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**Paper for the House Committee meeting on 18 December 2009**

**Report of the Bills Committee on  
Inland Revenue (Amendment) (No. 3) Bill 2009**

**Purpose**

This paper reports on the deliberation of the Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2009 (the Bill).

**Background**

2. To avoid the problem of double taxation, jurisdictions sign bilateral avoidance of double taxation agreements to clarify each other's taxing rights. Besides, a comprehensive avoidance of double taxation agreement (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 with Hong Kong's major trading partners<sup>1</sup> since 1998-1999.

3. 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. The EoI article currently adopted in Hong Kong's CDTAs is based on the 1995 version of the Organization for Economic Cooperation and Development (OECD) Model Tax Convention. 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 economies have, however, adopted the OECD 2004 version of the EoI article (the OECD Model Article). This version 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.

4. Hong Kong currently cannot adopt the OECD Model Article because under the Inland Revenue Ordinance (Cap. 112), IRD can only collect taxpayers' information for the ascertainment of liability, responsibility and obligation under the

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<sup>1</sup> So far, the Government has concluded CDTAs with Belgium (2003), Thailand (2005), Mainland China (2006), Luxembourg (2007) and Vietnam (2008).

domestic tax law. In other words, IRD cannot collect any tax information unless it is for domestic tax purposes. This constraint has reduced the number of Hong Kong's potential CDTA partners, and restricted the progress of the negotiations for CDTA.

5. According to the Administration, while the international community has generally accepted that 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, any negative perceptions on the transparency of Hong Kong's tax regime would harm its reputation as an international financial centre, and could lead to sanctions imposed by other economies.

6. The Administration consulted the business and professional sectors on the liberalization of EoI under CDTAs in 2005 and 2008. Following the consultation in 2008 in which most of the stakeholders in some 50 business chambers, professional bodies and advisory committees consulted indicated support for liberalization, the Financial Secretary (FS) announced in the 2009-2010 Budget that the Government would put forward legislative proposals to align Hong Kong's EoI arrangements with the international standard.

## **The Bill**

7. The Bill seeks to amend the Inland Revenue Ordinance (Cap. 112) and the Personal Data (Privacy) Ordinance (Cap. 486) to -

- (a) clarify that if a CDTA made with a foreign territory contains a provision that requires disclosure of information concerning tax of that territory (i.e. an EoI article), the CDTA shall have effect in relation to any tax of that territory that is the subject of that provision;
- (b) enable IRD to exercise the same power under section 51(4) of the Inland Revenue Ordinance to collect information concerning tax of a foreign territory for the purpose of EoI under a CDTA;
- (c) enable a magistrate to exercise the same power under section 51B of the Inland Revenue Ordinance to issue search warrants for information concerning tax of a foreign territory for the purpose of EoI under a CDTA;
- (d) provide that a person commits an offence if he, without reasonable excuse, gives any incorrect information in relation to any matter that affects his or another person's liability to a foreign tax covered by an EoI article under a CDTA; and

- (e) provide that the word "tax" in section 58(1)(c) of the Personal Data (Privacy) Ordinance includes a foreign tax covered by an EoI article under a CDTA.

### **The Bills Committee**

8. At the House Committee meeting on 10 July 2009, Members agreed to form a Bills Committee to study the Bill. Under the chairmanship of Hon Paul CHAN Mo-po, the Bills Committee has held eight meetings to discuss with the Administration and receive views from deputations in the business and professional sectors. The membership list of the Bills Committee is at **Appendix I**. A list of the organizations which have submitted views to the Bills Committee is at **Appendix II**.

### **Deliberations of the Bills Committee**

9. The Bills Committee generally supports the legislative intent of the Bill to enable Hong Kong to adopt the latest international standard for EoI under CDTAs. Members have expressed concerns about the provision of safeguards to protect an individual's right to privacy and confidentiality of the information disclosed to the requesting party (EoI safeguards). Deliberations of the Bills Committee on the legislative proposal are summarized in the ensuing paragraphs.

#### Approach for setting out the EoI safeguards

10. According to the Administration, in adopting the OECD Model Article, the following approach will be adopted to provide safeguards for protecting an individual's right to privacy and confidentiality of the information exchanged:

- (a) incorporating the most prudent safeguards acceptable under the OECD Model Article in individual CDTAs (which will be implemented as subsidiary legislation subject to the scrutiny of the Legislative Council (LegCo)) or in documents of record between the two contracting parties (The sample text of CDTA is at **Appendix III**);
- (b) putting in place domestic safeguards through a set of rules (the proposed Rules) to be made under section 49(6) of the Inland Revenue Ordinance; and
- (c) setting out the procedural guidelines for IRD in the processing of EoI requests in a Departmental Interpretation and Practice Note (DIPN).

