

**立法會**  
**Legislative Council**

LC Paper No. CB(1)2801/09-10

Ref: CB1/SC/10/09

**Subcommittee on the three  
Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with  
respect to Taxes on Income) Orders gazetted on 2 July 2010**

**Background Brief**

**Purpose**

This paper sets out the background to the three Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) Orders gazetted on 2 July 2010. The paper also summarizes the views and concerns of members of the Panel on Financial Affairs (FA Panel) and the Bills Committee on Inland Revenue (Amendment) (No.3) Bill 2009 on the subject of Comprehensive Agreements for Avoidance of Double Taxation (CDTAs).

**Background**

Comprehensive Agreements for Avoidance of Double Taxation

2. Double taxation refers to the imposition of comparable taxes in more than one tax jurisdiction in respect of the same source of income. The international community generally recognizes that double taxation hinders the exchange of goods and services, movements of capital, technology and human resources, and poses an obstacle to the development of economic relations between economies. As a business facilitation initiative, the Government has been seeking to enter into CDTAs with Hong Kong's major trading partners since 1998-1999.

3. While a local resident's income derived from sources outside Hong Kong would not be taxed in Hong Kong and hence would not be subject to double taxation, double taxation may occur where a foreign jurisdiction taxes its own residents' income derived from Hong Kong. Despite that many jurisdictions do provide their residents with unilateral tax relief for the Hong Kong tax they paid on income derived therefrom, the existence of a CDTA will provide enhanced certainty and stability in

respect of the elimination of double taxation. Besides, the tax relief provided under a CDTA may exceed the level provided unilaterally by a tax jurisdiction.

#### Inland Revenue (Amendment) (No.3) Bill 2009

4. A CDTA would normally include an article that provides for the exchange of information (EoI) necessary for the carrying out of the agreement between the two contracting parties. To enable Hong Kong to adopt the latest international standard for EoI under CDTAs, i.e. the 2004 version of the EoI article of the Organization for Economic Cooperation and Development (the OECD Model Article), the Administration introduced the Inland Revenue (Amendment) (No.3) Bill 2009 into the Legislative Council (LegCo) on 29 June 2009. The Bill was passed on 6 January 2010, and the Inland Revenue (Amendment) Ordinance 2010 came into operation on 12 March 2010.

5. The OECD Model Article 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. Before enactment of the Inland Revenue (Amendment) Ordinance 2010, the Inland Revenue Department (IRD) could only collect taxpayers' information for the ascertainment of liability, responsibility and obligation under the domestic tax law. In other words, IRD could not collect any tax information unless such information was for domestic tax purposes. This constraint had reduced the number of Hong Kong's potential CDTA partners, and restricted the progress of the negotiations for CDTA. Upon the commencement of operation of the Inland Revenue (Amendment) Ordinance 2010, IRD is authorized, among other things, to collect information concerning tax of a foreign territory for the purpose of EoI under a CDTA, and supply such information to the other contracting party of a CDTA.

#### Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) Orders in respect of CDTAs with Brunei, the Netherlands and Indonesia

6. Under section 49(1A) of the Inland Revenue Ordinance (IRO) (Cap. 112), the Chief Executive in Council may, by order, declare that arrangements have been made with the government of any territory outside Hong Kong with a view to affording relief from double taxation in relation to income tax and any tax of a similar character imposed by the laws of that territory. L.N. 89 to L.N. 91 are made by the Chief Executive in Council under section 49(1A) of the IRO to give effect to the following CDTAs respectively -

- (a) the Agreement between the Government of the Hong Kong Special Administrative Region of the People's Republic of China (HKSAR Government) and the Government of His Majesty the Sultan and Yang Di-Pertuan of Brunei Darussalam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income signed on 20 March 2010 (the Brunei Agreement);

- (b) the Agreement between HKSAR Government and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income signed on 22 March 2010 (the Dutch Agreement); and
- (c) the Agreement between HKSAR Government and the Government of the Republic of Indonesia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income signed on 23 March 2010 (the Indonesian Agreement).

