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Legislative Council

LC Paper No. CB(1)379/14-15
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by the Administration)

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Panel on Financial Affairs

Minutes of meeting
held on Monday, 3 November 2014 at 10:00 am
in Conference Room 1 of the Legislative Council Complex

Members present :	Hon CHAN Kin-por, BBS, JP (Chairman) Hon Christopher CHEUNG Wah-fung, SBS, JP (Deputy Chairman) Hon Albert HO Chun-yan Hon James TO Kun-sun Hon CHAN Kam-lam, SBS, JP Hon Abraham SHEK Lai-him, GBS, JP Hon WONG Kwok-hing, BBS, MH Hon Jeffrey LAM Kin-fung, GBS, JP Hon Andrew LEUNG Kwan-yuen, GBS, JP Hon WONG Ting-kwong, SBS, JP Hon Ronny TONG Ka-wah, SC Hon Starry LEE Wai-king, JP Hon Mrs Regina IP LAU Suk-yee, GBS, JP Hon James TIEN Pei-chun, GBS, JP Hon NG Leung-sing, SBS, JP Hon SIN Chung-kai, SBS, JP
Member attending :	Hon TANG Ka-piu, JP
Members absent :	Hon Kenneth LEUNG Hon Dennis KWOK

Public officers attending	**:**	Agenda Item IV Mr Norman CHAN, GBS, JP Chief Executive Hong Kong Monetary Authority Mr Peter PANG, JP Deputy Chief Executive (Development) Hong Kong Monetary Authority Mr Eddie YUE, JP Deputy Chief Executive (Monetary) Hong Kong Monetary Authority Mr Arthur YUEN, JP Deputy Chief Executive (Banking) Hong Kong Monetary Authority Agenda Item V Ms Elizabeth TSE, JP Permanent Secretary for Financial Services and the Treasury (Treasury) Ms Mable CHAN, JP Deputy Secretary for Financial Services and the Treasury (Treasury) 2 Ms Shirley KWAN Principal Assistant Secretary for Financial Services and the Treasury (Treasury) (Revenue) Mr Jackie LIU Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) 5 Mr CHIU Kwok-kit, JP Deputy Commissioner (Technical) Inland Revenue Department Agenda Item VI

Mr YEUNG Tak-keung
Deputy Secretary for Financial Services and the Treasury (Treasury)3

Mr Alan SIU, JP
Government Property Administrator

Mr LAM Chik-man
Chief Property Manager (Acquisition, Allocation and Disposal)
Government Property Agency

Mrs Sylvia LAM
Project Director 1
Architectural Services Department

Ms Monica LAM
Chief Project Manager 101
Architectural Services Department

Clerk in attendance: Ms Angel SHEK
Senior Council Secretary (1)4
(for Clerk to Panel)

Staff in attendance: Mr Jason KONG
Council Secretary (1)4

Ms Sharon CHAN
Legislative Assistant (1)4

Action

I Confirmation of minutes of meetings and matters arising

(LC Paper No. CB(1)73/14-15 — Minutes of the meeting on 9 October 2014)

The minutes of the meeting held on 9 October 2014 were confirmed.

II Information papers issued since the meeting on 7 July 2014

(LC Paper No. CB(1)1872/13-14	—	Referral from the Subcommittee on Inland Revenue (Exchange of Information relating to Taxes) (United States of America) Order
LC Paper No. CB(1)1931/13-14(01)	—	Half-yearly Economic Report 2014 and the press release
LC Paper No. CB(1)1939/13-14	—	Quarterly Report of the Securities and Futures Commission (April to June 2014)
LC Paper No. CB(1)1961/13-14(01)	—	Second quarterly report of 2014 on "Employees Compensation Insurance — Reinsurance Coverage for Terrorism"
LC Paper No. CB(1)1971/13-14(01)	—	Administration's letter on matters relating to tax treatment of lump sum spectrum utilization fee payment
LC Paper No. CB(1)2001/13-14(01)	—	Consultation paper on enhancements to the Deposit Protection Scheme
LC Paper No. CB(1)2011/13-14	—	Consultation paper on risk-based capital framework for Hong Kong's insurance industry)

2. Members noted the information papers issued since the regular meeting held on 7 July 2014.

III Date of next meeting and items for discussion

(LC Paper No. CB(1)122/14-15(01) — List of outstanding items for discussion)

3. Members agreed to discuss the following items proposed by the Administration at the next regular meeting scheduled for 1 December 2014:

(a) Briefing by the Financial Secretary ("FS") on Hong Kong's latest overall economic situation;

(b) 2015-2016 Budget consultation;

(c) Proposed revision of fees and charges for services under the Customs and Excise Department; and

(d) Proposed implementation of the first phase of the over-the-counter derivatives regulatory regime in Hong Kong.