11. The Bills Committee has noted that the majority of the deputations in the business and professional sectors indicate support for Hong Kong to adopt the OECD

Model Article, and some call for early enactment of the Bill to enable Hong Kong to catch up with the latest international standard for the EoI arrangement. A number of the deputations (such as the British Chamber of Commerce in Hong Kong, Hong Kong Institute of Certified Public Accountants, Hong Kong Trustees' Association Limited, Joint Liaison Committee on Taxation and PricewaterhouseCoopers Limited) have expressed concern about the importance of setting out EoI safeguards in the primary or the subsidiary legislation. To allay these concerns, the Bills Committee has requested the Administration to provide the proposed Rules and DIPN to provide a full picture of the provisions for EoI safeguards. Members including Hon Miriam LAU, Hon James TO and Hon Alan LEONG share the view that fundamental safeguards on the scope and usage of information exchanged, i.e. the safeguard provisions to be provided in the CDTAs, should be provided in the primary legislation instead. These Members are of the view that while individual CDTAs will be subject to LegCo's scrutiny, Members could hardly amend the provision at that stage since agreements would have already been reached with the treaty partners.

12. The Administration has explained that stipulating the EoI safeguards provided in CDTAs in primary legislation will significantly weaken the Administration's position and reduce its flexibility in CDTA negotiations, as OECD may from time to time revise the wording of individual safeguards for clarity or consistency. Many jurisdictions may also wish to adopt slightly different wording to meet their domestic needs. Such revised or alternative wording may not affect the real effect of the safeguards. If the safeguards are set out in primary legislation, the Administration may need to amend the principal Ordinance every time before it can accommodate any slight change proposed by the negotiation partners. This rigidity will severely reduce the attractiveness of Hong Kong as a treaty partner, and will affect the progress in complying with the prevailing international standard and in expanding Hong Kong's CDTA network.

13. Members including Hon Miriam LAU, Hon James TO, Hon Alan LEONG, Hon Starry LEE and Hon Paul CHAN have requested the Administration to make reference to the practices of other jurisdictions (such as Singapore and Switzerland) in providing for the EoI safeguards. Hon Miriam LAU and Hon James TO are of the view that the Administration should not be given excessive flexibility in treaty negotiations and sufficient checks and balances should be put in place to ensure that the safeguard provisions in CDTAs would not deviate from those proposed by the Administration in the sample text.

14. The Administration has explained that according to available official information and its enquiries with the relevant authorities, countries such as Australia, Canada, Japan, Malaysia, New Zealand, Singapore, Switzerland, United Kingdom and the United States do not provide standard OECD EoI safeguards in their primary legislations. It would not be necessary or desirable to stipulate in the primary legislation EoI safeguards that will be provided in individual CDTAs because each CDTA will be implemented as a piece of subsidiary legislation to be passed by the LegCo. The safeguards are already fully adopted in all the five CDTAs that are effective as subsidiary legislation under the same two-tier structure in the present

legislative framework. The Administration considers that the arrangement has been working well, with no complaints from any stakeholder in the past ten years. To facilitate Member's scrutiny of future subsidiary legislation for CDTAs, the Administration has undertaken to set out clearly in its submissions to LegCo the safeguards adopted in individual CDTAs and any deviation from the sample text. The Administration also proposes to set out the information that should be provided in an EoI request, along the lines of the Eighth Schedule of the Income Tax (Amendment) (Exchange of Information) Act of Singapore (the Singapore legislation) in the proposed Rules which provide the same level of legal protection as the Bill. In addition, the Secretary for Financial Services and the Treasury will reaffirm in his speech during the resumption of the Second Reading debate of the Bill the policy that the safeguards in the OECD Model Article will be adopted.

15. Members including Hon Miriam LAU and Hon Alan LEONG have noted the provision in the Singapore legislation requiring the taxation authority to apply for a court order to obtain certain information before acceding to EoI requests. These Members are concerned that IRD is not subject to a similar statutory requirement.

16. The Administration has advised that given the restriction of its domestic bank secrecy law, the Singapore authority has to seek a court order to obtain the restricted information from banks in order to accede to EoI requests for such information. This is not the case for Hong Kong as there is no bank secrecy law in Hong Kong. However, if no restricted information is involved in the EoI request, the Singapore authority will not be required to notify the person concerned nor apply for a court order. It will be a step backward for Hong Kong to impose more stringent control to obtain information for the purposes of EoI under the CDTAs than those stipulated in local laws. In fact, the absence of bank secrecy law is one of the reasons for the international community's acceptance that Hong Kong is not a tax haven.

