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Paris, June 17, 2015

Dear Mrs de Ruiter,

The Association Française de la Gestion financière (AFG) is grateful for the opportunity to answer to the OECD’s consultation on the revised discussion draft on BEPS action 6 : Prevent treaty abuse.

Our comments are limited to CIV and non-CIV funds.

We would like to reiterate our support to the conclusions of the 2010 CIV Report.

Moreover, we consider that the Report should be more conclusive and provide with more pragmatic approaches and concrete examples:

- Countries should be encouraged to consider a regulated widely held fund as a resident of the State in which it is constituted,

- Should a country wish to introduce a clause relating to the residence of beneficiaries, OECD should recommend administrative flexibility. AFG calls for pragmatic approaches: in many countries of continental Europe, fund’s shares/units are not kept on a register held by the fund but through financial institutions. Therefore, the fund does not know the identity of its investors. However, funds are regulated i.e.

1 AFG represents the France-based investment management industry, both for collective and discretionary individual portfolio managements. The 600 AFG members manage 3,000 billion euros, making the Paris fund industry a leader in Europe for the financial management of collective investments (with 1,500 billion euros managed from France, i.e. 19% of all EU assets managed in the form of investment funds). In the field of collective investment, our industry includes – beside UCITS – the whole range of AIFs, such as : employee savings schemes, regulated hedge funds/funds of hedge funds, private equity funds, real estate funds and socially responsible investment funds. AFG is an active member of the European Fund and Asset Management Association (EFAMA) and of PensionsEurope. AFG is also an active member of the International Investment Funds Association (IIFA).
have to obtain authorization from a Financial market regulator for creation and distribution. Therefore, it should be permitted to consider that the countries where the fund has been authorized to be marketed are taken as the countries of residence of the investors.

- These two options should be added to paragraph 2 f).

Sincerely,

Pierre Bollon

Delphine Charles-Péronne
18 June 2015

By email to: taxtreaties@oecd.org

Marlies de Ruiter
Head, Tax Treaties
Transfer Pricing and Financial Transactions Division
OECD/CTPA

Dear Marlies,

**BEPS action 6: Prevent treaty abuse**

**General comments**

AFME¹ and the BBA² welcome the opportunity to respond to the OECD’s discussion draft entitled: "BEPS action 6: Prevent treaty abuse” published on 22 May 2015. We wish to make clear that while AFME and the BBA have separate and distinct memberships, for the purposes of the OECD discussion draft, both organisations have decided to submit a single, combined response since our respective members share the same concerns with respect to the proposals in the discussion draft.

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¹ The Association for Financial Markets in Europe (AFME) represents a broad range of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks and other financial institutions. AFME advocates stable, competitive and sustainable European financial markets, which support economic growth and benefit society.

² The BBA is the leading trade association for the UK banking sector with more than 230 member banks headquartered in over 50 countries with operations in 180 jurisdictions worldwide. Our associate membership includes over 80 of the world’s leading financial and professional services organisations.
The relatively short time available to consider the discussion draft poses a challenge for all businesses and the OECD secretariat. Should it be of assistance we would be pleased to meet with the OECD Secretariat to discuss these matters in greater detail or provide further information upon request.

**Process for implementation**

The key objective of double taxation agreements (DTAs) is the promotion of growth and international trade. As noted in our letter to the OECD on 9 January 2015, DTAs require rules that provide certainty to taxpayers and tax authorities. As a general point, we believe that the final recommendations from the OECD should be appropriately targeted and as clear as possible in order that taxpayers may access treaty benefits in respect of genuine commercial and investment transactions.

The discussion draft indicates that governments are as yet unable to reach agreement on several outstanding issues. We are concerned that this could result in differences in the implementation of the OECD’s final recommendations across jurisdictions which could create uncertainty for investors and tax authorities.

**Timetable for implementation**

We note that discussions on several outstanding issues are still to take place at the OECD in June 2015. Given that the OECD does not intend to have a further round of consultation, it is disappointing that there will be no opportunity to comment on the outcome of the June 2015 discussions before the final recommendations are published in September 2015.

Furthermore, we expect that discussions regarding the process for implementation will continue beyond September 2015. Until agreement is reached, we are concerned that governments could introduce different approaches to validation and the processing of cross-border tax relief claims. We hope that the OECD will encourage governments to reach agreement on the implementation of the recommendations at the earliest opportunity.

**Application of the LOB and treaty entitlement for collective investment vehicles (CIVs)**

We note that Paragraph 14 states that “since there was general support for the conclusions of the 2010 CIV Report concerning the treaty entitlement of CIVs and since subparagraph 2 f) of the LOB rule dealt with the application of the LOB to CIVs in a way that reflected the conclusions of the 2010 CIV Report, there was no need for additional changes to the Report on Action 6 in order to address these issues.” In order to give certainty to investors, we believe that it is important that the OECD develops further guidance on the procedural requirements for the application of the LOB to CIVs.
We note that Paragraph 14 states that "It was also agreed, however, that the implementation of the recommendations of the TRACE project was important for the practical application of these conclusions." Whilst we welcome that the OECD has acknowledged the importance of implementing the recommendations of the TRACE project, we believe that governments should now provide a clear commitment to implementing the recommendations and set out clear steps with an agreed timetable for doing so. Without this, there is a risk that the procedural requirements for treaty claims may vary across jurisdictions.

