

# NARRATIVE REPORT ON HONG KONG



## PART 1: NARRATIVE REPORT

Hong Kong is in fourth position in the 2020 Financial Secrecy Index. It has a fairly high secrecy score of 66 out of 100, accounts for 4.44 per cent of the global market for offshore financial services and is growing – though its recent political instability could hamper that, and China has recently indicated its intention to build offshore financial services capacity in Macau, which could in the long term impact the sector in Hong Kong.

### The history of Hong Kong’s offshore financial centre

Hong Kong is one of the world’s fastest growing secrecy jurisdictions or tax havens today. Its fund management industry [had \\$3.1 trillion](#)<sup>1</sup> under management at of 2018; and \$973 billion in private banking assets.<sup>2</sup> It has the [third](#)<sup>3</sup> largest stock exchange in Asia after Tokyo and Shanghai; it [ranks second after New York](#)<sup>4</sup> for proceeds of initial public offerings, and hosts a wide range of financial services players. In 2018 [it had](#)<sup>5</sup> the world’s second-highest density of Ultra High Net Worth Individuals with personal wealth over \$30 million, at 136 per 100,000 adults. On paper, Hong Kong accounted for two-thirds of all foreign investment into China as of 2019, according to the Ministry of Commerce.<sup>6</sup> Much of this was round-tripped Chinese capital, however.

The government’s [promise](#)<sup>7</sup> to uphold the principle of “keeping intervention into the way in which the market operates to a minimum” is a classic see-no-evil approach to financial regulation, designed to attract offshore business, dirty and clean, with few questions asked. Hong Kong’s classification for many years at the top of the conservative Heritage Foundation’s ranking of economic freedom, is testament to this, as is its [No. 1 ranking](#)<sup>8</sup> in the World Economic Forum’s Financial Development Index in 2011 and its [No. 3 ranking](#)<sup>9</sup> on WEF’s 2019 Global Competitiveness report. Hong Kong’s reluctance to sign up to global transparency standards stems from this attitude. Hong Kong’s official role as a Special Administrative Region of China involves two essential components that underpin the offshore financial centre. First, the protections afforded to Hong Kong by China, which reassure offshore players of Hong Kong’s stability while at the same time allowing “a high degree of autonomy” from China in all matters except foreign relations and defence, involving minimal interference in the financial sector<sup>10</sup>. In this and other respects the Hong Kong-China link resembles Britain’s links with its [three crown dependencies and fourteen overseas territories](#),<sup>11</sup> which are partly independent from Britain yet also partly linked to and supported by it (with ten of these being recognised secrecy jurisdictions):. Given Britain’s long role in the development of financial services in Hong Kong, this similarity is hardly a coincidence.

The economist Milton Friedman famously [declared his love](#)<sup>12</sup> for Hong Kong’s laissez faire approach and cited this — as many have since — as a key reason for the territory’s undoubted economic success over the decades. Yet this argument represents a fundamental misreading of history, for two main reasons. First, the underlying reason for Hong Kong’s success in raising living standards lies not in its economic system but elsewhere. Most important is its unique location as the world’s English-speaking historic offshore gateway to China, with a world-class port on an island of political stability in a turbulent region once protected

Rank: 4 of 133

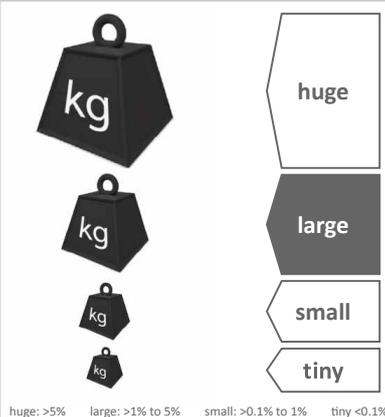
How Secretive?

66



How big?

4.44%



Hong Kong accounts for 4.44 per cent of the global market for offshore financial services. This makes it a large player compared to other secrecy jurisdictions.

The ranking is based on a combination of its secrecy score and scale weighting.

Full data is available here: <http://www.financialsecrecyindex.com/database>.

To find out more about the Financial Secrecy Index, please visit

<http://www.financialsecrecyindex.com>.

