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11 January 2002

Hon Ambrose Lau Hon-chuen  
Chairman of the Legislative Council  
Panel on Financial Affairs  
Legislative Council Building  
8 Jackson Road, Central  
Hong Kong

Dear Mr Lau,

**Inland Revenue (Amendment) (No.2) Bill 2001**

Thank you for giving us an opportunity on 7 January 2002 to explain to Members the objectives of the Inland Revenue (Amendment) (No.2) Bill 2001 and the security aspects on the proposals contained therein (i.e. filing of a return under the Electronic Service Delivery (ESD) Scheme by using a password, and the use of passwords in telefiling). We are grateful that Members were in general supportive of the policy of introducing the use of passwords in electronic filing of tax return, and of implementing telefiling. We understand that Members were in general satisfied with the security aspects of the systems. We also note that some Members would like to have these new services introduced as scheduled (which will be the second quarter of this year).

2. To facilitate Members' further consideration of the Amendment Bill, we provide hereunder our detailed response to and supplementary information on the questions/concerns Members raised at the meeting.

### **Security of the use of passwords in filing of tax returns**

3. The paper we issued to the Financial Affairs Panel has set out in detail the measures the Inland Revenue Department (IRD) would put in place to ensure that the systems enabling the use of passwords to file tax returns electronically and through telephone are secure.

4. As noted by some Members at the Panel meeting, the level of system integrity required or desired in an IT system has to be determined having due regard to the risk involved. With respect to the proposed system for the filing of a return under the Electronic Service Delivery (ESD) Scheme by using a password, the Information Technology Services Department (ITSD) has earlier on studied and endorsed the security of this proposal. ITSD's conclusion is that such a system will attain a high level of security in the transmission of tax data by meeting the "strong encryption" requirements and protecting the session key against third party access, and that the security level of the system is the same as in the case of digital certificate.

5. The use of a password is now widely adopted in the internet especially for most internet banking services. Internet filing of tax returns with the use of a password has been implemented in many other tax jurisdictions (including the United States, Canada and Singapore). The proposed introduction of this new means of electronic tax filing service by IRD is a move in line with these general trends of e-commerce development.

### **Telefiling Process**

6. Some Members asked what would be the usage of telefiling and what would be the procedures. The telefiling process is summarised in *Annex*. Before performing the filing, a taxpayer may put down all the information required in the tax return on the "Telefiling Record Sheet", which will be provided by IRD. The Sheet serves as a checklist and assists taxpayers in the filing process. After a filing has been performed, the system will repeat automatically the relevant tax return data keyed in by the taxpayer for his confirmation. He may then check the accuracy

of the inputted data against the record on the “Telefiling Record Sheet” and make changes to the data inputted if necessary. It will take a taxpayer around 4 to 5 minutes to complete the filing. The telefiling system will record and store the data captured during the whole return filing process in digitized format. Taxpayers may lodge a written request to IRD for a copy of the print-out of the data stored their own tax files.

7. We estimate that 800,000 taxpayers would meet the eligibility criteria for telefiling. In view of the fact that this will be a new service and that taxpayers may take some time to get used to it, the initial take-up rate may not be too high, but we expect the rate to gradually increase over time (perhaps 5% in the longer term). In other tax jurisdictions, the telefiling take-up rates range between 3% to 9% (4.1% for USA, 2.9% for Canada and 8.5% for Singapore). IRD will launch massive publicity activities to promote this new service upon enactment of the legislation.

8. The total cost of implementing the telefiling project is about \$4.8 million (\$4.2 million in non-recurrent expenditure and \$0.6 million non-recurrent staff cost). We also estimate that a staff saving of \$0.9 million a year could be achieved as a result of the lesser demand on manual filing and data input.

### **Interface with the Electronic Transactions Ordinance**

9. Some Members would like to know how the Inland Revenue (Amendment) (No.2) Bill 2001 would interface with the Electronic Transactions Ordinance (ETO) and whether the Administration would extend the use of passwords to other electronic government service applications.

10. The ETO was enacted to facilitate electronic transactions and drive e-business development by providing electronic records and digital signatures the same legal status as that of their paper-based counterparts. The Ordinance provides a generic framework that can be applied to other legislation. However, this does not preclude dealing with specific situations in the relevant ordinances in a self-contained manner. It is for

this purpose that section 14 of the ETO specifies that if an ordinance accepts the electronic process and contains an express provision with specific requirements, procedures or other specifications for the purpose, then the ETO is not to be construed as affecting that express provision. In other words, the ETO does not prevent other ordinances from providing for specific situations to facilitate electronic transactions and e-business. It is not our policy intent to put all legislative provisions concerning electronic transactions in the ETO, as such a approach may not be possible or practical.

