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**Panel on Financial Affairs**

**Meeting on 2 March 2020**

**Updated background brief on automatic exchange  
of information for tax purposes**

**Purpose**

This paper provides background information on the implementation of automatic exchange of financial account information in tax matters ("AEOI") and 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 relevant committees of the Legislative Council since the 2014-2015 legislative session.

**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 ("CRS") for implementation of 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 Administration'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.<sup>1</sup> To enable AEOI, the Inland Revenue Department ("IRD") will 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.<sup>2</sup> 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. 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)

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<sup>1</sup> 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)("IRO"). Such orders are subject to the negative vetting procedure of the Legislative Council ("LegCo").)

<sup>2</sup> 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.

(No.2) Ordinance 2017 in June 2017,<sup>3</sup> to mandate FIs to identify and collect information in relation to accounts held by tax residents of prospective 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 jurisdictions which are confirmed AEOI partners and prospective AEOI partners.

#### Convention on Mutual Administrative Assistance in Tax Matters

5. 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 EOI. The Convention has been opened for signature by states since 1 June 2011 and provides a basis for jurisdictions to conduct AEOI and in particular to implement the initiatives for combating base erosion and profit shifting<sup>4</sup> ("BEPS") on a multilateral basis by signing a multilateral CAA under the Convention. 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 initiatives, and it is necessary to seek to extend the application of the Convention to Hong Kong.

#### *Inland Revenue (Amendment) Ordinance 2018*

6. To provide a legal basis for the extension of the Convention to Hong Kong, 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

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<sup>3</sup> 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.

<sup>4</sup> Base erosion and profit shifting 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.

have effect in Hong Kong.<sup>5</sup> This will enable Hong Kong to, inter alia, take a multilateral approach in implementing AEOI.

7. In May 2018, CPG extended the territorial scope of the Convention to Hong Kong<sup>6</sup> and the Convention took effect in Hong Kong on 1 September 2018<sup>7</sup>

#### *Inland Revenue (Amendment) (No. 2) Ordinance 2019*

8. According to the Administration, OECD had examined Hong Kong's AEOI legislative framework and made a number of recommendations for better aligning the relevant provisions of IRO with the requirements of CRS it had promulgated. The Administration subsequently introduced the Inland Revenue (Amendment) (No. 7) Bill 2018 to implement the required legislative amendments and add 51 reportable jurisdictions to Schedule 17E to IRO in view of the extension of the Convention to Hong Kong. LegCo passed the Bill on 20 February 2019, which was enacted as the Inland Revenue (Amendment) (No. 2) Ordinance 2019. The proposed amendments relating to AEOI in the Bill came into operation on 1 January 2020.

### **Major views and concerns expressed by Members**

9. Matters relating to the implementation of the AEOI regime in Hong Kong were discussed at the meetings of the Panel on Financial Affairs ("FA Panel") on 3 November 2014, 6 July 2015 and 16 March 2017, as well as a number of the Bills Committees and Subcommittees on IRO and its Schedule

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<sup>5</sup> Before enactment of the Inland Revenue (Amendment) Ordinance 2018, section 49(1A) of 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.

<sup>6</sup> Hong Kong has taken forward the mandatory provisions of the Convention on Mutual Administrative Assistance in Tax Matters only and made reservations/declarations for the optional provisions so that such provisions will not apply (or will only apply partially) to Hong Kong.

<sup>7</sup> The Inland Revenue (Convention on Mutual Administrative Assistance in Tax Matters) Order, which was made by CE-in-C under section 49(1A) of IRO to declare that the Convention should have effect in Hong Kong on 13 July 2018, was tabled before LegCo on 10 October 2018. The date of gazettal was designated as the commencement date of the Order so that the first round of AEOI could be conducted by September 2018.

17E relating to the AEOI regime since 2016. Issues relating to the application of the Convention to Hong Kong were discussed at the meetings of FA Panel on 5 June 2017, 8 January and 3 July 2018, and the Bills Committee on Inland Revenue (Amendment) (No. 5) Bill 2017. The major views and concerns expressed by Members are summarized in the ensuing paragraphs.

Justifications for implementing automatic exchange of financial account information in tax matters

10. While some Members considered that Hong Kong should implement AEOI in order to fulfill its responsibility in international tax cooperation, some other Members queried the benefits for Hong Kong to pursue AEOI given its territorial-based tax regime. These Members cautioned that following the international standards of AEOI indiscriminately and too closely might risk eroding the edges of simple tax regime and flexible business environment of Hong Kong in the long run.

11. The Administration advised that the international community had 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 ("EU") had kicked off their respective exercises to draw up lists of "non-cooperative" tax jurisdictions. One of the listing criteria was the progress and the network of implementing AEOI. In the case of EU, a jurisdiction could be regarded as compliant on tax transparency if it fulfilled certain criteria, one of which was that arrangements had been in place for AEOI with all EU Member States by end 2017. A considerable number of jurisdictions had also indicated to OECD their interest in conducting AEOI with Hong Kong.