**Application of the LOB and treaty entitlement for non-CIVs**

*General comments*

We welcome the statement in Paragraph 22 that “as regards the broader question of treaty entitlement of non-CIV funds, the Working Party recognised the economic importance of these funds and the need to ensure that treaty benefits be granted where appropriate.” We note in Paragraph 24 that the OECD intends to continue exploring solutions to the issues related to the treaty entitlement of non-CIV funds. In particular we note that the OECD is still considering a specific provision on non-CIVs in the LOB rule and adding one or more examples on non-CIVs to the commentary on the PPT rule. We would encourage the OECD to follow through with these suggestions.

We note that the process of claiming treaty relief for non-CIVs under the LOB and PPT rules is likely to be complex. It is important that this does not impact the availability of treaty relief where appropriate. In that regard, we would encourage the OECD to consult further with businesses and other relevant stakeholders at the earliest opportunity.

*Securitisation SPVs*

An important area of concern is the access to treaty benefits - in particular due to the impact of an LOB rule - by securitisation companies and other special purpose vehicles used for repackaging various securities and other receivables (together “securitisation SPVs”). Securitisation SPVs play an important role in financial markets, and carry out activities such as acquiring debt securities, mortgages, or other receivables and issuing securities whose return is linked in some way to the underlying instruments. We would note that securitisation SPVs may not readily be able to identify the tax residence of the (possibly many) owners of the securities which they have issued (those securities might themselves be listed, and/or traded, and/or held within a clearing system). Such arrangements are typically used for commercial reasons, other than tax, and the obtaining of treaty benefits should therefore be compatible with the PPT. We believe that it should be made clear that the LOB rule should not deny treaty relief in such cases. As a fall back, in
such cases it would be helpful if it could be indicated that discretionary relief is likely to be available.

**Pension funds**

We welcome the confirmation provided in Paragraph 21 that a pension fund should be considered to be a resident of the state in which it is constituted regardless of whether it benefits from a limited or complete exemption from taxation in that state. We welcome that changes will be made to the OECD MTC to reflect that position.

However, we note that this may be at odds with the recommendations in Paragraphs 33 onwards regarding alternative LOB provisions for EU countries. In particular, these provisions introduce a new derivative benefits ‘safe harbour’ for pension funds provided that more than 90% of its beneficial interests are owned by individuals who are residents of the fund’s state or any other state with a comprehensive treaty with the source state. We believe that without a clear and workable procedure it would be extremely challenging to determine whether a pension fund meets the 90% test.

**Intermediate owners**

Paragraphs 41 to 46 set out the residence requirements for ‘intermediate owners’ for the purposes of the ‘publicly-traded test’ and the ‘derivative benefits test’. However, we believe that the residence of the ultimate parent entity should be more relevant than the residence of an intermediate owner. We believe that the approach suggested by the OECD could result in ineligibility for treaty benefits where in fact no treaty shopping is present.

**Discretionary relief provision of the LOB rule**

We welcome the proposals set out in Paragraphs 31 and 32 in relation to discretionary relief. However, in Paragraph 32 of the discussion draft, we note that the proposed new Paragraph 65 of the commentary relating to the LOB rule states that “the paragraph grants broad discretion to the competent authority and, as long as the competent authority has exercised that discretion in accordance with the requirements of the paragraph, it cannot be considered that the decision of the competent authority is an action that results in taxation not in accordance with the provisions of the Convention (see paragraph 1 of Article 25).” We believe that the OECD should introduce an appeals process against the decision of a competent authority.
Derivatives benefits provision and special tax regimes

In relation to the derivative benefits provision, we note that Paragraph 50 sets out two proposals concerning possible changes to the OECD model that would deal with ‘special tax regimes’.

General comments

We are concerned about the short timeframe within which the OECD is expected to discuss and finalise the derivatives benefits provision. We believe that it is important that the drafting for any “special tax regime” is considered alongside the OECD’s work under action item 5 (countering harmful tax practices more effectively) to avoid any duplication of efforts.

It would appear that the ‘special tax regime’ could be applied to deny treaty relief to taxpayers who would otherwise qualify for relief under the LOB rule. We should be grateful if the OECD could provide clear guidance on how the draft provisions for a ‘special tax regime’ might interact with other parts of the LOB rule.

Proposal 1 for a ‘special tax regime’

Under proposal 1 (new treaty provisions on “special tax regimes”), we note the new definition of a “special tax regime” to be included in Article 3 (General Definitions). We have the following specific comments.

• It would be helpful to have further guidance on what is meant by a “preferential effective rate of taxation”. For example, what rates does the OECD have in mind and how is the comparative analysis to be made?

• The current drafting of Paragraph X suggests that the general trading expenses of a company could be treated as benefiting from a special tax regime. It would be helpful if the OECD could clarify that this is not the case.