4. The Chairman said that for item (a) above, FS would be invited to report during the briefing the impact arising from the ongoing "Occupy Central" movement on the overall economy, in response to members' concerns raised at the meeting held on 9 October 2014.

5. Members further agreed that the next regular meeting on 1 December 2014 should start at 9:30 am so as to allow sufficient time for discussion of the above four items.

IV Briefing on the work of Hong Kong Monetary Authority

(LC Paper No. CB(1)122/14-15(02) — Paper provided by the Hong Kong Monetary Authority)

Briefing by the Administration

6. At the invitation of the Chairman, the Chief Executive, Hong Kong Monetary Authority ("CE/HKMA"), the Deputy Chief Executive (Development)/HKMA ("DCE(D)/HKMA"), the Deputy Chief Executive (Banking)/HKMA ("DCE(B)/HKMA") and the Deputy Chief Executive (Monetary)/HKMA ("DCE(M)/HKMA") updated members on the work of HKMA through a powerpoint presentation. Topics included assessment of risks to Hong Kong's financial stability, banking supervision, development of

financial market, Hong Kong as an offshore Renminbi ("RMB") centre, and investment performance of the Exchange Fund ("EF").

(*Post-meeting note*: The powerpoint presentation materials (LC Paper No. CB(1)201/14-15(01)) were issued to Members by a Lotus Notes e-mail on 6 November 2014.)

Discussion

Macroeconomic conditions

7. Mr WONG Kwok-hing expressed concern about the risks on the Hong Kong economy arising from uncertainties in the external environment, including further monetary easing by the European Central Bank ("ECB") and the Bank of Japan, as well as divergence in the monetary policy paths of the United States ("US") vis-à-vis Europe and Japan.

8. CE/HKMA said that as a small and open economy, Hong Kong was susceptible to external influences. Given that the economic growth rate of the Mainland at about 7% was still sound compared to some other economies, and as long as Hong Kong maintained a close link with the Mainland, this would continue to give impetus to the development of the Hong Kong economy.

9. Mr Jeffrey LAM enquired about the estimated timing of interest rate rise in US. CE/HKMA said that the US Federal Reserve mentioned that it would be a considerable period after the asset purchase programmed ended before the interest rate would rise. As to exactly how long "considerable period" meant, according to the recent remarks made by the Vice-Chairman of the US Federal Reserves, this could mean two-month to one-year's time. Market expectation in general was that the first increase in the Federal Funds Rate would come in mid 2015. It might take place earlier, taking into account the prevailing US' labour market conditions and inflation pressures, etc. but appreciation of the US Dollar ("USD") against the euro and other currencies and decline in commodity prices in the recent period should help relieve US from some imported inflationary pressure. As regards Mr LAM's enquiry about the measures to mitigate the impact of an interest rate hike on the business sector, CE/HKMA said that most enterprises had taken advantage of the low-interest rate environment to issue corporate bonds for financing their businesses. This should enable them to build sufficient liquidity at lower cost to withstand the impact of interest rate rise in the near future.

10. Referring to page 3 of the powerpoint presentation, Mr SIN Chung-kai sought the reasons for the sharp fall by 12% in the balance sheets of the ECB, i.e. from 33% of its Gross Domestic Product ("GDP") in 2012 to the recent

21%, in spite of the earlier European sovereign debt crisis. CE/HKMA advised that, unlike the US Federal Reserve which purchased bonds direct for quantitative easing, ECB introduced in 2011 a longer-term refinancing operation ("LTRO") by which ECB provided financing to eurozone banks at low interest rates for the banks to extend credit or purchase bonds. The fall in ECB balance sheets reflected repayment of LTRO loans by banks to ECB.

The Mainland economy and offshore RMB business

11. Mrs Regina IP sought assessment on the possibility of a hard landing of the Mainland economy and the potential impact on Hong Kong. CE/HKMA advised that the Mainland had introduced macroeconomic adjustment and controls to address the challenges brought by gradual opening up of its capital accounts and rapid economic expansion. While difficulties might be encountered in the process, it was likely that the Mainland could achieve a soft landing of its economy given the considerable monetary and fiscal space for the Central Government to stimulate the economy if necessary. In view of the geographical proximity and close relationship, Hong Kong could continue to leverage on the Mainland to develop its economy in the long run.

