Inland Revenue (Amendment) Bill gazetted

The Inland Revenue (Amendment) Bill 2013 (the Bill) was gazetted on 12 April 2013. The Bill seeks to amend the Inland Revenue Ordinance (the Ordinance) to enable Hong Kong to enter into tax information Exchange agreements (TIEAs) and to enhance the existing exchange of information (EoI) arrangements.

Background

Currently, Hong Kong can only exchange tax information with a jurisdiction in the context of a comprehensive double taxation agreement (CDTA). The question of whether Hong Kong should enter into TIEAs was the subject of an earlier alert - Tax alert - Issue 11, May 2012.

The Global Forum on Transparency and Exchange of Information for Tax Purposes ("The Global Forum") of the Organisation for Economic Cooperation and Development (OECD) recommended in its Phase 1 peer review of Hong Kong that Hong Kong should put in place the legal framework for TIEAs. This reflects its position that a jurisdiction should make available both CDTAs and TIEAs as instruments for Exchange of Information (EoI). Hong Kong is currently undergoing a two-phase peer review by the Global Forum to evaluate its compliance with the international EoI standard.

The question of whether Hong Kong can pass the Phase 2 peer review largely hinges on the availability of a legal framework for TIEAs. The Hong Kong government sees that there is a risk of Hong Kong being labeled an uncooperative jurisdiction, which would be highly undesirable for Hong Kong's international reputation and may undermine Hong Kong's position and competitiveness as an international business and financial centre. There is also the risk that other jurisdictions may impose unilateral sanctions on Hong Kong. Therefore, the Government considers it critical that Hong Kong have in place the legal framework for TIEAs by mid-2013 before the Global Forum finishes its Phase 2 peer review report on Hong Kong in September 2013.

In addition, some of the jurisdictions that Hong Kong has approached, particularly a number of major trading partners of Hong Kong, have yet to be convinced of the case for pursuing a CDTA with Hong Kong and are adopting a wait-and-see attitude. By providing flexibility in the coverage of tax types and modifying in the light of operational requirements the limitation on disclosure for EoI under the CDTA framework, the Government considers that Hong Kong stands a better chance of persuading the key jurisdictions to commence CDTA negotiations.

The Bill

The Government proposal adopts a minimum necessary approach to enhance EoI arrangements under CDTAs so that it complies with the prevailing international EoI standard under TIEAs. This will enable Hong Kong to continue with its efforts to negotiate CDTAs with existing as well as potential partners and provide a legal framework for TIEAs, thereby enabling Hong Kong to meet its international obligations.

Hong Kong's tax system extends to only three direct taxes - profits tax, salaries tax and property tax. For EoI purposes, Hong Kong has sought to restrict the EoI Article in its CDTAs to these direct taxes only. However, some jurisdictions with which Hong Kong has concluded CDTAs raised grave concerns during negotiations on Hong Kong's restrictive position in the coverage of tax types for EoI. The tax systems of most jurisdictions are far more complex than that of Hong Kong with a much wider range of tax types, e.g., value-added tax, inheritance tax, and often different level of taxes such as federal and state taxes. The tax authorities of these jurisdictions would like information from CDTA partners to facilitate their investigation of tax evasion cases concerning income taxes (i.e. those taxes covered by the relevant CDTA) to also be applicable to other tax types.

Comment

As noted in Tax alert - Issue 11, May 2012, Hong Kong runs the risk of being considered an uncooperative jurisdiction if it does not amend its law to allow it to enter into TIEAs with the further risk of sanctions being imposed by other jurisdictions. Equally, however, if Hong Kong does amend its law, there may be little incentive for jurisdictions to enter into a CDTA with Hong Kong when they already have a TIEA in force.

The Government considers that these concerns are outweighed by the need to expand its DTA network with its major trading partners. No doubt, the Bill will be the subject of close scrutiny by the Legislative Council.

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