

立法會

Legislative Council

LC Paper No. CB(1)518/15-16(03)

Ref: CB1/BC/7/15

Bills Committee on Inland Revenue (Amendment) Bill 2016

Background brief

Purpose

This paper provides background information on the Inland Revenue (Amendment) Bill 2016. It also summarizes the views and concerns expressed by Members when issues related to the implementation of automatic exchange of financial account information in tax matters ("AEOI") in Hong Kong were discussed by the committees of the Legislative Council ("LegCo") in the 2014-2015 legislative session.

Background

Existing regime on exchange of information for tax purposes

2. The existing legal framework of Hong Kong only allows for exchange of information ("EOI") for tax purposes with its treaty partners under either comprehensive agreements for avoidance of double taxation ("CDTAs")¹ or tax information exchange agreements ("TIEAs")². The EOI regime and related safeguards in Hong Kong are provided in the Inland Revenue Ordinance

¹ It has been the Government's policy priority to conclude CDTAs with Hong Kong's trading and investment partners which serve as a business facilitation initiative to minimize the incidence of double taxation. Double taxation is generally defined as the imposition of comparable taxes in two or more places on the same taxpayers in respect of the same subject matter for identical periods. All CDTAs signed embody a mechanism for EOI up to the international standard as far as practicable.

² A TIEA is a form of agreement for EOI which carries no double taxation relief. The Inland Revenue (Amendment) (No. 2) Ordinance 2013 enacted by LegCo at the meeting of 10 July 2013 has put in place a legal framework for Hong Kong to enter into standalone TIEAs with other jurisdictions.

(Cap. 112) ("IRO"), the Inland Revenue (Disclosure of Information) Rules (Cap. 112 sub leg BI) ("the Disclosure Rules")³ and the relevant Orders implementing individual CDTAs/TIEAs. These safeguards are generally based on the 2004 version of the EOI Article in the Organization for Economic Cooperation and Development ("OECD") Model Tax Convention on Income and on Capital, and the OECD 2002 version of TIEA model, except for certain modifications to address local needs. A number of safeguard measures are included in CDTAs/TIEAs to protect taxpayers' privacy and confidentiality of information exchanged. The current EOI under CDTAs/TIEAs is operated on a request basis, i.e. information will be exchanged upon specific requests from the competent authority of a treaty partner under either CDTAs or TIEAs.

International development on automatic exchange of financial account information in tax matters

3. For the purpose of enhancing tax transparency and combating cross-border tax evasion, OECD released in July 2014 the "Standard for Automatic Exchange of Financial Account Information in Tax Matters" ("AEOI Standard") calling on governments to collect from financial institutions ("FIs") financial account information of non-domestic tax residents and exchange the information with jurisdictions of residence of account holders on an annual basis. The Global Forum on Transparency and Exchange of Information for Tax Purposes ("Global Forum")⁴ of OECD has invited all its members including Hong Kong to commit to implementing the AEOI Standard. A summary of the key components of the AEOI Standard is in **Appendix I**.

4. In September 2014, the Government indicated to the Global Forum Hong Kong's support for implementing the AEOI Standard⁵ on a reciprocal basis with appropriate partners, with a view to commencing the first information exchange by end of 2018 (the latest timeline permissible by the Global Forum). The commitment was premised on the condition that Hong Kong could put in place necessary domestic legislation by 2017.

³ The Disclosure Rules stipulate the particulars to be contained in an EOI request made by an overseas jurisdiction to demonstrate that the requested information is "foreseeably relevant". It also provides for a notification and review system in handling EOI requests and related appeals.

⁴ The Global Forum consists of some 120 member jurisdictions including Hong Kong.

⁵ Specifically, the AEOI Standard comprises –

- (a) Model Competent Authority Agreement ("Model CAA");
- (b) Common Reporting Standard ("CRS");
- (c) Commentaries on the Model CAA and CRS; and
- (d) Guidance on Technical Solution.

Policy approach for automatic exchange of financial account information in tax matters

5. According to the Administration, under the AEOI Standard, FIs are required to conduct due diligence procedures, so as to identify reportable accounts held by tax residents of reportable jurisdictions (i.e. non-Hong Kong tax residents who are liable to tax by reason of residence in the AEOI partner jurisdictions), and collect the reportable information in respect of these relevant accounts. FIs are also required to report such information to the tax authority in specified format. Upon receipt of the information from FIs, the tax authority will exchange the relevant information with their counterparts in the reportable jurisdictions concerned on an annual basis. Hence, "automatic exchange" does not mean a free flow of information amongst jurisdictions.

