財 經 事 務 及 庫 務 局

香 港 添 馬 添 美 道 二 號
政 府 總 部 二 十 四 樓

FINANCIAL SERVICES AND THE TREASURY (TREASURY)

24/F, Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

傳真號碼 Fax No. : (852) 2523 0642
電話號碼 Tel. No. : (852) 2810 2229
本函檔號 Our Ref. : TsyB R2 183/800-1-1/29/0 (C) & TsyB R2 183/800-1-1/37/0 (C)
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By fax (2877 5029) & email (elee@legco.gov.hk)

26 September 2018

Miss Evelyn Lee
Assistant Legal Advisor
Legal Service Division
Legislative Council Secretariat
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

Dear Miss Lee,

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Republic of India) Order (L.N. 155)

Inland Revenue (Double Taxation Relief with respect to Taxes on Income and Prevention of Tax Evasion and Avoidance) (Republic of Finland) Order (L.N. 156)

Thank you for your letter dated 20 September 2018 on the captioned Orders. Our response is set out in the attached note.

Yours sincerely,

(Billy Lam)
for Secretary for Financial Services and the Treasury

c.c.
Commissioner of Inland Revenue (Attn: Mr K. K. Chiu)
Department of Justice (Attn: Miss Annet Lai)

Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Republic of India) Order (L.N. 155)

Inland Revenue (Double Taxation Relief with respect to Taxes on Income and Prevention of Tax Evasion and Avoidance) (Republic of Finland) Order (L.N. 156)

Government's Responses

Exchange of information ("EoI") arrangements under L.N. 155 and L.N. 156

a. Use of information exchanged for non-tax related purposes

As set out in the Legislative Council ("LegCo") Brief on the Inland Revenue (Amendment) Bill 2013[1], Hong Kong's EoI regime is generally based on the 2004 version of the EoI Article in the Model Tax Convention on Income and on Capital ("Model Tax Convention") promulgated by the Organisation for Economic Co-operation and Development ("OECD") (i.e. the sample article set out in Annex A to the LC Paper No. CB(1)466/09-10(02)) while the Government is also prepared to abide by the OECD's requirement set out in the 2012 version of the EoI Article ("2012 EoI Article") which provides for the use of information exchanged for non-tax related purposes. We set out the same position on the non-tax related purposes in the LegCo Brief on the Inland Revenue (Amendment) Bill 2016[2].

2. In line with the OECD's requirement, it is our policy that the use of information exchanged for non-tax related purposes should only be allowed when **such use is allowed under the laws of both contracting parties** and **the tax authority of the supplying party authorises such use**. As envisaged by the OECD, the sharing of tax information exchanged is only meant for certain high priority matters, such as those for combating money laundering, corruption and terrorism financing.

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[1] Please see paragraphs 14 and 15 of the relevant LegCo Brief at https://www.legco.gov.hk/yr12-13/english/bills/brief/b14_brf.pdf.

[2] Please see paragraph (f) of Annex C to the relevant LegCo Brief at http://www.legco.gov.hk/yr15-16/english/bills/brief/b201601081_brf.pdf.

3. Under the laws of Hong Kong, tax information may only be used for limited non-tax related purposes[3]. It follows that in reality, the tax authorities of the treaty partners may only use the tax information exchanged under the Comprehensive Avoidance of Double Taxation Agreements ("CDTAs") for the said limited non-tax related purposes if they also have similar laws permitting the use of tax information for the said non-tax related purposes. In addition, on every occasion of intended use of tax information for such specified non-tax related purposes, the tax authorities of the treaty partners have to seek prior authorisation from the Inland Revenue Department ("IRD"). The IRD will only indicate consent to the tax authorities of the treaty partners if such use of information is covered by the current exemption provided under section 58 of the Personal Data (Privacy) Ordinance (Cap. 486) in relation to crimes under the laws of a place outside Hong Kong with which Hong Kong has legal or law enforcement cooperation.

b. Disclosure of information exchanged to oversight bodies

4. There are situations where our tax treaty partners are required by their respective domestic laws to disclose the information exchanged to the oversight bodies of the tax authorities concerned. Indeed, both the 2004 version of the EoI Article of the OECD Model Tax Convention and the 2012 EoI Article allow the disclosure of exchanged information to designated persons and authorities and their oversight bodies.