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by British colonial power, and now by China's. Second, for all its unusual economic freedoms — and Hong Kong has certainly been an exception in a fast-growing Asian region spurred by heavily state-led industrialisation — Hong Kong was never the free-market economy that its cheerleaders claim, as this report shows.

Hong Kong's secrecy score of 66 places it at the higher end of the secrecy scale, roughly on a par with Panama, and higher than all of the major British-linked secrecy jurisdictions. It offers a wide range of offshore services including tax exemptions, transfer pricing facilities, escape routes from Chinese exchange controls and various forms of financial secrecy, including the use of opaque companies and trusts that can assist tax evasion and other crimes. A [massive exposé](#)<sup>13</sup> in 2014 by the International Consortium of Investigative Journalists revealed a wide array of assets owned by mainland Chinese élites held in secret via offshore trusts, shell companies and other vehicles. Hong Kong was often part of the ownership structures.

Hong Kong has meanwhile been busy adding and expanding a range of offshore facilities to grow its role as an all-purpose global offshore financial centre. Significantly, it has been more resistant to global transparency initiatives than many other financial centres (including its closest regional rival, Singapore). It was a late signer (September 2018) of the [multilateral agreement](#)<sup>14</sup> for adopting the OECD's Common Reporting Standards. Hong Kong has consequently attracted some of the region's less savoury financial flows.

## British colonial roots

Hong Kong was created in 1842 after Chinese rulers tried to crack down on the [traffic in opium](#),<sup>15</sup> which British traders were then pushing aggressively into China. In response to the Chinese crackdown, Britain sent a naval fleet that killed some 20,000 people and shattered the Chinese Empire, leading to the 1842 Treaty of Nanking, under which China ceded a long-term leasehold over Hong Kong to Britain. From these ignoble beginnings, the territory became Britain's main commercial gateway to China.

Along with shipping and general trading, finance was a central ingredient of Hong Kong's economic success from the outset and a pillar of British China policy, which was anchored in a collaboration between the Foreign Office and the Hong Kong and Shanghai Bank, the forerunner of today's global giant, HSBC.<sup>16</sup>

British administrators in Hong Kong espoused a strong — and at times, rather extremist flavor of liberal capitalism — a trait common to most secrecy jurisdictions. This *laissez-faire* approach included a high degree of tolerance for smuggling and other illicit commercial activities. In the 1860s, Britain's Jardine Matheson and other trading houses (which were, to a large degree, officially approved drug-trafficking organisations) even protested in London at British efforts to help the weakened Chinese state collect taxes. The Hong Kong government, for its part, declined to co-operate with the Chinese.<sup>17</sup>

In the 19<sup>th</sup> century and for much of 20<sup>th</sup> century, the “difficult” Chinese market never turned out to be the fabled source of riches that many British financiers had hoped, and even the City of London's limited role in funding Chinese infrastructure nurtured considerable resentment. As one Chinese revolutionary leader put it in 1910 ([p441](#)):<sup>18</sup>

“If [China] is not conquered by partition it will be lost by invisible financial control by foreign powers.”

After the Chinese revolution of 1911, China turned inwards, and while the turmoil did divert some trade to the relative stability of Hong Kong, British opportunities were somewhat meagre. However, the subsequent Chinese civil war of 1945 to 49 saw a new influx of Chinese refugees and capital to Hong Kong, setting the stage for rapid industrialisation.

## Dirty money, then the Open Door, then the Handover

Hong Kong's reputation as a free-market outpost in Asia was popularised by the US economist Milton Freedman in the 1960s and 1970s. He [was inspired](#),<sup>19</sup> in turn, by Sir John Cowperthwaite, Hong Kong's Financial Secretary from 1961 to 1971, who had such stridently anti-government views that he even [refused](#)<sup>20</sup> to collect official statistics for fear they would give government officials too much power. In the modern age, Hong Kong's widely touted economic freedoms have placed it in first position on the Heritage Foundation's [Index of Economic Freedom](#)<sup>21</sup> for many years.

