

28 June 2012

Prof K C Chan, SBS, JP
Secretary for Financial Services and the Treasury
Financial Services and the Treasury Bureau
24/F, Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

Dear K C,

Submission on Consultation Paper on
**Provision of a Legal Framework for
Entering into Tax Information Exchange Agreements**

Background

Since enacting legislation in 2010 concerning double taxation agreements and provisions within such treaties for the exchange of tax information with treaty partners, Hong Kong has entered into 19 comprehensive double taxation agreements (**CDTAs**) and has four further agreements pending formal signatures.¹ By law, exchange of information agreements (**EoIs**) may be incorporated into CDTAs, but may not be signed in the absence of a CDTA.

The Global Forum on Transparency and Exchange of Information for Tax Purposes, of which Hong Kong is a member, is pressing for legislation permitting stand-alone tax information exchange agreements (**TIEAs**). The group consists of 34 OECD members and 75 non-members. Hong Kong is the sole member not in compliance with this requirement. Continued non-compliance may lead to unspecified sanctions against Hong Kong.

Hong Kong has earned a very positive reputation for cooperating with international and national authorities in investigating and prosecuting cross-border crime, terrorism, smuggling, human trafficking, money laundering and other threats to national and international security. We are a long-standing and respected member of INTERPOL, and therefore are expected to do the right thing when there is a serious criminal case to answer.

¹ The 19 are Brunei, the Netherlands, Indonesia, Hungary, Kuwait, Austria, the United Kingdom, Ireland, Liechtenstein, France, Japan, New Zealand, Portugal, Spain, the Czech Republic, Switzerland, Malta, Jersey and Malaysia. Agreements awaiting formal signing exist with India, Mexico, the United Arab Emirates and Guernsey. Previous agreements are in force with Belgium, Thailand, the Mainland of China, Luxembourg and Vietnam. The key omissions are the United States, Australia and Germany.

Consultation Questions

a. Should Hong Kong proceed to work on a legal framework for TIEAs?

The question is moot, as the government has already strongly signalled its intention to proceed with legislation allowing independent TIEAs. The circumstances leading up to the consideration of TIEAs for Hong Kong are particularly regrettable in view of the OECD's increasingly extreme demands, which encroach on the SAR's internal taxation policies.

Such misgivings aside, we recognise that there is an inexorable push in the international arena towards a higher degree of tax transparency and that Hong Kong is a minority of one as we have yet to provide statutory backing for TIEAs. We also note that there is the risk of being labelled as an uncooperative jurisdiction, which could be used as a pretext by other jurisdictions to impose sanctions on Hong Kong or apply administrative measures that would have negative implications on our trade and investment activities.

The Chamber therefore does not object to the introduction of legislative amendments for the purpose of enabling TIEAs **on the condition that the safeguards in paragraphs (2) and (3) of our comments to question c. below are adopted** but would like to make the distinction that it is not in favour of entering into negotiations on TIEAs.

b. What are the considerations that we should take into account in choosing CDTA and TIEA partners?

The current fiscal disarray evident in key OECD economies suggests that tax authorities in those countries will redouble their efforts to attract revenue. We are concerned that the current push to require TIEAs among Global Forum members is part of a revenue enhancement campaign. As a precaution, we would wish Hong Kong negotiators to carefully assess the economic conditions of potential treaty partners and consider most favourably those with a track record of solid fiscal discipline. This will help to reduce the prospect for abuse of the information exchange provisions.

We suggest that TIEAs be considered only for tax neutral jurisdictions or those with low taxes and that CDTAs be the default negotiating position in discussions with other jurisdictions in so far as is practical.

c. Do you have any other suggestions on the implementation of the CDTA and TIEA programmes?

Members' key concerns are as follows:

- 1) We already have laws permitting the required information exchanges, but only with jurisdictions willing to enter into CDTAs with us. Independent TIEAs, i.e., those standing apart from any tax agreement, serve only to benefit jurisdictions unwilling to negotiate a CDTA with Hong Kong. As such, we would trade away one of our last bargaining chips useful for obtaining CDTAs, in exchange for protection from the threat of unspecified sanctions.

