

Bills Committee on Inland Revenue (Amendment) Bill 2013
Follow-up to the meeting on 21 May 2013

As a form of international cooperation in the taxation arena, jurisdictions conduct exchange of information (“EoI”) for the purpose of enhancing tax transparency and preventing fiscal evasion. To this end, the Organisation for Economic Cooperation and Development (“OECD”)’s Model Tax Convention on Income and on Capital itself envisages exchange of information that existed prior to the entry into force of the Convention, as long as the assistance with respect to the said information is provided after the provisions of the Convention have become effective. In practice, we thus far are not aware of other jurisdictions which openly prohibit EoI for tax assessments for periods before their comprehensive avoidance of double taxation agreements (“CDTAs”) come into effect. The above, however, is subject to the overriding prerequisite that the standard of “foreseeable relevance” is met so as to guard against “fishing expeditions”.

Limitation on Disclosure

Policy of Imposing a Limitation on Information to be Exchanged

2. In the case of Hong Kong, when conducting EoI under the CDTA framework, we have adopted a policy of imposing a limitation on the information to be exchanged. That is, the information disclosed to CDTA partners must relate to the carrying out of the provisions of the relevant CDTA or the administration or enforcement of the tax laws of the CDTA partner concerning taxes imposed in periods **after** the provisions of the CDTA come into effect. In introducing the Bill, we have no intention to deviate from the above-mentioned policy. Our proposal of fine-tuning the current limitation on disclosure serves to allow for the exchange of information generated prior to the effective date of the relevant CDTA or tax information exchange agreement (“TIEA”), **provided that** the standard of “**foreseeable relevance**” is satisfied upon examination of the particulars provided by the CDTA/TIEA partner in its EoI request, and the requested information relates to the carrying out of the provisions of the relevant CDTA/TIEA or the administration or

enforcement of the tax laws of the CDTA/TIEA partner concerning taxes imposed in periods **after** the CDTA/TIEA becomes effective. Such information at stake is expectedly related to identity information of individual taxpayers or information concerning transactions of assets which occur after the CDTA/TIEA comes into operation (e.g. the original purchase prices of assets). Our policy objective is to ensure that Hong Kong is able to meet our CDTA/TIEA partners' practical requirements, whilst not following the practice of other jurisdictions in providing for EoI for tax assessments for periods before the CDTA/TIEA comes into effect.

No Additional Record-keeping Requirements for the Purpose of EoI

3. From the legal perspective, the existing record-keeping requirements are provided in sections 51C and 51D of the Inland Revenue Ordinance (Cap. 112) ("IRO"). Section 51C requires, among others, that every person carrying on a trade, profession or business in Hong Kong shall keep sufficient records in the English or Chinese language of his income and expenditure to enable the assessable profits of such trade, profession or business to be readily ascertained. Such records shall be retained for a period of not less than seven years after the completion of the transactions, acts or operations to which they relate. Section 51D requires, among others, that every person who is the owner of a property situated in Hong Kong shall keep sufficient records in the English or Chinese language of the consideration, in money or money's worth, payable or deemed to be payable to him, to his order or for his benefit in respect of the right of use of that property to enable the assessable value of that property to be readily ascertained. Such records shall be retained for a period of not less than seven years after the completion of the transactions, acts or operations to which they relate.

4. Section 51(4)(a) of the IRO provides that for domestic tax purposes (i.e. profits tax, salaries tax and property tax purposes), information in possession by a person in Hong Kong is subject to disclosure to the Inland Revenue Department ("IRD"). Any such information which is in possession by a person in Hong Kong for domestic tax purposes may be subject to disclosure for EoI purposes, but the information so requested would have to meet the provisions of the

respective CDTAs that we have made with other jurisdictions, including the standard of “foreseeable relevance” as required under the CDTAs.

5. Notwithstanding that we propose to fine-tune the disclosure limitation in the current Bill, we have no plan to change the existing record-keeping requirements under sections 51C and 51D of the IRO. As such, a person has no obligation to provide to IRD, for EoI purposes, information which is either not required to be kept or beyond the statutory retention period under the IRO, even when IRD acts on a valid EoI request and exercises its information-gathering power under section 51(4AA) of the IRO to approach him for the relevant information. There will not be any question of non-compliance of a request for information under section 51(4) if the person is “not in possession” of the information referred to in the request.