Operational arrangements for automatic exchange of information with reportable jurisdictions

12. Members noted that FIs should start conducting due diligence procedures and collect information from account holders who were tax residents of an AEOI partner jurisdiction, in the calendar year following LegCo's approval of the inclusion of the AEOI partner as a reportable jurisdiction. FIs should lodge the AEOI returns within five months after the calendar year to which the information related and IRD would then commence the first information exchange with the tax authorities of the reportable jurisdictions in the following September (and September annually thereafter). Given the bulk of information involved, Members enquired about the feasibility of spreading out the deadlines for FIs to submit the AEOI returns in respect of different jurisdictions over different months of a reporting year. There was also concern about whether sufficient assistance would be rendered to FIs when Hong Kong conducted its

first round of AEOI with other jurisdictions in September 2018.

13. The Administration responded that the automatic exchange of information among tax authorities in September each year was a common timeframe for all reportable jurisdictions. To meet this timeframe, FIs would be required to submit their AEOI returns to IRD by May in the reporting year concerned. OECD would put in place a Common Transmission System for exchange of information among tax authorities. At the domestic level, IRD had put in place the AEOI Portal for FIs to submit notifications and file returns on required information of reportable accounts electronically. As such, the processing and exchange of data would not create too much administrative burden on IRD. It was observed that the AEOI Portal had been operating smoothly and FIs had not indicated difficulty in using the system. IRD would adopt a facilitating approach and step up its work in helping FIs to submit AEOI returns including arranging publicity to enhance FIs' awareness of their obligations for submitting the returns and ensuring the returns would meet the required format and standard.

#### Due diligence procedures

14. Members expressed concern that the surge in the number of reportable jurisdictions might create undue compliance burden on FIs in carrying out the due diligence procedures in verifying reportable financial accounts. Some Members enquired about how FIs would be taken as having exercised all reasonable due diligence in identifying the tax residences of account holders. Some Members further considered that the Administration should adopt a lenient approach in handling non-compliances of FIs at the initial stage of AEOI implementation.

15. The Administration advised that OECD's essential requirements regarding AEOI standard, including the obligations on FIs to establish, maintain and apply due diligence procedures in respect of new accounts and pre-existing accounts, had already been incorporated in IRO. Besides, FIs were required under the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615) ("AMLO") to conduct due diligence for their customers, so as to identify and verify their identities. In order to reduce their compliance burden in conducting the due diligence procedures for AEOI, FIs might resort to information collected pursuant to the AMLO procedures in performing the relevant due diligence requirements under the AEOI regime. FIs would be taken as having exercised reasonable due diligence in identifying the tax residences of account holders so long as they had followed the relevant requirements in IRO. Self-certification by account holders would be an important tool for FIs to fulfill their reporting and due diligence obligations, in particular to determine the tax residences of account holders. FIs were not

expected to carry out independent legal analyses of relevant tax laws or carry out investigation to determine the tax residences of the account holders. IRD would promulgate guidelines, which would include a sample self-certification form for reporting FIs' reference and brief them on the due diligence and reporting requirements

#### Safeguards to protect taxpayers' privacy and confidentiality of information exchanged

16. Members enquired how the privacy of personal data would be protected in implementing AEOI including measures to safeguard against misuse of information by Hong Kong's AEOI partners, and the penalties, if any, on IRD staff for leaking information in the course of handling AEOI data.

17. The Administration emphasized that Hong Kong would only conduct AEOI with jurisdictions which had fulfilled OECD's standard and the relevant safeguards for protecting data privacy and confidentiality of the information exchanged. The scope and use of information to be exchanged followed CRS of AEOI set by OECD strictly. Moreover, OECD and the international community at large reckoned the importance and benefits of adhering to the safeguard provisions for the effective implementation of AEOI. OECD would continue to monitor jurisdictions' progress in this regard. At the domestic level, the Administration had kept the Office of the Privacy Commissioner for Personal Data informed of the AEOI initiative and would ensure compliance with the relevant requirements in confidentiality and personal data privacy.

18. As regards the handling of AEOI data by IRD staff, the Administration advised that there were established procedures on appointment or authorization of persons to carry out duties including AEOI arrangements under IRO. By virtue of sections 4(1) and 81(1)(b) of IRO, returns containing the required information furnished to IRD by FIs were subject to official secrecy protection, contravention of which constituted an offence. Furthermore, the information from FIs would be transmitted via IRD's AEOI Portal system and stored in the IRD's back-end system with encryption under a high level of security. The Expert Panel team from the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes conducted an on-site examination at IRD in April 2016, and considered that Hong Kong had put in place the key risk management processes and adequate controls in relation to AEOI.

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

19. Members enquired about the types of tax information to be exchanged among parties to the Convention, whether the scope of information to be

exchanged would be different from that under a CDTA or TIEA, and how the exchanges would be conducted among parties. Members also expressed concern as whether there would be measures to protect confidentiality of the information exchanged under the Convention.

20. The Administration advised that the Convention contained various provisions on mutual assistance in tax matters among parties to the Convention including EOI on request, automatic EOI, spontaneous EOI, simultaneous tax examinations and tax examinations abroad. As a matter of policy, Hong Kong would participate in three forms of EOI, namely, EOI on request, automatic EOI and spontaneous EOI on tax rulings under the Convention. 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). 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.