This *laissez-faire* spirit has deliberately turned a blind eye to tainted foreign money for many decades. A memo written by Chase Manhattan Bank economists in 1966 provides a revealing window into Hong Kong's role as a British offshore financial centre, long before the handover to China. In his book *Hot Money* ([p199-200](#))<sup>22</sup> the Canadian economist Tom Naylor publishes part of that 1966 memo:

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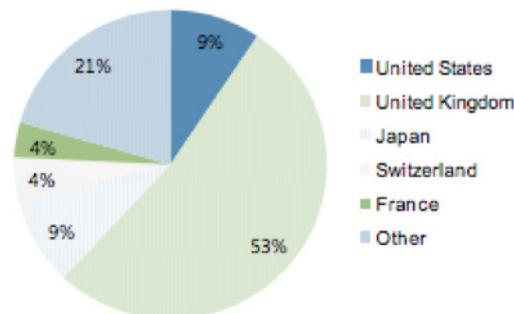
“Hong Kong has long been the flight money center for Southeast Asia and the Far East. Its stature in the postwar era has apparently grown year by year with the intensification of the cold war and mounting revolutionary crises in the area. All the trouble spots, Indonesia, Vietnam, Thailand, Burma, Malaysia, Singapore, India, now contribute to the flow. One of the largest contributors is the relatively stable and prosperous Philippines, whose smuggling operations are a continued source of funding. Hong Kong is also Communist China’s major foreign-exchange earner and window on the Free World, and could be shut down at any time. Although Hong Kong, like Beirut, is an imperfect flight center in comparison to the relative security of Switzerland or the US, it has the advantage of physical closeness and cultural similarity to the flight areas it serves.”

The Chase Manhattan economists estimated that flight money made up 30 to 50 per cent of all Hong Kong bank deposits in 1965, “one of the highest components of flight money in any banking system outside of Switzerland.” A similar per centage was evident in the real estate sector, they added.

Subsequently, China’s Open Door policy announced by Deng Xiaoping in 1978, began a new era in Hong Kong’s role as a financial centre and secrecy jurisdiction. Visible trade grew by an astonishing 28 per cent per year from 1978 to 1997, according to historian [Catherine Schenk](#),<sup>23</sup> and by the time of the British handover in 1997, an estimated 80 per cent of foreign investment in China’s rapidly industrialising Guangdong province was at least nominally from Hong Kong.

Ahead of the handover in 1997, Britain began to consult and negotiate policy changes with China to ensure continuity in what was known locally as a “through train.” Britain hoped that this, plus Hong Kong’s legal system based on English common law, would help City of London financial interests retain their foothold in this gateway to China. Almost two decades later it is clear that the City has had significant successes in this respect. Today, more than half of all foreign financial claims in Hong Kong [are](#)<sup>24</sup> from British banks, as the graphic below shows.

Claims of foreign banking sector on Hong Kong SAR (in percent)



Indeed, in a [fascinating paper](#)<sup>25</sup> on the global networks of offshore, Haberley and Wojcik note:

“the transfer of Hong Kong to Chinese control seems to have pulled China into the orbit of Britain’s financial “second empire.” At the same time, the UK itself loads more strongly as an FDI host on this component than the other three, suggesting that Chinese offshore capital has in turn begun to have a major influence on The City.”

At the time of the handover, Hong Kong was given a wide degree of autonomy under its [Basic Law](#),<sup>26</sup> with China taking responsibility for defence and foreign relations and gaining powers to appoint Hong Kong’s chief executive and top officials. This setup is strikingly similar to the arrangements Britain has with its Crown Dependencies and Overseas Territories, most of which are secrecy jurisdictions: Britain also retains responsibility for defence and foreign relations and appoints top officials. This close similarity is no coincidence, given the history, and the Chinese leadership’s personal incentives with respect to Hong Kong’s longstanding role in hiding assets certainly helped smooth the handover.

Hong Kong was always intended to be a familiar, trusted, Chinese-speaking offshore centre for the Chinese leadership and élites — a place where business could be partly controlled but also significantly protected from mainland scrutiny. For added secrecy, however, Hong Kong structures are often combined with structures in other jurisdictions outside the Chinese orbit. In particular, the British Virgin Islands<sup>27</sup> became the secrecy jurisdiction of choice for Chinese and Hong Kong élites from the mid-1990s, amid fears of Chinese control. A relaxed, see-no-evil attitude continues to prevail.

