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The Characteristics, Formation, and Evolution of Hong Kong's Tax Structure: The Feature Research from 2010 -2024

Zhihao Dong

Central University of Finance and Economics, Beijing, China
dongzhihao1217@gmail.com

Abstract. This study investigates the characteristics, historical evolution, and structural vulnerabilities of Hong Kong's tax system between 2010 and 2024. The regime is distinguished by its reliance on direct taxation, with corporate income tax consistently contributing around 40% of government revenue and personal income tax accounting for 15–22%. Rooted in colonial legacies and reinforced by globalization, this model has been sustained through low statutory rates and the territorial-source principle, thereby consolidating Hong Kong's status as an international financial center. Yet, the high concentration of the tax base in finance, real estate, and high-income groups generates systemic risks. Global reforms, notably the OECD's minimum tax initiative, are expected to erode Hong Kong's comparative advantage, while demographic aging is projected to diminish the personal income tax base in the coming decades. Domestic vested interests, particularly from property and financial sectors, further constrain efforts to broaden the tax base or diversify fiscal instruments. The analysis suggests that while the existing framework once enabled fiscal expansion amid globalization, it is increasingly unsustainable under shifting international and domestic conditions. A reorientation toward diversification, tax base broadening, and fiscal resilience will be essential to safeguarding Hong Kong's long-term competitiveness and financial stability.

Keywords: Hong Kong tax structure, corporate income tax, globalization, fiscal reform.

1. Introduction

1.1. Research background and theme

Hong Kong has long been recognized as a global financial hub and one of the world's most distinctive low-tax economies. Since the colonial era, its fiscal system has been characterized by a philosophy of "low rates and simple taxes," which has remained largely intact after the 1997 handover. According to Professor Xinyue Chen, the current tax system in Hong Kong adopts "a classified tax system, with income tax being the main component, supplemented by transaction taxes and property taxes. The income tax collection model in Hong Kong ... adopts the "territorial taxation principle" based on the source of income [1]." Within this institutional framework, the city's tax

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structure has developed into a model dominated by direct taxation, particularly corporate income tax supplemented by personal income tax. Between 2010 and 2022, direct taxes consistently accounted for more than 60% of total tax revenue, with corporate income tax alone contributing around 40%. This concentration reflects both deliberate institutional design and the dividends of globalization, as multinational corporations were drawn to Hong Kong's comparatively low statutory rates, territorial-source principle, and status as an open entrepôt.

However, the same structural features that once bolstered Hong Kong's competitiveness also expose vulnerabilities. There are many professors also pointed that "In the future, the Hong Kong government will still attach great importance to maintaining the competitiveness of the tax system in order to maintain its advantageous position as a location for effective investment holding. However, it is undeniable that this reform has objectively posed certain challenges to the tax system's competitiveness in Hong Kong [2]." Heavy reliance on a limited set of sectors—finance, real estate, and trade—renders fiscal revenues highly sensitive to market volatility and global capital flows. The COVID-19 pandemic, demographic aging, and international tax reforms such as the OECD's global minimum tax have further challenged this system, eroding its long-term sustainability. It is obvious that "(This situation) has objectively posed certain challenges to the tax system's competitiveness [3]." Against this backdrop, understanding the characteristics, formation, and evolution of Hong Kong's tax structure has become an important academic and policy issue. The theme of this study is therefore to critically examine the trajectory of Hong Kong's tax regime over the past decade and explore its future reform prospects in the context of global and domestic transformations.

1.2. Research objectives and significance

The primary objective of this study is to provide a systematic analysis of the structural features, historical drivers, and future challenges of Hong Kong's tax system. By examining both corporate and personal income taxation, the research aims to clarify the underlying logic of a regime that has long relied on a narrow but highly concentrated revenue base. In doing so, it seeks to explain how historical legacies, globalization dynamics, and domestic interest group politics have jointly shaped the persistence of a "direct tax–dominated" model. Another key objective is to assess how external shocks—ranging from international tax reforms to demographic shifts—are reshaping the fiscal landscape and compelling the government to reconsider its long-standing reliance on low tax rates as the cornerstone of competitiveness.

The significance of this research lies in its dual academic and policy relevance. From an academic perspective, the study contributes to the literature on fiscal regimes in small open economies, highlighting how institutional path dependence interacts with global structural change. It also illustrates the trade-offs between maintaining tax competitiveness and achieving fiscal sustainability. From a policy standpoint, the findings shed light on the urgent need for reform in Hong Kong's tax system, which remains constrained by vested interests and a limited economic base. By identifying structural risks and exploring potential reform pathways, this research provides valuable insights for policymakers seeking to strike a balance between institutional flexibility and long-term stability.

