr B will be regarded as a Chinese Mainland resident.

Question 20

Question: Mr C holds a domiciliary registration in the Chinese Mainland. He successfully applied to work in Hong Kong through a talent admission scheme and is employed by a Hong Kong company. He owns or rents property in Hong Kong. Mr C works in Hong Kong from Monday to Friday and returns to the Chinese Mainland on weekends. His spouse and children still live in the Chinese Mainland, and his children attend school in the Chinese Mainland. Mr C stays in Hong Kong for more than 180 days during a year of assessment. Mr C is at the same time both a resident of Hong Kong and of the Chinese Mainland under the definition set out in the HK / Chinese Mainland CDTA. How should Mr C's residence status be determined?

Answer highlights: Since Mr C's family remains in the Chinese Mainland and he previously lived there, he likely has a permanent home in the Chinese Mainland. However, whether Mr C's residence in Hong Kong is of a permanent nature needs further assessment based on his actual facts and circumstances. If Mr C's residence in Hong Kong is not of a permanent nature, he will be regarded as a Chinese Mainland resident.

Question 21

Question: Further to Question 20, if Mr C has permanent homes in both Hong Kong and the Chinese Mainland, how should Mr C's residence status be determined?

Answer highlights: Same as Question 18, one has to comprehensively consider Mr C's personal and economic relationship with both sides and compare which side he has closer relationship with.

Observation: Based on the FAQs above, when applying the tie-breaker rules, the primary consideration is whether the individual has a **permanent home** in Hong Kong or the Chinese

*Mainland. If they have a permanent home in both sides, one should then compare their **personal and economic relationship** with each side and assess which side they have a closer relationship with, thereby determining their residence status.*

Based on Circular 75, the following factors should be considered when applying the criteria regarding permanent home and personal and economic relationship:

- *Permanent home: includes a house, apartment or room rented by the individual, provided that the dwelling is arranged for the individual's permanent use, and not for short-term stays for purposes such as leisure travel or business trips.*
- *Personal and economic relationship: needs to comprehensively consider the individual's family and social relations, occupations, political, cultural or other activities, place of business, the place from which they administer their property, etc. Special emphasis is placed on the actual behaviour of the individual, i.e. the side where they always live, work and maintain their family and possessions is generally where they retain their centre of vital interests.*

When determining whether an individual is a Hong Kong tax resident under domestic tax law in Hong Kong, if the individual does not satisfy the '180/300-days' test as mentioned above, the IRD will normally consider the 'totality of facts' relating to the individual. This includes considering which jurisdiction the individual has a closer personal and economic relationship with, alongside the 'permanent home' factor.

Based on our practical observations, when assessing the 'permanent home' factor, the IRD not only considers whether the individual has owned or rented a residence in Hong Kong, but also reviews aspects such as how the Hong Kong residence is being used by them or their family, the duration for which the Hong Kong residence is occupied, the type of accommodation they arrange in the Chinese Mainland and if applicable, how any Chinese Mainland property is being used during the relevant year of assessment.

In addition, because these individuals who travel to Hong Kong from the Chinese Mainland typically already have annual tax filing records with the relevant tax authorities, any changes in their filing position may prompt enquiries from the relevant Chinese Mainland tax authorities.

The takeaway

We welcome the IRD's updates to the relevant FAQs. The newly added Questions 17 to 21, which use as examples individuals who hold domiciliary registration in the Chinese Mainland and come to Hong Kong under a talent admission scheme, offer strong practical guidance. However, it remains common for individuals to maintain permanent homes in both jurisdictions. In such cases, the analysis must turn on determining their centre of vital interests. That determination carries an inherent degree of subjectivity, and the outcome often depends on the tax authorities' interpretation and enforcement. As a result, applying the tie-breaker rules in individual cases remains complex and challenging.

Please note that the determination of tax residence status is not a 'one-off' assessment. Any changes to the facts and circumstances in any year of assessment can affect the individual's status. Hence, individual taxpayers should understand the relevant tax rules in order to plan ahead and execute appropriate arrangements. They should also retain proper and complete documentation to support their position.

Nevertheless, there may still be situations in which dual residence status cannot be resolved, and such individuals may be subject to individual income tax in both sides. It is important for them to understand the availability of any tax relief, income exemptions or tax credits under the respective domestic tax rules to alleviate double taxation where possible.

Given the differences in individual income tax laws between the two jurisdictions, even if the issue of dual residency has been resolved and an individual has been recognised as a tax resident of one jurisdiction, income sourced from the other jurisdiction may still be subject to taxation in that other jurisdiction.

In addition, under the international tax transparency framework, both Hong Kong and the Chinese Mainland have implemented the Common Reporting Standard (CRS) established by the OECD. When opening a bank account or accounts with other specified financial institutions in either Hong Kong or the Chinese Mainland, individuals are required to self-declare their tax residence status. If an individual is a tax resident of another jurisdiction participating in the CRS, the financial institution may be required to report the relevant financial account information annually to the tax authority where the account is maintained, which will then transmit the information to the corresponding tax jurisdiction.

The determination of tax residence status is a complex subject matter. The concept of a 'tax resident' differs significantly from the definition of resident under statutory law and from its interpretation in an immigration context. If you have any questions about the matters covered in this news flash, please seek professional advice tailored to your specific circumstances.

Endnotes

1. The IRD's updated FAQs can be accessed via this link:
https://www.ird.gov.hk/eng/faq/dta_2006.htm
2. Circular 75 can be accessed via this link (Chinese version only):
<https://fgk.chinatax.gov.cn/zcfgk/c100012/c5194181/content.html>

Let's talk

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Hong Kong Tax News Flash

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