• Under Paragraph X(ii), “financing income, that satisfies a substantial activity requirement” could not fall within one of the exceptions. We should be grateful if the OECD would provide further guidance on what is to be covered under Paragraph X(ii).

• Under Paragraph X(vi), the “special tax regime” would not apply to “persons substantially all of the activity of which is to provide or administer pension or retirement benefits”. It would be helpful to have further guidance on what is to be covered under Paragraph X(vi).
• Under Paragraph X(viii) we note that the “special tax regime” would not apply where “Contracting States have agreed [that legislation, a regulation or administrative practice] shall not constitute a special tax regime because it does not result in a low effective rate of taxation”. It is not clear what the OECD envisages should be covered under this provision and why such an agreement would be necessary where there is no “low effective rate of taxation”.

**Permanent establishments (PEs) located in third states**

We note from Paragraph 107 that the OECD is still considering amendments to the draft rule which would disallow treaty benefits to PEs in circumstances where the effective rate of tax in the jurisdiction of a branch is less than 60% of the general rate of corporation tax in the home country.

We wish to reiterate the concerns which we raised in the AFME/BBA letter of 9 January 2015 that, where the exemption for banking, insurance and securities dealing would not apply, the wording of the “60% rule” introduces an unwarranted restriction to doing business from branches whose home country tax rate is ‘high’. For example, we do not believe that the activities of UK branches should necessarily be considered abusive if their home country has a nominal tax rate above 33.3% even though they are paying the same 20% tax rate as UK companies. In addition, we do not believe that a branch should lose treaty benefits if its effective rate of tax is low because it makes a loss in a particular year.

We believe that the appropriate test needs to be between effective rates in the branch country and what would have been paid in the home country (if the branch income were taxable) or between nominal rates, but not between the effective rate in the branch country and a nominal rate in the home country.

We note the summary of the OECD’s discussions set out in Paragraph 106. We believe that the “60% rule” should be revised to focus on the targeted abuse where there has been a transfer of income producing assets in order to qualify for a treaty exemption that provides double non-taxation. If the current approach is retained, we believe that the OECD should consider whether the 60% threshold for the purposes of the “60% rule” should in fact be much lower (e.g. 25%).

**Simplified LOB rule**

We understand that the simplified LOB rule is intended to be used by those states which wish to adopt both the PPT and an LOB rule in their treaties. However, if an arrangement is compatible with the PPT (i.e. the PPT does not deny treaty benefits in that case), it is difficult to see why treaty benefits should nonetheless be denied due to the ownership of a party to the arrangement.
We are grateful for the opportunity to share our comments with the OECD on the discussion draft. We would be happy to discuss any of the above in greater detail with the OECD and would be pleased to contribute further as the OECD’s work develops.

Yours sincerely,

Richard Middleton
Managing Director
Tax and Accounting Policy
AFME

Sarah Wulff-Cochrane
Director of Policy
Taxation
BBA
Dear Sirs

OECD revised discussion draft 22 May 2015
BEPS Action 6: Preventing the granting of treaty benefits in inappropriate circumstances

The Alternative Investment Management Association\(^1\) responded to the initial OECD discussion draft on BEPS Action 6 which preceded the Report (3 April 2014) and to the follow-up work set out in the last discussion draft (21 November 2014), and now wishes to comment on the revised discussion draft released on 22 May 2015.

In our 3 April 2014 letter we stated:

AIMA is concerned that the measures proposed to be introduced into the OECD Model Tax Convention concerning entitlement to benefits will, if adopted in their present form, have significant effects on the ability of collective investment schemes in general (and not limited to those in the alternative investment sector which AIMA represents) to obtain the benefit of double tax treaties. The part of the new Article proposed in the discussion draft which is concerned with limitation of benefits broadly requires a fund that wishes to claim treaty benefits to have a significant connection with the country in which it is resident for tax purposes, be it an effective listing or a majority of investors there. Many funds are not listed and pool capital from investors across a number of countries and so will not pass such a limitation of benefits threshold. The “derivative benefits” provision considered in the discussion draft is too narrowly drawn to be of assistance.

We repeated the point in our 9 January 2015 letter:

We, like other respondents, requested the OECD to consider further the application of the measures to collective investment schemes. We welcome the decision to carry out more work on this aspect. However, we are concerned that some of the issues identified in the 21 November 2014 discussion draft for further work focus only on the details of the limitation on benefits (LOB) rule and the principal purposes test (PPT) whereas the difficulties caused for collective investment schemes are more fundamental and arise from the formulation of the LOB and PPT.

We consider that the 22 May 2015 revised discussion draft has not entirely addressed our concern regarding the treaty entitlement of collective investment schemes, both CIVs and non-CIVs. We believe that this will remain a concern for other respondents also. In principle, we agree that a ‘simplified version’ of an LOB could bring more certainty on its interpretation and practical implementation, so that different jurisdictions and tax authorities will apply the agreed framework more consistently. AIMA is very keen to participate in any work that the OECD initiates on this, should any working group be set up to develop rules related to non-CIVs after the final report is delivered in September 2015. AIMA welcomes the willingness of the OECD to continue stakeholder engagement but considers that the position of the alternative investment fund industry is inadequately taken into account.

