

立法會
Legislative Council

LC Paper No. CB(1)1197/17-18(01)

Ref: CB1/PL/FA

Panel on Financial Affairs

Meeting on 3 July 2018

**Background brief on the application of the Convention on
Mutual Administrative Assistance in Tax Matters in Hong Kong**

Purpose

This paper provides background information on the application of the Convention on Mutual Administrative Assistance in Tax Matters ("the Convention") in Hong Kong. It also summarizes the major views and concerns expressed by Members when related matters were discussed by the Panel on Financial Affairs ("FA Panel") in 2017 and 2018, and the Bills Committee on Inland Revenue (Amendment) (No. 5) Bill 2017 ("the Bills Committee").

Background

Automatic exchange of financial account information in tax matters

Inland Revenue (Amendment) (No. 3) Ordinance 2016

2. For the purpose of enhancing tax transparency and combating cross-border tax evasion, the Organisation for Economic Co-operation and Development ("OECD") released in July 2014 the Common Reporting Standard for implementation of automatic exchange of financial account information in tax matters ("AEOI"). In September 2014, Hong Kong indicated its support for implementing AEOI on a reciprocal basis with appropriate partners with a view to commencing the first exchanges by the end of 2018. The Government's policy then was to conduct AEOI only with partners with which Hong Kong had signed Comprehensive Avoidance of Double Taxation Agreements ("CDTAs") or Tax Information Exchange Agreements ("TIEAs") on a bilateral basis under

the exchange of information ("EOI") mechanism.¹ To enable AEOI, the Inland Revenue Department ("IRD") will have to sign a new Competent Authority Agreement ("CAA"), which sets out the modalities of transfer of information collected pursuant to the AEOI standard, with the tax authority of the CDTA/TIEA partner concerned before the exchange of the relevant information takes place.

3. To provide for the legal framework for implementing AEOI in Hong Kong, the Legislative Council ("LegCo") passed the Inland Revenue (Amendment) Bill 2016 in June 2016, which were subsequently enacted as the Inland Revenue (Amendment) (No. 3) Ordinance 2016.² The Amendment Ordinance 2016 amended the Inland Revenue Ordinance (Cap. 112) ("IRO") to add a new section 50J to the Ordinance empowering the Secretary for Financial Services and the Treasury to amend, among others, Schedule 17E to IRO to provide for a list of reportable jurisdictions. A reportable jurisdiction refers to a jurisdiction with which Hong Kong has entered into CDTA/TIEA and CAA for the conduct of AEOI (i.e. Hong Kong's AEOI partner). Financial institutions ("FIs") are required to conduct due diligence procedures to identify reportable accounts held by tax residents of confirmed AEOI partners as included in the list of reportable jurisdictions and collect the required information in respect of these reportable accounts. FIs are also required to furnish such information to IRD from a specific reporting year for onward exchange with the relevant AEOI partners.

Inland Revenue (Amendment) (No.2) Ordinance 2017

4. The international community has been closely monitoring jurisdictions' progress in the implementation of AEOI and putting emphasis on a wide network of AEOI to ensure a level-playing field. Both OECD and the European Union have kicked off their respective exercises to draw up lists of non-cooperative tax jurisdictions and non-compliant jurisdictions on tax transparency. Among the listing criteria are the progress and the network of implementing AEOI as well as participation in the Convention.

¹ Comprehensive avoidance of double taxation agreements ("CDTAs") are tax agreements which seek to minimize incidence of double taxation between the contracting parties and provide a mechanism for the exchange of information ("EOI") between tax authorities, whereas tax information exchange agreements ("TIEAs") serve as EOI instruments without offering any taxation relief. CDTAs and TIEAs signed between Hong Kong and other jurisdictions are giving effect in Hong Kong by orders made under section 49(1A) of the Inland Revenue Ordinance (Cap. 112). Such orders are subject to the negative vetting procedure of the Legislative Council ("LegCo").

² The Inland Revenue (Amendment) Bill 2016 was introduced into LegCo in January 2016. The Bill was passed by LegCo on 22 June 2016 which came into effect on 30 June 2016.

5. Hong Kong faces constraints in the negotiations of bilateral CAA because such discussions with individual jurisdictions take time, and in many cases, Hong Kong's bilateral tax treaties (i.e. CDTAs or TIEAs) will need to be amended to allow for AEOI. Moreover, FIs are mandated to identify and collect information in relation to accounts held by tax residents of confirmed AEOI partners as included in the list of reportable jurisdictions only. To overcome the above challenges, the Administration introduced amendments to IRO, which were subsequently enacted as the Inland Revenue (Amendment) (No.2) Ordinance 2017 in June 2017,³ to mandate FIs to identify and collect information in relation to accounts held by tax residents of prospective AEOI partners, in addition to confirmed AEOI partners, of Hong Kong. The Amendment Ordinance 2017 has amended Part 1 of Schedule 17E to IRO to expand the list of reportable jurisdictions to cover 75 jurisdictions, comprising 13 confirmed AEOI partners and 62 prospective AEOI partners.