6. It is the Administration's intention to conduct AEOI only with its CDTA or TIEA partners⁶ on a bilateral basis, taking into account their capability in meeting the OECD standard and in protecting data privacy and confidentiality of the information exchanged in their domestic laws. Under such an approach, Hong Kong will make use of the bilateral EOI instruments (i.e. CDTAs or TIEAs) as the legal basis for implementing AEOI. The Inland Revenue Department ("IRD") would still have to sign a new Competent Authority Agreement, which sets out the modalities of transfer of information collected pursuant to the AEOI Standard, with the tax authority of CDTA/ TIEA partners concerned.

Public consultation

7. The Government launched a two-month consultation from April to June 2015 to seek public views on proposals to apply the AEOI Standard in Hong Kong. According to the Government, stakeholders generally support the overall direction to catch up with the latest international standard and implement AEOI in Hong Kong.

⁶ By the end of December 2015, Hong Kong has signed 33 CDTAs and seven TIEAs. CDTAs have been signed with Belgium, Thailand, Mainland of China, Luxembourg, Vietnam, Brunei, the Netherlands, Indonesia, Hungary, Kuwait, Austria, the United Kingdom, Ireland, Liechtenstein, France, Japan, New Zealand, Portugal, Spain, the Czech Republic, Switzerland, Malta, Jersey, Malaysia, Mexico, Canada, Italy, Guernsey, Qatar, Korea, South Africa, the United Arab Emirates and Romania. TIEAs have been signed with the United States, Norway, Denmark, Sweden, Iceland, Greenland and the Faroes.

Legislative Proposals under the Inland Revenue (Amendment) Bill 2016

8. The Inland Revenue (Amendment) Bill 2016 ("the Bill") was gazetted on 8 January 2016, and received its First Reading at the LegCo meeting of 20 January 2016. The major proposals in the Bill include:

- (a) obligations on certain FIs to establish, maintain and apply due diligence procedures to identify reportable accounts;
- (b) obligations on FIs to furnish returns to IRD in relation to the reportable accounts with respect to any reportable jurisdictions that are maintained by the FIs, and the information required in such returns;
- (c) powers for IRD to gather information on reportable accounts and require FIs to furnish such information in specified format;
- (d) safeguards on taxpayers' rights and confidentiality of information exchanged; and
- (e) sanctions to ensure compliance.

9. Details of the main provisions of the Bill are set out in paragraph 18 of the Legislative Council Brief (File Ref: TsyB R 183/700-6/7/0(C) issued on 7 January 2016), and paragraphs 6 to 15 of the Legal Service Division Report on the Bill (LC Paper No. LS28/15-16). The Bill, if passed, would come into operation on the day when the Amendment Ordinance is published in the Gazette.

Concerns and views expressed by Members

10. The Administration briefed the Panel on Financial Affairs on the latest international development in enhancing tax transparency and its initiative to pursue the AEOI regime in Hong Kong at the meetings on 3 November 2014 and 6 July 2015. Issues related to the AEOI regime were discussed during the session on public finance of the special meetings of the Finance Committee to examine the Estimates of Expenditure 2015-2016 on 30 March 2015. The major views and concerns expressed by Members on related issues are summarized in the ensuing paragraphs.

Benefits of implementing AEOI

11. While some Members considered that Hong Kong should uphold its responsibility in international tax cooperation to implement AEOI and expressed concern about Hong Kong losing its competitiveness as an international financial centres if it failed to do so, some other Members had

reservation about the benefits on Hong Kong in pursuing AEOI and concern that implementing AEOI might undermine Hong Kong's simple taxation system in attracting businesses and talents.

12. The Administration advised that over 90 jurisdictions had already publicly committed to the implementation of AEOI in 2017 or 2018. 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. On the benefits of AEOI, the Administration pointed out that there were previous cases in which information exchanged with other jurisdictions had enabled IRD to detect unreported taxable income of Hong Kong taxpayers sourced from Hong Kong and held in overseas financial accounts.

Compliance cost

13. Given that FIs were already required by law to carry out specific due diligence requirements for Anti-Money Laundering and Counter Terrorist Financing ("AML") purposes, some Members enquired if the reporting requirements and procedures under AEOI could be aligned with those of AML so that they could be simplified, which in turn could minimize compliance costs on FIs and inconvenience caused to account holders. Some Members also stressed the need to minimize the compliance burden and costs on FIs in implementing the AEOI Standard and enquired about exemptions for FIs from reporting on accounts below a certain threshold.