5. In the case of Hong Kong, we will allow the tax information provided to our CDTA and Tax Information Exchange Agreement ("TIEA") partners to be disclosed **only** to the persons or authorities concerned with the assessment or collection of, the enforcement or prosecution in respect of and the determination of appeals in relation to taxes falling within the scope of EoI **but** not for release to their oversight bodies **unless** there are legitimate reasons given by the treaty partners and, where applicable, such oversight bodies are positively listed in the relevant agreement or its protocol ("positive listing approach"). As compared to the EoI Article of the OECD Model Tax Convention, such approach provides additional protection on taxpayers' privacy and enhanced confidentiality of the exchanged information. Furthermore, the oversight bodies concerned are subject to the same safeguards which are also applicable to the tax authorities for the protection of taxpayers' privacy and confidentiality of the information exchanged.

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[3] This covers purposes relating to recovery of proceeds from drug trafficking, organised and serious crimes and terrorist acts under the Drug Trafficking (Recovery of Proceeds) Ordinance (Cap. 405), the Organised and Serious Crimes Ordinance (Cap. 455) and the United Nations (Anti-Terrorism Measures) Ordinance (Cap. 575) respectively.

6. As for the Hong Kong/India CDTA, India requested in the course of negotiation to allow the disclosure of information exchanged under the CDTA to its oversight bodies, namely the Indian Parliamentary Committees and the Special Investigation Team constituted by the Indian Government, so as to fulfil the requirements of its domestic laws. We understand that other CDTAs concluded by India also allow the disclosure of information exchanged to their oversight bodies in general. At present, we do not contemplate other oversight bodies apart from those listed in Paragraph 5(b) of the Protocol to the Hong Kong/India CDTA.

7. The above positive listing approach has already been adopted in the Hong Kong/United Kingdom ("UK") CDTA[4], the Hong Kong/New Zealand CDTA[5], the Hong Kong/Malta CDTA[6], the Hong Kong/Guernsey CDTA[7] and the Hong Kong/United States of America TIEA[8].

c. Disclosure of information pertaining to a period before CDTA comes into effect

8. In response to the question on the relevant provision in the Protocol to the Hong Kong/India CDTA which provides that the requested Contracting Party shall disclose any information that precedes the date on which the CDTA has effect for the taxes covered by the CDTA ("pre-date information"), you may wish to note that the Government set out in the LegCo Brief on the Inland Revenue (Amendment) Bill 2013[9] its position on the disclosure of the pre-date information. In gist, there is a need to disclose the pre-date information generated prior to the effective date of the relevant provisions of the CDTA as such information may also be foreseeably relevant of the tax administration and

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[4] Please refer to Paragraph 4 of the Protocol to the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income and Capital Gains) (United Kingdom of Great Britain and Northern Ireland) Order (Cap. 112BP).

[5] Please refer to Paragraph 4 of the Protocol to the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (New Zealand) Order (Cap. 112BV).

[6] Please refer to Paragraph III(c) of the Protocol to the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Malta) Order (Cap. 112CB).

[7] Please refer to Paragraph 3(c) of the Protocol to the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Guernsey) Order (Cap. 112CH).

[8] Please refer to Paragraph 2 of the Protocol to the TIEA, see Inland Revenue (Exchange of Information relating to Taxes) (United States of America) Order (Cap. 112CK).

[9] Please see paragraphs 8 and 10 of the LegCo Brief at https://www.legco.gov.hk/yr12-13/english/bills/brief/b14_brf.pdf.

enforcement after the relevant provisions of the CDTA come into effect[10]. If the information to be disclosed is confined to information generated after the CDTA takes effect, it would pose practical problems for Hong Kong to conduct EoI with its treaty partners and hinder the efforts of the international community to enhance tax transparency and combat tax evasion.