12. Referring to pages 23 and 24 of the powerpoint presentation on RMB trade settlement, Mr SIN Chung-kai enquired about the significance of having more RMB payments from the Mainland to Hong Kong than from Hong Kong to the Mainland in the past two years. CE/HKMA said that there was remarkable growth in the use of RMB in cross-border transactions with the Mainland and in offshore market activities. In recent years, the RMB pool (including RMB customer deposits and RMB certificates of deposits) was expanding while RMB loans by banks were also increasing. Meanwhile, RMB bonds were issued by the Ministry of Finance and other Mainland financial institutions in Hong Kong which would be repatriated back into Mainland China. However, overall speaking, a greater inflow of RMB from Hong Kong to the Mainland than the outflow would enhance the RMB liquidity pool in Hong Kong for supporting RMB activities.

13. As regards Mr WONG Kwok-hing's enquiry about the timeframe for abolishing the daily conversion limit of RMB20,000 per person for Hong Kong residents, CE/HKMA said that no updates were available at this stage.

Impact of the "Occupy Central" movement

14. Mr WONG Kwok-hing criticized that the ongoing "Occupy Central" movement had dealt a severe blow to the rule of law which was a core value of Hong Kong, and posed negative impacts on the tourism, hotel and retail industries. Besides, commencement of the Shanghai-Hong Kong Stock

Connect ("S-HK SC") was postponed without a firm date of implementation. He sought CE/HKMA's views on how to minimize the adverse impact arising from the movement on the Hong Kong economy.

15. Mr CHAN Kam-lam cautioned that an overly active political environment would heighten risks of social and financial instability in Hong Kong, and universal suffrage might not necessarily bring about greater prosperity and stability to an economy, as demonstrated by the case of the Philippines and Thailand. Although the organizers of the "Occupy Central" movement claimed that they would ultimately accept legal sanctions for staging the illegal protest and road occupation, the damages caused by the movement to the economy and reputation of Hong Kong might be irreparable. He further criticized that some Legislative Council ("LegCo") Members in the legal profession appeared to support the movement or show blatant disregard to the illegality of the movement.

16. Mr NG Leung-sing warned that the adverse impact of the movement might only be reflected at a later stage. In particular, he was worried that the disorderly situation would deter Mainland from granting further economic concessions to Hong Kong. Mr NG considered that HKMA should make efforts in terms of expectation management and communication with the relevant Mainland authorities to ensure realization of the prospective cross-border initiatives for the development of financial services. Opportunity should also be taken of the upcoming Finance Ministers' Meeting ("FMM") of the Asia-Pacific Economic Cooperation ("APEC") in Beijing to invite the financial ministers to hold informal meetings in Hong Kong with a view to mitigating their concerns about the "Occupy Central" movement and financial stability of Hong Kong.

17. Mr Christopher CHEUNG shared the view that the adverse effects of the "Occupy Central" movement to the financial market would gradually surface. Referring to the recent remarks made by Mr Peter WONG, Chief Executive of The Hongkong and Shanghai Banking Corporation Limited, and some other bankers, Mr CHEUNG expressed grave concern that some individuals/entities had put on hold their plans to invest, list companies or issue corporate bonds in Hong Kong. He urged HKMA to devise contingency plans to avert possible deterioration of the situation and preserve the financial stability of Hong Kong. Mr Jeffrey LAM requested HKMA to convey messages to overseas investors to maintain or restore their investment confidence in Hong Kong.

18. Ms Starry LEE sought HKMA's assessment of the worst scenario about the movement's impact on financial stability if the "Occupy Central" movement persisted. She pointed out that HKMA and the community at large should be

vigilant of the repercussions in the aftermath of the movement, including possible heightening of tension in the relationship between Hong Kong and the Mainland, as preluded by the Central Government's earlier decision to hold the FMM of APEC in Beijing instead of Hong Kong, and postponement of implementation of S-HK SC. She was particularly worried that the movement would adversely affect future discussions between Hong Kong and the Mainland in taking forward financial initiatives of mutual benefits.

19. Mr Ronny TONG considered that, as long as the conflicts over the constitutional reform remained unresolved, the political deadlock in Hong Kong might linger on for some years and cause instability across the society including operation of LegCo and implementation of new government policies and initiatives. He suggested HKMA conduct a longer-term assessment of the potential impact on Hong Kong's financial stability and sovereign rating.

20. Mr Albert HO said that the "Occupy Central" movement was not meant to challenge the rule of law but the profound political system of Hong Kong. In his view, if the deep-rooted social conflicts and controversies surrounding the constitutional reform did not abate, they would continue to stir up protests in future whereas the relationship between the Legislature and the Administration would likely worsen.