21. 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 Administration would evaluate whether the receiving party was able to meet the data protection obligations under the Convention. 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

Impact of the Convention on Mutual Administrative Assistance in Tax Matters on Comprehensive Avoidance of Double Taxation Agreements and Tax Information Exchange Agreements entered by Hong Kong with other jurisdictions

22. Noting that the jurisdictions with which Hong Kong had signed CDTAs/TIEAs might have also participated in the Convention, Members



enquired 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 it would take if conflicting provisions were identified between the Convention and the respective CDTAs/TIEAs signed with the jurisdictions.

23. 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, 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.

### **Latest development**

24. At the FA Panel meeting on 2 March 2020, the Administration will brief members on the implementation of AEOI regime in Hong Kong and proposed amendments to IRO for addressing the recommendations of OECD on the regime.

### **Relevant papers**

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

## List of relevant papers

Date	Event	Paper
3 November 2014	Meeting of the FA Panel	<p><a href="#">Administration's paper</a> (LC Paper No. CB(1)122/14-15(03))</p> <p><a href="#">Background brief</a> (LC Paper No. CB(1)122/14-15(04))</p> <p><a href="#">Minutes</a> (paragraphs 38-51) (LC Paper No. CB(1)379/14-15)</p>
30 March 2015	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2015-16 (session on public finance)	<p><a href="#">Speaking note of the Secretary for Financial Services and the Treasury</a></p> <p><a href="#">Report on the examination of the Estimates of Expenditure 2015-2016</a></p>
6 July 2015	Meeting of the FA Panel	<p><a href="#">Administration's paper</a> (LC Paper No. CB(1)1034/14-15(06))</p> <p><a href="#">Updated background brief</a> (LC Paper No. CB(1)1034/14-15(07))</p> <p><a href="#">Minutes</a> (paragraphs 54-64) (LC Paper No. CB(1)1258/14-15)</p>
22 June 2016	The Legislative Council passed the Inland Revenue (Amendment) Bill 2016	<p><a href="#">Hansard</a></p> <p><a href="#">The Bill passed</a></p> <p><a href="#">Report of the Bills Committee</a> (LC Paper No. CB(1)984/15-16)</p>
2 November 2016	Subcommittee on Inland Revenue Ordinance (Amendment of Schedule 17E) Notice 2016	<p><a href="#">Report</a> (LC Paper No. CB(1)281/16-17)</p>

<b>Date</b>	<b>Event</b>	<b>Paper</b>
16 March 2017	Meeting of the FA Panel	<p><a href="#"><u>Administration's paper</u></a> (LC Paper No. CB(1)660/16-17(09))</p> <p><a href="#"><u>Updated background brief</u></a> (LC Paper No. CB(1)660/16-17(10))</p> <p><a href="#"><u>Minutes</u></a> (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><a href="#"><u>Hansard</u></a></p> <p><a href="#"><u>The Bill passed</u></a></p> <p><a href="#"><u>Report of the Bills Committee</u></a> (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><a href="#"><u>Speaking note of the Secretary for Financial Services and the Treasury</u></a></p> <p><a href="#"><u>Report on the examination of the Estimates of Expenditure 2017-2018</u></a></p>
5 June 2017	Meeting of the FA Panel	<p><a href="#"><u>Administration's paper</u></a> (LC Paper No. CB(1)1030/16-17(08))</p> <p><a href="#"><u>Updated background brief</u></a> (LC Paper No. CB(1)1030/16-17(09))</p> <p><a href="#"><u>Minutes</u></a> (paragraphs 52-62) (LC Paper No. CB(1)1356/16-17)</p>
8 January 2018	Special meeting of the FA Panel	<p><a href="#"><u>Administration's paper</u></a> (LC Paper No. CB(1)402/17-18(03))</p> <p><a href="#"><u>Background brief</u></a> (LC Paper No. CB(1) 402/17-18(04))</p> <p><a href="#"><u>Minutes</u></a> (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	<a href="#">Hansard</a> <a href="#">The Bill passed</a> <a href="#">Report of the Bills Committee</a> (LC Paper No. CB(1)497/17-18)
3 July 2018	Meeting of the FA Panel	Administration's papers <a href="#">1</a> and <a href="#">2</a> (LC Paper Nos. CB(1)1166/17-18(02) and (03))  <a href="#">Updated background brief</a> (LC Paper No. CB(1)1197/17-18(01))  <a href="#">Minutes</a> (paragraphs 3-24) (LC Paper No. CB(1) 1372/17-18)
10 October 2018	The Inland Revenue (Convention on Mutual Administrative Assistance in Tax Matters) Order was tabled before the Legislative Council	<a href="#">The Order</a>  <a href="#">Legislative Council brief</a>
20 February 2019	The Legislative Council passed the Inland Revenue (Amendment) (No. 7) Bill 2018	<a href="#">Hansard</a>  <a href="#">The Bill passed</a>  <a href="#">Report of the Bills Committee</a> (LC Paper No. CB(1)566/18-19)