17. In response to Hon James TO's request, the legal adviser to the Bills Committee has examined whether the same level of protection will be provided to a taxpayer who seek legal remedies, if the information of an EoI request is set out in the primary legislation like the Eighth Schedule to the Singapore legislation, the subsidiary legislation, or the DIPN. Having examined the level of protection for an aggrieved person in the three above-mentioned scenarios, the legal adviser has concluded that the level of protection for an aggrieved person in the scenario where the information of an EoI request is set out in the primary or subsidiary legislation is comparable to each other. The aggrieved person may seek remedies as provided for in the legislation. If there is no internal recourse in the legislation, the aggrieved person may seek judicial review of the Commissioner of Inland Revenue (the Commissioner)'s decision. As to the scenario where the information of an EoI request is set out in the DIPNs, the aggrieved person must establish to the court in a judicial review that the DIPNs justify legitimate expectation. Having done that, it would raise difficult questions as to how the court should balance individual expectations against the necessity for official bodies to act in the public interest as they see it. Finally, the DIPNs could be changed administratively, whereas amendment to primary or subsidiary legislation is subject to the legislative process.

18. As the proposed Rules will set out the domestic safeguards such as the approval of the EoI request and the notification system, Hon James TO has requested the Administration to consider subjecting the proposed Rules, when made, to the positive vetting procedure instead of the negative vetting procedure, so that Members' right to object to any future amendments will be less restricted. Having carefully considered Members' view, the Administration agrees to subject the proposed Rules, when made, to positive vetting procedure. The relevant Committee Stage amendment (CSA) to section 49 of the Inland Revenue Ordinance proposed by the Administration is at **Appendix IV**.

19. Members including Hon Miriam LAU, Hon James TO, Hon Starry LEE and Hon Paul CHAN are concerned that procedural safeguards in relation to IRD's processing of EoI requests will have significant implications on the operation of the business and professional sectors. These Members have requested that the procedural safeguards be provided in the proposed Rules, instead of in the DIPN which is not legally binding.

20. The Administration has advised that the DIPN will provide administrative guidelines of how an authorized officer of IRD will process an EoI request. The Administration has also advised that the proposed Rules will require the authorized IRD officer to ensure that an EoI request has complied with the stipulated procedures before approving the request. Since such administrative guidelines may be refined from time to time in line with international practice or operational needs, it is not appropriate to set them out as subsidiary legislation. The Administration has pointed out that the DIPN will be a public document drawn up after wide consultation. As with other DIPNs issued by IRD that set out guidelines on how it would implement Hong Kong's tax laws, IRD will consult stakeholders on any future amendment to the DIPN. Having considered Members' views, the Administration agrees to make reference to the Eight Schedule to the Singapore legislation and add similar provisions in the proposed Rules. Any further change to the Rules will be subject to the scrutiny of the LegCo. As the information that should be provided in an EoI request is set out in the proposed Rules, the DIPN will provide examples and illustrations on the operation and implementation of these provisions.

#### No retrospective effect for EoI arrangement under CDTAs

21. Members including Hon James TO, Hon Starry LEE, Hon CHAN Kin-por and Hon Paul CHAN are concerned that the EoI arrangement under CDTAs shall have no retrospective effect, i.e. the Administration will not entertain any request for information relating to a period before the effective date of the respective CDTAs. As some deputations have also expressed similar concern, Hon James TO and Hon Paul CHAN have requested the Administration to set out this policy clearly in the primary legislation or in the proposed Rules.

22. The Administration has advised that a standard article will be included in all CDTAs setting out that all provisions under the CDTA shall have effect from a

stipulated date as agreed and shall only apply to taxes after the effective date. Hong Kong has not entertained and will not entertain any request for any information relating to a period before the effective date. This will be set out in a protocol which formed part of the CDTA (and hence part of the subsidiary legislation) or in other documents of records. Having considered Members' views, the Administration proposes to add a provision in the proposed Rules that IRD must not disclose any information in response to a disclosure request unless the information does not relate to any period before the relevant CDTAs that are applicable to the request come into operation.