This 2012 [analysis](#)<sup>28</sup> of a court case by anti-money-laundering specialist Christine Duhaime illustrates current attitudes:

“The Court of Appeal quashed a conviction of a woman who admitted using the Chinese and Hong Kong illegal underground currency exchanges to receive proceeds of crime from fraudulent transactions. The Court noted, as part of its Reasons, that there was a well-known underground banking economy in Hong Kong for illegal currency exchanges and overturned the conviction despite the admission of the accused that her activities were illegal and the fact that she dealt with proceeds of crime to launder them... The facts of the case shed some light on the underground flow of currency from Mainland China to Hong Kong and the extent to which such activities are accepted as part of the normal way of doing business between China and Hong Kong.”

It is hardly surprising that Hong Kong has served as the prime conduit for Chinese bribery and other corrupt activities.

## **Laissez faire, but within limits**

Notwithstanding its lax attitude towards money-laundering, Hong Kong has been far from the free-market paradise that Friedman and other cheerleaders have asserted. As Schenk [notes](#),<sup>29</sup> large public subsidies for housing and education, for instance, meant that “the reality was very different from the myth of complete laissez-faire.” Another [account](#)<sup>30</sup> goes further:

“Friedman mistook Hong Kong’s colonial economic system as a free market, despite Hong Kong’s highly orchestrated colonial command economy.

...Even during the best of times, the average local Chinese small and medium businesses had to operate under the dictates of British colonial policy and at the mercy of monopolistic British trading firms and banks, not to mention that the average worker never had it good at all. British monopolies needed an unregulated supply network of ruthless predatory competition to keep costs low.

...The so-called rule of law, so frequently touted these post-colonial days in Hong

Kong, merely meant that no local Chinese business ever won a case against any British trading firm in 150 years of colonial justice.”

This represented freedom for the wealthy and influential, and something rather different for everyone else — a classic characteristic of secrecy jurisdictions, we have found. Historian Steven Tsang adds<sup>31</sup> that, behind the scenes,

“the government remained the largest employer, the biggest developer of real estate, the leading constructor, the largest landlord, and the biggest provider of health and education services.”

Joe Studwell, founder of the China Economic Quarterly, explains that Hong Kong has been “a patchwork of de facto cartels” since the colonial era. Vital sectors such as land ownership are carved up, often through monolithic cross-sector corporate entities. In the ports, for example, container handling fees are among the world’s highest, despite low labour costs.<sup>32</sup> Until 2012 Hong Kong did not even have a functioning competition law — and the first ever legislation on this, passed in 2012, [only came into full effect in](#)<sup>33</sup> December 2015, and contains [important exemptions](#).<sup>34</sup>

## **Statist Singapore versus “free market” Hong Kong: the verdict**

A comparison with Singapore is instructive here. The two centres dominate (and compete for) offshore financial services in Asia, with Hong Kong focused more on north Asia and China, and Singapore focusing on Southeast Asia. Hong Kong’s most immediate hinterland is Southern China, though the closing of the mainland to most trade between 1949 and 1979 also forced the city to focus on business with southeast Asia more than it may otherwise have done, giving it a broader regional and international base.

The two centres have followed very different economic policies, but share similar growth trajectories. The former Singaporean premier Lee Kuan Yew, who visited Hong Kong regularly, summarised the different approaches:<sup>35</sup>

“In Hong Kong what is not expressly forbidden is permitted; in Singapore, what is not expressly permitted is forbidden.”

This underpinned very different economic and social policies too, as Lee continued:

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“The few trade unions they had did not fight market forces... There was no social contract between the colonial government and [Hong Kong’s people.] Unlike Singaporeans they could not and did not defend themselves or their collective interests. They were not a nation – indeed, were not allowed to become a nation. China would not have permitted it, and the British never tried it.”