21. CE/HKMA said that overseas investors would consider investment by taking into account the general business environment, the rule of law and financial stability of a place vis-à-vis other financial centres. He noted that investors, bankers and credit agencies alike were still observing the development of the "Occupy Central" movement in Hong Kong. It would be difficult at this stage to address some investors' concerns unless the picture became clearer as to when and how the "Occupy Central" movement would end and impact on different sectors. While currently the impact on the Hong Kong financial market was mild, if the movement dragged on indefinitely, it would further undermine the spirit of the rule of law and financial stability in Hong Kong in the long run, and possibly affect its sovereign rating. As regards the suggestion of an impact assessment in relation to the political situation, CE/HKMA said that it would be difficult and outside the expertise of HKMA to define and assess the political issues in question for conducting the analysis.

22. CE/HKMA further said that HKMA would uphold its role to maintain the stability of Hong Kong's monetary and financial systems through banking supervision and other measures. It was an ongoing initiative of HKMA to maintain close dialogue with market players and promote Hong Kong as an international financial centre and offshore RMB business hub. As regards the suggestion of inviting APEC finance ministers to Hong Kong, CE/HKMA said

that HKMA hosted meetings of representatives from the central banks from time to time, and would continue to capture such opportunities in future.

23. On members' concerns about postponement of implementation of S-HK SC, CE/HKMA said that HKMA's role was mainly to discuss with the relevant Mainland authorities issues relating to cross-border fund flows arising from the potential increase in stock trading activities and put in place necessary measures to enhance liquidity management by banks. He assured members that the relevant measures were ready for implementation. CE/HKMA said that he was not aware of any intention or decision of the Central Government to postpone commencement of S-HK SC on the ground of the "Occupy Central" movement. Pending further observation of the movement's development, it would be premature at this stage to assess the implications on future discussions of cross-border financial initiatives. CE/HKMA informed members that he would take the opportunity of an upcoming trip with FS and the Secretary for Financial Services and the Treasury to Beijing to discuss with the relevant Mainland authorities issues relating to the development of Hong Kong as an international financial centre and the timeframe for commencement of S-HK SC.

24. Mr WONG Ting-kwong enquired whether HKMA observed any illegal short-selling or other market misconduct activities associated with the "Occupy Central" movement, as reported by the media earlier on.

25. CE/HKMA said that HKMA had been maintaining close communication with the relevant frontline regulators, i.e. the Securities and Futures Commission ("SFC") and the Hong Kong Exchanges and Clearing Limited which had been watching out for abnormalities in the index futures market in terms of the trading volume and open interest. Based on the information provided by SFC, no drastic changes were observed after commencement of the "Occupy Central" movement. CE/HKMA added that HKMA would also monitor the changes in the Hong Kong Dollar ("HKD") market and the Hong Kong Interbank Offered Rate, with a view to detecting market manipulative activities early. As observed, these indicators remained stable during the ongoing "Occupy Central" movement. While the equity market did experience some volatilities earlier on, it had rallied in the recent period to the pre-movement level or even higher.

Property market and credit risks

26. Noting that the property market had turned more active with housing prices and household debt ever rising, Mr CHAN Kam-lam, Mr Jeffrey LAM and Mr NG Leung-sing enquired about HKMA's risk management measures to minimize the negative impact on banks and property mortgage loan borrowers

arising from potential interest rate reversal and asset price adjustment. Mr NG sought assessment of the timing that a downward cycle of the property market would set in and estimation of the resulting negative assets, taking into account the increase in flat supply and easing of housing demand in the coming years.

27. Ms Starry LEE expressed concern that the property transaction volume had picked up from recent lows whereas housing prices resumed moderate growth, and queried the effectiveness of the three rounds of demand-management measures starting from November 2010 (i.e. introduction of Special Stamp Duty, Buyer's Stamp Duty and doubling of the ad valorem stamp duty rates). She sought information on the number of property transactions categorized by investors or genuine homebuyers since imposition of the additional and higher stamp duties.

28. CE/HKMA said that the current upward adjustment of the property market cycle had lasted for a long period, and given the complicated mechanism of the phenomenon, it would be difficult to predict when a downward cycle would occur. However, when the interest rates started to rise, it was expected to have profound impact on the property market and housing prices.

29. CE/HKMA further said that, to enhance risk management against interest rate rise and the possible adverse effects on the property market, HKMA had since October 2009 introduced six rounds of countercyclical macroprudential measures. The macroprudential and demand-management measures together were meant to counteract the effects of monetary easing and cooling down the overheated property market by increasing property acquisition costs, thereby discouraging speculative activities and reducing demand for flats. If these measures had not been put in place, it would be difficult to imagine the state of property market would now have been in. Amongst the measures, the maximum loan-to-value ratio for residential properties with a value below $6 million had been tightened to 70%, and to 50% or less for properties of higher value. Moreover, the assumed increase in mortgage rate for stress testing property mortgage loan applicants' debt servicing ability had also been increased over the years to three percentage points at present. These measures would help strengthen the ability of the property mortgage loan borrowers to cope with the potential impact of interest rate rise and asset price adjustment. In view of the rapid growth in personal loans, HKMA had also requested banks to adopt more prudent measures for assessing the repayment ability of borrowers before underwriting such loans.

