

File Ref: (TsyB R2 183/800-3/3/0 (C))

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance
(Chapter 112)

INLAND REVENUE ORDINANCE (AMENDMENT OF SECTION 50A) NOTICE 2020

INLAND REVENUE ORDINANCE (AMENDMENT OF SCHEDULE 17D) NOTICE 2020

INTRODUCTION

In exercise of the powers conferred by sections 50A(16A)(b) and 50J of the Inland Revenue Ordinance (Cap. 112) (“IRO”), the Secretary for Financial Services and the Treasury has made the following two notices to revise the implementation arrangements for the automatic exchange of financial account information in tax matters (“AEOI”) having regard to the recommendations of the Organisation for Economic Co-operation and Development (“OECD”) –

A (a) Inland Revenue Ordinance (Amendment of Section 50A) Notice 2020 (at **Annex A**); and

B (b) Inland Revenue Ordinance (Amendment of Schedule 17D) Notice 2020 (at **Annex B**).

JUSTIFICATIONS

2. The AEOI is an international initiative on exchange of tax information advocated by the OECD to enhance tax transparency and combat cross-border tax evasion. Hong Kong has implemented the AEOI since September 2018. To ensure consistent application of the Standard for Automatic Exchange of Financial Account Information in Tax Matters (i.e. the Common Reporting Standard (“CRS”)), the OECD conducts assessments on the compliance of participating jurisdictions (including Hong Kong) from time to time.

3. In the latest round of assessment, the OECD has made two improvement recommendations on Hong Kong's AEOI legislative framework. As the assessment forms part of the peer review process on Hong Kong's overall effectiveness in implementing the AEOI, we need to introduce the necessary amendments to the IRO so as to ensure that our AEOI regime complies with the prevailing international standard.

4. The first recommendation from the OECD is about the definition of "controlling person" in the IRO. At present, the identification of beneficial owners of a partnership under the IRO for the purpose of the AEOI is only applicable to, amongst others, those individuals who are entitled to or control more than 25% of the capital/profits/voting rights of the partnership (see section 50A(6)(b) and 50A(7) of the IRO). The OECD considers that the scope of beneficial owners of partnerships should not be subject to any thresholds on the stakes held¹. To comply with the OECD's requirement, we need to remove the 25% threshold applicable to partnerships. We will also take the opportunity to remove a similar threshold applicable to trusts for the sake of completeness².

5. The second recommendation from the OECD is for enhancing the legislative clarity. Currently, the IRO provides that a reporting financial institution ("FI") may rely on information collected and maintained pursuant to the anti-money laundering/know your customer ("AML/KYC") procedures for the purpose of determining the controlling persons of an account holder of a new entity account. The OECD considers that Hong Kong should clearly specify that such AML/KYC procedures, if relied upon, must be consistent with Recommendations 10 and 25 of the Financial Action Task Force Recommendations ("FATF Recommendations")³.

¹ CRS requires that the controlling persons that need to be identified in relation to legal arrangements other than trusts (such legal arrangements cover partnerships in the case of Hong Kong) are those in an equivalent position or a similar position as settlor, trustee, protector and beneficiary of a trust, regardless of the stake held.

² In relation to trusts (which are also regarded as legal arrangements under the CRS), while the 25% threshold still exists under section 50A(6)(c)(i) and 50A(7) of the IRO, the Inland Revenue (Amendment) (No. 2) Ordinance 2019 has already amended section 50A(6)(c)(ii) to (vi) to the effect that all controlling persons as defined by the CRS, regardless of the stake held, have to be identified by the reporting FIs. We propose to take the opportunity of this legislative exercise to remove the 25% threshold applicable to trusts for the sake of completeness.

³ The definition of the term "controlling persons" under the CRS corresponds to the term "beneficial owner" as described in Recommendation 10 of the FATF Recommendations, and must be interpreted in a manner consistent with the FATF Recommendations. The FATF Recommendations set out a comprehensive and consistent framework of measures which jurisdictions should implement in order to combat money laundering and terrorist financing, as well as the financing of proliferation of weapons of mass destruction. Recommendation 10 sets out the customer due diligence measures that FIs are

THE NOTICES

6. The Inland Revenue Ordinance (Amendment of Section 50A) Notice 2020 amends the specified percentage in section 50A(7) of the IRO to the effect that the threshold applicable to partnerships and trusts is reduced from 25% to 0%.

7. The Inland Revenue Ordinance (Amendment of Schedule 17D) Notice 2020 amends section 5 of Part 6 of Schedule 17D to the IRO to specify that for the purpose of determining the controlling persons of an account holder of a new entity account, a reporting FI may rely on information collected and maintained pursuant to AML/KYC procedures if those procedures are consistent with Recommendations 10 and 25 of the FATF Recommendations.

LEGISLATIVE TIMETABLE

8. The legislative timetable is as follows –

Publication in the Gazette	17 April 2020
Tabling at the Legislative Council (“LegCo”)	22 April 2020
Commencement of the Notices	1 January 2021

IMPLICATIONS OF THE LEGISLATIVE AMENDMENTS

9. On economic implications, while reporting FIs may need to undertake additional compliance work in light of the reduced threshold applicable to partnerships, this is crucial for maintaining Hong Kong’s compliance with the international tax standard and minimising the risk of Hong Kong being considered by the OECD as a non-cooperative tax jurisdiction, thereby preserving Hong Kong’s competitiveness and reputation as an international financial and business centre.