Yet at the end of the day, different economic policies mask the core reason for both Hong Kong’s and Singapore’s success. Studwell explains:

“As relatively easily managed city states, Hong Kong and Singapore perform a simple economic trick: they arbitrage the relative economic inefficiency of their hinterlands... Since colonial inception they have offered tariff-free trade (with few or no questions asked about where the money came from) . . . the regional offshore roles of Hong Kong and Singapore have been absolute constants since their founding, and show no sign of change.”<sup>36</sup>

...  
Under Mr. Lee – who never much liked private businessmen – Singapore followed a statist model, with the government taking public control of most significant companies. Hong Kong pursued an apparently opposite free market model

...  
At the end of the 20<sup>th</sup> Century, the result of ostensibly diametrically opposite approaches to economic management was GDP per capita in the two cities that varied by less than \$1,000. The lesson? That a city state with a strategic deep water port in a region that has relatively higher levels of mismanagement, corruption and political uncertainty will prosper, with little reference to official economic philosophy. ... Hong Kong and Singapore were destined to succeed. All they had to do was to be one degree more efficient, one degree more attractive to capital than surrounding countries.”<sup>37</sup>

## Hong Kong today

Hong Kong is currently one of the world’s fastest growing international and offshore financial centres, depending heavily on international business. According to [the IMF in 2014](#),<sup>38</sup> 95 per cent of licenced banks were branches of foreign banks

(see chart below), and 53 per cent of foreign bank deposits came from Britain.



Note: The largest four foreign banks account for one half of the banking system assets

According to [a 2018 Deloitte survey](#),<sup>39</sup> Hong Kong’s wealth management industry achieved a 127 per cent growth rate between 2010 and 2017, faster than any other financial centre: adding US\$410 billion in cross-border client assets at a time when some other major financial centres like Switzerland were seeing significant outflows. Boston Consulting Group estimated in 2019<sup>40</sup> that Hong Kong’s offshore wealth sector would grow by 7.8 per cent annually to 2020, the fastest rate for any major centre, thanks to a combination of growth in the region and its position as an attractive regional “booking centre.”

Hong Kong provides a growing range of offshore offerings, and private banking, strongly reliant on secrecy, is among the most important. Since 2009, when G20 leaders declared that the “the era of banking secrecy is over” and promised a crackdown on secrecy, there has been a significant displacement of corrupt, criminal and other abusive financial activities — both in terms of assets and the structures holding those assets — away from Western centres and towards Asian tax havens, notably Singapore and Hong Kong. These two centres are now attracting wealth from abroad at more than [twice the rate of Switzerland](#).<sup>41</sup> Hong Kong held over [US \\$840bn](#)<sup>42</sup> in private banking assets in 2018, though this activity is still eclipsed by Switzerland’s private banking sector, with over [\\$2.7 trillion in assets](#)<sup>43</sup> under management.

There is also a large [trust administration](#)<sup>44</sup> industry in Hong Kong — US \$4.3 trillion was held by Hong Kong trusts in 2018. Hong Kong’s Trust Law (Amendment) bill of 2013, while modernising the laws and making some improvements, also [provides](#)<sup>45</sup> enhanced powers to settlors of trusts that could make it easier for them to pretend to give away assets — thus

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creating an impenetrable secrecy wall — while still retaining a large degree of control.

## Secrecy and phantom foreign investment

Hong Kong’s secrecy offerings have for years [made it](#)<sup>46</sup> a major round-tripping turntable, particularly for China. Round-tripping involves Chinese investors shifting their capital to Hong Kong, dressing it up in offshore secrecy and returning it to China as phantom foreign investment in order to obtain special privileges afforded to foreigners. The Asian Development Bank [remarked](#)<sup>47</sup> in 2004 that “the scale of round tripping FDI in PRC [China] is very large” and the State Administration of Foreign Enterprises [admitted](#)<sup>48</sup> that Chinese mainlanders, not foreigners, were significantly behind the flow of speculative “hot money” into China.

Round-tripping activity largely explains the fact that of the total US\$2.7 trillion in nominal inward investment into China in 2017, over US\$1.2 [trillion was sourced](#)<sup>49</sup> (nominally) from Hong Kong. The second largest direct “investor” in China by far — at US\$285 billion — was the British Virgin Islands. This compares to US\$78 billion in recorded direct US investment into China in 2015. In any case, much of the investment originating from the US is also likely to be Chinese origin capital, routed via family links within the US-Chinese diaspora. As scholars [have noted](#),<sup>50</sup> “the great majority of foreign direct investment in China has come from the Chinese diaspora.”