30. Mr Albert HO enquired on whether the massive fund inflows seen in the recent period were mainly associated with speculative activities in the property market. CE/HKMA said that the funds could be channeled to different

market activities in Hong Kong, i.e. business transactions, setting up of companies, purchase of equities and properties, and making of other investments. While not much net inflow of funds was observed recently, the risk of fund flow reversal would arise with the potential interest rate rise in US.

Exchange Fund

31. Noting the substantial growth in investment income from EF's "Other investments" in the past three years (i.e. $0.7 billion in 2011, $6.4 billion in 2012 and $16.8 billion in 2013), Mrs Regina IP enquired about the investment nature and HKMA's plans, if any, to increase investment in the relevant areas.

32. CE/HKMA said that HKMA had been diversifying part of EF's investment for some years into a greater variety of asset classes housed under the Long-Term Growth Portfolio ("LTGP"), as distinct from conventional investments in bonds and equities in the developed markets. DCE(M)/HKMA supplemented that EF's income under the item "Other investments" was mainly derived from investment returns from LTGP. The target investment size of LTGP was equivalent to one-third of the Accumulated Surplus of EF, or around $220 billion at present. As at end 2013, assets held in LTGP had reached about $90 billion. He said that HKMA would expand the LTGP investments incrementally and manage them in a prudent manner with a view to yielding greater returns in the medium and long term.

33. Mr NG Leung-sing noted with concern that EF's investment income from foreign exchange recorded losses of over $20 billion in the first nine months of 2014 and in the third quarter respectively. He enquired whether HKMA would review the investment portfolio/strategy concerned. DCE(M)/HKMA advised that EF's currency mix was 77% in USD and 23% in other currencies. HKMA would review the currency mix and asset allocation each year in the light of EF's investment performance over a longer term.

Linked Exchange Rate

34. Mr TANG Ka-piu enquired whether HKMA would review the Linked Exchange Rate System ("LERS") and consider linking HKD to RMB instead of USD, having regard to the declining value of USD after 1997, the strengthening trend of RMB against USD, and the weakening purchasing power of Hong Kong people for foreign goods and services including those of the Mainland.

35. CE/HKMA said that HKMA had reviewed the LERS from time to time and considered it remained the best monetary system for Hong Kong as it was a small and open economy. The LERS was a cornerstone of Hong Kong's financial system ensuring that HKD had a stable exchange value against major

world currencies, with a view to maintaining monetary and financial stability. As observed, the experience of some emerging economies with floating exchange rate regimes underscored the problems arising from large fluctuations in the exchange rate of their respective currencies and massive capital inflows/outflows. While there were views that a floating exchange rate regime could help overcome overheating in Hong Kong's property market, the crux of the problem was related to shortage of housing and land supply and could not be resolved by a new exchange rate regime. Looking forward, as US ended its bond-buying programme and would normalize interest rate in the near future, USD was expected to appreciate, which should help improve Hong Kong people's purchasing power with HKD. However, he stressed that the suitability of LERS for Hong Kong should not predicate on cyclical currency movements.

Development of Islamic finance

36. Mrs Regina IP enquired about the strategies for Hong Kong to catch up with Kuala Lumpur, a leading Islamic capital market, in the development of Islamic finance.

37. CE/HKMA said that the recent inaugural issuance of US$1 billion 5-year sukuk (i.e. Islamic bonds) under the Government Bond Programme in September 2014, which was the world's first US dollar-denominated sukuk originated by an AAA-rated government, was only a first step to take forward the development of Islamic finance in Hong Kong. He observed that, apart from Kuala Lumpur, Dubai and London were also active in the development of Islamic financial services, riding on the prospect of a growing demand for the services both regionally and globally. Although Islamic finance in Hong Kong was at its early stage of development and Hong Kong might be less well placed than other Islamic financial centres, HKMA would continue to strengthen collaboration with the major Islamic financial centres to capture market opportunities in this area.