11. A Member asked us to ensure that consistent terminologies would be used in different ordinances and quoted the Import and Export (Electronic Transactions) Bill 2001 as an example. The Import and Export (Electronic Transactions) Bill 2001 is intended to provide legal backing for the electronic submission of cargo manifests, and remove the requirement that the security device (i.e. the authentication apparatus) must be issued by Tradelink so as to allow for flexibility. The focus of the Inland Revenue (Amendment) (No. 2) Bill 2001 is to provide an alternative to the mode of authentication in satisfying the signature requirement in filing tax returns and the necessary legislative backing for the use of passwords in filing tax returns electronically. These two Bills contain provisions which cater for electronic processing in their own specific and different situations. Both are consistent with the policy intent and spirit of the ETO.

12. The Information Technology and Broadcasting Bureau (ITBB), which is the policy bureau for the promotion of e-business in Hong Kong and for the operation of the ETO, supports the use of passwords in filing tax returns and telefiling as proposed in the Amendment Bill in order to drive the development of E-government in Hong Kong. ITBB will consider whether or not the use of passwords should be widely adopted in other electronic processes. It will consult the public on the issue shortly in the context of the coming ETO review.

### **Commissioner of Inland Revenue's power in relation to specification**

13. Members asked about the Commissioner of Inland Revenue (CIR)'s power under the Amendment Bill. In clause 8 of the Amendment Bill, the Commissioner is empowered to specify certain cases where the furnishing of a return by electronic filing and the use of the telefiling system are applicable, to specify technical or other details concerning an electronic record or any attachment required to be furnished with an electronic record, and to approve a password. These eligibility criteria and form and manner of the returns are routine and operational matters, and may change from time to time. As these matters do not carry any significant policy implications, we propose to allow the Commissioner to deal with them.

14. In other tax jurisdictions like USA, Singapore, United Kingdom, Australia and Canada, their CIR equivalents are also given the power to make regulation or specifications in respect of eligibility criteria, the form and manner as well as the signature requirements of furnishing an electronic return.

### **Specific Drafting Issues**

15. Some Members referred us to the specific drafting suggestions forwarded by the Hong Kong Society of Accountants (ref. Appendix to the Society's letter to CIR dated 4 January) and urged us to review our position.

16. We have carefully examined the Society's suggestions. The Department of Justice's advice is that the wordings of "affixed" and "approved by the Commissioner" used in our Bill are appropriate. The Society's proposed wordings are inadequate in supporting the functions that a "password" is required to perform on tax returns as a "signature". The ordinary meaning of the word "affix" includes "adding something" and "attaching something", so a "password" can be "affixed" to tax returns. CIR has set out detailed comments in her reply dated 11 January 2002 to the Society.

17. The Society also suggests that we remove “any other signing device” from clause 8 of the Amendment Bill. This clause was included to cater for future technological development, such that when there is some signing device other than electronic signature and password, which attains the same level of security, the legislation would not have to be amended. We note the Society’s and Members’ concern about the uncertainty this clause could give rise to. Having reviewed our position, we are prepared to move a Committee Stage Amendment to delete this clause.

18. We hope our position as set out above would help allay any concern Members may have about the drafting of the Bill. We look forward to Members’ support of the Amendment Bill.

Yours sincerely,

(Miss Erica Ng)  
for Secretary for the Treasury

Encl.

c.c. Members of the LegCo Panel on Financial Affairs

**Internal**

CIR (Attn: Mrs Alice Lau Mak Yee-ming)  
SITB (Attn: Miss Adeline Wong)  
D of J (Attn: Mr MY Cheung)  
Law Draftsman (Attn: Ms Lonnie Ng)

### Telefiling Process

- (i) First, the taxpayer has to enter his Taxpayer Identification Number (TIN). With this TIN, the telefiling system will check whether there is any outstanding tax return for the taxpayer before he is allowed to proceed further.
- (ii) Then, the taxpayer will be asked to state the details of his income and claim for allowances for the relevant year of assessment. During this process, the system will also check whether the taxpayer's return is acceptable to be filed through telephone. If the taxpayer's information indicates that he does not fulfill the criteria (for example the taxpayer has income from business), the system will advise the taxpayer that his return is not suitable for telefiling.
- (iii) After the taxpayer has inputted the required information, the system will repeat the relevant tax return data again for the taxpayer's confirmation. The taxpayer can amend the data if necessary.
- (iv) If the taxpayer confirms that the information is in order, he will then be required to sign the tax return by inputting his password.
- (v) After verifying the taxpayer's password, the system will generate an Acknowledgement Reference Number to acknowledge that the return has been received. The taxpayer is advised to jot down this Number on the Tax Record Sheet, which can serve as an acknowledgement of receipt by IRD. This Number will also facilitate the taxpayer in case he wishes to obtain a copy of the return data as he would do in the case of a paper return.