\(^1\) AIMA is the trade body for the hedge fund industry globally; our membership represents all constituencies within the sector – including hedge fund managers, funds of hedge fund managers, prime brokers, fund administrators, accountants and lawyers. Our membership comprises over 1,300 corporate bodies in over 50 countries.
As we (and others) have noted before, collective investment schemes exist to receive investment monies from a range of investors and to deploy that capital in order to generate investment returns. They are not designed or promoted as vehicles for tax avoidance. Many investors (and increasingly the majority) are not liable to tax, being pension funds, sovereign wealth entities, not for profit organisations, charities and other entities that would be entitled to treaty benefits in their own right if they invested directly in the underlying investments. Accordingly, “double non-taxation” is not an aim of such collective investment schemes but rather to achieve tax neutrality as far as possible for a diverse investor base. The principle of tax neutrality, which has been acknowledged by the OECD in the 2010 CIV report is that the tax regime should not influence investors’ choices between investing directly or through a collective investment scheme in the same underlying investments.

Collective investment schemes, whether CIVs or non-CIVs, are established for commercial purposes. They provide access to various investment strategies, for a diversity of portfolio investors in an efficient and cost-effective manner. When compared to direct investment, investment funds offer professional management of investors’ monies, greater reliance on economies of scale, and a higher degree of risk-spreading. EU regulation (i.e. the UCITS Directives) is a notable example of a legal framework aimed at enhancing the cross-border capacity of collective investment schemes, while protecting retail investors, as laid down in the COM(2005)314 green paper.

Schweppes interest and meet the proportionality test (arrangements, set up for non-tax purposes (see next footnote)). Even if a particular collective investment scheme structure were to be
context, those would include for instance ‘balanced allocation of taxing rights’ or ‘preventing wholly artificial arrangements’ (i.e. (and equally the more abusive the structure, the less likely a fundamental freedom will be triggered). But two non-tax related cases

In the particular case of non-CIV funds, AIMA acknowledges two concerns that the 22 May 2015 revised discussion draft identifies governments to be raising at Working Party 1 but believes these are misplaced:

- **Whether non-CIVs are used to provide treaty benefits to investors that are not themselves entitled to them.** As we have argued above, tax is not the first consideration when establishing any type of collective investment scheme, and that is as much the case for alternative investment funds or other non-CIVs as it is for CIVs. While protecting the tax base is a legitimate policy concern, governments should recognize that the practical operation of capital markets through the efficient pooling of capital, local law requirements, the regulatory framework, market practices and administrative burdens do not permit the creation of alternative investment fund vehicles that would perfectly segregate different types of investors and different types of investments in different jurisdictions. Some thresholds or proportionate benefits should be identified to balance such concerns against the practical difficulties and unfair treatment that would result for the majority of investors;

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2 See e.g., Preqin industry research at https://www.preqin.com/docs/reports/preqin_global_investor_report_hedge_funds.pdf
3 The granting of treaty benefits with respect to the income of collective investment vehicles, 2010 OECD
4 The revised discussion draft notes the work done in the context of hybrid mismatch arrangements (action 2) and the tax treatment of fiscally transparent entities, but the proposed rules lack express reference to the concept of tax neutrality, which is key for collective investment schemes.
5 Commission staff working paper, annex to the “Green paper on the enhancement of the EU framework for investment funds”, COM(2005)314
6 Given the CJEU rulings that directly relate to investment funds, the OECD should evaluate comprehensively the interaction of the proposed double tax treaty framework with EU law and its fundamental freedoms. In principle, the more economic substance there is to an intermediary entity, the more likely that the creation of the establishment itself will be prima facie covered by the freedom of establishment (and equally the more abusive the structure, the less likely a fundamental freedom will be triggered). But two non-tax related cases (Centros/Überseering) dealing with corporate forum-shopping show that just because secondary establishments lacked economic substance and were set up to circumvent company law requirements, did not necessarily mean that the freedom of establishment was withdrawn. EU jurisprudence has laid down a number of justifications which must be satisfied in order to restrict a fundamental freedom. In the tax law context, those would include for instance ‘balanced allocation of taxing rights’ or ‘preventing wholly artificial arrangements’ (i.e. Cadbury Schweppes case). Collective investment scheme structures cannot be assessed as wholly artificial, but rather they are commercial arrangements, set up for non-tax purposes (see next footnote). Even if a particular collective investment scheme structure were to be deemed wholly artificial, the restriction of a fundamental freedom would have to be justified by imperative requirements in the general interest and meet the proportionality test (Gebhard case).
7 As the OECD has often acknowledged, bona fide commercial structures should not be considered as enabling treaty shopping. The structures used for collective investment schemes are legitimate arrangements. There is a risk that some of the current proposals will undermine tax treaty networks that States have spent decades putting together to facilitate international trade and promote economic growth, and which reflect widespread practices and reasonable business organisations. Rethinking treaty-shopping lessons for the EU (Reuven S. Avi-Yonah and Christiana HJI Panayi, 2010) analyses some of the theoretical objections to treaty shopping (i.e. lack of reciprocity, revenue loss or the
• **Whether investors in alternative funds may defer recognition of income on which treaty benefits have been granted.** As we have argued above, many, if not the majority, of investors in non-CIV funds, including alternative investment funds, are tax exempt so that deferral of recognition of income and capital gains offers no tax advantage. In any event, many funds - especially those investing in private equity, real estate and infrastructure - are structured to pass all cashflows out to investors as quickly as possible. Further, where investors are taxable, domestic tax law requirements often force current recognition of income and gains either through advantaging the use of tax transparent fund vehicles or under anti-deferral regimes such as controlled foreign company rules and offshore fund regimes (e.g. US passive foreign investment company rules or UK reporting fund rules) which deem recognition and/or penalise deferral.