V Automatic exchange of financial account information in tax matters

(LC Paper No. CB(1)122/14-15(03) — Administration's paper on "Automatic Exchange of Financial Account Information in Tax Matters"

LC Paper No. CB(1)122/14-15(04) — Background brief on automatic exchange of financial account information in tax matters prepared by the Legislative Council Secretariat)

Briefing by the Administration

38. With the aid of a powerpoint presentation, the Permanent Secretary for Financial Services and the Treasury (Treasury) ("PS(Tsy)") briefed members on the current policy on exchange of tax information ("EOI"), the key components of the new global standard of automatic exchange of financial account information ("AEOI") in tax matters, the possible legal framework to enable AEOI, Administration's engagement with relevant stakeholders and the way forward.

(*Post-meeting note*: The powerpoint presentation materials (LC Paper No. CB(1)201/14-15(02)) were issued to Members by a Lotus Notes e-mail on 6 November 2014.)

Discussion

Benefits of AEOI and compliance cost

39. Mr Ronny TONG queried the purpose of consulting the Panel on implementation of the AEOI as the Government had already indicated its commitment to meet the new standard to the Global Forum on Transparency and Exchange of Information for Tax Purposes ("Global Forum") of the Organization for Economic Cooperation and Development ("OECD"). Mr TONG pointed that, while it was in the interest of some jurisdictions like the United States ("US") to pursue AEOI as they practised global taxation, the financial benefits for Hong Kong and its taxpayers arising from any crackdown on tax evasion cases by way of AEOI would be limited given that the tax regime of Hong Kong was simple and territorial-based.

40. Mr CHAN Kam-lam considered that Hong Kong should uphold its responsibility in international tax cooperation including implementation of AEOI. The Chairman remarked that Hong Kong might lose its competitiveness if it did not keep in pace with the international trend of moving towards AEOI. Ms Starry LEE stressed the need to preserve Hong Kong's edge of a simple and low tax regime for attracting business and talents. She enquired about the alternative path to take and potential adverse impact on Hong Kong if it would not pursue AEOI. Mr NG Leung-sing opined that it would be difficult for

Hong Kong not to follow suit to implement AEOI since it was an international trend, in particular as the Mainland had also publicly committed to its implementation. He stressed that Hong Kong financial institutions had all along attached importance to complying with relevant international standards and rules.

41. The Deputy Commissioner (Technical), Inland Revenue Department ("DCIR(T) ") said that AEOI and other international tax cooperation initiatives were mainly advocated by OECD and the Global Forum, and Hong Kong, as one of the Global Forum members, was being called upon to support and implement the new standard. It was not the Administration's intention to make Hong Kong a forerunner in the international arena in terms of exchange of tax information matters.

42. PS(Tsy) advised that over 90 jurisdictions, which adopted either territorial-based tax regime (e.g. Singapore) or global taxation (e.g. US), had already publicly committed to the implementation of AEOI in 2017 or 2018. Some of these jurisdictions were amongst the top 20 trading partners of Hong Kong. In view of the increasing aspirations of the international community for AEOI as a more efficient mode of international tax cooperation and a new global standard, it was necessary for Hong Kong to put in place the required legal framework for effecting AEOI. Otherwise, it might run the risk of being labeled as an uncooperative jurisdiction or a "tax haven", which in turn would undermine its position and competitiveness as an international business and financial centre. In fact, the Global Forum would launch a peer review exercise amongst its member jurisdictions to evaluate their compliance with the AEOI standard in future. PS(Tsy) assured members that it would remain a policy priority to seek to conclude Comprehensive Avoidance of Double Taxation Agreements ("CDTAs") with Hong Kong's trading and investment partners. She added that the Administration was more inclined to make use of the bilateral EoI instruments (i.e. CDTA or tax information exchange agreements ("TIEAs")) as the legal basis for implementing AEOI at the present stage. This might serve as an impetus for Hong Kong to further expand its CDTA network.

43. As regards the benefits of AEOI, PS(Tsy) and DCIR(T) said that there were previous cases in which information exchanged enabled the Inland Revenue Department ("IRD") to detect unreported taxable income of Hong Kong taxpayers sourced from Hong Kong and held in overseas financial accounts.

44. Ms Starry LEE and Mr NG Leung-sing said that the Administration should consider how to minimize the compliance cost on financial institutions

in respect of retention and reporting of tax information under AEOI. PS(Tsy) responded that the Administration would consider the details of implementation and the implications arising from AEOI on the compliance costs of financial institutions and the manpower resources of IRD.

Common Reporting Standard

45. Mr CHAN Kam-lam pointed out that the assets of a Hong Kong taxpayer might be held in overseas financial accounts and subject to protection of privacy and confidentiality of information by the financial institutions concerned. He expressed concern about how to ensure consistency in the application of the Common Reporting Standard ("CRS") of AEOI by local and overseas financial institutions. Mr Christopher CHEUNG enquired whether consideration would be given to granting exemptions from compliance to financial institutions which did not have a fixed place of business outside of Hong Kong or did not have any connected entity overseas.