6. Given the above, we do not see the need to restrict IRD in its request for information, for EoI purposes, to that generated within seven years prior to the effective date of the relevant CDTA/TIEA, taking into consideration that there is no such restriction on IRD in so far as domestic tax purposes are concerned. If Hong Kong were to adopt an approach in respect of EoI requests under CDTAs/TIEAs that is more restrictive than that for domestic tax purposes, Hong Kong would be perceived as an un-cooperative tax jurisdiction in not adopting the prevailing international standard.

Procedures for Handling EoI Requests

7. The Inland Revenue (Disclosure of Information) Rules (Cap. 112 sub. leg. BI) (“the Disclosure Rules”) provide for domestic statutory safeguards in addition to those provided in individual CDTAs to protect taxpayers’ privacy and confidentiality of information exchanged. The Disclosure Rules stipulate the particulars to be contained in an EoI request made by our CDTA and future TIEA partners to demonstrate that the standard of “foreseeable relevance” is met. It also provides for a notification and review system in handling EoI requests and related appeals.

8. Under the existing EoI arrangements, upon receipt of an EoI

request, Hong Kong's competent authority (i.e. IRD) will examine, with reference to the particulars provided by the requesting partner for EoI, whether the information requested is foreseeably relevant according to the conditions laid down in the relevant CDTA (CDTA protection) and the conditions laid down in the Disclosure Rules (Disclosure Rules protection). The particulars that a CDTA partner has to provide in its EoI request are set out in the Schedule to the Disclosure Rules (see **Annex A**). If the conditions are not fulfilled, the Commissioner of Inland Revenue ("CIR") will not approve the EoI request.

9. For an approved EoI request, CIR will notify in writing the person who is the subject of the request (including the taxpayer concerned even if the information requested is in possession by a third party) of the nature of the information requested by a CDTA partner and of his right to request within 14 days after the date of notification a copy of the information that CIR is prepared to disclose to the CDTA partner concerned. Within 21 days after CIR provides a copy of the information to be disclosed, the taxpayer can ask CIR to amend any part of the information on the grounds that the information is factually incorrect or does not relate to him. CIR may make full amendment, partial amendment or no amendment. If the person remains not satisfied, he can within 14 days after CIR's notice of decision further ask the Financial Secretary to direct CIR to make the amendments requested. If the person is aggrieved by any of the administrative decisions, he can apply to the court for judicial review.

10. Given that the above mechanism has been operating smoothly without any complaints since its implementation in 2010, we propose that the same mechanism should be applicable to EoI under CDTAs and TIEAs to be signed in future.

Application of the Standard of "Foreseeable Relevance"

11. As mentioned in paragraph 8 above, for each and every EoI request received, IRD will in the first instance examine whether the standard of "foreseeable relevance" is met. We set out in **Annex B** a few hypothetical cases to illustrate how certain information which was generated prior to the effective date of the CDTA may be foreseeably

relevant to the carrying out of a relevant CDTA or to tax assessment in respect of any tax imposed in periods commencing after the CDTA comes into effect. We need to stress that the cases are for illustrative purposes only. Each and every case will have to be examined on its own merits.

Statistics on EoI Requests

12. From 2009 to 2012, IRD received a total of 61 EoI requests. Out of them, six requests concerned information in relation to transfer pricing. Amongst the 61 requests, we have not provided the information requested in five cases for reason that the requesting parties failed to demonstrate the “foreseeable relevance” of the information requested.

13. Since the operation of the existing notification and review mechanism, IRD has not received any objections or complaints received from taxpayers or other parties about the disclosure of information.

Financial Services and the Treasury Bureau
May 2013

Inland Revenue (Disclosure of Information) Rules (Cap. 112BI)

Schedule

**PARTICULARS TO BE CONTAINED
IN DISCLOSURE REQUEST**

1. The identity of the person or authority that makes the disclosure request (“competent authority”).
2. The purpose of the disclosure request and the tax type concerned.
3. The identity of the person who is the subject of the disclosure request.
4. A statement on the information requested, including -
 - (a) the nature of the information;
 - (b) the relevance of the information to the purpose of the disclosure request; and
 - (c) the form in which the competent authority wishes to receive the information from the Commissioner.
5. The ground for believing that the information requested is held by the Commissioner or is in the possession of a person in Hong Kong.
6. The name and address of any person believed to have possession of the information requested.
7. A statement that -
 - (a) the disclosure request complies with the laws and administrative practices of the requesting government’s territory;
 - (b) the competent authority is able to obtain the information under the laws of the requesting government’s territory or in the normal course of the administrative practices of the requesting government’s territory; and
 - (c) the disclosure request complies with the relevant arrangements.