#### Scope of information exchange

23. The Bills Committee has noted that under Paragraph 1 of the OECD Model Article, the relevant authority of the requesting party must satisfy IRD that the information it requests is "foreseeably relevant" for the carrying out of the CDTAs or to the administration or enforcement of its local tax laws. This is a safeguard against "fishing expeditions". On the types of taxes covered, the Administration has advised that while Paragraph 1 of the OECD Model Article allows information exchange in respect of "taxes of every kind and description" imposed by a contracting party, it will seek to confine the scope of information exchange to "taxes covered by the Agreement" (i.e. income taxes as stated in Article 2 of the CDTA). Such modification is allowable under the OECD standard.

24. Members including Hon Miriam LAU, Hon James TO and Hon Paul CHAN have expressed concern whether the term "foreseeably relevant" could provide adequate restrictions to the scope of information exchange, as some deputations have also expressed similar concerns. Mr TO has requested the Administration to examine, with reference to case laws in Hong Kong or other jurisdictions, whether an alternative term such as "relevant" could be adopted to prevent "fishing expeditions", and to provide better protection to the right of the persons concerned to seek legal remedies in the context of domestic law.

25. The Administration has explained that the term "foreseeably relevant" is recommended by OECD and adopted internationally in EoI article of CDTAs to guard against "fishing expeditions". It is unlikely that the treaty partners will agree to adopt any alternative term which Hong Kong proposes unilaterally. The Administration has advised that the concept of "foreseeability" is the most common test of proximate cause in tort law. The test (in tort context) is basically whether the harm resulting from an action is reasonably able to be predicted. In the context of CDTAs, the test will be whether it is reasonably able to predict that the piece of information requested would be relevant to the case in question. As no Hong Kong case could be found where a reference to "foreseeably relevant" was made in the judgement and only two United Kingdom cases have been found where the term "foreseeably relevant" was mentioned without elaboration, the term "foreseeably relevant" will have to be construed in accordance with its ordinary dictionary meaning, which is to be applied to the facts of each case.

26. To provide greater clarity in the restriction of the scope of information exchange, the Administration has agreed to expand Section V of the DIPN (i.e. the administrative guidelines on processing of EoI requests), 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.

27. Noting that the Administration will seek to confine the scope of information exchange to income taxes, Hon Paul CHAN has enquired whether this will be accepted by potential treaty partners and be successfully incorporated in CDTAs. The Administration has advised that despite anticipated difficulties in the negotiation process, it will insist in confining the scope of information exchange to income taxes. So far, it has successfully incorporated such modifications in the CDTA negotiations with its potential treaty partners.

28. Noting that the OECD Model Article stipulates that a contracting party has no obligation to supply information which would disclose any trade, business and other secrets, Hon Miriam LAU, Hon James TO and Hon Paul CHAN have asked the Administration to provide explanation and definition on the types of information which will fall under these categories and the possibility of judicial challenges to the Administration's interpretation in future EoI.

29. The Administration has explained that sub-paragraph 3(c) of the OECD Model Article provides that a contracting party is not obliged "to supply information which would disclose any trade, business, industrial, commercial or profession secret or trade process, or information, the disclosure of which would be contrary to public policy (ordre public)." According to OECD, a trade or business secret is generally understood to mean facts and circumstances that are of considerable economic importance and that can be exploited practically and the unauthorized use of which may lead to serious damage. Financial information, including books and records, does not by its nature constitute a trade, business or other secret. Examples of a trade, business or other secret include certain purchase contracts which may reveal the proprietary formula used in the manufacture of a product or information about a pending patent application being made by the taxpayer in question, or a secret trade process or formula owned by or in the custody of the taxpayer.

30. The Administration has also advised that its policy is to exchange information only upon request from treaty partners in pursuance to a CDTA. It will not accept any treaty obligation for automatic or spontaneous exchange and will seek to agree with the negotiation partners on adopting only this mode of information exchange. The agreed mode may be set out in the agreement, in its protocol, which forms part of the agreement, or in other documents of record (e.g. a Memorandum of Understanding between the two contracting parties), which although not being part of the agreement, have to be observed by both parties in carrying out the agreement. This is in line with the OECD standard as well as international practice.



Confidentiality and usage of information exchanged

31. The Bills Committee has noted the safeguards for the confidentiality of information exchanged provided in paragraph 2 of the OECD Model Article, including –

- (a) the information exchanged shall be treated as secret information under the domestic laws of the requesting party;
- (b) the information shall be disclosed only to persons or authorities (or their oversight) concerned with the collection or assessment of taxes, or the enforcement, prosecution or determination of appeals in relation to taxes; and
- (c) the requesting party shall only use the information provided for tax purposes.

