

Deloitte.
德勤

德勤·關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F One Pacific Place
88 Queensway
Hong Kong

電話：+852 2852 1600
傳真：+852 2541 1911
電子郵件：mail@deloitte.com.hk
www.deloitte.com/cn

Tel: +852 2852 1600
Fax: +852 2541 1911
Email: mail@deloitte.com.hk
www.deloitte.com/cn

By Email (yhcheung@legco.gov.hk)
Your Ref: CB1/BC/10/08

16 September 2009

Chairman of the Bills Committee
Legislative Council
Legislation Council Building
8 Jackson Road
Central, Hong Kong

Dear Sir,

SUBMISSION ON INLAND REVENUE (AMENDMENT) (NO. 3) BILL 2009

We have the pleasure in furnishing our comments on the Inland Revenue (Amendment) (No. 3) Bill 2009 (the "Bill"). Please refer to the enclosure for details.

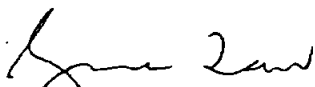
The Bill amends the Inland Revenue Ordinance to enable Hong Kong to adopt the latest international standard for exchange of information in a comprehensive avoidance of double taxation agreement. We believe the introduction of the Bill is a welcome move to promote transparency in Hong Kong's tax regime, which will, as a result, enhance interactions between Hong Kong and its economic partners and reinforce the status of Hong Kong as an international financial centre.

Whilst we support the enactment of the Bill into law, we trust it is also important for us to preserve privacy and confidentiality of information exchanged. Therefore, we have made several suggestions concerning the safeguards to protect privacy and confidentiality under the new law which we believe could further improve the enactment of the Bill.

We appreciate the opportunity to share our insights in response to the Bill, and hope that you find the comments and suggestions to be of use. As previously communicated, we will also send representatives to attend the meeting held by the Bills Committee on 8 October 2009.

Please do not hesitate to contact Mr. Davy Yun, Tax Director at 2852 6538 or the undersigned at 2852 1667 if you would like to discuss our recommendations in more detail.

Yours sincerely,
For and on behalf of
Deloitte Touche Tohmatsu



Yvonne Law
National Chief Knowledge Officer & Partner

YSL/evalee
Enclosures

Audit . Tax . Consulting . Financial Advisory.
審計 . 稅務 . 企業管理諮詢 . 財務諮詢 .

Member of
Deloitte Touche Tohmatsu

**COMMENTS ON INLAND REVENUE (AMENDMENT) (NO.3) BILL 2009
SUBMISSION BY DELOITTE TOUCHE TOHMATSU**

BACKGROUND

The Bill amends the Inland Revenue Ordinance (IRO) to enable Hong Kong to adopt the latest international standard for exchange of information (EoI) in a comprehensive avoidance of double taxation agreement (CDTA).

Currently, the EoI article adopted in our CDTAs is based on the 1995 version of the Organization for Economic Cooperation and Development (OECD) Model Tax Convention of which the Inland Revenue Department (IRD) may refuse to collect and supply the information requested by another contracting party if the IRD does not need it for domestic tax purposes. Most economies have, however, adopted the latest OECD 2004 version of the EoI article. This version categorically states that the lack of domestic tax interest does not constitute a valid reason for refusing to collect and supply the information requested by another contracting party.

Under the existing IRO, the IRD can only collect taxpayers' information for the purpose of administering the domestic tax law. In other words, IRD cannot collect any tax information unless it is for domestic tax purposes. Therefore, Hong Kong currently cannot adopt the latest international standard (i.e. 2004 version) of the EoI article. The Bill has been drafted with the aim to removing this legal constraint on the IRD's information gathering power, so that Hong Kong can adopt the latest international standard of the EoI article.

Relevant Provisions to be amended

The explanations of major proposed amendments on IRO are summarized below:

1. Section 49(1A) is added to the IRO to clarify that if any arrangements made with the government of a territory outside Hong Kong for the avoidance of double taxation contain a provision that requires disclosure of information concerning tax of that territory, then, for the purpose of that provision, those arrangements also have effect in relation to any tax of that territory that is the subject of that provision.
2. Section 51(4AA) is added to the IRO to enable specified officers of the IRD to exercise the power to require a person to provide information, to produce documents or to answer questions for the purpose of obtaining full information in regard to any matter that may affect any liability, responsibility or obligation of any person under the laws of a territory outside Hong Kong concerning tax of that territory.
3. Section 51B(1AA) is added to the IRO to enable a magistrate to exercise the power to issue search warrants in respect of a person if the magistrate is satisfied that there are reasonable grounds for suspecting that the person has made an incorrect return or supplied false information having the effect of understating the person's income or profits chargeable to tax of a territory outside Hong Kong.

4. Section 80(2D) is added to the IRO to provide that a person who without a reasonable excuse gives any incorrect information in relation to any matter or thing affecting the person's own liability (or the liability of any other person) to tax of a territory outside Hong Kong also commits an offence under the IRO. Therefore, the IRD can impose penalty on the person under the IRO.