7. According to the Legislative Council Briefs on L.N. 89 to L.N. 91, the above CDTAs set out clearly the allocation of taxing rights between Hong Kong and Brunei/the Netherlands/Indonesia and the relief on tax rates on different types of income. It will help investors of the economies to better assess their potential tax liabilities from cross-border economic activities, foster closer economic and trade links between the two places, and provide added incentives for enterprises of Brunei, the Netherlands and Indonesia to do business with or invest in Hong Kong, and vice versa.

8. During the scrutiny of the Inland Revenue (Amendment) (No. 3) Bill 2009, the Administration presented a sample EoI Article to the Bills Committee vide LC Paper No. CB(1)106/09-10(02). According to the relevant Legislative Council Briefs, the Brunei Agreement and the Indonesian Agreement have adopted all the safeguards in the sample EoI Article. In respect of the Dutch Agreement, the EoI Article therein has adopted some of the safeguards sample EoI Article. However, in relation to the disclosure of information concerning tax covered by the Agreement, the Administration had requested to confine the disclosure to the Dutch tax authorities as provided in the sample EoI Article, but not their "oversight body". The Dutch side insisted that the reference to "oversight body" in the EoI Article is necessary to cater for submission of information relating to cases being considered by "de Algemene Rekenkamer" (the Court of Audit) or "de Nationale Ombudsman" (the National Ombudsman). The Administration considered this a justifiable request and had therefore accepted the Dutch proposal.

9. L.N. 89 to L.N. 91 will come into operation on 18 November 2010.

## **Members' concerns and views**

### Panel on Financial Affairs

10. The Administration briefed the FA Panel on 4 May 2009 before introducing the legislative amendments to enable Hong Kong to adopt the OECD Model Article in signing CDTAs. The following views were expressed by members at the Panel meeting:

- (a) taking into consideration the uniqueness of Hong Kong's small and open financial market and the possible number of EoI requests from the contracting parties, the proposed extension of IRD's powers to gather information from taxpayers and provide the information to contracting parties should be examined with extra caution;
- (b) EoI under CDTAs should be limited to the information on a specific taxpayer in a case, but not those on his business counterparts and associates; and
- (c) measures and mechanisms should be in place to protect the confidentiality of the information exchanged and the privacy of the taxpayers concerned

#### Bills Committee on Inland Revenue (Amendment) (No.3) Bill 2009

11. During the deliberations of the Bills Committee on the Inland Revenue (Amendment) (No.3) Bill 2009, members were mainly concerned about the adequacy of safeguards to protect taxpayers' right to privacy and confidentiality of the information disclosed to the requesting party in the EoI under CDTAs. In this connection, apart from scrutinizing the Bill, the Bills Committee also examined the various safeguards to be provided in the form of subsidiary legislation and departmental guidelines. The specific concerns of members and the Administration's responses were summarized in the ensuing paragraphs.

#### *Approach for setting out the EoI safeguards*

12. Some members and deputations considered that the fundamental safeguards on the scope and usage of information exchanged should be provided in the primary legislation. The Administration explained that according to available information and its enquiries, other jurisdictions did not provide standard OECD EoI safeguards in their primary legislation. Instead, the following safeguards would be put in place –

- (a) incorporating the most prudent safeguards acceptable under the OECD Model Article in individual CDTAs, which would be implemented as subsidiary legislation subject to the negative vetting procedure, or in documents of record between the two contracting parties;
- (b) putting in place domestic safeguards through a set of rules (known as the Inland Revenue (Disclosure of Information) Rules) to be made under section 49(6) of the Inland Revenue Ordinance<sup>1</sup>; and

---

<sup>1</sup> At the Council meeting on 3 March 2010, LegCo approved the Inland Revenue (Disclosure of Information) Rules by way of a resolution made under section 49 of the Inland Revenue Ordinance (Cap. 112).

- (c) setting out the procedural guidelines for IRD in the processing of EoI requests in a Departmental Interpretation and Practice Note (DIPN).