32. The Administration has advised that it will seek to confine disclosure of information to the tax authorities but not their oversight body (unless the negotiation partners' domestic laws require their oversight bodies to have access to tax information for statutory purposes). A provision will be included either in the agreement or in its protocol to explicitly state that the information shall not be disclosed to any third jurisdiction. These modifications do not deviate from the OECD standard.

33. Hon Jeffrey LAM has enquired whether IRD would be allowed to use the information collected at the request of a CDTA contracting party for investigation of local taxation cases, as a deputation has expressed such concerns. The Administration has explained that IRD is currently empowered under the Inland Revenue Ordinance to collect any information in regard to any matter which may affect the tax liability of any person under the Ordinance. IRD may use the information collected for the purpose of EoI and/ or for domestic tax purposes as appropriate, and this will be set out in the notice issued by IRD requesting for information.

34. Regarding the sharing of information exchanged, Hon Jeffrey LAM has enquired whether such will be shared with other jurisdictions, such as among European Union members. Hon CHAN Kin-por has asked whether the proposed additional protection measures to restrict the sharing of information will be accepted by the potential treaty partners.

35. The Administration has 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). As the proposed safeguards are mostly adopted from the OECD Model Article, or with modification allowable under the OECD standard, the majority of the safeguards should be accepted by the international community. Some of the

additional measures such as confining disclosure of information to the tax authorities but not their oversight bodies will need to be worked out during the negotiation of individual CDTAs.

#### Processing and approval of an EoI request

36. The Administration has proposed to stipulate in the proposed Rules that an EoI request may be approved only by the Commissioner personally, or any officer of IRD not below the rank of chief assessor authorized in writing by the Commissioner. Referring to the concerns expressed by some deputations about the authority for approval of EoI request, Hon Miriam LAU has opined that an EoI request should be approved by the Commissioner only.

37. The Administration has explained that the decision on whether to accede to an EoI request will be based on the information provided by the requesting party and in accordance with laid-down criteria. The level of responsibilities required and the scope of duties involved are comparable with those other responsibilities and duties specified in the Inland Revenue Ordinance that require the personal attention of a chief assessor. Under the present proposal, accession to an EoI request will have to be approved by a directorate officer, which will be a chief assessor, according to a set of transparent departmental procedures. The information to be disclosed in response to an EoI request will need to be personally signed off by the Commissioner or a Deputy Commissioner of Inland Revenue who are designated as the Competent Authority in the CDTAs.

38. Hon Miriam LAU has expressed concern about the discretionary power of the Commissioner to refuse an EoI request under the proposed rule 4 of the proposed Rules. Ms LAU has requested the Administration to refine the proposed Rules by making reference to section 105D(2) of the Singapore legislation. Having considered Ms LAU's view, the Administration has agreed to revise rule 4 of the proposed Rules by making reference to the Singapore legislation. Responding to Hon James TO's view that the Commissioner should only exercise such discretion "on reasonable grounds", the Administration has undertaken to revise the proposed Rules to address Mr TO's view.

#### Notification of proposed disclosure

39. The Bills Committee notes that the Administration has proposed to put in place a notification system and set out the notification procedures in the proposed Rules. The notification system requires that the Commissioner must, before any information is disclosed, give notice in writing to the person who is the subject of the request. The procedure includes the following –

- (a) notify the person of the request and the nature of the information sought;

- (b) notify the person that he / she may, in writing, within 14 days after the notice is given, request a copy of the information that the Commissioner is prepared to disclose to the requesting government;
- (c) notify the person that he / she may request the Commissioner to amend the information on the grounds that the information does not relate to the person; or the information is factually incorrect, within 14 days after a copy of the information is given by the Commissioner under (b) above.

40. Under the proposed notification system, if a person makes a request for amendments of the information, the Commissioner may fully approve, partially approve or refuse the request. The Commissioner has to notify the person of the Commissioner's decision, with reasons of the refusal (if applicable) and a copy of the information that has been so amended (if applicable).

41. Hon James TO shares the view expressed by some deputations that a copy of the information to be disclosed to the requesting party should be provided to the person concerned automatically when notification was given, instead of upon request of the person concerned.

42. The Administration has explained that as the information to be disclosed contains confidential personal information, IRD will need to correctly identify and locate the person concerned by the initial notification before supplying him with a copy of the information. It is therefore considered prudent to provide a copy of the information upon request made by the person concerned.

43. Hon Paul CHAN has suggested the Administration to examine the feasibility of giving prior notification to the person concerned at an earliest possible date upon receipt of the EoI request, so that more time will be allowed for the person concerned to respond (instead of 14 days as proposed by the Administration) and take necessary actions in respect of the information to be disclosed.