46. PS(Tsy) and DCIR(T) explained that AEOI involved periodic transmission of financial account information by the source jurisdiction to the jurisdiction of residence of the account holders on an annual basis. It would only involve transmission of information pertaining to overseas tax residents who had opened an account in the financial institutions in Hong Kong to a jurisdiction, which was Hong Kong's CDTA or TIEA partner and had signed a Competent Authority Agreement with Hong Kong. The information which was exchanged was collected in the source jurisdiction on a routine basis, through the reporting by the financial institutions to the tax authority. PS(Tsy) added that only financial institutions incorporated or had permanent establishment in Hong Kong would be required to report financial account information of the overseas tax residents to IRD.

47. Mr Christopher CHEUNG expressed concern about the potential financial loss caused to financial account holders and adverse impact on the business of financial institutions arising from reporting of financial account information and tax enforcement. In particular, he was concerned about the liabilities of financial institutions if the account holders provided false information on their tax residence.

48. PS(Tsy) and the Deputy Secretary for Financial Services and the Treasury (Treasury)2 ("DS(Tsy)2") advised that reportable persons under the AEOI standard were defined with reference to tax residence (rather than citizenship or nationality). The CRS included due diligence procedures to be performed by financial institutions for identification of reportable accounts, such as review of the most recent documentation maintained by the institutions with respect to an account holder, self-certification by new account holder to

establish his/her status, and the steps to take if the financial institutions had reasons to know that the original self-certification was incorrect or unreliable. As long as the financial institutions had followed the relevant due diligence requirements, they would be treated as complying with the requirements. PS(Tsy) further said that the Administration would keep close liaison with relevant stakeholders on the AEOI matter to address their concerns and seek clarification from the Global Forum where necessary and appropriate.

Safeguards to protect privacy and confidentiality of information exchanged

49. Mr NG Leung-sing stressed that IRD should identify AEOI partner carefully, and strike a proper balance between tax transparency and protection of data privacy in the exchange of financial account information. He also raised concern about the potential difficulties and resource implications on IRD to ascertain the nature and source of reportable income and genuine recipient/beneficiary of the income, in particular if the funds involved political donations or receipts by a third party on behalf of an undisclosed individual/entity. Ms Starry LEE sought information on the mechanism to prevent fishing expedition by AEOI partners in tax information exchange.

50. PS(Tsy) explained that "automatic exchange" did not mean that there would be free flow of information to all other jurisdictions. The exchange of information under AEOI would be conducted on an annual basis within the confines of an EOI agreement signed between the tax authorities of two or more jurisdictions. The scope of information to be reported covered financial holders' personal data and financial data (e.g. interest, dividends, account balance/value). The Administration would identify appropriate AEOI partners which could meet relevant requirements on protection of privacy and confidentiality of information exchanged and ensuring proper use of data. PS(Tsy) and DS(Tsy)2 further said that, similar to the safeguards available in the existing EOI mechanism for CDTAs or TIEAs, the AEOI standard contained specific rules on the confidentiality of the information exchanged, including ensuring that the information exchanged should be foreseeably relevant, i.e. no fishing expeditions.

51. Mr NG Leung-sing enquired whether commercial information exchanged under AEOI could be disclosed/referred to an enforcement authority (e.g. Commerical Crime Bureau in Hong Kong or comparable authorities of the contracting partner). PS(Tsy) and DS(Tsy)2 advised that the information (including commercial information) would only be disclosed to tax authorities concerned with assessment or collection of, and enforcement or prosecution in respect of and the determination of appeals in relation to taxes falling within the scope of AEOI, but not for release to their oversight bodies or enforcement

authorities for non-tax purposes (e.g. enforcement against money laundering or other serious crimes), unless otherwise agreed between the contracting parties.

VI Consultancy services for the proposed Joint-user Government Office Building in Cheung Sha Wan

(LC Paper No. CB(1)122/14-15(05) — Administration's paper on "Consultancy Services for the Proposed Joint-user Government Office Building in Cheung Sha Wan")

Briefing by the Administration

52. At the invitation of the Chairman, the Deputy Secretary for Financial Services and the Treasury (Treasury)3 ("DS(Tsy)3") briefed members on the proposal to carry out pre-construction consultancy services for a new joint-user government office building, to be named the Treasury Building, in Cheung Sha Wan, at an estimated cost of $103.2 million in money-of-the-day prices. DS(Tsy)3 said that the proposal was in accordance with the government's policy to accommodate its offices in government-owned properties as circumstances permitted and relocate non-location-bound government offices out of high-value areas. It was expected that the Treasury Building would provide an estimated total net operational floor area ("NOFA") of around 23 600 square metres ("m^2"), and would be used to reprovision the offices of five bureaux/departments accommodated in the three government office buildings at the Wan Chai waterfront, and three departments accommodated in leased private premises in Wan Chai, Mong Kok, Cheung Sha Wan and Kowloon Bay. The Administration planned to submit the proposal to the Public Works Subcommittee ("PWSC") and the Finance Committee ("FC") for funding approval in early 2015 on the pre-construction consultancy services.