The same [IMF database shows](#)<sup>51</sup> the top sources of inward direct investment into Hong Kong and destinations for funds out of Hong Kong contain notorious secrecy jurisdictions and corporate tax havens:

## Other offshore attractions

Beyond secrecy, Hong Kong offers a range of other offshore attractions, notably in the areas of tax and financial regulation. In 2009 China launched a pilot scheme in Hong Kong for the settlement of offshore trade in renminbi, rather than in US dollars, the first step towards an eventual goal of making the renminbi a global reserve currency, a matter of potentially profound geo-strategic importance.<sup>52</sup> The market has grown significantly. The share of Chinese trade settled in renminbi [rose](#)<sup>53</sup> from less than one per cent in 2010 to [12 per cent](#)<sup>54</sup> in 2013, and then to [26 per cent before shrinking back to 16 per cent](#)<sup>55</sup> in 2016; the IMF meanwhile added it to its [reserve currency club](#).<sup>56</sup> In September 2011 China and the UK [agreed](#)<sup>57</sup> to start developing the City of London, via its age-old Hong Kong links, as another offshore renminbi trading centre, and by September 2013 [nearly a third](#)<sup>58</sup> of offshore renminbi trading transactions were conducted in London.

Tax is another powerful component of Hong Kong’s offshore offering. Hong Kong does not tax capital gains, dividends or deposit interest, and it has no inheritance taxes. In common with many secrecy jurisdictions, it adopts a territorial principle which only taxes income arising in Hong Kong, while profits from overseas trading operations accruing to Hong Kong wealth managers are generally not taxed. Hong Kong is widely used as a base for [transfer mispricing](#),<sup>59</sup> where corporations shift profits offshore to escape tax.

## Pushed towards change

There have been some efforts to tighten Hong Kong’s controls on dirty money — albeit from a low base — not least with its Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance in 2012, the first piece of legislation to address money laundering as a primary focus. This was prompted by a critical [2008 review](#)<sup>60</sup> from the Financial Action Task Force (FATF), which reviews countries’ anti-money laundering provisions. The new law led to a [steep rise](#)<sup>61</sup> in suspicious-transaction reports, though enforcement remains a problem.

Country (China, P.R.: Hong Kong)		Time (2016)	
<b>China, P.R.: Hong Kong</b>			
<b>Inward Direct Investment from Top Five Counterpart Economies, 2016, US Dollars, Millions</b>			
Total Investment	1,414,922	100 %	
Brit Virgin Islands	546,173	39	
China, P.R.: Mainland	337,325	24	
Cayman Islands	110,601	8	
Netherlands	91,479	6	
Bermuda	70,780	5	
<b>China, P.R.: Hong Kong</b>			
<b>Outward Direct Investment in Top Five Counterpart Economies, 2016, US Dollars, Millions</b>			
Total Investment	1,384,539	100 %	
China, P.R.: Mainland	617,507	45	
Brit Virgin Islands	514,900	37	
Cayman Islands	57,735	4	
Bermuda	30,618	2	
United Kingdom	28,800	2	

Source: IMF Data Portal. Coordinated Direct Investment Survey (CDIS)

Following the 2016 Panama Papers revelations, [which showed that Hong Kong was Mossack Fonseca's most active centre for the creation of shell companies](#),<sup>62</sup> Hong Kong finally sought to impose a licensing regime on the agents who set up such companies.

FATF had been pointing out this deficiency since 2008 (p6).<sup>63</sup> By the time of its fourth [follow-up report in 2012](#),<sup>64</sup> the Hong Kong authorities had got as far as issuing “practice circulars” and “guidelines for compliance” about the customer-identification obligations to the sectors involved in setting up companies, such as lawyers and trust- and company-service providers, but this still didn't tackle the lack of statutory regulation.