The alternative asset management industry plays an important role in the capital market as investors\(^8\) and liquidity providers as well as stewards of companies and projects that result in better allocation of resources and higher economic growth rates\(^9\). The EU has acknowledged the role that investment funds play in the economy and their importance in the capital markets union (CMU) which the EU sees as its priority to complete, with the aims of enhancing financial markets integration, improving the means of financing businesses (and its sources) and making markets work more effectively and efficiently\(^{10}\). AIMA has recently produced a paper on the role of alternative asset managers in the non-bank lending environment\(^{11}\). The study demonstrates the important role that credit funds are assuming as providers of finance, as capital requirements on banks have led to a reduction in their capital markets participation. The paper has also demonstrated that non-bank lending can greatly mitigate the systemic risk associated with direct lending by banks, because of the nature of the investors and funds.

Given, therefore, that treaty access should generally be available to collective investment schemes, the process for obtaining relief must be made as clear as possible, and should be consistent and straightforward to determine. AIMA considers that these considerations are relevant:

• **Tax relief should not depend upon funds being able to ascertain their status on a daily basis, since, as subscriptions and redemptions at net asset value must generally be freely permitted on stated dealing days, collective investment schemes have a body of investors that may continually change. The attributes of investors, including their tax residence status and other information required for the LOB, will be subject to frequent change. Even with the evolving requirements of anti-money laundering legislation and tax reporting regimes, not all such information may be available. For instance, where an investor is a fund of funds, the investee collective investment scheme may not have or be entitled to obtain information on the persons investing in the fund of funds. Similarly, where a financial institution invests in a collective investment scheme on behalf of its own clients (i.e. nominee accounts) or for the purposes of structured investments which it sells to its own clients, or where interests in the collective investment scheme are sold through a fund platform, the collective investment scheme may have no knowledge of the ultimate investors\(^{12}\).**

• **The work carried out in the 2010 CIV report and under the Tax Relief and Compliance Enhancement (TRACE) project should be further developed, and the practicalities of the proposals assessed. Other projects which principle of economic allegiance) and disproves the connection between those and alleged treaty shopping, concluding that those objections are somewhat removed from reality.**

\(^5\) The OECD has recognised the economic importance of investment funds in its last revised discussion draft on BEPS 6.

\(^9\) AIMA has commissioned a broad-based academic study (Capital Markets and economic growth: Long-term trends and policy changes (Christoph Kaserer, Marc Steffen Rapp - March 2014), which explores the link between financial market development and economic growth. Capital markets play a crucial role in the financial sector, and a direct relationship can be traced between an equity market’s size and its liquidity.

\(^{10}\) Parallel to the EU proposals for a capital markets union, the OECD has recently released the updated Policy Framework for Investment 2015: “However, public policies aimed at promoting SMEs should be focused, aimed at making markets work efficiently and sustainably, and at providing incentives for the private sector to assume an active role in SME finance ... Institutional investors are increasingly looked upon as alternative sources of long-term financing, in particular in light of the tightening liquidity and capital constraints being placed on the banking sector. The government can play a supporting role in developing the institutional investor sector, which can in turn contribute to growth and development of private capital markets”. These quotations relate to the non-bank lending space that is increasingly being filled by alternative funds as we set out in our recent research paper (see next footnote). Therefore, adding complexities to their cross-border operations would only reduce the role of collective investment schemes as private credit vehicles and liquidity providers. On the broader picture we also believe that some of the proposals need to be reconsidered if the OECD is not to discourage cross-border investment as some of the recommendations will lead to less balanced geographical allocation of investments by collective investment schemes which will be detrimental for both governments and investors.

