Enforcement Trends and Compliance Challenges

Judicial Review: A legal challenge, towards better regulatory

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Highlights of presentation

- Quick recap on managing tax compliance
- Concept and application of judicial review in tax matter
- Impact of judicial review on tax enforcement
- Regulatory policy and governance
Managing tax compliance

Tax compliance is an ever-changing landscape ...
Compliance challenges

Key issues for corporation tax compliance
- Transfer pricing issues
- Intra-group transactions
- Financing arrangements
- Tax avoidance issues

International challenges
- International tax avoidance
- Cross-border transactions
- Permanent establishment issues (under tax treaty)
- Abuse of tax treaty benefits
- Hybrid mismatch arrangements
Compliance challenges

- HKSAR being an open economy with substantial trade and investments has a high potential for tax disputes
- Globalization trend, increasing tax disputes in terms of number and complexity
- Aggressive/abusive tax positions and transactions associated with large corporate taxpayers which are represented by sophisticated tax/legal professionals
- Exploiting differences in the tax treatment of instruments, entities or transfer between different tax jurisdictions
Enforcement on tax compliance

- **Risk management**
  - Risk-based approach
  - Taskforces focusing on high-risk sectors/ taxpayers
  - Technical teams for special business sectors
  - IT-assisted tools for better case selection across the compliance spectrum & identification of anomalies

- **Audit strategy**
  - Compliance audit
  - 3-tier audits: desk audit, field audit, in-depth investigation

- **Building up capabilities**
  - Staff training and development
  - Enhanced computer/ statistical tools
  - Expanded intelligence/ databases cross-matching
Managing tax compliance

**Domestic level**
- Enforcement power -
  - wide range of information seeking power under tax law, Inland Revenue Ordinance (IRO)
  - general and specific anti-avoidance provisions
  - penal provisions

**International front**
- International cooperation, enhanced dialogues
- Technical cooperation / sharing of best practices
- Expanded tax treaty network, TIEAs (pending)
- exchange of information
Enforcement on tax compliance

Legal challenges on

- Contravention of civil rights
- Protection of personal privacy
- Impropriety of administrative decisions
- Judicial review
What is judicial review?

- **Judicial review** is a formal mechanism for challenging both administrative actions or judgments of tax authority.
- It enables courts to ensure that the administration’s decisions are:
  - *legal,*
  - all relevant considerations are taken into account and irrelevant considerations ignored,
  - *procedurally fair,* &
  - all relevant interests to be properly addressed & assessed,
  - *rational*
  - avoiding arbitrary and illogical decisions.
Judicial review of a tax matter

- **Theoretical basis of judicial review** under administrative law

- **Constitutional basis of judicial review**
  - Administrative review is part of the Common Law
  - **Article 35 of the Basic Law of HKSAR**, “Hong Kong residents shall have the right to institute legal proceedings in the court against the acts of the executive authorities and their personnel”
Why is judicial review important?

- Judicial review provides an oversight of the tax administration by an independent and free judiciary.
- It is an important means by which the administration can be held accountable and ensures that the administration performs in a lawful manner.
- By ensuring that it exercises those powers given to it under statutes &
- That it exercises those powers fairly and reasonably.
Law and administrative power

Rule of law

- Rules based on elementary concepts of legality, reasonableness and fairness
- Equality before the law
- Rules which restrict discretionary power

All administrative powers must be based on law
- The doctrine of “ultra vires”
Legal principles on judicial review

**Illegality**

- unconstitutional
- ultra vires subsidiary legislation
- improper purposes
- bad faith
- unfettering decision
- acting in excess of power
- error of law
- material error of fact
- irrelevancy
- uncertainty
- inordinate delay
Legal principles on judicial review

- **Irrationality**
  - Wednesbury unreasonableness
  - proportionality
  - margin of appreciation

- **Procedural impropriety**
  - natural justice
  - right against biased decision
  - right to a fair hearing
  - substantive legitimate expectation
  - duty to give reasons
**Decisions – the exercise of discretion**

**Inland Revenue Ordinance, HKSAR Law**

- **Section 59(3)**
  - power to raise an estimated assessment

- **Section 64(1)**
  - Commissioner may extend the time for filing an objection

- **Section 64(2)**
  - Commissioner determines an objection within a reasonable time

- **Section 69(1)**
  - taxpayer may apply to Board of Review to state a case on a question of law

- **Section 71(2)**
  - Commissioner may order tax be held over unconditionally (or conditionally upon purchase of tax reserve certificates or banker’s undertaking) pending objection or appeal
Common grounds raised in notable judicial review cases

- **Validity of the assessment**
  - the assessment is ultra vires

- **Objection and appeal procedures**
  - Commissioner’s refusal to grant an extension of time to lodge an objection
  - Commissioner’s failure to determine objections to the assessments within a specified time
  - challenging the constitutionality of section 69 which requires an appeal from the Board of Review to proceed by way of case stated

- **Payment of tax under objection**
  - Commissioner’s refusal to holdover the tax in dispute unconditionally pending the determination of objection
Statistics of judicial review (JR) applications in recent years