44. To address the concern of the Bills Committee, the Administration has agreed to extend the time allowed for the person concerned to submit proposed amendments to the Commissioner from 14 days to 21 days. IRD will also send out the first notice as soon as practicable upon its decision to proceed with the EoI request. The Administration proposes to revise the proposed Rules accordingly to reflect the change.

45. The Bills Committee has noted that notification is not required if the Commissioner has reasonable grounds to believe that (a) all the addresses of the person known to the Commissioner are inadequate for the purpose of giving the notification; or (b) the notification is likely to undermine the chance of success of the investigation in relation to which the request is made. Prior notification is not required if the Commissioner is under a tight time constraint to disclose the information to the requesting government and the failure of disclosing the information

within the time constraint will likely frustrate the efforts of the requesting government in enforcing its tax laws. However, the Commissioner must notify the person at the same time when the information is disclosed.

46. Members including Hon James TO, Hon Miriam LAU and Hon Alan LEONG have expressed concern about the "reasonable grounds" for the Commissioner to decide that notification is not required as "notification is likely to undermine the chance of success of the investigation in relation to which the request is made". They have also questioned the criteria for the Commissioner to decide that prior notification is not required if "failure of disclosing the information within the time constraint will likely frustrate the efforts of the requesting government in enforcing its tax laws".

47. The Administration has advised that in case a requesting party requires IRD not to give notification on the ground that doing so would likely undermine the chance of success of its investigation, IRD would ask the requesting party to substantiate its claim. For example, the requesting party would be asked to provide information and reasons to explain why it believes the subject person would destroy or deface records, whether similar offences were committed in the past, or whether the subject person is the target of a covert criminal investigation. IRD would have to be satisfied that sufficient information is available to reasonably justify such requests.

48. The Administration has further advised that in case of an urgent request where prior notification would frustrate the timely enforcement of the requesting party's tax laws, IRD must be satisfied that there is genuine urgency. OECD has issued detailed guidelines on what information should be contained in an EoI request. IRD would be able to see the background of a case and be able to have an assessment whether there is any deliberate or undue delay in making a request. For example, IRD would ask the requesting party to substantiate why the request could not have been made earlier if the information is required before a certain date because there is an imminent statutory time limit of raising the relevant tax assessment. The relevant procedure will be provided in the DIPN.

49. The Administration has also advised that while a notification system is acceptable under the OECD standard, this should not undermine the efficiency and effectiveness of EoI, which is one of the compliant standards required by OECD. The proposed notification system has in fact imposed a more stringent requirement, requiring the requesting party to substantiate its claim for not giving a notification or prior notification to the person concerned. In implementing the notification system, a proper balance has to be struck between the confidentiality of investigation for certain cases and protection of the rights of the persons concerned. Regarding the details required by IRD for a requesting party to substantiate its request for not giving notification or prior notification to the person concerned, the Administration proposes to set out in the Schedule to the proposed Rules further elaboration on such information to be required.

Review of the decision of IRD

50. Under the proposed Rules, where the Commissioner partially approves or refuses a request for amendments, the person concerned may request FS to direct the Commissioner to make the amendments. The request has to be made in writing, within 14 days after the Commissioner's notice of the decision on the amendments. FS may fully approve, partially approve or refuse the request and his decision shall be final. FS has to notify the person of his decision, with reasons of the refusal (if applicable) and a copy of the information that has been so amended (if applicable).

51. Hon Paul CHAN has expressed concern about the authority for reviewing IRD's decisions on amendments to the requested information. Some deputations have also suggested that an independent tribunal/appeal panel/the Board of Review, instead of FS, should be responsible for the reviews. In this connection, the Administration has advised that it would not be cost-effective to set up a new board/panel for review of IRD's decisions, given the anticipated small number of EoI requests. Moreover, putting in place a complicated review mechanism may affect the efficiency of information exchange. The Administration has to balance all factors, such as personal privacy, effective implementation of EoI and compliance with international treaty obligations.

52. Given the standard 90-day response time set by OECD for EoI, Hon Starry LEE is concerned whether the information of the person concerned would have been transmitted to the requesting party before completion of the review by FS. Hon Andrew LEONG has also expressed concern about the real effect of the review procedures where prior notification is not given due to time constraint and the requested information has been transmitted to the requesting party before the person concerned seeks amendment and/ or review of IRD's decision on the amendment.

