

羅兵咸永道有限公司

PricewaterhouseCoopers Ltd.
21/F, Edinburgh Tower
15 Queen's Road Central
Hong Kong
Telephone +852 2289 8888
Facsimile +852 2810 9888
pwchk.com

By email (yhcheung@legco.gov.hk) and by post

Hon Paul CHAN Mo-po, MH, JP
Chairman,
Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2009
Legislative Council
Hong Kong SAR Government

5 November 2009

Dear Hon Paul Chan,

We refer to your letter dated 21 October 2009 inviting us to give comments on the following documents provided by the Administration in connection with the Inland Revenue (Amendment) (No. 3) Bill 2009 ("Bill"):

1. Outline of the Proposed Safeguards to be covered by the Inland Revenue (Disclosure of Information) Rules ("Rules"); and
2. Departmental Interpretation and Practice Notes – Implementation Details of Exchange of Information Provisions under Comprehensive Double Taxation Agreements (Extract of the part on "Administrative Guidelines") ("DIPN Extract").

PricewaterhouseCoopers welcome and commend the Hong Kong SAR Government's positive response to the submissions made by various organisations and its swift actions of putting in place the above two draft documents. While we are happy to see some of the comments in our submission (as well as the other submissions) have been taken into account by the Administration, we, however, have the following comments on the Rules, the DIPN Extract and the Administration's response to the issues raised at the meeting of the Bills Committee on 8 October 2009 as summarised in LC Paper CB(1)106/09-10(02) ("Paper"):

The Rules

- Provision 4(c) refers to "any other procedures that may be specified by the Commissioner". The approvers of disclosure requests are legally obligated under the Rules to consider if the requests comply with the procedures referred to in this provision. At present, it appears to us that this refers to the procedures set out in the Appendix of the proposed DIPN. If this is the case, we consider that a clarification to the legal status of those procedures is required given that the content of the proposed DIPN will not be legally binding.
- Provision 5(c) sets out two specific grounds on which the person may request the Commissioner to amend the information to be disclosed, namely (i) the information does not relate to the person or (ii) the information is factually incorrect. We consider that the right to verification and appeal should not be confined to these two grounds but should also be with respect to whether such information is complete and within the

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scope of exchange under the relevant Comprehensive Double Tax Agreement (“CDTA”). It would be helpful if the Administration can explain the rationale and legislative intent of restricting the basis of making a request for amendment to these two grounds.

- Provision 7(b) of the Rules states that notification is not required if the Commissioner has reasonable grounds to believe that the notification is likely to undermine the chance of success of the investigation in relation to which the request is made. To minimise uncertainty and avoid unnecessary misconception, we suggest that this provision be amended in such a way that application of this exception would be confined to specific cases where the requesting government has indicated such likelihood and where the Commissioner agrees with the requesting government’s view.

The DIPN Extract

- Paragraph (b) on page 2 of the DIPN Extract refers to “any procedures applicable to the request that may be specified in any instrument that amends or supplements the relevant arrangement”. In cases where the international safeguards listed under paragraph 9 of the Legislative Council Brief dated 24 June 2009 are prescribed in a memorandum of understanding, agreed minutes of meetings, or an exchange of correspondence instead of a protocol, we presume that those safeguards would not have the same legal status as those in a protocol which forms part of the CDTA. If this is the case, we consider it is important for the Hong Kong SAR Government to make its best effort to incorporate those international safeguards into a protocol instead of the other instruments mentioned above in future negotiation of CDTAs.
- As stated above (i.e. point 1 under “the Rules”), the legal status of the procedures specified in the Appendix to the proposed DIPN should be clarified.
- Paragraph 3 of the Appendix specifies a list of information that the requesting party must provide in its disclosure request as one of the measures to ensure the request is specific and made on a legitimate basis. In particular, paragraph 3(b) requires the requesting party to provide the identity of the person(s) in relation to whom the information is requested i.e. the so called “subject person”.
- We are of the view that based on the spirit of no fishing expeditions, the information obtained by the requesting party from a disclosure request made with respect to the subject person should only be used for the purpose of investigating the tax matters of that subject person and not any other persons. If the requesting party would like to carry out an investigation of persons other than the subject person, it should initiate a separate disclosure request in respect of that other person so that that other person is given the rights specified in Provision 5 of the Rules.