Base erosion and profit shifting

6. In October 2015, OECD and the Group of Twenty released a package of 15 actions to combat base erosion and profit shifting ("BEPS"). BEPS refers to tax planning strategies of multinational enterprises that exploit the gaps and mismatches in tax rules among economies to artificially shift profits to low or no-tax locations where there is little or no economic activity, resulting in little or no overall corporate tax being paid. Hong Kong indicated to OECD in June 2016 its commitment to implementing the BEPS package. To meet the four minimum standards⁴ in the BEPS package, Hong Kong needs to take forward automatic exchange of Country-by-Country ("CbC") reports for the assessment of transfer pricing risks of multinational enterprises and spontaneous exchange of information ("SEOI") on tax rulings. The Government considers it more practical to adopt the Convention as a basis to implement the BEPS initiatives.

Convention on Mutual Administrative Assistance in Tax Matters

7. The Convention is jointly developed by OECD and the Council of Europe to provide for all possible forms of administrative cooperation between state parties in the assessment and collection of taxes including various modes of

³ The Inland Revenue (Amendment) (No. 3) Bill 2017 was introduced into LegCo in March 2017. The Bill was passed by LegCo on 22 June 2017 which came into effect on 1 July 2017.

⁴ The four minimum standards are: countering harmful tax practices (Action 5), preventing treaty abuse (Action 6), imposing Country-by-Country reporting requirement (Action 13) and improving cross-border dispute resolution mechanism (Action 14).

EOI, in particular with a view to combating tax avoidance and evasion. The Convention provides a basis for jurisdictions to conduct AEOI and implement the initiatives to combat BEPS on a multilateral basis by signing a multilateral CAA under the Convention. The Convention has been opened for signature by states since 1 June 2011. According to the Administration, as at 11 June 2018, 122 jurisdictions (including China) participated in the Convention, of which 17 jurisdictions covered by territorial extension. In view of the continued expansion in the scope of tax information exchanges in the international community, the Administration considers that the bilateral approach which Hong Kong has adopted is no longer effective or efficient in implementing the AEOI and BEPS initiatives, and it is necessary to seek to extend the application of the Convention to Hong Kong.

Inland Revenue (Amendment) Ordinance 2018

8. To provide a legal basis for the extension, LegCo passed the Inland Revenue (Amendment) (No. 5) Bill 2017 on 24 January 2018, which was enacted as the Inland Revenue (Amendment) Ordinance 2018. The Amendment Ordinance 2018 amended section 49(1) of IRO to empower the Chief Executive in Council ("CE-in-C") to declare, by order, that any tax arrangements specified in that order having been made by Hong Kong with more than one government of any territories outside Hong Kong, or having been made by the Central People's Government ("CPG"), shall have effect in Hong Kong.⁵ This will enable Hong Kong to take a multilateral approach in implementing AEOI and taking forward the automatic exchange of CbC reports and SEOI on tax rulings under the BEPS package.

9. The Administration has sought the assistance of CPG to deposit a declaration to OECD for territorial application of the Convention in Hong Kong, together with the reservations and declarations applicable to Hong Kong.⁶ In May 2018, CPG extended the territorial scope of the

⁵ Before enactment of the Inland Revenue (Amendment) Ordinance 2018, section 49(1A) of the Inland Revenue Ordinance (Cap. 112) ("IRO") provides that the arrangements specified in an order declared by the Chief Executive in Council under that section, of which Hong Kong has entered into with another government shall have effect in Hong Kong if, among other things, such arrangements are made for the purpose of exchanging tax information. The relevant power under the then IRO does not cover multilateral tax agreements or international tax cooperation arrangements for purposes other than affording relief from double taxation and exchanging of information in relation to tax.

⁶ Hong Kong intends to take forward the mandatory provisions of the Convention on Mutual Administrative Assistance in Tax Matters only while making suitable reservations/declarations for the optional provisions so that such provisions will not apply (or will only apply partially) to Hong Kong.

Convention to Hong Kong and the Convention will start to have effect in Hong Kong on 1 September 2018. Pursuant to section 49(1A) of IRO, CE-in-C shall make an order⁷ to declare that the Convention shall have effect in Hong Kong.