Discussion

Reprovisioning of government offices at the Wan Chai waterfront

53. Ms Starry LEE, Mr CHAN Kam-lam and Mr NG Leung-sing expressed support for the proposal. Ms LEE said that Members belonging to the Democratic Alliance for the Betterment and Progress of Hong Kong had been urging the Administration to reprovision its offices at the Wan Chai waterfront as early as possible to release high value land for commercial use. She also considered it desirable to build new government office buildings in different

districts as this would help boost the local economy. In this connection, she enquired about when the three government office buildings at the Wan Chai waterfront would be fully reprovisioned, and whether the Administration would plan to build more joint-user government office buildings in the New Territories. Mr CHAN expressed concern about the possibly long timeframe to make available substantial amount of office space for reprovisioning the three government office buildings at the Wan Chai waterfront which currently took up as much as 175 000 m^2 of office space. He enquired about the details of other new government office buildings under planning.

54. DS(Tsy)3 said that, apart from the proposed Treasury Building and the West Kowloon Government Offices ("WKGO") (which was pending FC's funding approval for the construction works in mid 2015), the Administration had earmarked sites at the Kai Tak Development Area ("KTDA") and in the New Territories, i.e. Tseung Kwan O ("TKO"), for the construction of other new government office buildings for reprovisioning. As the relocation of the three government office buildings at the Wan Chai waterfront was a large exercise involving 29 departments and over 10 000 staff, it would be taken forward in phases, having regard to the time required to deliver new government office buildings and to discuss the implementation details with the bureaux/departments concerned.

55. As regards the timing for completing the phased relocation exercise, DS(Tsy)3 said that it was envisaged that the proposed WKGO would be delivered in 2018-2019, while the construction of the proposed Treasury Building would commence in 2017, both subject to FC's funding approval. The Government Property Administrator ("GPA") supplemented that the Trade and Industry Tower in KTDA, which was expected to be completed in April 2015, would accommodate departments currently housed in the Trade and Industry Department Tower in Mong Kok, a high-value area. Other sites at KTDA had been earmarked for relocating some government offices accommodated in the three government office buildings at the Wan Chai waterfront. DS(Tsy)3 and GPA said that the Administration would consult the Panel in due course on the proposals relating to the new government office buildings at KTDA and TKO.

Design and usage of the proposed Treasury Building

56. Mr NG Leung-sing enquired whether consideration had been given to maximizing the NOFA of the proposed Treasury Building within the approved plot ratio of the site, with a view to providing more storeys/spaces to accommodate needy public facilities (e.g. elderly service and recreational facilities). GPA advised that the current design of the Treasury Building of about 100 m high and around 20 storeys had taken into account the need to fully utilize the plot ratio while minimizing adverse visual impact on the buildings

nearby, and the design was accepted by the Sham Shui Po District Council. GPA further said that public open spaces for leisure activities would be provided at the project site.

57. Mr CHAN Kam-lam enquired whether all the offices of departments concerned (e.g. the Treasury) would be relocated to the proposed Treasury Building with a view to centralizing resources, enhancing coordination and achieving greater operational efficiency. DS(Tsy)3 confirmed that all the offices of the Treasury would be relocated to the proposed Treasury Building.

58. Mr CHAN Kam-lam queried the need to relocate Hongkong Post ("HKP")'s Cheung Sha Wan Delivery Office to the Treasury Building under the proposal, given that HKP operated on a self-financing mode under the Trading Fund. GPA advised that the Delivery Office in question was currently accommodated at leased private premises. Relocating it to the proposed Treasury Building would help save some rental expenditure for HKP.

59. The Chairman directed that the meeting be extended by 15 minutes to 1:00 pm.

Conclusion

60. The Chairman concluded that Panel members generally supported the submission of the funding proposal to PWSC and FC in early 2015 for seeking approval of the pre-construction consultancy services for the proposed Treasury Building.

61. Mr NG Leung-sing suggested that the Administration should consult other Panel members not present at the meeting before seeking funding approval from PWSC/FC. The Administration took note of the suggestion.

VII Any other business

62. There being no other business, the meeting ended at 12:45 pm.

Council Business Division 1
Legislative Council Secretariat
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