\(^{11}\) Financing the economy - the role of alternative asset managers in the non-bank lending environment (AIMA research, 2015)

\(^{12}\) As an example of the complexities that the BEPS 6 proposals would generate in practice, see special purpose vehicles (SPVs), collateralised loan obligations and the securitisations market. The entities involved are owned by multiple investors, have very little access to determine the ultimate beneficial owners of securities or cleared notes issued, and therefore it is not feasible to determine the final noteholders (source: Clifford Chance Client briefing 26 May 2015: BEPS Action 6 - Revised discussion draft on treaty abuse: What do the latest proposals mean for securitisations and SPVs?).
seek to improve tax transparency and reporting standards should be aligned with BEPS and their effect on tax compliance taken into account. These include in particular the Foreign Account Tax Compliance Act (FATCA), the Common Reporting Standard (CRS). There should be a holistic system, rather than separate and duplicative measures. FATCA and other reporting regimes identify only that individuals are resident in a jurisdiction or are US citizens and that entities are compliant with FATCA or other regimes. They do not provide information on entitlement to treaty benefits.

- Widely held entities are generally not established for the purposes of tax avoidance, but, as stated above, it is impractical for collective investment schemes to demonstrate their status. We (and other bodies) have suggested in previous submissions that there should be an alternative filter, based on a “genuine diversity of ownership” (GDO) principle, as a means of determining general entitlement to treaty access. Similarly, holding companies controlled by a collective investment scheme which meets the GDO principle should be treated as satisfying the LOB test. The advantage of a test of this type is that: (i) it can be used as a kitemark such that certification of a collective investment scheme by the tax authorities of the jurisdiction(s) in which it (or alternatively its manager) is tax resident as meeting the GDO would satisfy tax authorities of other treaty jurisdictions; and (ii) it does not require definitive verification of the identity and residence status of investors and therefore offers administrative advantages to both the manager of the collective investment scheme and relevant tax authorities. Such a principle would complement the position proposed in the 22 May 2015 revised discussion draft for pension funds, that these should be considered to be per se residents of the State in which they are constituted. This status would be without prejudice to whether a particular transaction undertaken by a collective investment scheme (or pension fund) is held to be abusive in all the circumstances, so that treaty relief should be denied.

- In the absence of a GDO-type provision, there would be a need for an effective and prompt pre-clearance process so that the status of collective investment schemes would be clear to investors, fund managers, market intermediaries and tax authorities. Such an upfront confirmation that a specific fund has treaty access would reduce the operational complexities that the proposed LOB would generate and any impact on cross-border investment will be minimised. This will apply both where a LOB applies on a discretionary basis and where a treaty instead incorporates a PPT.

- The 22 May 2015 revised discussion draft proposes new treaty provisions on “special tax regimes” that would be included in the general definitions of article 3 of the Model Treaty and would exclude entities from treaty relief, even when the LOB conditions are satisfied. The limited safe harbours included (although they recognise the position of CIVs) suggest that this test could be failed by other types of collective investment scheme and by entities within the securitisation tax regimes in the UK, Ireland, Luxembourg, and other jurisdictions, which embody the tax neutrality principle discussed above. This reinforces our point that treaty access should be wide with the focus rather on denying relief to abusive transactions. It is also important to have: (i) clear commentary on how the draft provisions might interact with other parts of the LOB; and (ii) specific provision on entities owned by non-CIVs in the exceptions to the new “special tax regimes” rule (in the manner it has been agreed to consider provisions for the LOB pursuant to paragraph 24 of the revised discussion draft).

AIMA considers that, if these concerns are not addressed, the ability of collective investment schemes to operate across borders will be affected so that the range of collective investment schemes available to investors will be reduced and the sources of finance to businesses will be limited.

Yours faithfully,

Paul Hale

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13 The revised discussion draft references the GDO test, but we strongly encourage the OECD to take further steps and analyse the practical implications that such a regime would trigger, and what could be the better approach towards its implementation. This test has been adopted in UK tax legislation in a number of situations and has proved a useful filter which is practical to operate for the tax authority as well as other parties.
Managing Director, Global Head of Tax Affairs
Re: Response to OECD Public Discussion Draft
   Follow-up Work on BEPS Action 6: Preventing Treaty Abuse

Dear Ms. de Ruiter,

The Association of the Luxembourg Fund Industry (ALFI) has taken note of the OECD Revised Discussion Draft dated 22 May 2015.

This Revised Discussion Draft was issued further to the release of the report “BEPS Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances” in September 2014 (hereafter referred to as the “September Report”).

ALFI is pleased to provide its comments on the Follow-up Discussion Draft in the Position Paper attached thereto.

We thank you for your attention and remain at your entire disposal should you require further details.

Camille Thommes
Director General

Marc-André Bechet
Director Legal & Tax

By email: taxtreaties@oecd.org
The Association of the Luxembourg Fund Industry (ALFI) is the representative body of the Luxembourg investment fund community. Created in 1988, the Association today represents over 1300 Luxembourg domiciled investment funds, asset management companies and a wide range of service providers such as custodian banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax experts, auditors and accountants, specialist IT providers and communication companies. The Luxembourg Fund industry is the largest fund domicile in Europe and a worldwide leader in cross-border distribution of funds. Luxembourg-domiciled investment structures are distributed on a global basis in more than 70 countries with a particular focus on Europe, Asia, Latin America and the Middle East. For further information, do not hesitate to consult our website at www.alfi.lu.