1.3. Research methodology and structure

The research adopts a qualitative and historical-institutional approach, combining descriptive statistics, comparative analysis, and interpretive evaluation. First, tax revenue data from 2010 to 2022 are analyzed to reveal the composition and concentration of Hong Kong's fiscal system.

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Corporate income tax, personal income tax, and property-related revenues are examined in detail to identify their relative weight and sectoral distribution. This empirical foundation is complemented by a comparative perspective, situating Hong Kong's tax rates and structural features against those of similar economies such as Singapore and Ireland. Second, the study applies historical analysis to trace the institutional path dependence of Hong Kong's tax structure, focusing on colonial legacies, post-handover consolidation, and globalization-induced "institutional arbitrage." Third, policy documents and international tax reform initiatives are reviewed to assess external pressures, including the OECD's global minimum tax and demographic projections.

Structurally, the study is organized into several parts. The first section introduces the research theme and contextualizes Hong Kong's fiscal model. The second section analyzes the internal characteristics of the tax structure, with a focus on corporate and personal income taxation. The third section examines the historical formation of the system, including colonial policies, globalization, and domestic lobbying. The fourth section highlights external shocks and structural vulnerabilities, such as sectoral volatility, demographic aging, and international reforms. Finally, the conclusion synthesizes the findings and proposes directions for reform, emphasizing diversification, tax base broadening, and fiscal resilience. This structure ensures a comprehensive and systematic exploration of Hong Kong's tax regime, linking historical foundations with contemporary challenges and reform imperatives.

2. Formation of the tax structure: historical trajectories and globalization dynamic

The formation of Hong Kong's tax structure is shaped by both historical legacies and contemporary economic imperatives. Historically, colonial governance and the continuation of its free-port orientation played decisive roles. The degree of openness of financial institutions in Hong Kong is extremely high. Hong Kong treats local and foreign financial institutions equally. Foreign financial institutions can engage in business together with local institutions on the basis of fair competition [4]. The tax structure's origins can be traced back to British colonial rule, during which the principle of "low rates and simple taxes" was established to preserve Hong Kong's role as an entrepot. Following the 1997 handover, this system was retained and even strengthened to consolidate its position as an international financial center. For example, the absence of a capital gains tax was designed to attract international investors, while the territorial-source principle reduced compliance costs for multinationals.

From an economic standpoint, globalization-induced "institutional arbitrage" also contributed to shaping this structure. Hong Kong's relatively low corporate income tax rate (16.5%)—below key competitors such as Singapore (17%) and Ireland (12.5%)—has attracted multinationals to engage in profit shifting through Hong Kong. In 2018, approximately 40% of corporate income tax revenue originated from regional headquarters of multinational enterprises. The territorial-source principle further enabled firms to optimize their tax liabilities through transfer pricing, which, while advantageous in earlier phases of globalization, faces growing challenges in the digital economy era.

Domestic vested interests also help entrench this structure. Due to the strong lobbying power of real estate and financial sectors, property-related taxes such as rates and stamp duties have remained low or selectively exempt, protecting the interests of major developers. Between 2010 and 2022, real estate-related revenues averaged 18% of total government revenue, yet political lobbying repeatedly obstructed property tax reforms. Likewise, Hong Kong's middle class, facing an effective tax burden of only 5–8% of income, has consistently resisted any proposals to broaden the tax base (e.g., through a consumption tax), thereby contributing to prolonged reform stagnation.

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3. Core characteristics of the tax structure: the high concentration of direct taxes

3.1. Corporate income taxation

From the perspective of corporate income taxation, Hong Kong's fiscal revenue directly reflects the dividends of globalization. The most salient feature of its tax structure is the predominant role of corporate income tax. The outcome of data analysis is not incidental but rather the product of deliberate institutional design to meet the government's revenue needs.

3.2. Comparetive tax burden

In terms of tax burden, Hong Kong's corporate tax rate stands at 16.5%, significantly lower than the global average of 23% (OECD, 2022), thereby attracting numerous multinational corporations to establish regional headquarters or profit centers in the territory. Moreover, under the territorial-source principle, only profits derived from within Hong Kong are taxable, minimizing barriers to cross-border capital flows and reinforcing its role as an international financial hub. The high proportion of corporate tax revenue directly reflects Hong Kong's export-oriented economy. For instance, in 2022, the financial, real estate, and trade sectors contributed 72% of total corporate tax receipts, with the top five property developers alone accounting for more than 35%. Such tax base concentration allows fiscal revenue to expand rapidly during globalization upswings (e.g., the surge of Mainland capital inflows in 2012), but it simultaneously heightens fiscal sensitivity to sectoral volatility.