8. A statement that the requesting government has pursued all means available in its territory to obtain the information, including getting the information directly from the person who is the subject of the disclosure request.
9. The tax period for which information is requested.
10. The period within which the competent authority wishes the disclosure request to be met.
11. If applicable, a statement -
 - (a) confirming that the competent authority is of the opinion that notification to the person who is the subject of the disclosure request is likely to undermine the chance of success of the investigation in relation to which the request is made; and
 - (b) giving reasons for the opinion.
12. If applicable, a statement -
 - (a) confirming that the competent authority is of the opinion that prior notification to the person who is the subject of the disclosure request is likely to frustrate the timely enforcement of the tax laws of the requesting government's territory; and
 - (b) giving reasons for the opinion.

**Hypothetical Illustrations for
the Standard of “Foreseeable Relevance”**

Below are a few hypothetical cases to illustrate how certain information which was generated prior to the effective date of the CDTA may be foreseeably relevant to the carrying out of a relevant CDTA or to tax assessment in respect of any tax imposed in periods commencing after the CDTA comes into effect.

Illustration 1

The tax authority of a CDTA partner has to verify the **identity** of an individual resident in Hong Kong for tax refund purposes in respect of tax collected on a withholding basis, as two taxpayers having the same name appear in its records. IRD is requested to provide identification documents of the individual, i.e. a copy of the birth certificate or identity card, so as to effect the tax refund for the taxable period commencing on 1 January 2012. The relevant CDTA comes into effect on 1 April 2011 but the birth certificate and identity card of the individual were issued on 10 November 1985 and 5 December 2003 respectively. Pursuant to the existing section 4 of the Disclosure Rules, IRD should not provide copies of birth certificate or identity card, even though they are foreseeably relevant for effecting the tax refund.

Illustration 2

A Hong Kong company received dividends on 1 June 2012 paid by a company which is a resident of a CDTA partner. The Hong Kong company has made a claim for CDTA benefits, i.e. reduced withholding tax rate under the provisions of the relevant CDTA that came into effect on 1 April 2011. The CDTA partner has to verify the **identity and resident status** of the company and requests IRD to provide a copy of the Certificate of Incorporation of the company as evidence that the Hong Kong company is a Hong Kong tax resident. The Certificate of Incorporation of the company was issued on 1 April 2009. Pursuant to the existing section 4 of the Disclosure Rules, IRD should not provide the requested information

to the CDTA partner, even though the copy of the Certificate of Incorporation should be necessary for the CDTA partner to ascertain whether the Hong Kong company is eligible for claiming tax benefits under the provisions of the CDTA after 1 April 2011.

Illustration 3

The tax authority of a CDTA partner is examining the financial statements of its resident company for tax assessment purposes in respect of the taxable period ended 31 March 2012. The financial statements reveal a sale of stock during the said taxable period and the relevant stock was acquired from a related company in Hong Kong in December 2010. The relevant CDTA came into effect on 1 April 2011. The CDTA partner has to verify the **purchase price of the stock concerned** for determining the profit arising from the sale and requests IRD to provide the purchase invoices relating to the stock. Pursuant to the existing section 4 of the Disclosure Rules, IRD should not provide the requested information to the CDTA partner, even though the purchase invoices issued in Hong Kong should be relevant for determining the profits of the resident company in 2012 after the relevant CDTA came into effect.

2. In the hypothetical case mentioned in footnote 3 in the Legislative Council brief for the present Bill, the example has been provided to illustrate the need to verify the identity of a person when the issue of his identity is at stake, such as when the person denies that the relevant bank account is held by him but by another person having the same name. In that case, the tax authority of an overseas jurisdiction has demonstrated to IRD that the signature card containing identification details such as name, date of birth and passport number, etc. is foreseeably relevant to its tax assessment for the period from 1 April 2011 to 31 March 2012, from which the CDTA with that jurisdiction came into effect. Pursuant to the existing section 4 of the Disclosure Rules, IRD is only able to provide the bank statements requested but not the copy of the signature card, even though the latter is foreseeably relevant to the tax assessment of a period after the CDTA came into effect.]

3. As shown in the above illustrations, our proposed fine-tuning of the current limitation on disclosure would enable Hong Kong to meet the

practical needs of our CDTA/TIEA partners while complying with the standard of “foreseeable relevance”.