Major views and concerns expressed by Members

10. FA Panel was consulted on the application of the Convention to Hong Kong at the meetings on 5 June 2017 and 8 January 2018. The major views and concerns expressed by FA Panel and the Bills Committee are summarized in the ensuing paragraphs.

Procedures for applying the Convention on Mutual Administrative Assistance in Tax Matters to Hong Kong

11. Members enquired about the procedures for applying the Convention to Hong Kong, given that the Convention was only opened for signature by state parties.

12. The Administration advised that upon the request of Hong Kong, CPG had given in-principle approval in May 2017 to extend the application of the Convention to Hong Kong. It was the Government's policy that Hong Kong would take forward the mandatory provisions of the Convention while making suitable reservations/declarations for the optional provisions so that such provisions would not apply or would only partially apply to Hong Kong. It was necessary to amend IRO to provide for the legislative framework for Hong Kong to participate in the Convention. Upon enactment of the amendment ordinance, the Administration would seek CPG's assistance to deposit a declaration to OECD for territorial application of the Convention to Hong Kong, together with the reservations/declarations applicable to Hong Kong. After that, the Administration would recommend CE-in-C to make an order under section 49(1A) of IRO to declare that the Convention should have effect in Hong Kong. Such order was subject to the negative vetting procedure of LegCo.

Implementation strategy of Hong Kong

13. The Bills Committee sought clarification on whether Hong Kong would take forward the provisions of the Convention on simultaneous tax examinations and tax examinations abroad (i.e. Articles 8 and 9 of the Convention). Bills Committee members noted that while these two provisions were mandatory, it

⁷ The order is subject to the negative vetting procedure of LegCo.

would be up to a jurisdiction to decide whether to participate in a simultaneous tax examination and to make a declaration not to accept requests for participating in tax examinations abroad as a general rule.

14. The Administration explained that simultaneous tax examination referred to an arrangement which jurisdictions, each in its own territory, to examine tax affairs of persons in which they had a common or related interest, with a view to exchanging any relevant information which they so obtained. Given that Hong Kong had been practising a territorial-based tax regime, it appeared unlikely that Hong Kong would need to conduct tax examinations with other jurisdictions. It was therefore the Government's policy that Hong Kong, as a general rule, would not participate in any simultaneous tax examinations. In addition, Hong Kong would not accept requests from other jurisdictions allowing their representatives to be present at a tax examination of Hong Kong given that tax examinations abroad was an optional provision of the Convention.

15. As regards the types of taxes that Hong Kong intended to cover under the Convention, the Administration advised that a wide range of taxes were covered under the Convention and Hong Kong would only provide assistance on information exchange for taxes on income or profits, taxes on capital gains which were imposed separately from the tax on income or profits, and taxes on net wealth (i.e. the minimum requirement under the Convention).

Impact on Comprehensive Avoidance of Double Taxation Agreements and Tax Information Exchange Agreements entered by Hong Kong with other jurisdictions

16. Noting that the jurisdictions with which Hong Kong had signed CDTAs/TIEAs might have also participated in the Convention, the Bills Committee sought information on how the Administration would determine whether to use the Convention, the respective CDTAs or TIEAs for EOI with the relevant jurisdictions and the follow-up actions the Administration would take if conflicting provisions were identified between the Convention and the respective CDTAs/TIEAs signed with the jurisdictions.

17. The Administration advised that the Convention, CDTAs, or TIEAs were different platforms to facilitate EOI on tax matters. IRD would continue to use CDTAs/TIEAs as a legal basis for the exchange of tax information with Hong Kong's CDTA/TIEA partners where appropriate. In general, the Convention would be used as the instrument for EOI if the jurisdiction concerned was a party to the Convention but not a CDTA/TIEA partner of Hong Kong. A jurisdiction when making an EOI request must identify the basis of the request (i.e. whether it was made in accordance with the

Convention, a CDTA or TIEA) and state the information requested. As regards whether there would be conflicting provisions among a CDTA, a TIEA or the Convention, the Administration advised that OECD had taken the bilateral modules of EOI and CDTAs into account when it designed the Convention, and the Administration had not identified any conflicting provisions among the Convention, CDTAs and TIEAs signed by Hong Kong in general.

Exchange of information under the Convention on Mutual Administrative Assistance in Tax Matters

18. The Bills Committee enquired about the scope of information to be exchanged under the Convention and whether there was any difference from the information exchanged under a CDTA or TIEA, as well as measures to protect confidentiality of the information exchanged under the Convention, in particular if such information involved personal data.

