

**Legislative Council  
Panel on Financial Affairs**

**Exchange of Information under  
Agreements for Avoidance of Double Taxation**

**PURPOSE**

This paper briefs Members on the proposed legislative amendments to the Inland Revenue Ordinance (IRO) to enable Hong Kong to adopt the latest international standard for exchange of information (EoI) in our comprehensive avoidance of double taxation agreements (CDTAs).

**BACKGROUND**

*Double Taxation Agreements*

2. Double taxation, which arises when the same source of income or profits is subject to tax in more than one jurisdiction, impedes trade, investment and the flow of talent among economies. To avoid this problem, jurisdictions sign bilateral avoidance of double taxation agreements to clarify each other's taxing rights. Besides, a CDTA will normally result in reduced withholding tax rates on passive incomes such as dividends, royalties and interest. As a business facilitation initiative, the Government has been seeking to sign CDTAs<sup>1</sup> with our major trading partners since 1998-99.

*EoI Article*

3. A CDTA would normally include an EoI article that provides for the exchange of information necessary for the carrying out of the agreement between the two contracting parties. The EoI article Hong Kong currently adopts in our CDTAs is based on the 1995 version of the Organisation for Economic Cooperation and Development (OECD) Model Tax Convention (see Annex A). According to this version, the Inland Revenue Department (IRD) may refuse to collect and supply the information requested by another contracting party if the Department does not need it for domestic tax purposes. Most developed economies have, however, adopted the OECD 2004 version of the EoI article (see Annex B). This version categorically states that the lack of domestic tax interest

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<sup>1</sup> So far, we have concluded CDTAs with Belgium (2003), Thailand (2005), Mainland China (2006), Luxembourg (2007) and Vietnam (2008) and are negotiating CDTAs with 11 economies.

does not constitute a valid reason for refusing to collect and supply the information requested by another contracting party.

#### *Constraints under Hong Kong's tax law*

4. Hong Kong currently cannot adopt the 2004 version of the EoI article because under the IRO, IRD can only collect taxpayers' information for the ascertainment of liability, responsibility and obligation under the domestic tax law. In other words, IRD cannot collect any tax information unless it is for domestic tax purposes. This legal constraint on IRD's information gathering power has been a major obstacle to our CDTA negotiations because most economies have adopted the 2004 version of the EoI article. This constraint has reduced the number of our potential CDTA partners, and restricted the progress of our negotiations.

#### *Consultations on liberalisation of EoI*

5. Despite our legal constraints, Hong Kong has been very supportive of efforts by the international community to promote transparency of tax administration. As early as in 2005, we openly endorsed OECD's Principles of Transparency and Effective Exchange of Information at the OECD Global Forum on Taxation held in Melbourne. On the domestic front, we consulted the business and professional sectors on the liberalisation of EoI under CDTAs in 2005 and 2008. While views were divided in the 2005 consultation exercise, most of the stakeholders in some 50 business chambers, professional bodies and advisory committees we consulted between July and October last year indicated support for liberalisation so that we can expand Hong Kong's CDTA network. In view of this consultation outcome, the Financial Secretary announced in the 2009-10 Budget that the Government would put forward legislative proposals by the middle of this year to align our EoI arrangements with the international standard.

#### *Recent development*

6. Our inability to adopt the 2004 EoI version has also caused negative perceptions on the transparency of Hong Kong's tax regime. At the London Summit held on 2 April 2009, G20 Leaders called on countries to adopt the international standard for exchange of information. After the Summit, the OECD published three lists identifying tax jurisdictions which have substantially implemented the OECD standard, tax jurisdictions which have committed to the OECD standard but have not yet substantially implemented it, and tax jurisdictions which have not committed to the standard. The OECD has not put Hong Kong on the lists, but pointed out our commitment to implement the OECD

standard in a footnote to the lists. G20 Leaders also agreed to develop a toolbox of counter measures by the end of 2009 and review countries' implementation of the OECD standard at the next G20 Finance Ministers and Central Bank Governors Meeting to be held in November 2009.