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The Association of the Luxembourg Fund Industry (ALFI) has taken note of the OECD Revised Discussion Draft on Action 6: Preventing Treaty Abuse” dated 22 May 2015 (the “Revised Discussion Draft”). This Revised Discussion Draft was issued further to the release of the report “BEPS Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances” in September 2014 (hereafter referred to as the “September Report”) and the “Follow-up Work on BEPS Action 6: Preventing Treaty Abuse” dated 21 November 2014 (the “Follow-up Discussion Draft”).

ALFI is pleased to provide its comments on the Revised Discussion Draft. These comments mainly focus on the situation of collective investment vehicles (“CIV”) being widely-held, diversified, and subject to investor-protection regulation in the country of establishment of the CIV, as previously defined by the 2010 OECD report on treaty eligibility for investors in CIVs (the “2010 Report”).

We would like also to draw your attention to the comments that we have made to the OECD in our previous submission on 8 January 2015 which are still valid.

- Definition of CIVs and non-CIVs

CIVs are defined as “funds that are widely-held, hold a diversified portfolio of securities and are subject to investor-protection legislation in the country in which they are established.” We understand that, so far, there is no consensus on the distinction between CIVs and non-CIVs. In particular, the qualification will clearly depend on certain criteria, e.g. the notion of widely distributed. The final report should clearly foresee how this criterion has to be applied, i.e. according to the law and regulatory system, according to the statutes of the CIVs or on a factual basis. For example, a fund that is owned by a single investor would be deemed to be widely distributed by some States, provided that its statutes and the law allow for the distribution to a wider number of investors. In other words, it is not the actual composition of the shareholder base that counts but the principle or the law under which the fund is established.

- CIVs: application of the LOB and treaty entitlement

Subparagraph 2 f) of the LOB rule provides for the inclusion, in the list of “qualified persons”, of a provision dealing with CIVs which shall be either drafted, or omitted, based on how CIVs are treated in the Convention and are used and treated in each Contracting State. The Commentary on the LOB rule includes a number of alternative provisions that correspond to the various approaches included in the 2010 OECD Report “The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles”.

We still believe that certain CIVs should per se be considered as qualified persons for the purpose of the LOB provision, according to the position described in paragraph 13 of the Revised Discussion Draft.

In particular, we are of the view that a widely-held open ended CIV is indistinguishable in practice from a company quoted on a recognized stock exchange. Maintaining a distinction in the LOB between CIVs listed on a stock exchange (so called Exchange Traded Funds or ETFs) and other CIVs creates potential distortions which are based on an arbitrary distinction.

As a result, the final report on Action 6 should contain the relevant provisions to ensure that all CIVs set up as UCITS or non-CIVs with similar characteristics will automatically qualify as resident for the purpose of the application of Article 1 of the OECD Model Tax Convention and the LOB clause / simplified LOB clause.
• TRACE

We believe that the proposed amendment of the OECD Model Tax Convention and the LOB provision should not be implemented without the implementation of the TRACE program. The current procedures in certain States are complex, onerous and time consuming – not in line with the constraints of CIVs. We believe that the OECD should do what it can to ensure that the TRACE program is implemented in parallel, in order to avoid having individual OECD Member States defining their own distinctive rules for the practical application of the LOB clause.

• Non-CIV Funds

As stated above, we recommend that the final report on Action 6 should foresee that all widely-distributed non-CIVs whose characteristics are similar to those of UCITS will automatically qualify as resident for the purpose of Article 1 of the OECD Model Convention and that they will also be considered as qualified residents for the purpose of the LOB clause and the simplified LOB clause.

For other non-CIVs, we welcome the proposal in paragraph 24 to address these vehicles specially.

• Issues related to the derivative benefits provision and new concept of “special tax regime”

Paragraph 53 of the Revised Discussion Draft suggests including a new concept into the OECD Model Tax Convention: the concept of “special tax regimes”. According to the proposal, income which falls under one of these regimes would be denied the benefits provided in Article 11 (interest), Article 12 (royalties) and Article 21 (other income).

As an introductory comment, we are concerned that the introduction of this new concept at such a late stage does not allow for thoughtful review and comment. Submitting comments is all the more difficult that the new provisions have been inserted in the Revised Discussion Draft without any further proposed commentaries or guidelines explaining the contemplated definitions or scope (e.g., the concept of “preferential effective rate of taxation” is not defined, same for “administrative practice”, etc.).

According to the Revised Discussion Draft, the aim of this proposal would be to address some of the objections to the addition of a derivative benefits provision in the LOB rule. The derivative benefits provision is however not included in the simplified LOB (only in the “standard” draft LOB). We recommend that a derivative benefits provision is included in the simplified LOB.