14. The Administration advised that when considering the scope of exemptions for FIs and accounts, it would apply the overriding criteria as set out under the AEOI Standard. According to the AEOI Standard, certain accounts were not subject to reporting, such as pre-existing entity accounts below US Dollar 250,000. The Administration was mindful of the need to avoid creating undue burden of compliance on FIs and account holders.

15. Members were concerned about the potential financial loss caused to financial account holders and adverse impact on the business of FIs arising from reporting of financial account information and tax enforcement, and whether the FIs concerned would be held liable if the relevant account holders had provided false information on their tax residence.

16. The Administration advised that reportable persons under the AEOI Standard were defined with reference to tax residence (rather than citizenship or nationality). The Common Reporting Standard included due diligence

procedures to be performed by FIs for identification of reportable accounts. As long as FIs had followed the relevant due diligence requirements, they would be treated as complying with the requirements. The Administration would keep close liaison with the relevant stakeholders on AEOI matter to address their concerns and seek clarification from the Global Forum where necessary and appropriate.

17. On the scope of FIs to which Hong Kong's AEOI regime would apply, the Administration advised that only FIs incorporated or had permanent establishment in Hong Kong would be required to report financial account information of the overseas tax residents to IRD.

18. Some Members expressed concern about the resources implication on IRD, particularly the manpower requirement, arising from the implementation of AEOI, and increasing workload in relation to expanding the networks of CDTA and TIEA. The Administration agreed that the implementation of AEOI in Hong Kong would create additional workload for IRD. The Administration would closely monitor the situation and would consider the need to strengthen the manpower resources of IRD when necessary taking into account the operational needs.

Protection of privacy and confidentiality of information exchanged

19. Members stressed the importance to strike a proper balance between tax transparency and protection of data privacy in the exchange of financial account information in implementing the proposed AEOI regime. They also highlighted the need for IRD to identify AEOI partners carefully and prevent fishing expedition by partners and disclosure of commercial information exchanged under AEOI to enforcement authorities for non-tax purposes.

20. The Administration pointed out that 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 the jurisdictions concerned instead of a free flow of information among jurisdictions. 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. Similar to the safeguards available in the existing EOI mechanism for CDTAs or TIEAs, the AEOI Standard would contain specific rules on the confidentiality of the information exchanged, including ensuring that the information exchanged should be foreseeably relevant, i.e. no fishing expeditions.

21. As regards protection of the confidentiality of the tax information exchanged with another jurisdiction under the existing EOI mechanism, the Administration advised that the existing Disclosure Rules provided for domestic statutory safeguards in addition to those provided in individual agreements for EOI under CDTAs/TIEAs. The EOI mechanism provided that any information received by a contracting party, including commercial information, should be treated confidential and might be disclosed only to persons or authorities (including courts and administrative bodies) in the jurisdiction concerned for the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes covered by the agreement; and such persons or authorities should use such information only for such purposes. The exchanged information could not be released 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. If treaty partners were considered to have violated their obligations, including the confidentiality requirements, Hong Kong would, where warranted, take necessary action against the treaty partner in question, including termination of the relevant agreement.

Legislative timetable

22. Members expressed concern about the tight legislative timetable as LegCo had to pass the relevant bill before end 2016 in order to meet the Government's commitment of commencing the first automatic information exchange by the end of 2018. They asked if the Government could seek extension from the Global Forum on the commencement of AEOI in Hong Kong, and the possible consequences if Hong Kong did not implement AEOI or meet the above commitment.

23. The Administration said that commencing the first automatic information exchange by the end of 2018 was indeed the latest timeline allowable by the Global Forum for AEOI implementation, and most Global Forum member jurisdictions had committed to implementing the new standard by the end of 2017. Moreover, the Global Forum would conduct a peer review on member jurisdictions regarding AEOI implementation from 2017 onwards and committed jurisdictions were expected to go through review on aspects including effectiveness of their legal framework in and progress of implementing AEOI. It would be crucial for Hong Kong to pass the peer review to avoid being labelled as a "non-compliant" or "non-cooperative" jurisdiction or a "tax haven", as being so labelled could seriously undermine Hong Kong's competitiveness as an international business and financial centre.