3.3. Personal income tax

With respect to personal income tax, the government primarily relies on stabilizing high-income earners, thereby securing a relatively narrow tax base. As the second-largest revenue source, personal income tax has consistently accounted for 15–22% of total tax receipts, representing another distinctive feature of Hong Kong's system. Although the statutory top marginal rate is 17%, various deductions such as Mandatory Provident Fund contributions and dependent allowances reduce the effective top rate to about 14%, significantly below that of other advanced economies (e.g., Singapore's top rate of 22%). Furthermore, the tax base is highly concentrated: the top 10% of high-income earners—predominantly in finance and law—contribute over 70% of personal income tax revenue. During the COVID-19 pandemic in 2020, the share of personal income tax rose countercyclically to 21.61%, reflecting the relative income stability of top earners. Yet this "resilience" is essentially a byproduct of the system's narrow base, concealing structural weaknesses such as insufficient contributions from the middle class and emerging industries.

4. Shocks and structural vulnerabilities: challenges in a changing global context

External In the current era of heightened global uncertainty, Hong Kong's tax system faces mounting reform pressures.In order to prevent the spread of the COVID-19 pandemic, the Hong Kong authorities had to increase their financial expenditure on public health. El Shagi Makram & Schweinitz Gregor von pointed that “the expansionary policy in response to the great recession has pushed up debt levels across the globe and many countries are overindebted when applying pre-crisis standards [5].” A key challenge is the erosion of its corporate tax base under international tax reforms. The OECD's 2021 initiative on a global minimum tax rate of 15% directly undermines Hong Kong's low-tax advantage. Estimates from the Inland Revenue Department suggest that if

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multinational firms must make up the differential abroad, Hong Kong's corporate tax revenue could fall by 12–18%. Additionally, the European Union has placed Hong Kong on its "watchlist of non-cooperative jurisdictions," raising the prospect of sanctions and further constraining fiscal policy space.

Structural vulnerabilities also stem from the narrowness of Hong Kong's economic base. The connections between financial markets have become increasingly close. Fluctuations in one market can easily be transmitted among various markets, ultimately causing certain fluctuations in other financial markets, which means that Hong Kong is precisely facing such rapid and dangerous systemic financial risks [6]. Heavy reliance on financial markets and property cycles poses significant fiscal risks. Professor Xinchun Wang also support this view, pointed that “The rampant epidemic has significantly curbed the consumption, and investment demands of countries around the world. Coupled with the negative wealth effects brought about by the significant fluctuations in the financial market, there is a risk that the economy may fall into recession [7].” In 2022, stamp duty on securities transactions accounted for 13.4% of total tax revenue; a 10% drop in the Hang Seng Index was projected to reduce revenue by 2.1%. Likewise, revenue from rates and land premiums constituted 15% of government income, but property transaction volumes had already declined 37% from their 2018 peak, signaling potential cascading effects from further market corrections.

Demographic pressures compound these risks. The share of the population aged 65 and above is projected to rise from 20% in 2022 to 33% by 2040, leading to labor force contraction and an estimated 1.2% annual shrinkage of the personal income tax base. If the current structure persists, personal income tax revenue could decline by 8–10% by 2040. Thus, broadening the tax base will be an urgent challenge for the next decade.

5. Policy recommendations for the future reform of Hong Kong’s tax system

5.1. Broadening the tax base through diversified revenue instruments

A central weakness of Hong Kong’s fiscal regime lies in its excessive reliance on a narrow set of revenue sources, notably corporate and personal income tax, as well as property-related revenues. This narrowness generates volatility, particularly when property or financial markets experience downturns. In the post-pandemic era, the trend of globalization is clearly weakening. The global supply chain is accelerating its adjustment, inflationary pressure remains high, the downside risks to the world economy are increasing, and external demand is further contracting. As professor Xiaoying Li pointed, against this backdrop, the market demand for “the four pillar industries” in Hong Kong may face negative impact [8]. Thus, a more diversified tax structure is therefore essential to ensure resilience. International experience offers valuable lessons: Singapore, for instance, successfully introduced a Goods and Services Tax (GST) in 1994 at a modest rate of 3%, gradually raising it to 9% by 2024. Importantly, the government simultaneously implemented offsetting measures such as subsidies and rebates to protect lower-income groups, thereby mitigating regressive impacts. A similar incremental approach could be adopted in Hong Kong, where the gradual introduction of a GST or value-added tax (VAT), combined with targeted relief measures, would broaden the tax base while maintaining social acceptability. Moreover, the introduction of a modest environmental or carbon tax—following the model of Sweden’s carbon tax—could align fiscal reform with global sustainability goals, diversifying revenue while supporting climate policy objectives.

