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1 June 2011

Mr Bonny LOO
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Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central, Hong Kong

Dear Mr LOO,

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Japan) Order (L.N. 64)
Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income and Capital) (French Republic) Order (L.N.65)

Thank you for your letter of 23 May 2011 on the captioned Orders. Our responses to your questions are set out in the following paragraphs.

The Comprehensive Agreement for Avoidance of Double Taxation (CDTA) with Japan

Article 2

2. Article 2 of the Japanese CDTA covers the types of taxes to which the CDTA applies. According to the Japanese side, "enterprise tax" is not strictly an income tax but a local (prefecture) government tax charged on the existence of

business in Japan. Hence, this tax is not included in Article 2 of the Japanese CDTA which is intended to cover taxes on income.

Article 5(6)

3. According to the Commentaries on the Articles of the Organisation for Economic Co-operation and Development Model Tax Convention on Income and on Capital (OECD Model Tax Convention), while independent status is less likely if the activities of the agent are performed wholly or almost wholly on behalf of only one enterprise over the lifetime of the business or a long period of time, this fact is not by itself determinative and all the facts and circumstances must be taken into account, e.g. if the agent bears risk. As the OECD Commentaries is a common reference source for the interpretation of the OECD Model Tax Convention, it is not necessary to explicitly set out such understanding in our CDTAs (e.g. Japanese, New Zealand and Liechtenstein CDTAs).

4. The last sentence in Article 5(6) of the French CDTA was included at the request of the French side to deviate from the understanding in the OECD Commentaries and provides that when the activities of the agent are performed wholly or almost wholly on behalf of only one enterprise, he will not be considered as an agent of independent status and no other factors will be taken into account.

Article 16

5. Article 16(1) sets out examples of an "entertainer". Such examples are not exhaustive. A musician is generally understood to include vocalists and players of musical instruments. The same examples are adopted in our other CDTAs (including France, New Zealand and Liechtenstein).

Article 24

6. On the date of "first notification" under Article 24(1), in most cases, it will be the date of a notice of assessment, official demand or other instrument for the collection or levy of tax. For Hong Kong, under section 58(3) of the Inland Revenue Ordinance (Cap. 112)(the Ordinance), any notice sent by post shall be deemed, unless the contrary is shown, to have been served on the day succeeding the day on which it would have been received in the ordinary course by post. Cases are to be presented in writing and there are no prescribed forms.

7. In computing the two-year period under Article 24(5)(b), according to the OECD Commentaries, a case will only be considered to have been presented to the competent authority of the other treaty partner if sufficient information has been presented to that competent authority to allow it to decide whether the objection underlying the case appears to be justified.

Article 25

8. While the arbitration panel might in appropriate cases refer to confidential information received under Article 25 in its arbitration decisions, arbitration decisions in general are not open to the public.

9. The exchange of information (EoI) Article, as presently drafted, does not impose any obligation for "spontaneous or automatic exchange". Furthermore, we are obliged to comply with the Inland Revenue (Disclosure of Information) Rules (Cap. 112 BI) (the Rules) which prevent spontaneous or automatic exchange by requiring case-specific information to be provided by our treaty partners before the Inland Revenue Department can accede to their EoI requests. We have explained the legal requirements of the Rules to all treaty partners and have as a matter of practice provided them with copies of the Rules during the course of negotiation. Depending on the stance of the particular partner, the issue may or may not be dealt with in the Protocol.

Protocol

10. The "additional tax" under section 82A of the Ordinance is an amount which represents a penalty or interest, and hence is excluded from the term "tax" pursuant to paragraph 1 of the Protocol. The interpretation is in line with the corresponding paragraph in the French, New Zealand and Liechtenstein CDTAs.

Chinese Text

11. As a general response, unlike some of our CDTAs of which the Chinese text is a translated version, the Japanese CDTA is signed in Chinese, English and Japanese. The Chinese text adopted has therefore incorporated comments of the Japanese side and is not amenable to unilateral change by Hong Kong. Our specific responses to the detailed suggestions are set out in the following paragraphs.

12. While the term "擁有" is used in some provisions in the CDTA to denote "ownership", the term itself is not confined to mean "ownership" as such. It may also mean "have" in other contexts such as Article 4(1)(a)(i).

13. In the context of Article 4(1)(b) and Article 12(5), there is no substantial difference between the terms "義務" and "法律責任".

14. The term "variable or fixed payments" in Article 6(2) may be rendered as either "不固定或固定付款" as suggested, or as "不固定或固定收入" as in the present text. Reading the paragraph in its context, the term "不固定或固定收入" should not give rise to confusion.

15. "事業税" is the term used by the Japanese side to denote "enterprise tax", and we understand it is the generic term under the tax laws of Japan.

16. In the context of the whole of Article 9 which concerns transfer pricing, the term "wilful default" in Article 9(3) primarily refers to cases in which the taxpayer intentionally evades his tax obligations, and this is reflected in the term "蓄意瞞税".

17. The term "amount of tax" in Article 22(2) may be rendered in Chinese as either "税項款額" as suggested, or simply as "税額" as in the present text. Reading the paragraph in its context, the term "税額" should not give rise to confusion. Similarly, the term "委託人" as specified under paragraph 8 of the Protocol should not give rise to confusion.

CDTA signed with France

Article 2

18. The French "tax on salaries"(*la taxe sur les salaries*) referred to in paragraph 3(a)(iv) of Article 2 is a tax borne by employers who were not liable for value-added tax and is therefore a business expenditure. The provisions of Article 14 apply to income of employees earned from exercising their employment.

Article 21

19. The suggestion is noted. The English text of Article 21(1)(b) is the negotiated text agreed between the two parties and not amenable to unilateral

changes by Hong Kong.

Article 23

20. The paragraph shall not apply to persons who are not residents of one or both of the Contracting Parties.

Article 24

21. Please refer to paragraphs 6 and 7 above on the calculation of relevant periods. The use of arbitration to resolve cross-border tax disputes is a recent development in the OECD and the relevant provisions were only added to the OECD Model Tax Convention published in 2008. We have started to adopt provisions on arbitration in our CDTAs with the Netherlands, Japan and Liechtenstein. Whether arbitration or any other method of dispute resolution is to be adopted is a matter to be agreed with our treaty partners. Depending on the circumstances, we will continue to consider the need to include provisions for arbitration in our future CDTAs.

Article 25

22. The confinement of EoI to taxes covered by the Agreement is effected by the removal of "Article 2" from the last sentence of Article 25(1) which reads "The exchange of information is not restricted by Articles 1 and 2." in the OECD Model Tax Convention. Article 25(1) is the same as the sample EoI article (as recapped at Annex B to the Legislative Council brief on the French CDTA) that we have submitted to the Bills Committee during the scrutiny of the Inland Revenue (Amendment)(No. 3) Bill 2009.

Protocol

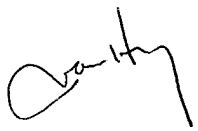
23. Commercial income is income generated from commercial activities, i.e. doing business (as contrasted with royalties which one can receive as long as one has ownership of the rights in question). Business profits would be the net amount receivable from the commercial activities.

Chinese Text

24. The terms "local authority" or "local authorities" may be rendered as either "地方當局" as suggested, or as "地區主管當局" as in the present text. We

are of the view that "地區主管當局" can reflect the meaning of the English text in this situation and should not give rise to confusion.

Yours sincerely,



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