

Charities in Hong Kong: Section 88 tax exemption status and related matters

In Hong Kong, S.88 of the Inland Revenue Ordinance (“IRO”) provides that a charity is exempt from Hong Kong profits tax. For profits derived from trade or business by the charity, specific conditions would need to be fulfilled for tax exemption.

In this guide, we will focus on two aspects:

- (1) Once a charity has obtained S.88 tax exemption status from the Inland Revenue Department (“IRD”), what are the ongoing compliance requirements?
- (2) Is it true that all income earned by a charity with S.88 status is exempt from Hong Kong profits tax?

(1) Once a charity has obtained S.88 tax exemption status from the IRD, what are the ongoing compliance requirements?

Obtaining S.88 tax-exempt status from the IRD is only the beginning. Maintaining it requires ongoing compliance. Charities are legally required to fulfill the following obligations:

Notify IRD of changes	<i>Within 1 month, notify the IRD in writing if there are changes in address, amendments to governing instruments, termination of subsidiary, or cessation of operations.</i>
Notify IRD of tax chargeability	<i>Notify the IRD in writing within 4 months of year-end (even if no tax return has been issued) if taxable profits are derived.</i>
Report employee remuneration and other key changes	<i>File employer returns annually. Notify the IRD in writing if an employee’s employment commences or ceases, or if they leave Hong Kong for a substantial period of time.</i>
Keep financial records and respond to IRD’s enquiries	<i>The IRD performs regular reviews on each charity (typically every 3 to 4 years) and requests charities to reply to a questionnaire within 1 month. The information required includes financial accounts, list of activities performed, list of members, changes in operation or governing instruments, etc. In this regard, charities shall keep proper documentary records for providing timely reply to the IRD’s requests. Such information allows the IRD to assess whether the charity’s activities remain charitable and are aligned with the charity’s stated objects. If there is evidence of unlawful conduct, activities unaligned with stated objects, or misuse of income or assets for non-charitable purposes, etc, the IRD may initiate a detailed review on the charity.</i>

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(2) Is it true that all income earned by a charity with S.88 status is exempt from Hong Kong profits tax?

a. What S.88 status really means

When a charity is granted S.88 status, the charity is formally recognized by the IRD as a charitable institution or trust of a public character. A donation made to any charity with S.88 status is a deductible approved charitable donation in the hands of the donor (i.e. the donor can claim tax deduction for that donation).

S.88 does not guarantee that **all** income derived by a charity is exempt from tax without condition. In other words, just because a charity has been granted S.88 status by the IRD, that does not guarantee that all its income will be exempt from profits tax. Profits from trade or business are exempt only if the three conditions under S.88 are fully met:

- i. Profits are applied solely to charitable purposes;
- ii. Profits are not spent substantially outside Hong Kong; and
- iii. The relevant activity is in the course of carrying out the charity's objects or is mainly carried out by its beneficiaries.

b. Examples of tax-exempt income

- i. Activities which further the charity's objects

A Hong Kong-based charity is committed to serving the deaf community. It earns profits from the provision of training courses on sign languages. Its profits will be wholly used for the charity's operation in Hong Kong.

- ii. Activities carried out by the charity's beneficiaries

A Hong Kong-based charity is dedicated to supporting children from underprivileged families. Profits were earned from the sales of artwork designed by these children, which were used to subsidize the children's education fees.

c. What if the three exemption conditions under S.88 are not satisfied?

If the exemption conditions under S.88 are not satisfied, the charity can explore other exemption provisions in the IRO such as those regarding sales of capital assets, offshore income, dividend income from entities subject to Hong Kong profits tax, bank interest income from deposits placed in financial institutions in Hong Kong, financial income from specific bonds, funds or debt instruments, etc.

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Quick reminders for charities



DO:

- Keep activities aligned with your charitable objects and public benefit purpose
- Keep spending primarily within Hong Kong
- Ensure all profits are applied to your charitable objects
- Ensure revenue-generating activities fulfill the three S.88 conditions before launching
- Prepare financial statements and activity reports annually
- Consult professionals if changes to operations are foreseen



DON'T

- Don't ignore the filing and notification obligations owed to the IRD
- Don't run commercial ventures unrelated to your charitable objects without evaluating tax risks

Summary

Obtaining S.88 tax-exempt status from the IRD is just the first step. Charities must continue to monitor their activities to ensure ongoing compliance with exemption requirements. Determining whether a charity remains eligible for tax exemption and whether specific profits are taxable is often complex. Where uncertainty arises, professional advice should be sought without delay.

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