10. The legislative amendments are in conformity with the Basic Law, including the provisions concerning human rights. They do not affect the binding effect of the existing provisions of the IRO and its subsidiary

required to undertake, whereas recommendation 25 sets out the requirement in relation to transparency and beneficial ownership of legal arrangements.

legislation. They have no civil service, environmental, family, financial, gender and productivity implications, and no sustainability implications other than those set out in paragraph 9 above.

PUBLIC CONSULTATION

11. In November 2019, we issued letters to relevant stakeholders from the financial, business, accounting and legal sectors to brief them on the OECD's recommendations and seek their views on the proposed legislative amendments. Most of the submissions received indicate no objection or no comment towards the way forward.

12. We also briefed the LegCo Panel on Financial Affairs on the proposed legislative amendments on 17 March 2020, and members had no objection.

PUBLICITY

13. A spokesperson is available for answering media enquiries.

BACKGROUND

14. The implementation of the AEOI is underpinned by the CRS promulgated by the OECD. To comply with the CRS, a reporting FI⁴ is required to identify financial accounts held by tax residents of reportable jurisdictions (as specified in Part 1 of Schedule 17E to the IRO) in accordance with the due diligence procedures. FIs need to collect the reportable information of these accounts⁵ and furnish such information to the tax authority, i.e. IRD in the case of Hong Kong. IRD then exchanges the information with the tax authorities of Hong Kong's AEOI partner jurisdictions on an annual basis. We amended the IRO in June 2016 to provide a legal framework for implementing the AEOI in Hong Kong, and

⁴ Under section 50A(1) of the IRO, "financial institution" means a custodial institution, a depository institution, an investment entity or a specified insurance company. The term principally refers to banks, securities firms, insurance companies and investment funds. On the other hand, "reporting financial institution" is defined to mean, in general, a FI that is resident in Hong Kong or a Hong Kong branch of a FI that is not resident in Hong Kong.

⁵ The financial information to be reported with respect to reportable accounts includes all types of investment income (including interest, dividends, income from certain insurance contracts and other similar types of income), account balances and sales proceeds from financial assets.

have conducted the AEOI since September 2018.

ENQUIRIES

15. For enquiries, please contact Mr Stephen Lo, Principal Assistant Secretary for Financial Services and the Treasury (Treasury) at 2810 2317.

Financial Services and the Treasury Bureau
15 April 2020

Inland Revenue Ordinance (Amendment of Section 50A) Notice 2020

(Made by the Secretary for Financial Services and the Treasury under section 50A(16A)(b) of the Inland Revenue Ordinance (Cap. 112))

1. Commencement

This Notice comes into operation on 1 January 2021.

2020

2. Inland Revenue Ordinance amended

The Inland Revenue Ordinance (Cap. 112) is amended as set out in section 3.

3. Section 50A amended (interpretation)

Section 50A(7)—

Repeal

everything after “percentage”

Substitute

“is—

- (a) in relation to paragraph (a) of that subsection—25%;
- (b) in relation to paragraph (b) of that subsection—0%;
and
- (c) in relation to paragraph (c) of that subsection—0%.”.

Secretary for Financial Services and
the Treasury

Explanatory Note

Section 50A(1) of the Inland Revenue Ordinance (Cap. 112) (*Ordinance*) defines the expression *controlling person*, which is used in Part 8A of the Ordinance. According to paragraph (a), (b)(ii) and (c)(ii) of that definition, certain persons who exercise control over an entity (*Entity A*) or another particular entity are regarded as controlling persons in respect of Entity A.

2. Section 50A(6) of the Ordinance further explains who would be regarded as a person who exercises control over an entity that is a corporation, partnership or trust, or other entity for the purpose of the definition of *controlling person*.
3. This Notice amends section 50A(7) of the Ordinance to reduce the specified percentage mentioned in section 50A(6)(b) and (c) of the Ordinance from 25% to 0%. Section 50A(6)(b) and (c) relates respectively to an entity that is a partnership and trust.
4. The specified percentage mentioned in section 50A(6)(a) of the Ordinance remains unchanged at 25%. That section relates to an entity that is a corporation.

Inland Revenue Ordinance (Amendment of Schedule 17D) Notice 2020

(Made by the Secretary for Financial Services and the Treasury under section 50J of the Inland Revenue Ordinance (Cap. 112))

1. Commencement

This Notice comes into operation on 1 January 2021.

2. Inland Revenue Ordinance amended

The Inland Revenue Ordinance (Cap. 112) is amended as set out in section 3.

3. Schedule 17D amended (due diligence requirements)

Schedule 17D, Part 6, section 5—

Repeal

“procedures.”

Substitute

“procedures if those procedures are consistent with Recommendations 10 and 25 of the FATF Recommendations (as defined by section 50A(1)).”.

Secretary for Financial Services and
the Treasury

2020

Explanatory Note

This Notice amends Schedule 17D to the Inland Revenue Ordinance (Cap. 112) to comply with the relevant requirement mentioned in the Commentaries on the Common Reporting Standard contained in the Standard for Automatic Exchange of Financial Account Information in Tax Matters (Second Edition), published by the Organisation for Economic Co-operation and Development on 27 March 2017.