7. We have explained our case to overseas authorities that Hong Kong maintains a simple and highly transparent tax regime and our relatively low tax rate is a result of our prudent fiscal policy. While Hong Kong should not be compared to those jurisdictions which seek to attract tax evading foreign capitals through zero or nominal tax rates, complicated and opaque tax rules, as well as bank secrecy laws, continued negative perceptions on the transparency of our tax regime would harm Hong Kong's reputation as an international financial centre, and could lead to sanctions imposed by other economies.

## **PROPOSAL**

### *Legislative amendments*

8. To adopt the OECD 2004 version of the EoI article in our CDTAs, we propose to amend the IRO to expand IRD's powers to gather information. Specifically, we propose to expand the following powers of IRD –

- Section 51(4)(a) - the power to request taxpayers and any other persons to provide information; and
- Section 51B - the power to issue search warrants for documents containing the required information which may afford evidence material in assessing the tax liability of a taxpayer.

9. Currently, the above information gathering powers of IRD are confined to the ascertainment of Hong Kong taxes. We propose to amend the above provisions to the effect that IRD can also exercise these powers and share the information obtained in response to requests for information made by our CDTA partners for their own tax purposes.

### *Confidentiality of information exchanged*

10. In adopting the OECD 2004 version of EoI article in our CDTAs, we will deploy the most prudent safeguards available under the version to protect the confidentiality of the information exchanged. The information exchange will be conducted on a case-specific basis in response to legitimate requests. There will not be any automatic or wholesale exchange of information. Besides, the relevant authority of a contracting party must observe the following protocols –

- It must satisfy IRD that the information it requests is “necessary” or “relevant” for the carrying out of the CDTA or the administration or enforcement of its local tax laws. This is a safeguard against “fishing expeditions”.
- It must treat the information provided as secret information under its domestic laws.
- It must not share the information provided with any third party (including a third jurisdiction or another government department of its own jurisdiction).
- It must only use the information provided for purposes specified in the CDTA.

## **WAY FORWARD**

11. We are drafting the relevant legislative amendments and aim at introducing the relevant amendment bill into the Legislative Council later this year.

**Financial Services and the Treasury Bureau**  
**April 2009**

**Organisation for Economic Co-operation and Development Model  
Tax Convention on Income and on Capital  
Exchange of Information Article (1995 version)**

1. The competent authorities of the Contracting States shall exchange such information as is necessary for carrying out the provisions of this Convention or of the domestic laws of the Contracting States concerning taxes covered by this Convention insofar as the taxation thereunder is not contrary to this Convention. Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes covered by this Convention. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.

2. In no case shall the provisions of paragraph 1 be construed so as to impose on a Contracting Party the obligation:

- (a) to carry out administrative measures at variance with the laws and the administrative practice of that or of the other Contracting Party;
- (b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting Party;
- (c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information, the disclosure of which would be contrary to public policy (*ordre public*).

**Organisation for Economic Co-operation and Development  
Model Tax Convention on Income and on Capital  
Exchange of Information Article (2004 version)**

1. The competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of this Convention or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. The exchange of information is not restricted by Articles 1 and 2.
  
2. Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes referred to in paragraph 1, or the oversight of the above. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.
  
3. In no case shall the provisions of paragraphs 1 and 2 be construed so as to impose on a Contracting State the obligation:
  - (a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State;
  
  - (b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State;
  
  - (c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (*ordre public*).

4. If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall use its information gathering measures to obtain the requested information, even though that other State may not need such information for its own tax purposes. The obligation contained in the preceding sentence is subject to the limitations of paragraph 3 but in no case shall such limitations be construed to permit a Contracting State to decline to supply information solely because it has no domestic interest in such information.

5. In no case shall the provisions of paragraph 3 be construed to permit a Contracting State to decline to supply information solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.