[New proposals](#)<sup>65</sup> to bring non-financial businesses within the scope of the 2012 Anti-Money Laundering Ordinance were the subject of a consultation in early 2017. Discussing FATF's impending new review in 2018, the [consultation document](#)<sup>66</sup> made Hong Kong's motives explicit:

As a matter of priority, we need to rein in DNFBPs [non-financial businesses] under the AMLO [Anti Money Laundering Ordinance], so as not to adversely affect the overall rating of Hong Kong in the mutual evaluation. Our compliance in this respect has a bearing on our hard-earned reputation as a major international financial and business centre in the world.

Under the [amendments](#),<sup>67</sup> which came into force in March 2018, trust and company service providers have a new licensing process overseen by the Registrar of Companies, while the industry bodies that currently oversee estate agents, lawyers and accountants are given statutory powers to do so for AML purposes. Non-financial businesses will be required to do due diligence to identify their customers. That, it should be noted, is already a legal requirement in other secrecy jurisdictions that populate the upper ranks of the Financial Secrecy Index.

As elsewhere, these proposals would be more effective in reducing secrecy if they were combined with a requirement to list, in a public registry, the beneficial owners of the Hong Kong-incorporated companies that providers set up. But there is no mention of this. The amended law only requires [companies themselves](#)<sup>68</sup> to identify and keep a register of their own beneficial owners, with a threshold of 25 per cent ownership. Trusts still do not have to be registered.

On automatic exchange of tax information, Hong Kong [committed in June 2016](#)<sup>69</sup> to begin exchanging under the OECD's Common Reporting Standard in 2018. After initially going the bilateral route, forcing any country wanting to obtain information with Hong Kong to sign an agreement with it, Hong Kong signed the Multilateral Competent Agreement (MCAA) that facilitates automatic exchange of information with 82 signatory jurisdictions.<sup>70</sup>

Hong Kong has also chosen “voluntary secrecy,”<sup>71</sup> which means it will provide information to its exchange partners, but will choose not to receive any.

In June 2016 Hong Kong [joined the OECD's Inclusive Framework](#)<sup>72</sup> on Base Erosion and Profit Shifting, which commits it to implementing the [country-by-country reporting component](#)<sup>73</sup> of the BEPS action plan. This standard is limited, however, to requiring country-by-country reports from large multinationals headquartered in a jurisdiction and domestic branches or subsidiaries of large groups in that jurisdiction —subject to strict OECD conditions ([see KFSI 9](#)).<sup>74</sup> This is a much lower and less effective level of disclosure than full public reporting of this information.

Hong Kong passed a BEPS law in 2018 that [requires](#)<sup>75</sup> multinational companies with annual revenue of HK\$6.8 billion (US\$870 billion) or more to file a country-by-country report in Hong Kong if their ultimate holding company is resident in Hong Kong.

## A lopsided economic success?

Hong Kong's offshore offerings have drawn large amounts of wealth to Hong Kong from elsewhere, and the territory enjoys high per capita incomes relative to others in the region. However, this is not the end of the story, as the Financial Times [notes](#):<sup>76</sup>

“There is a growing perception that Hong Kong's free market model is designed to benefit the wealthy. The city has the worst income disparity of all developed economies, according to a UN report, and one in five households lives below the poverty line.”

A [wave of protests](#)<sup>77</sup> and civil disobedience in 2014 was ostensibly about reductions in political freedoms, but the steepening wealth divide — and concerns about Hong Kong's role as a *laissez-faire* international financial centre — fired the protests, according to [many observers](#).<sup>78</sup> In the [words of](#)<sup>79</sup> Rebecca Lai, one of the protestors:

“We need to think if Hong Kong should stay an international financial centre and a paradise for global capitalism... “We need to think if this is still good for the citizens.”

The Boston Consulting Group reported that in 2012 Hong Kong had the world’s highest density of billionaire households, at 15 per million, while a fifth of the population lives in poverty and the minimum wage is US\$4.82 an hour.<sup>80</sup> Manufacturing began to plateau in about 1990 and was eclipsed by huge growth in finance and service. From 1980 to 1997 employment in manufacturing fell<sup>81</sup> from 46 per cent of total employment to just under 10 per cent. It seems likely that this dramatic fall is partly the result of [finance curse](#)<sup>82</sup> factors we have identified in other jurisdictions. Another reason for such extremes of wealth is the high ongoing cartelisation of the economy, as described above. One [account](#),<sup>83</sup> looking at rising protests in Hong Kong amid stagnant median incomes, summarises the underlying economic structure:

“a handful of the richest families hold monopolies and duopolies on everything from supermarket chains and property developments to public transportation systems, electricity providers and public service companies.”