Personal Data (Privacy) Ordinance is also amended to provide that the word "tax" in Section 58(1)(c) of that Ordinance includes tax of a territory outside Hong Kong which is the subject of Section 49(1A).

Safeguards on privacy and confidentiality

The Legislative Council Brief has mentioned various safeguards concerning the privacy and confidentiality of information exchanged. Below is a summary of the suggested type of safeguards:

1. Safeguards on individual CDTAs

In adopting the latest OECD version of EoI article in Hong Kong's CDTAs, it is suggested that the most prudent safeguards acceptable under the version to protect an individual's right to privacy and confidentiality of the information exchanged will be included. Specifically, there will be restrictions or requirements imposed on the "scope of information exchanged", the "usage of the information obtained" by the requesting party and restrictions imposed by "domestic laws of the requesting party".

2. Domestic safeguards by a set of rules under subsidiary legislation

Apart from adopting the safeguards provided by individual CDTAs, the Legislative Council Brief suggests that subsequent to the introduction of the Bill, the Council will proceed to prepare a set of rules under Section 49(6) of the IRO to set out the domestic safeguards under subsidiary legislation.

3. Procedural safeguards by Departmental Interpretation and Practice Note (DIPN)

The IRD will issue a DIPN setting out the procedural safeguards IRD must adopt in processing EoI requests.

OUR COMMENTS

Executive Summary

We trust that the introduction of the Bill is a welcome move to promote transparency in Hong Kong's tax regime, which will, as a result, enhance interactions between Hong Kong and its economic partners and reinforce the status of Hong Kong as an international financial centre.

Whilst we support the enactment of the Bill into law, there are some administrative aspects concerning the privacy and confidentiality which require careful consideration before the enactment of the Bill. We welcome that the Council has considered a number of safeguards on privacy and confidentiality of information exchanged. Our concern is how these safeguard rules can be properly set out and implemented. In particular, we have the following concerns:

1. Detailed contents of domestic safeguard rules to be set out in subsidiary legislation under Section 49(6) of the IRO are currently not available for public review and comments. Therefore, we would urge for an earlier drafting of the subsidiary legislation for public consultation.
2. The domestic safeguard rules suggest that there will be "exceptional circumstances" under which the IRD will not provide prior notification to the person being investigated nor will it need to provide the person the information that the IRD is going to transmit to the requesting party. To be fair to the person being investigated, we strongly suggest the Government define clearly the "exceptional circumstances" and set up necessary criteria and procedures for determination of these "exceptional circumstances".
3. We suggest setting up an independent tribunal for resolving any issues and disputes regarding the collection of information to be exchanged. The person being investigated should have the right to object or appeal if he is aggrieved or feels being unfairly treated during the process of the collection of information to be exchanged.
4. There will be restrictions on the usage of information exchanged by the requesting party (i.e. the CDTA partners). However, it appears that there is no similar restriction imposed on the usage of this information by the IRD on its own. We do have a concern about how the IRD will use the information. For example, if the IRD should use the information collected (which originally was requested for the purpose of exchange to our CDTA partners) for domestic tax purpose, it may be unfair to the person being investigated.

Details of our submission are set out below for your consideration.

Detailed submission

Benefits of the Bill

We believe the introduction of the Bill to align our exchange of information arrangements with the international standard is a welcome move. It not only facilitates our CDTA negotiations but also promotes transparency in Hong Kong's tax regime and interactions with economic partners. Without such move, our existing legal constraint would be a major obstacle to our CDTA negotiations. Also, any negative perceptions on the transparency of our tax regime would harm Hong Kong's reputation as an international financial centre, and may lead to sanctions imposed by other economies. This will be potentially disastrous for the Hong Kong economy as a whole.

Many Asian countries, such as Singapore, have substantial network of CDTA which provides tax benefits to multinational corporations. To maintain the competitiveness of Hong Kong as a premiere jurisdiction for holding companies or headquarters in Asia, it is necessary for us to extend our CDTA networks to avoid migration of businesses to other Asian countries. We believe with the enactment of the Bill to allow the adoption of the latest international standard for exchange of information under the CDTA, the negotiation process of CDTA will be greatly improved. It will definitely help the development and extension of our CDTA network.

Promoting transparency in tax regime is the current world trend which was emphasized by the G20 leaders at the London Summit held in April 2009. G20 Leaders called on countries to adopt the international standard for exchange of information. We trust the Bill is a significant step of showing Hong Kong's commitment to promote transparency in tax regime if Hong Kong should adopt the latest international standard for exchange of information with treaty partners.