53. The Administration has explained that the relevant information will not be transmitted to the requesting party before completion of the review procedures, if a review is requested. This arrangement will be stipulated in the DIPN. If a prior notification has not be given where the requesting party's claim of a tight time constraint is accepted, the person concerned will be notified of the exchange concurrently when the information is transmitted to the requesting party. The amended information will be transmitted to the requesting party if the Commissioner or FS has agreed to make any amendment as requested by the person concerned.

54. Noting that FS is only empowered under the proposed Rules to review objections to the accuracy of information to be exchanged, Hon James TO has expressed concern about the channels available to the persons concerned to raise objection against the collection or disclosure of information under the EoI arrangements. In this connection, Mr TO has suggested that consideration should be given to empowering FS to review the question of law on the decision of IRD on the collection or disclosure of information, in addition to the current procedure for FS to review the question of fact only. Hon Andrew LEUNG nevertheless holds a different

view that FS should not be involved in handling reviews on question of law, which should be dealt with by the court.

55. The Administration has advised that under the current proposal, FS, as the oversight body under the law, will review submissions on factual accuracy of the information. On the other hand, if a person thinks that IRD has not properly discharged its responsibility to ensure that the information requested is within the scope of the relevant CDTA or the law, he can challenge the Government's actions through the judicial review. Apart from requesting FS to review the factual correctness of the information, the person concerned may also challenge in the court the IRD's decision on information collection or disclosure. In accordance with section 51(4B) of the Inland Revenue Ordinance (Cap. 112), if a person fails to comply with the notice for information IRD issues under the proposed section 51(4AA), IRD may bring his case to the court. He will then have the opportunity to present his objection to the court. At Hon Andrew LEUNG's suggestion, the Administration agrees to report to the Panel on Financial Affairs on the effectiveness of the proposed notification and appeal system 18 months after implementation.

Proposed amendments to section 49 of the Inland Revenue Ordinance (Cap. 112) (Clause 3)

56. Referring to the proposed section 49(1A)(a) which stipulates that arrangements specified in CDTAs "shall have effect in relation to tax under this Ordinance despite anything in any enactment", Hon James TO is concerned that this provision may result in excessive overriding effect on provisions concerning protection of fundamental human rights in other ordinances.

57. The Administration has explained that CDTAs allocate taxing rights between two treaty partners. A company that would otherwise be subject to tax at a certain rate under Hong Kong laws may be entitled to a lower rate (or not taxed at all) because of a piece of subsidiary legislation that implements a CDTA. In such a case, that piece of subsidiary legislation would take precedence over the said Hong Kong laws. The intention of the phrase "despite anything in any enactment" in the proposed section 49(1A) is to ensure that as far as the current law and any subsequent legislation in future may be concerned, they would not inadvertently override a piece of subsidiary legislation that implements CDTAs "in relation to tax under the Inland Revenue Ordinance (Cap. 112)". The effect of any CDTA and its implementing subsidiary legislation would already be limited to "tax under the Inland Revenue Ordinance (Cap. 112)" and any precedence effect would also be accordingly limited. As each CDTA will be implemented as subsidiary legislation subject to LegCo's scrutiny, the Administration does not consider it appropriate to impose further limitation on the precedence effect in section 49(1A).

58. For the sake of tidiness, the Administration has agreed with Hon Miriam LAU and Hon Jeffrey LAM to replace "notwithstanding" in section 49(1) with "despite", as the provisions in section 49(1) and the proposed section 49(1A) mirror each other.

### **Committee Stage amendments**

59. The Bills Committee agrees with the Administration's proposed CSAs at **Appendix IV** in relation to paragraphs 18 and 58. The Bills Committee has noted that Hon James TO may propose CSA to the proposed section 49(1A) (clause 3 of the Bill) to address his concern in paragraph 56 above. The Bills Committee has not proposed any CSAs to the Bill.

### **Recommendation**

60. The Bills Committee supports the resumption of the Second Reading debate on the Bill on 6 January 2010.

### **Advice sought**

61. Members are invited to note the Bills Committee's recommendation in paragraph 60.

Council Business Division 1  
Legislative Council Secretariat  
17 December 2009

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

**Membership list**

<b>Chairman</b>	Hon Paul CHAN Mo-po, MH, JP
<b>Members</b>	Hon James TO Kun-sun Hon CHAN Kam-lam, SBS, JP Hon Mrs Sophie LEUNG LAU Yau-fun, GBS, JP Hon Miriam LAU Kin-yee, GBS, JP Hon Jeffrey LAM Kin-fung, SBS, JP Hon Andrew LEUNG Kwan-yuen, SBS, JP Hon Alan LEONG Ka-kit. SC (since 8 October 2009) Hon CHIM Pui-chung Hon Starry LEE Wai-king Hon CHAN Kin-por, JP (since 8 October 2009)