Latest development

24. At the House Committee meeting on 22 January 2016, Members agreed to form a Bills Committee to study the Bill.

Relevant papers

25. A list of relevant papers is in **Appendix II**.

Council Business Division 1
Legislative Council Secretariat
1 February 2016

Key Components of the Standard on Automatic Exchange of Financial Account Information in Tax Matters ("Standard on AEOI") published by the Organisation for Economic Cooperation and Development in July 2014

The Standard on AEOI comprises the following –

- (a) **Model Competent Authority Agreement ("Model CAA"):**
This forms the legal basis for the exchange of information, allowing the financial account information to be exchanged. It provides for the modalities of the exchange to ensure the appropriate flow of information. It also contains provisions on confidentiality and safeguards for an effective exchange of information.
- (b) **Common Reporting Standard ("CRS"):**
This defines the reporting and due diligence rules for financial institutions for identification of reportable accounts, which has to be translated into domestic law by participating jurisdictions. Specifically, it covers the following key aspects –
 - (i) The financial institutions covered include banks, custodians, insurance companies, brokers and investment entities (such as certain collective investment vehicles), unless they present a low risk of being used for evading tax and are excluded from reporting (such as prescribed retirement schemes).
 - (ii) The scope of information to be reported covers financial accountholders' personal data (i.e. name, address, tax residence and taxpayer identification number of the account holder) and financial data (i.e. interest, dividends, account balance or value, income from certain insurance products, sales proceeds from financial assets and other income generated with respect to assets held in the account or payment made with respect to the account).
 - (iii) Reportable accounts include accounts held by individuals and entities (which include foundations and trusts), and the standard includes a requirement to look through passive entities to report on the relevant controlling persons (i.e. the beneficial owners).
 - (iv) The due diligence procedures to be performed by financial institutions distinguish between individual and entity accounts, and they also make a difference between pre-existing and new accounts

(c) Commentaries on the Model CAA and the CRS:

In order to ensure consistent application and operation of the AEOI standard, there is a detailed Commentary for each section of the Model CAA and the CRS. For certain limited situations, alternatives are also provided in the Commentaries. In particular, it provides that both bilateral treaties (such as the exchange of information article under the comprehensive agreements for avoidance of double taxation and the tax information exchange agreements) and the Multilateral Convention on Mutual Administrative Assistance in Tax Matters are legal instruments readily available for effecting AEOI. In other words, a jurisdiction should first sign a bilateral treaty or the Multilateral Convention and then sign the Model CAA before proceeding to actual AEOI.

(d) Guidance on Technical Solutions:

This includes a schema to be used for exchanging the information and provides a standard in relation to the information technology aspects of data safeguards and confidentiality, and transmission and encryption for the secure transmission of information under the CRS.

[*Source:* Extract from the paper provided by the Administration for the meeting of the Panel on Financial Affairs on 3 November 2014 (LC Paper No. CB(1)122/14-15(03)).]

List of relevant papers

Date	Event	Papers/Minutes of meeting
15 September 2014	The Government indicated to the Global Forum on Transparency and Exchange of Information for Tax Purposes Hong Kong's support for the new global standard on automatic exchange of information	Press release issued by the Financial Services and the Treasury Bureau
3 November 2014	FA Panel was briefed by the Administration on the latest development on tax transparency and the Administration's preliminary thinking on how to pursue automatic exchange of financial account information in tax matters ("AEOI") in Hong Kong	Background brief (LC Paper No. CB(1)122/14-15(04)) Administration's paper (LC Paper No. CB(1)122/14-15(03)) Minutes (LC Paper No. CB(1)379/14-15)
30 March 2015	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2015-16 (session on public finance)	Speaking note of the Secretary for Financial Services and the Treasury Administration's replies to Members initial written questions Report on the examination of the Estimates of Expenditure 2015-2016
24 April 2015 to 30 June 2015	The Administration launched a consultation exercise on AEOI in Hong Kong	Press release Consultation document Consolidated response of the Government

Date	Event	Papers/Minutes of meeting
6 July 2015	FA Panel was briefed by the Administration on the proposed policy and legal framework for the implementation of AEOI in Hong Kong	<p data-bbox="922 255 1453 376">Updated background brief (LC Paper No. CB(1)1034/14-15(07))</p> <p data-bbox="922 427 1453 548">Administration's paper (LC Paper No. CB(1)1034/14-15(06))</p> <p data-bbox="922 600 1453 678">Minutes (LC Paper No. CB(1)1258/14-15)</p>
20 January 2016	The Inland Revenue (Amendment) Bill 2016 was introduced into the Legislative Council	<p data-bbox="922 725 1453 936">The Bill Legislative Council Brief (File Ref: TsyB R 183/700-6/7/0(C))</p> <p data-bbox="922 987 1453 1066">Legal Service Division Report (LC Paper No. LS28/15-16)</p>