13. To address members' concerns, the Administration presented a sample EoI Article to the Bills Committee (LC Paper No. CB(1)106/09-10(02) and undertook to set out clearly all the safeguards adopted in individual CDTAs and any deviation from the sample text in its submissions to LegCo on subsidiary legislation to implement CDTAs. The Administration also agreed to subject the proposed Inland Revenue (Disclosure of Information) Rules (the Rules) to the positive vetting procedure, rather than the negative vetting procedure as originally proposed.

*No retrospective effect of EoI arrangements under CDTAs*

14. Members considered that the EoI arrangements under CDTAs should have no retrospective effect, i.e. IRD would not entertain any request for information relating to a period before the effective date of the respective CDTAs. The Administration advised that a standard article would be included in all CDTAs setting out that all provisions under the CDTA should have effect from a stipulated date as agreed and should only apply to taxes after the effective date, and IRD would not disclose any information in response to a disclosure request unless the information did not relate to any period before the relevant CDTA came into operation.

15. Having considered members' views, the Administration agreed to add a provision in the Rules stipulating that there shall be no retrospective effect for EoI arrangements under CDTAs, and that no information existing at any time prior to the effective date of a CDTA shall be disclosed.

*Scope of information exchanged*

16. Under the OECD Model Article, the requesting party should satisfy IRD that the information requested was "foreseeably relevant" for the carrying out of the CDTAs or to the administration or enforcement of the requesting party's local tax laws. Members were concerned whether the term "foreseeably relevant" could adequately restrict the scope of information exchanged. The Administration explained that the term "foreseeably relevant" was recommended by OECD and adopted internationally in the EoI article of CDTAs to guard against "fishing expeditions".

17. To provide greater clarity in the restriction of the scope of information exchanged, the Administration agreed to make reference to the Eighth Schedule of the Income Tax (Amendment) (Exchange of Information) Act of Singapore, and set out in the Rules the information that should be provided in an EoI request. Moreover, the Administration would expand the relevant part of IRD's DIPN to set out the principle that the test of relevancy should be based on the information provided by the requesting party in the EoI request, and that the EoI request must contain information on the relevance of the information to the purpose of the request.

*Confidentiality and usage of information exchanged*

18. Members expressed concern about the disclosure of information exchanged to a third party such as the oversight body of the tax authorities and/or another jurisdiction. The Administration advised that as part of the safeguards in CDTAs, the requesting party should be restricted from sharing the information provided with any third party (including a third jurisdiction or another government department of its own jurisdiction). Some of the additional measures such as confining disclosure of information to the tax authorities but not their oversight bodies would need to be worked out during the negotiation of individual CDTAs.

*Notification of disclosure of information*

19. On the mechanism for notifying the relevant taxpayers, the Bills Committee noted that the Administration would prescribe in the Rules the notification procedures that the Commissioner of Inland Revenue shall follow before any information was disclosed. The person concerned might request a copy of the information, make a request for amendments to the information, and apply to the Financial Secretary for a review of the IRD's decision on the request for information amendments. To address the concern of the Bills Committee, the Administration agreed to extend the time allowed for the person concerned to submit proposed amendments to the Commissioner of Inland Revenue from 14 days to 21 days. The IRD would also send out the first notice as soon as practicable upon its decision to proceed with the EoI request.

20. Some members were concerned that on request of the requesting party, IRD might give no notification or prior notification to the person concerned, thus depriving the person of the protection of the right of being notified. In this connection, the Administration explained that a requesting party who made such a request must provide explanations and evidence relating to the making of such a request. The Administration agreed to elaborate further on the details to be provided by the requesting party in this aspect in the Schedule to the Rules.

*Review of decision of IRD*

21. Under the Rules, where the Commissioner partially approves or refuses a request for amendments, the person concerned may request the Financial Secretary (FS) to direct the Commissioner to make the amendments. Given the standard 90-day response time set by OECD for EoI, members were concerned whether the information would have been transmitted to the requesting party before completion of the review procedure. The Administration advised that it would be stipulated in the DIPN that the relevant information would not be transmitted to the requesting party before completion of the review procedure, if a review was requested.