(Total: 11 Members)

<b>Clerk</b>	Ms Rosalind MA
<b>Legal Adviser</b>	Mr Stephen LAM
<b>Date</b>	8 October 2009



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

**List of organizations which have submitted views to the Bills Committee**

1. Association of Chartered Certified Accountants of Hong Kong
2. The American Chamber of Commerce in Hong Kong
3. The British Chamber of Commerce in Hong Kong
4. The Chinese General Chamber of Commerce
5. The Chinese Manufacturers' Association of Hong Kong
6. CPA Australia Limited
7. Deloitte Touche Tohmatsu
8. Ernst & Young Tax Services Limited
9. Federation of Hong Kong Industries
10. The Hong Kong Association of Banks
11. Hong Kong Bar Association
12. The Hong Kong Federation of Insurers
13. Hong Kong General Chamber of Commerce
14. Hong Kong Institute of Certified Public Accountants
15. Hong Kong Small and Medium Enterprises Association
16. Hong Kong Trustees' Association Ltd.
17. International Chamber of Commerce – Hong Kong, China

18. Joint Liaison Committee on Taxation
19. KPMG Tax Limited
20. The Lion Rock Institute
21. The Law Society of Hong Kong
22. Office of the Privacy Commissioner for Personal Data, Hong Kong
23. PricewaterhouseCoopers Limited
24. The Real Estate Developers Association of Hong Kong
25. The Society of Chinese Accountants & Auditors
26. Society of Trust and Estate Practitioners, Hong Kong Limited
27. The Taxation Institute of Hong Kong

**Extracts of Hong Kong's Sample CDTA Text**

**ARTICLE 25**

**EXCHANGE OF INFORMATION**

1. The competent authorities of the Contracting Parties shall exchange such information as is foreseeably relevant for carrying out the provisions of this Agreement or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting Parties, or of their political subdivisions or local or territorial authorities, insofar as the taxation thereunder is not contrary to the Agreement. The exchange of information is not restricted by Article 1<sup>1</sup>.
2. Any information received under paragraph 1 by a Contracting Party shall be treated as secret in the same manner as information obtained under the domestic laws of that Party 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, the determination of appeals in relation to the taxes referred to in paragraph 1. 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 Party the obligation:
  - a) to carry out administrative measures at variance with the laws and 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;

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<sup>1</sup> Article 1: "PERSONS COVERED: This Agreement shall apply to persons who are residents of one or both of the Contracting Parties."

- 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 Party in accordance with this Article, the other Contracting Party shall use its information gathering measures to obtain the requested information, even though that other Party 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 Party 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 Party 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.

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## PROTOCOL

At the time of signing of the Agreement between the Government of Country A and the Government of the Hong Kong Special Administrative Region of the People's Republic of China for the Avoidance of Double Taxation with respect to Taxes on Income and the Prevention of Fiscal Evasion, the two Governments have agreed on the following provisions which shall form an integral part of the Agreement.

1-9. ....

10. It is understood that Article 25 does not create obligations as regards automatic or spontaneous exchanges of information between the Contracting Parties. In respect of the same Article, it is also understood that information requested shall not be disclosed to a third jurisdiction. In the case of the Hong Kong Special Administrative Region, the judicial decisions in which information may be disclosed include the decisions of the Board of Review.

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INLAND REVENUE (AMENDMENT) (NO. 3) BILL 2009

**COMMITTEE STAGE**

Amendments to be moved by the Secretary for  
Financial Services and the Treasury

<u>Clause</u>	<u>Amendment Proposed</u>
2	<p>By deleting the clause and substituting –</p> <p><b>"2. Commencement</b></p> <p>(1) This Ordinance, except this section and sections 1 and 3(3), comes into operation on a day to be appointed by the Secretary for Financial Services and the Treasury by notice published in the Gazette.</p> <p>(2) This section and sections 1 and 3(3) come into operation on the day on which this Ordinance is published in the Gazette."</p>
3	<p>By adding –</p> <p>"(1A) Section 49(1) is amended, in the English text, by repealing "notwithstanding" and substituting "despite"."</p>
3	<p>By adding –</p> <p>"(3) Section 49 is amended by adding –</p>

"(7) Rules made under subsection (6) are subject to the approval of the Legislative Council.".