

TO: Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA

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Comments on the OECD Public Discussion Draft *BEPS Action 6 Discussion Draft on Non-CIV examples* against the background of the general situation of investment funds after the implementation of BEPS Action 6

Dear Sirs,

I. INTRODUCTION AND BACKGROUND

EFAMA¹ is grateful for the opportunity to comment¹ on the new OECD Public Discussion Draft on BEPS Action 6 and the treaty entitlement of non-CIV funds *Discussion Draft on non-CIV examples*. In addition EFAMA would like to make positive use of this opportunity and comment as well on the general situation of CIVs as well as of Non-CIVs against the background of the BEPS Action 6 implementation.

The paper at hand sets the views and concerns of the European investment management industry with regards to the impact of OECD BEPS Action 6 on this industry. Below we made some general comments before responding to the OECD Public Discussion Draft.

¹ EFAMA is the representative association for the European investment management industry. EFAMA represents through its 28 member associations and 61 corporate members EUR 21 trillion in assets under management of which EUR 12.6 trillion managed by 56,000 investment funds at end 2015. Just over 30,000 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 25,900 funds composed of AIFs (Alternative Investment Funds). For more information about EFAMA, please visit www.efama.org

II. GENERAL REMARKS

EFAMA fully supports the aim of BEPS Action 6 to prevent treaty abuse by preventing the granting of treaty benefits in inappropriate cases and by avoiding double non-taxation. However, EFAMA is of the opinion that the lack of specific clarifications for investment funds may have significant unintended consequences for investor outcomes.

EFAMA already commented on the OECD Public Discussion Draft dated 24 March 2016 as to how the new provisions included in the Report on Action 6 could affect the treaty-entitlement of non-CIVs.

In this context EFAMA recommended to limit the definition of Non-CIVs (and extend the definition of CIVs accordingly). Regulated investment vehicles that are sold to the public or that are open-ended and capable of having an unlimited number of investors should qualify as CIVs, irrespective of the legal form and the kind of assets the vehicle is invested in.

The 2010 CIV Report defines CIVS as investment funds that are widely held, hold a diversified portfolio of securities and are subject to investor protection regulation in the country in which they are established.

EFAMA understands that the new public discussion draft dated 06 January 2017 is still referring to this definition.

As no further definitions regarding “widely held “or “diversified” are provided in this context EFAMA has concerns that this is another source of legal uncertainty. The fact that the examples that have been received by the OECD in response to the March 2016 discussion draft were “either too long, too specific or too controversial for inclusion in the Commentary on the PPT rule” may partially reflect this uncertainty.

The economies of scale from investments held through investment funds give access to markets, appropriately diversified, in which investors would otherwise not be able to invest. In case small investors had to invest directly, they would incur substantial time and costs, not to mention the lack of market diversification. In the current investment climate it is imperative that investors are able to diversify risks across investments and international markets.

Governments have long recognized the importance of investment funds as an important complement to other savings vehicles. In many countries, participants, through defined contribution retirement plans, invest primarily in investment funds. With ageing populations in many countries they will become increasingly important and their relevance cannot be overstated. Investment funds allow small investors to gain benefits of economies of scale even if they have relatively little invested.

It is therefore important that investment funds can operate under tax laws that give them greater certainty as to the tax impact at investment level, be it withholding tax or capital gains tax so that investors can manage their savings more effectively.

The text of the *Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting* which has been released by the OECD on 24 November 2016 leaves very great discretion to tax authorities in acting bilaterally which leads again to a situation of uncertainty regarding whether treaty relief will be provided.

As parts of the Multilateral Convention are just reflecting the text of BEPS Action 6, EFAMA would strongly recommend to produce further guidance on the interaction between BEPS Action 6 and investment funds (CIVs as well as Non-CIVs) to improve this situation of uncertainty for investment funds.

III. LoB and PPT

EFAMA understands that the OECD is providing three alternative rules to address situations of treaty abuse:

1. General Anti-Abuse rule based on the PPT
2. Simplified LoB
3. Detailed LoB

EFAMA is of the opinion that a wider adoption of a LoB approach to prevent abusive strategies would mean more cases where the lack of data about underlying beneficial owners is problematic, resulting in most investment funds operating on a cross-border basis being deprived from treaty benefits. The

OECD already took a specific look at the situation for CIVs in 2010 (see the OECD report “The granting of treaty benefits with respect to the Income of Collective Investment Vehicles” dated 23 April 2010). EFAMA would welcome an additional examination of the situation of non-CIVs with regard to the implementation of a LoB clause.