<table>
<thead>
<tr>
<th>JR application – Court of First Instance</th>
<th>2012/13</th>
<th>2011/12</th>
<th>2010/11</th>
<th>2009/10</th>
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<tbody>
<tr>
<td>Application for leave granted</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>4</td>
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<tr>
<td>Application for leave refused</td>
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<td>3</td>
<td>1</td>
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<td>Withdrawn before leave granted</td>
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<td>Withdrawn after leave granted</td>
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<td>Full hearing by Court of First Instance</td>
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<td>Application dismissed</td>
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<td>4</td>
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<tr>
<td>Remedies granted</td>
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<td>Partial remedies granted</td>
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<td>Appeal hearing by Court of Appeal</td>
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<td>Appeal by taxpayer dismissed</td>
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<td>Appeal by Revenue allowed #</td>
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<tr>
<td>Remedies granted</td>
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<td>Appeal hearing by Court of Final Appeal</td>
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<td>Appeal dismissed</td>
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<td>Remedies granted</td>
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### Application of judicial review

**Statistics of judicial review (JR) applications in recent years**

**(by application grounds)**

<table>
<thead>
<tr>
<th>Grounds for Judicial Review</th>
<th>No of application covering the relevant ground</th>
<th>Application dismissed</th>
<th>Remedies granted (order of mandamus)</th>
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</thead>
<tbody>
<tr>
<td>Ultra vires assessments</td>
<td>3</td>
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<td>Refusal to allow late objection</td>
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<td>Refusal to allow unconditional holdover of tax pending objection</td>
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<td>Requesting the issue of determination</td>
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<td>Challenging the appeal mechanism</td>
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For the period 2009 to 2013
Role of court in judicial review

Seeking a judicial review

- **NOT** a correct forum for determining the substantive issues or resolving the disputes relating to the bases of assessment
- a more appropriate means of addressing a public officer’s exercise of his statutory powers or duties on administrative law
- deals with public law: not every decision by a decision maker is amenable to judicial review
Remedies

Most common relief for successful application

- **An order of certiorari**
  - By which the decision impugned be quashed
  - No such order was given in all the judicial review applications in the past six years

- **An order of mandamus**
  - To enforce the exercise of statutory duties or discretion in accordance with the law
  - An order of mandamus was granted to two judicial review applications in the past six years

- **Allow damages**
  - No such relief was granted in all the judicial review applications in the past six years
Growing trend of judicial review application has changed the compliance landscape

Effect on compliance management process

- Taxpayers start judicial review proceedings rather than trying to resolve the matter in other cheaper and quicker ways
- May create the incentives for proceeding shopping or for frivolous and vexatious appeals by those affected by regulatory decisions
- Reduces regulatory certainty, not conducive to the approach of timeliness in compliance management process
Impact on enforcing compliance

- **Resources implications**
  - Unnecessarily ties up the resources of tax administration
  - Higher administrative costs
  - Requires special resources and expertise
  - Needs to respond in faster timescales
  - Cost implication on the taxpayers as well
Improves the justice
- Courts have a legitimate role to play in ensuring that the administration acts in accordance with the rule of law
- Taxpayers have a real and adequate opportunity to challenge the administration’s decisions before independent courts
- The availability of judicial review by itself improves confidence

Improves the quality of the decisions themselves
- Judicial review is an important instrument of quality control
- Good administration requires decision-makers to have proper regard both to all relevant legal considerations and to the interests of the taxpaying public which they serve

Gets in the way of efficient decision-making
- The tax administration is doing its best to make decisions and get things done efficiently
Internal complaints systems

- The relative speed and the modest costs
- Not independent, may be biased, whether internal systems are imbued with the value necessary to promote justice

Recourse to Ombudsman

- Independent of the tax administration against which a compliant is made
- Free service to the aggrieved person, operating using investigation techniques
- Have a role in promoting principles and standards of good administration

Mediation

- Emerging trend in resolving disputes beyond judicial review
Effective implementation, compliance and enforcement of tax law are essential for meeting tax policy objectives ...
Policy implications on regulatory process

- Exercise its authority only within the scope permitted by its legal powers
  - proper delegation of authorities under tax law (IRO)
- Treat like cases consistently and in a like manner
  - Issue of Departmental Interpretation and Practice Notes
  - Internal assessing guidelines, procedure handbooks & etc
- Require justifiable reasons for decisions and for any departure from normal regular practices
  - Department of Justice – issue Guide to Judicial Review “JOYS”
  - Notifying taxpayers the decisions, giving reasons
- Prevent abuse of discretionary authority
  - has effective objection and appeals processes under tax law (IRO)
- Preserve the integrity of the regulatory system
  - has internal complaint system, ombudsman
Regulatory policy and governance

Judicial review and good governance

- Public participation
- Justice and fairness
- Transparency
- Accountability
- Proportionality
Fundamental to good governance that public powers be exercised within legal limits and with fairness

- the tax administration’s commitments to openness, transparency, fairness
- the tax administration applies and enforces regulations systematically and fairly

Mission statements and Values

Taxpayers’ right (Taxpayer’s charter)

- access to administrative and judicial review procedures for disputes relating to rules/ laws that bind them as well as
- timely decisions on appeal
Thank you