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- While we understand that the above may be beyond the control of the Hong Kong SAR Government, we would like to ask if the Hong Kong SAR Government has considered this issue and the possibility of incorporating the above restriction on the usage of information into say, a protocol to a CDTA.
- Paragraph 4 of the Appendix allows the Commissioner to add, amend or remove any of the procedures set out in the Appendix, either generally *or in any particular case*, as he or she sees fit. While we understand that there needs to be certain flexibilities for the Commissioner to amend the procedures set out in the Appendix from time to time for the effective implementation of exchange of information (“Eol”), we believe adequate mechanism or measures should be put in place to monitor/review, in particular, discretion exercised by the Commissioner over amending or removing any of the specified procedures in individual cases in order to protect the interests of the person concerned.
- As we were only provided with the extract of the Part on “Administrative Guidelines” instead of the full version of the draft DIPN, we were unable to comment on the adequacy and usefulness of the other guidelines contained in the DIPN. We consider that it is particularly important for the DIPN to explain in sufficient details how requests to Commissioner for amendments under provision 9 of the Rules and requests to Financial Secretary for directions under provisions 10 & 11 of the Rules will be handled and how such process will take place for fair and transparency purposes.

The Paper

- Paragraph 7 of Annex A refers to the commencement Article in a CDTA as the basis of declining any request from treaty partners to give retrospective effect of the Eol arrangement. The Administration’s response on page 8 of Annex D further mentions that Eol will neither take place retrospectively nor involve information coming into existence before the CDTAs are signed.

While we support the view that the Eol provisions in any newly signed CDTAs/protocols/memoranda of understanding, etc. should not have retrospective effect, we believe it is important for the Hong Kong SAR Government to agree with the treaty partners on what does “retrospective effect” mean and seek to incorporate the agreed interpretation in a protocol or memorandum of understanding or instrument with a similar nature for the avoidance of doubt. For example, it is possible for a piece of information that exists before the signing of a CDTA to be relevant to a taxable period after the CDTA is signed. In such case, there could be different views as to whether a request for such information constitutes retrospective application of the Eol provisions and whether the commencement Article of the CDTA can form the basis of declining such request. On a without prejudice basis, we are of the view that the Eol provisions in any newly signed CDTAs/protocols/memoranda of understanding, etc.

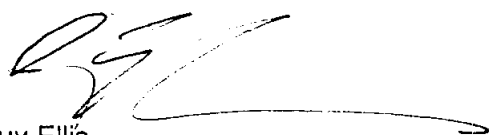
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should not have effect with regard to the taxable periods before such documents are signed.

- The Administration's response to the concerns on prior notification and the opportunity to object prior to the exchange takes place on page 10 of Annex D states that "in case there is a correction, we will inform the requesting party accordingly". This should be clearly stated in the DIPN (if not already done so) together with the details of how this will be done. For example, by when will such amendment be passed on to the requesting party?
- Similarly, the Administration's response on page 12 of Annex D that "the Inland Revenue Department ("IRD") will not send out the information until a **final decision** has been made" in cases where a decision is pending from a higher authority should be specified in the DIPN and more ideally, be incorporated as part of the Rules. A clarification of what is meant by a "final decision" is also warranted. For example, the Rules stipulate that the decision made by the Financial Secretary shall be final but we presume that such decision could be subject to a judiciary review. In such cases, will the IRD wait for the outcome of the judiciary review before it proceeds with dealing with the information request?
- Likewise, we would suggest that the Administration's response on page 4 of Annex D that "the IRD will decline any request for records that go beyond the 7-year statutory time limit for record keeping under the IRO" should be specified in the proposed DIPN.

If you have any questions on our submission, please feel free to contact me at guy.ellis@hk.pwc.com or Mr Fergus Wong, our technical director, at fergus.wt.wong@hk.pwc.com.

Yours faithfully,
For and on behalf of PricewaterhouseCoopers Limited


Guy Ellis
Partner
Tax Services