- 2) Other jurisdictions may have domestic or third party (e.g., intra-EU) legal obligations to share information across agency or jurisdictional boundaries. Although CDTAs and TIEAs may specify that information shared between two treaty partners may not be disclosed to third parties or jurisdictions, we are concerned that these obligations may not be fully and always honoured. We therefore consider adopting a 2-tier protection mechanism incorporating these safeguards as standard legal provisions in the negotiation of TIEAs:
- (a) The Inland Revenue Ordinance should be amended to provide that Hong Kong will only enter into TIEAs with contracting parties that by their laws provide not less legal protection of confidential information and personal data than that of Hong Kong and the Financial Secretary is satisfied that such contracting parties implement such legal protection in practice; and
 - (b) All TIEAs must include the provisions that contracting parties are required to provide no less legal protection of confidential information and personal data than that of Hong Kong, that only the tax administration of the contracting parties will have access to information obtained pursuant to an EoI request and will not disclose such information whether to other agencies or authorities within the same country or to other jurisdictions; and the SAR Government is entitled to renegotiate or terminate the TIEA if the contracting parties fail to comply with the above.

We also suggest that treaties should include a provision on the use of and access to information provided under TIEAs as a privilege that is restricted only to tax authorities.

- 3) There is compelling need to rewrite Hong Kong's tax code for the purpose of aligning this with provisions in the Basic Law and terms of the model TIEA that offer protection on fundamental human rights, which include the right to privacy, the right to legal professional privilege, and the right to access the courts. It is noted that current language in the Inland Revenue Rules on Disclosure of Information, specifically Rule 5(1), Rule 5(3)(b), Rules 6 and 7, do not lend themselves to informed decisions by taxpayers nor do they allow recourse to the courts. We would therefore suggest introducing legislative amendments so that other than situations relating to factually incorrect information, the right to raise objections and/or pursue these in the courts can also be exercised if the information sought is legally privileged; involve trade, business, industrial, commercial or professional secret or trade process; or is not foreseeably relevant. In the interest of consistency, clarity and certainty, we would suggest enshrining in legislation any DIPN issued by the Inland Revenue Department in relation to the conduct of information exchange.

- 4) The provision for tax examinations abroad is particularly lacking in detail. We would wish to have more information on the consequences to Hong Kong taxpayers of *not* agreeing to discuss their financial activities with other tax authorities. Further, we do not fully understand the authority or investigatory powers of such officials when they are on Hong Kong soil, nor the consequences for failure to fully or honestly comply with their demands. Given that the Terms of Reference of the Global Forum Peer Review Group do not regard such a provision as being mandatory, we would advise that the provision for tax examinations abroad should not be included in any TIEA that Hong Kong may enter into.

d. What are the specific concerns for not supporting the legal framework for TIEA?

The threatened sanctions that may be imposed on Hong Kong for failing to comply with the Global Forum TIEA requirement are unspecified. We do not have enough information to weigh the pros and cons, and would wish to know more before giving support to TIEAs.

There is also an ill-understood administrative burden imposed on us when we seek to fulfil the information requirements obligated under existing CDTAs, and we anticipate that this obligation would only increase with the introduction of TIEAs. When the information exchange enhancement provisions were being debated in 2008-09, we were told that only about 100 such requests were made, worldwide, in any given year. According to the information we have received, Hong Kong alone has handled 35-40 such requests since March 2010. Such administrative burden will have to be borne by Hong Kong (which in turn will be borne by the Hong Kong taxpayers) and will impose considerable work and staffing pressure on the IRD. We suggest that the SAR Government consider making it a condition to processing an EoI request that the treaty partner which makes the EoI request share our administrative cost. We appreciate that this may give rise to a reciprocal request. However, as Hong Kong adopts a territorial taxation system, subject to Government's statistics which we have not been provided, we believe that on the whole it should be less likely that Hong Kong will make an EoI request than its treaty partners, and so such reciprocal request may not be imposing undue burden on Hong Kong.

e. Are there any possible ways to address these concerns?

Clearly, the threatened sanctions must be better understood before we go forward. Further, we believe Hong Kong law should specify that strict TIEA safeguards will apply regardless of other treaties or domestic legal requirements in the treaty partners' jurisdictions. Finally, we would strongly require that the current requirement to inform those about whom cross-border tax information is sought of the intent to provide specific information to a foreign jurisdiction be upheld and strengthened. (see C2 above)

Yours sincerely,

Shirley Yuen
CEO

c.c. Revenue Division, Financial Services and the Treasury Bureau (Treasury Branch)