Due to the typically insurmountable practical difficulties for investment funds caused by the LoB, EFAMA welcomes that the Multilateral Convention is implementing a PPT in the first place and just offering the LoB variations as possible alternatives. In addition EFAMA welcomes that most countries seem to be in favour of a PPT. Nevertheless, with respect to the special nature of investment funds and the subjective character of the PPT EFAMA would strongly ask for further guidance in the form of an additional OECD commentary.

CIVs as well as Non-CIVs operate under different tax regimes around the world with the intention that investors are not impacted by an unnecessary additional taxation at fund level. Divergence in the interpretation of a PPT by different tax administrations can reinforce and create further uncertainty on the ability of investment funds to meet treaty qualification.

Regulated investment vehicles that are sold to the public or that are open-ended and capable of having an unlimited number of investors represent a low risk of being used for treaty shopping purposes. First, an unlimited number of investors can subscribe and redeem their fund units freely. This limits the capacity of a single investor to control the vehicle for treaty shopping purposes. Second, they must fulfil risk spreading requirements, i.e. cannot be used to hold a certain position in order to benefit from a specific treaty relief on investments. Due to the rather small number of shares invested in these regulated investment vehicles, that are sold to the public or that are open-ended and capable of having an unlimited number of investors, they should normally not be able to exert any influence on the companies in which they invest. In addition, investors in these funds are also not able to influence any treaty shopping politics of those funds.

EFAMA would be grateful for additional guidance regarding the interaction between the PPT and CIVs as well as Non-CIVs. Example D on pages 72-73 of the BEPS Action 6 2014 Deliverable provides an

example to illustrate the application of the PPT on CIVs. However, this example assumes that the majority of the investors are resident in the CIV's country of residence and in addition that the CIV RCo distributes almost all of his income on an annual basis to its investors and pays taxes in its residence country on the remaining accumulated income. Due to these specifications the example ignores the biggest part of practical application scenarios. This illustrates that a lot of uncertainty remains, even for CIVs.

IV. BEPS Action 6 – Discussion Draft on Non-CIV examples

With regard to the examples that have been provided in relation to Non-CIVs EFAMA would ask for an additional clarification saying that the three examples are only illustrative and do not target all situations. EFAMA feels that the greater part of the practical application scenarios is not covered. As a result the examples leave wide discretion to the rather subjective judgment of tax administrations and non-CIVs remain in a situation where they are not able to operate under tax laws that give them any certainty.

We also feel example 2 and 3 are confusing. After reading example 3 it would be our understanding that the treaty benefits are not denied to RCo because the decision to locate RCo in State R has mainly been taken for other reasons than just taxation benefits. However, example 3 underlines that RCo does not obtain treaty benefits that are better than the benefits to which its investors would have been entitled if they had made the same investments directly in these states. This example would be therefore clearer and less confusing if the treaty benefits RCo finally obtains were higher than those obtainable under the treaty with state C. In EFAMA's view it would already be helpful to delete the last sentence of example 3 "*RCo, however, does not obtain treaty benefits that are better than the benefits to which its investors would have been entitled if they had made the same investments directly in these States and had obtained treaty benefits under the treaties concluded by their States of residence.*" to avoid any confusion.

In addition, EFAMA notices that the examples do not respond to the following scenario which is very common for investment funds: Cases where the fund manager is economically distinct from the Non-

CIV itself. The related uncertainty even grows where the investment management is delegated cross-border.

EFAMA would highly appreciate further specifications in this regard.

V. CONCLUSION

EFAMA appreciates the very hard work of the OECD in relation to Base Erosion and Profit Shifting and EFAMA is aware of the complexity in relation to CIV / Non-CIV issues. We would like to call for continued vigilance on the part of the OECD so that the practical implementation by tax authorities does not lead to real impact on investment flows. In addition we would ask for an additional OECD Commentary document in due course on all the open questions in relation to the applicability of BEPS Action 6 on CIVs and Non-CIVs. EFAMA, as the representative association for the European investment management industry would like the ability to meet with members of Working Party 1 to present case studies and clarify the points being made here. In addition we would be happy to assist with any kind of further advice.

We are grateful in advance for your attention to the concerns expressed in this letter and we welcome the opportunity to discuss these with you. In case there is any additional information that we can provide, please contact EFAMA at info@efama.org or [+32 \(0\) 2 513 39 69](tel:+3225133969).

Yours sincerely,

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Director General