19. The Administration responded that, in general, the scope of information to be exchanged, be it conducted on a bilateral basis under a CDTA or TIEA or on a multilateral basis under the Convention, was the same. As a matter of policy, Hong Kong would participate in three forms of information exchange, namely, EOI on request (Article 5), automatic EOI (Article 6) and SEOI (Article 7) on tax rulings under the Convention.

20. As regards confidentiality and data protection safeguards, the Administration stressed that the high level of privacy and confidentiality safeguards currently applicable to the handling of tax information (including personal data) under IRO would apply while conducting information exchange under the Convention. In considering whether to exchange information pursuant to the Convention with a particular jurisdiction, the Government would evaluate whether the receiving party was able to meet the data protection obligations under the Convention. These considerations would include whether the receiving party had put in place sufficient safeguards to ensure data protection as required under the laws of Hong Kong (including the Personal Data (Privacy) Ordinance (Cap. 486)). If the receiving party was unable to meet the required standard, depending on the circumstances, Hong Kong might decline to provide information to the receiving party or enter into an arrangement with the receiving party whereby the receiving party agreed to comply with the data protection requirements of Hong Kong before proceeding with EOI. Where the receiving party did not comply with its obligations regarding data protection under the Convention or the data protection arrangement with Hong Kong, the Administration might suspend EOI with the receiving party under the Convention.

Latest development

21. At the FA Panel meeting on 3 July 2018, the Government will brief members on the latest development on the application of the Convention to Hong Kong.

Relevant papers

22. A list of relevant papers is set out in the **Appendix**.

Council Business Division 1
Legislative Council Secretariat
28 June 2018

List of relevant papers

Date	Event	Paper
3 November 2014	Meeting of the FA Panel	<u>Administration's paper</u> (LC Paper No. CB(1)122/14-15(03)) <u>Background brief</u> (LC Paper No. CB(1)122/14-15(04)) <u>Minutes</u> (paragraphs 38-51) (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)	<u>Speaking note of the Secretary for Financial Services and the Treasury</u> <u>Report on the examination of the Estimates of Expenditure 2015-2016</u>
6 July 2015	Meeting of the FA Panel	<u>Administration's paper</u> (LC Paper No. CB(1)1034/14-15(06)) <u>Updated background brief</u> (LC Paper No. CB(1)1034/14-15(07)) <u>Minutes</u> (paragraphs 54-64) (LC Paper No. CB(1)1258/14-15)
22 June 2016	The Legislative Council passed the Inland Revenue (Amendment) Bill 2016	<u>Hansard</u> <u>The Bill passed</u> <u>Report of the Bills Committee</u> (LC Paper No. CB(1)984/15-16)
2 November 2016	Subcommittee on Inland Revenue Ordinance (Amendment of Schedule 17E) Notice 2016	<u>Report</u> (LC Paper No. CB(1)281/16-17)

Date	Event	Paper
16 March 2017	Meeting of the FA Panel	<p><u>Administration's paper</u> (LC Paper No. CB(1)660/16-17(09))</p> <p><u>Updated background brief</u> (LC Paper No. CB(1)660/16-17(10))</p> <p><u>Minutes</u> (paragraphs 56-61) (LC Paper No. CB(1)1178/16-17)</p>
29 March 2017	The Legislative Council passed the Inland Revenue (Amendment) (No.3) Bill 2017	<p><u>Hansard</u></p> <p><u>The Bill passed</u></p> <p><u>Report of the Bills Committee</u> (LC Paper No. CB(1)1008/16-17)</p>
3 April 2017	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2017-18 (session on public finance)	<p><u>Speaking note of the Secretary for Financial Services and the Treasury</u></p> <p><u>Report on the examination of the Estimates of Expenditure 2017-2018</u></p>
5 June 2017	Meeting of the FA Panel	<p><u>Administration's paper</u> (LC Paper No. CB(1)1030/16-17(08))</p> <p><u>Updated background brief</u> (LC Paper No. CB(1)1030/16-17(09))</p> <p><u>Minutes</u> (paragraphs 52-62) (LC Paper No. CB(1)1356/16-17)</p>
8 January 2018	Special meeting of the FA Panel	<p><u>Administration's paper</u> (LC Paper No. CB(1)402/17-18(03))</p> <p><u>Background brief</u> (LC Paper No. CB(1) 402/17-18(04))</p> <p><u>Minutes</u> (paragraphs 53-58) (LC Paper No. CB(1)830/17-18)</p>

Date	Event	Paper
24 January 2018	The Legislative Council passed the Inland Revenue (Amendment) (No. 5) Bill 2017	Hansard The Bill passed Report of the Bills Committee (LC Paper No. CB(1)497/17-18)