With the adoption of the latest international standard of exchange of information and increase in transparency of our tax regime, we trust the likelihood that Hong Kong being viewed as a tax haven by international community would be minimized. Actually, the discussion on tax haven in a number of public forums has pointed out that the refusal or inability to exchange information with other jurisdictions is one of the criteria in accessing whether a jurisdiction should be treated as a tax haven. The existing legal constraint on Hong Kong's exchange of information has placed a major obstacle for Hong Kong to exchange information with other jurisdictions. Therefore, it is necessary for Hong Kong to review the existing provisions and remove such obstacle. We believe the Bill is the right move to achieve it.

In view of the above, we support the enactment of the Bill.

Concerns – privacy and confidentiality

Whilst we support the enactment of the Bill into law, there are some practical aspects concerning privacy and confidentiality which require careful consideration before the enactment of the Bill.

The public may inevitably raise privacy concerns with regard to changing the legislation under Section 49(6) of the IRO to expand the IRD's power for collection and disclosure of information. We note that various safeguards have been considered to protect an individual's right to privacy and confidentiality of the information exchanged. To strike a balance between the protection of secrecy and the power of collection and disclosure of information under the EoI article, it is critical that the various "safeguards" on privacy and confidentiality of information exchanged could be properly set out and implemented.

Regarding the safeguards proposed in the Legislative Council Brief, we have the following concerns:

1. Earlier release of the contents of domestic safeguard rules

We welcome the inclusion of domestic safeguard rules in the form of subsidiary legislation to protect taxpayers' right to privacy and confidentiality of the information exchanged. Our concern, however, is that the rules will only be available subsequent to the introduction of the Bill. The domestic safeguard rules to be set out in subsidiary legislation are important for the protection of the privacy and confidentiality of information exchange. Therefore, we believe the earlier release of these rules in the form of draft legislation for public review is more desirable. Preferably, the rules should be available for public review and comment at the same time when the current Bill is considered. So the public can have a whole picture of the Bill and give precise comment accordingly.

2. Clear definition of the "exceptional circumstances" under which notification is not required

It has been proposed that under normal circumstance, the IRD has to notify and provide the person the information that the IRD is going to transmit to the requesting party. However, under "exceptional circumstances", such notification is not required. The exceptional circumstances will include where notification would prevent or unduly delay the effective exchange of information or where prior notification would otherwise undermine the chance of success of the investigation conducted by the requesting party.

We are of the view that the right of being notified should be preserved as far as possible and we believe that there will only be a few and rare cases where "exceptional circumstances" should apply. To be fair to the person being investigated, we strongly suggest that the Government clarify and define clearly what will lead to the situation so called "exceptional circumstances" and apply the following measures:

- a) Set up clear criteria and guideline to define the "exceptional circumstances";
- b) Establish necessary procedures for the determination of "exceptional circumstances";
- c) Only very senior authorized persons are empowered to approve the type of situations which will fall within the "exceptional circumstances"

To ensure a fair treatment is given to every person being investigated, we trust the above measures are necessary. Also, with clear criteria and guidelines, it will minimize the chance of unnecessary disputes in this regard.

3. Establishment of an independent tribunal for resolving disputes

Under the domestic safeguards, it is suggested that the person being investigated can verify the accuracy of information with the IRD and if the IRD refuses to accept the proposed correction to the information, the person may seek a review by a higher authority (which is now proposed to be the Financial Secretary), whose decision on the matter shall be final. We are pleased to note that the Government will set up such a mechanism for taxpayers to seek review by a higher authority. However, the public may have concerns on the objectivity of the final decision if the review is conducted by a government personnel. Thus, we suggest that an independent tribunal be set up for resolving the disputes, instead of a final review conducted by the Financial Secretary. The tribunal could be similar to the Board of Review which is currently responsible for deciding on tax disputes between taxpayers and the IRD.

The independent tribunal can also help to resolve any other issues and disputes regarding the collection of information to be exchanged. We trust it is fair that the person being investigated should have the right to object or appeal if the person is aggrieved or feels being unfairly treated during the process of the collection of information to be exchanged.

4. Restricted usage of the information obtained under the new law by domestic party

The restriction imposed on the usage of information exchanged to be set out in the individual CDTAs under the latest OECD model only applies to the "requesting party", i.e. the foreign CDTA party. It seems there is no restriction on the usage of the information by the domestic party (i.e. the IRD). As the underlying objective of the collection of the information is for the use of the requesting party, we are of the opinion that information collected should be treated as secret information and restricted for access by any other party for purpose other than the stated purpose, including the use of this information for domestic tax purpose by the domestic party (i.e. IRD) so as to avoid any unfair treatment to the person being investigated. We will be glad to see if the Bills Committee can consider setting out such restriction by either domestic safeguards through subsidiary legislation or the procedural safeguards in DIPN issued by the IRD.

Conclusion

The Bill amends the IRO to enable Hong Kong to adopt the latest international standard for exchange of information in CDTA with the objective to promote Hong Kong's tax and economic developments. Overall, we support the enactment of the Bill. We trust the Bill is a right and welcome move as long as there are proper safeguards to protect privacy and confidentiality of information exchanged.