9. Since the enactment of the Inland Revenue (Amendment) (No. 2) Ordinance 2013 in July 2013, Hong Kong has been able to exchange pre-date information insofar the information is foreseeably relevant for a taxable period or taxable event following that date. We have also, upon the request of treaty partners, incorporated the relevant provision in our CDTAs where appropriate. CDTAs with such a provision include the Hong Kong/Korea CDTA[11] and the Hong Kong/India CDTA.

10. As regards the enquiry on whether the pre-date information may be used for purposes not related to the original request, in case India requests the exchanged information to be used for other non-tax related purposes, Hong Kong will scrutinise the request prudently pursuant to Article 26 of the CDTA (i.e. the EoI Article) (see paragraphs 2 and 3 above).

<u>The meaning of "substantially supported by public funds" in Hong Kong/India CDTA</u>

11. While there is no specific parameter, it is the general understanding in the international tax arena that public funds should account for more than half of the total funding support in order for activities performed by entertainers or sportspersons to be considered as "substantially supported by public funds".

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[10] For instance, a UK resident opened a savings account with a bank in Hong Kong on 1 March 2010 and received interest therefrom. The tax authority in the UK suspects that the UK resident has failed to report his worldwide income attributable to the interest income arising in Hong Kong. The UK authority is investigating the tax affairs of the UK resident for the period from April 2011 onwards and requests the IRD of Hong Kong to provide bank statements of the account in Hong Kong for the period from 1 April 2011 to 31 March 2012 as well as a copy of the signature card for the account in question. The Hong Kong/UK CDTA has effect in Hong Kong for any year of assessment beginning on or after 1 April 2011, but the bank account was opened by the UK resident on 1 March 2010. Pursuant to the pre-amended section 4 of the Inland Revenue (Disclosure of Information) Rules (Cap. 112BI), IRD was only able to provide the bank statements for the period from 1 April 2011 to 31 March 2012 but not copy of the signature card for the account in question, even though the latter is foreseeably relevant to a request relating to a period after the CDTA comes into operation.

[11] Please refer to Paragraph 6 of the Protocol to the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income) (Republic of Korea) Order (Cap. 112CL).

Entitlement of benefits under the Hong Kong/Finland CDTA

12. Prevention of fiscal evasion is one of the purposes of concluding a CDTA and the benefits under a CDTA should only be granted in accordance with the object and purpose of the relevant provisions of the CDTA. To this end, specific clauses are incorporated in the CDTA and the two commonly adopted approaches are (a) the addition of a general anti-abuse rule based on the principal purpose of transactions or arrangements (the principal purposes test or "PPT") as a **separate article** of the CDTA; and (b) the inclusion of the PPT provision into the **individual relevant articles** (e.g. articles on "Dividends", "Interest", "Royalties", "Fees for Technical Services" and "Capital Gains") as appropriate.

13. The Hong Kong/Finland CDTA adopts approach (a) and adds a separate general provision which is applicable to all the provisions of the CDTA, covering different types of income. The "exception" clause (i.e. *"unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Agreement"*) is in fact a reinstatement of the principle in applying the PPT provision against other provisions / different types of income of the CDTA. The same exception clause can be found in the Hong Kong/Belarus CDTA[12].

14. On the other hand, the Hong Kong/India CDTA adopts approach (b). PPT provisions are added to individual relevant articles and such articles have clearly stipulated the conditions for applying the PPT provisions in relation to the income concerned. It is therefore not necessary to include the "exception" clause, which makes a reference to other provisions of the CDTA, under this approach.

Financial Services and the Treasury Bureau
Inland Revenue Department
September 2018

[12] Please refer to Article 27 of the CDTA, see Inland Revenue (Double Taxation Relief and Prevention of Fiscal Evasion with respect to Taxes on Income and Capital) (Republic of Belarus) Order (Cap. 112CY).