Indeed, the months-long wave of violent protests and crackdowns in 2019, ostensibly about local-control being eroded to China, also had stark economic disparities as its backdrop, with The New York Times saying Hong Kong “may be the world’s most unequal place to live.”<sup>84</sup>

The protests have rocked Hong Kong’s reputation as an island of stability in an unstable region, causing China to react by offering [political concessions](#)<sup>85</sup> to the former Portuguese colony of Macau which could lead to expansion of offshore financial services on that territory, potentially at Hong Kong’s expense. It remains to be seen what the long-term impact of the protests will be, but already there are signs that capital is fleeing Hong Kong for safer environs, particularly Singapore.<sup>86</sup>

## Further Reading:

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## PART 2: SECRECY SCORE

### OWNERSHIP REGISTRATION

- 74 1. Banking Secrecy
- 50 2. Trust and Foundations Register
- 90 3. Recorded Company Ownership
- 100 4. Other Wealth Ownership
- 100 5. Limited Partnership Transparency

### LEGAL ENTITY TRANSPARENCY

- 90 6. Public Company Ownership
- 100 7. Public Company Accounts
- 90 8. Country-by-Country Reporting
- 88 9. Corporate Tax Disclosure
- 100 10. Legal Entity Identifier

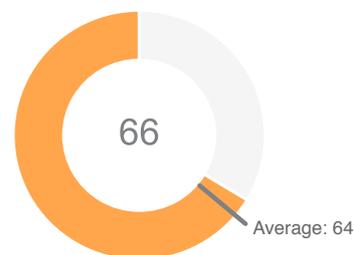
### INTEGRITY OF TAX AND FINANCIAL REGULATION

- 75 11. Tax Administration Capacity
- 38 12. Consistent Personal Income Tax
- 100 13. Avoids Promoting Tax Evasion
- 100 14. Tax Court Secrecy
- 50 15. Harmful Structures
- 20 16. Public Statistics

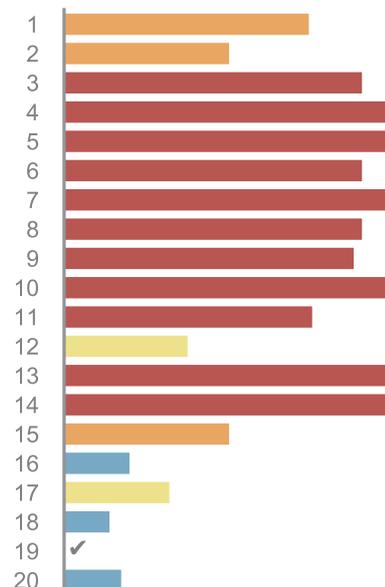
### INTERNATIONAL STANDARDS AND COOPERATION

- 32 17. Anti-Money Laundering
- 14 18. Automatic Information Exchange
- 0 19. Bilateral Treaties
- 18 20. International Legal Cooperation

### Secrecy Score



### Key Financial Secrecy Indicators



### Notes and Sources

The FSI ranking is based on a combination of a country's secrecy score and global scale weighting (click [here](#) to see our full methodology).

The secrecy score is calculated as an arithmetic average of the 20 Key Financial Secrecy Indicators (KFSI), listed on the right. Each indicator is explained in more detail in the links accessible by clicking on the name of the KFSI.

A grey tick in the chart above indicates full compliance with the relevant indicator, meaning least secrecy; red indicates non-compliance (most secrecy); colours in between partial compliance.

This report draws on data sources that include regulatory reports, legislation, regulation and news available as of 30 September 2019 (or later in some cases).

Full data is available here: <http://www.financialsecrecyindex.com/database>.

To find out more about the Financial Secrecy Index, please visit <http://www.financialsecrecyindex.com>.