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5.2. Adjusting corporate tax policy to global regulatory changes

Hong Kong's corporate tax system has historically been central to its attractiveness as an international financial hub. Yet, the OECD's global minimum tax (GMT) agreement challenges its longstanding low-tax advantage. The need for enterprises to make further investments, the pursuit of better business environments, and the desire for market efficiency and fair welfare all prompt the governments of developed regions to strive to maximize their comparative advantages by either increasing taxes or strengthening tax collection and management, as another scholar pointed out [9]. Jurisdictions such as Ireland and Singapore have already begun to adapt: Ireland, once known for its 12.5% corporate tax rate, announced in 2021 that it would raise its rate to 15% for large multinational firms, while maintaining the original rate for small businesses. This two-tiered model balances compliance with international standards and support for local enterprises. Hong Kong could adopt a similar approach by maintaining preferential rates for small and medium enterprises (SMEs) while adjusting the effective rate for multinational corporations in line with GMT requirements. Such a strategy would prevent revenue leakage through foreign tax adjustments while preserving competitiveness for local firms. In addition, Hong Kong should strengthen transfer pricing regulations and adopt more rigorous anti–base erosion measures, echoing the reforms undertaken in jurisdictions like Australia, which has tightened profit-shifting rules while sustaining its role as an investment destination.

5.3. Enhancing equity and resilience through personal income tax reform

The realization of effective tax reform...is not only to reduce the negative externalities caused by the tax base erosion and profit transfer to the local finance, but also to optimize the regional allocation of digital and market resources [10]. As what is mentioned by Professor Bai Fan, Hong Kong is experiencing vertical unfairness in tax burden, which may lead to waste in resource allocation. Hong Kong's personal income tax base remains highly concentrated, with the top 10% of earners contributing more than 70% of revenues. It is obvious that "under unchanged policies, population aging could adversely affect growth and living standards in Hong Kong [11]". While this concentration has historically provided stability, demographic aging and labor market changes threaten to undermine fiscal sustainability. Comparative experiences suggest possible reform directions. For instance, Singapore has progressively adjusted its personal income tax system by raising top marginal rates (now 24% for high earners) while simultaneously broadening the base through gradual adjustments to allowances. Similarly, South Korea has successfully diversified its personal tax base by expanding taxation on capital gains and digital economy activities, thereby reducing overdependence on wage income. Hong Kong could draw on these examples by lowering its effective tax thresholds, revising deductions, and introducing supplementary levies on emerging sectors such as digital services. Moderate increases in progressivity would enhance redistributive capacity while ensuring that the middle class contributes more proportionally to fiscal stability.

6. Limitations and future research directions

This study offers a systematic account of Hong Kong's tax structure, yet several limitations constrain its scope and suggest directions for further inquiry.

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6.1. The limited temporal coverage

Most data extend only to 2022, with interpretive discussion up to 2024. Such truncation prevents a full assessment of post-pandemic fiscal adjustments and the long-term impacts of the OECD global minimum tax and demographic aging. Moreover, the COVID-19 shock created structural breaks that complicate comparisons with earlier periods. Future research should therefore extend the temporal horizon with updated administrative data, apply structural-break detection, and employ dynamic models to capture regime shifts and persistent compositional changes.

6.2. Over-reliance on data

The analysis relies on aggregate revenue statistics, which restrict insight into the distributional incidence of taxation and behavioral responses of firms and households. Without taxpayer- or firm-level microdata, the concentration of revenue among high-income earners and leading sectors can only be described rather than rigorously measured. Incorporating anonymized microdata and using causal identification strategies such as difference-in-differences or event studies would allow future work to evaluate elasticities, incidence, and behavioral adaptation with greater precision.

6.3. Summary

In sum, while the present research provides a descriptive and historically informed foundation, it should be complemented by longitudinal data, micro-level analysis, causal methods, comparative designs, and dynamic modeling. Addressing these gaps will not only refine academic understanding of Hong Kong’s tax regime but also strengthen the policy relevance of future work on fiscal resilience and reform.

7. Conclusion

Hong Kong's tax structure is the product of historical path dependence, global institutional competition, and local interest group dynamics. While its direct tax–dominated model has effectively supported fiscal expansion during periods of globalization, it now faces systemic risks due to its narrow tax base, sectoral dependence, and the reconfiguration of international tax rules. Future reforms must move beyond the entrenched paradigm of "low rates as sole advantage," and instead pursue diversification, tax base broadening, and more precise fiscal calibration. Only by striking a new balance between institutional flexibility and fiscal sustainability can Hong Kong reinforce its status as an international financial center and withstand the long-term disruptions of global economic transformation.

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