22. There were views that an independent tribunal/appeal panel/the Board of Review should be authorized to review IRD's decisions on disclosure of information

under a CDTA, and that the Financial Secretary (FS) be empowered to review the question of law on the decisions of IRD on collection or disclosure of information, in addition to the power to review the question of fact, i.e. the accuracy of the information to be disclosed by IRD.

23. The Administration advised that FS, as the oversight body under the law, would review submissions on factual accuracy of the information. If a person thought that IRD had not properly discharged its responsibility to ensure that the information requested was within the scope of the relevant CDTA or the law, he could challenge IRD's decisions/actions through judicial review. The Administration agreed to report to the Panel on Financial Affairs on the effectiveness of the proposed notification and appeal system 18 months after implementation.

#### *Precedence effect of arrangements in CDTAs*

24. Members were concerned that the proposed section 49(1A)(a) of IRO, which stipulated that arrangements specified in CDTAs "shall have effect in relation to tax under this Ordinance despite anything in any enactment", might result in excessive overriding effect on provisions concerning protection of fundamental human rights in other ordinances.

25. The Administration explained that CDTAs allocated taxing rights between two treaty partners. A company that would otherwise be subject to tax at a certain rate under Hong Kong laws might be entitled to a lower rate (or not taxed at all) because of a piece of subsidiary legislation that implemented a CDTA. In such a case, that piece of subsidiary legislation would take precedence over the said Hong Kong laws. The effect of any CDTA and its implementing subsidiary legislation would be limited to "tax under the IRO" and any precedence effect would be accordingly limited.

#### **Relevant papers**

26. Relevant papers are available at the following links:

The Administration's paper for the FA Panel meeting on 4 May 2009  
<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0504cb1-1408-3-e.pdf>

Minutes of FA Panel meeting on 4 May 2009 (paragraphs 8 to 26)  
<http://www.legco.gov.hk/yr08-09/english/panels/fa/minutes/fa20090504.pdf>

Report of the Bills Committee on Inland Revenue (Amendment) (No.3) Bill 2009  
<http://www.legco.gov.hk/yr08-09/english/bc/bc10/reports/bc100106cb1-755-e.pdf>

LC Paper No. CB(1)106/09-10(02) on sample EoI Article  
<http://www.legco.gov.hk/yr08-09/english/bc/bc10/papers/bc101027cb1-106-2-e.pdf>

The Inland Revenue (Disclosure of Information) Rules  
<http://www.legco.gov.hk/yr09-10/english/subleg/positive/hc0226cb3-456-a-e.pdf>

LegCo Brief provided by the Financial Services and the Treasury Bureau on  
Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Brunei Darussalam) Order  
[http://www.legco.gov.hk/yr09-10/english/subleg/brief/89\\_brf.pdf](http://www.legco.gov.hk/yr09-10/english/subleg/brief/89_brf.pdf)

LegCo Brief provided by the Financial Services and the Treasury Bureau on  
Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Kingdom of the Netherlands) Order  
[http://www.legco.gov.hk/yr09-10/english/subleg/brief/90\\_brf.pdf](http://www.legco.gov.hk/yr09-10/english/subleg/brief/90_brf.pdf)

LegCo Brief provided by the Financial Services and the Treasury Bureau on  
Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Republic of Indonesia) Order  
[http://www.legco.gov.hk/yr09-10/english/subleg/brief/91\\_brf.pdf](http://www.legco.gov.hk/yr09-10/english/subleg/brief/91_brf.pdf)

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Brunei Darussalam) Order  
<http://www.legco.gov.hk/yr09-10/english/subleg/negative/ln089-10-e.pdf>

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Kingdom of the Netherlands) Order  
<http://www.legco.gov.hk/yr09-10/english/subleg/negative/ln090-10-e.pdf>

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion  
with respect to Taxes on Income) (Republic of Indonesia) Order  
<http://www.legco.gov.hk/yr09-10/english/subleg/negative/ln091-10-e.pdf>

Legislative Council Secretariat Legal Service Division report  
<http://www.legco.gov.hk/yr09-10/english/hc/papers/hc07091s-85-e.pdf>