We appreciate the fact that a carve-out has been inserted for vehicles that facilitate investment in widely-held entities that hold real property (immovable property), a diversified portfolio of securities, or any combination thereof, and that are subject to investor-protection regulation in the Contracting State in which the investment entity is established. However, we consider that this additional restriction on treaty benefits constitutes an additional layer of legal uncertainty for tax payers, so we do not recommend the introduction of this new concept in the OECD Model Tax Convention. Should such clause be maintained in the final report, we would recommend to ensure that the definition of investment funds which is used is consistent with the definitions of CIVs (and non-CIVs) that will be used for the purpose of the other provisions of the Model Tax Convention and in particular for the LOB rule. We refer in this respect to our comments above. In addition, we recommend that the clause is amended in order to ensure that Member States have the possibility to clarify which type of investment fund will actually benefit from such a carve-out, by adding an exhaustive list of investment funds during their bilateral negotiations.
Finally, we do not see what would be the benefit of the introduction of such new concept as we have already the LOB provision / simplified LOB and PPT rules with, in practice, the same objective. On top of that, we consider that such provision should not be implemented in the Multilateral Instrument and therefore it should only be put in place on a bilateral basis. As a result, OECD’ Member States should be aware of this specific tax regime and could act accordingly in the bilateral agreement.

- Action 15 and Multilateral Instrument

The “simplified” LOB rule should be applied by OECD’ Member States that would like to combine LOB / PPT rule. The question of the incorporation of the simplified LOB provision in the articles of the OECD Model Tax Convention has been covered in section 6 and the Annex. However, our concern is the articulation of the LOB, the simplified LOB and action 15. The Multilateral Instrument should be sufficiently precise to cover all the cases that could be applied differently in practice by each individual OECD Member State.

- EU law

We are of the view that EU law matters are essential in formulating Action 6. Failure to take these into account will create uncertainty and potentially protracted litigation on EU law matters.

For example, on the simplified LOB, in subparagraph 3, it seems necessary to us to apply the same threshold (50%) as in subparagraph 2 (e) for EU residents. Equally in paragraph 40 of the Revised Discussion Draft, we believe that the threshold in subparagraph 2 a) (ii) should be the same (i.e. 50%) for EU resident beneficiaries.

- Additional recommendation

ALFI suggests to include a statement that Contracting States are encouraged to consider that UCITS and comparable non-CIVs will not be considered as creating opportunities for treaty shopping.
Amsterdam, 16 June 2015

Re: BEPS Action 6, comments to the Revised Discussion Draft

Dear Madam,

The Tax Committee of the American Chamber of Commerce in the Netherlands (AmCham) is grateful for the opportunity to provide you with its comments to the OECD’s Revised Discussion Draft “Beps Action 6: Prevent Treaty Abuse” published on 22 May 2015 (“RDD”). This letter complements our earlier comments on BEPS Action 6.

Please find below our comments.

1. **General.** Similar to the prior work by the OECD on BEPS Action 6, the RDD continues to propose broad rules to deny treaty benefits in many cases without much apparent regard for the negative impact that the uncertainty created by these changes will have on cross border investments and tax disputes. While the proposed simplification of the LoB rules is welcome, other important issues, including the (non-)application of treaty benefits to (regional) headquarter operations of multinationals that have genuine economic activity continue to be unresolved.

2. **Simplified LoB.** The proposed simplified LoB is a significant improvement over the original proposal for an LoB. With the further revisions described in points 3 through 7 herein, the
simplified LoB can become the standard provision to be included in the OECD Model Commentary.

3. **Derivative benefits.** AmCham is in favour of a broad “derivative benefits” provision as a tool to prevent treaty shopping. AmCham therefore welcomes the revised “derivative benefits” provision contained in the simplified LoB rule that no longer imposes undue limitations on intermediate owners.

4. **Intermediary owners.** AmCham firmly believes that the potential for intermediary owners to engage in BEPS activities should be addressed by the other BEPS Action Plans, and should not be dealt with through Action 6. In this regard, AmCham supports the decision of Working Party 1 to refrain from imposing any qualifications on intermediary owners in the derivative benefits clause of the simplified LoB rule. Should the BEPS concern for intermediaries prevail in the meetings later this month, however, AmCham suggests a solution in line with the recently proposed changes to the US model treaty. To qualify under the derivative benefits test in the proposed revised US model treaty, every intermediary must be a "qualified intermediary owner". If required for purposes of Action 6, a similar approach would effectively deal with BEPS concerns at the level of any intermediaries.

5. **Special tax regime.** AmCham believes the new U.S. proposal on “special tax regimes” is very broadly applicable and not limited to conduit situations which are in scope for Action 6. The issues targeted should be addressed in the context of the OECD work on Harmful Tax Practices and/or Hybrids instead, but not in the context of the application of tax treaties.

6. **Cliff effect.** For purposes of the derivative benefits test, AmCham advocates a solution whereby the treaty claimant is eligible for the benefits of the treaty between the ultimate beneficial owner and the source state, if the terms of that treaty are less favorable as compared to the benefits of the treaty between the state of the claimant and the source state. Such a mechanism is required to allow multinationals sufficient time to restructure their international activities to account for BEPS 6 and effectively deals with any treaty shopping concerns.

7. **Active trade or business.** The distinction made between headquarter companies and trading companies for the qualification for treaty benefits is not fair if a headquarters operation has substance and carries on active functions through own qualified employees. Additionally, if a headquarters operation directs or oversees the operations of a connected
persons in the treaty country of residence, their activities should be aggregated for purposes of this test. It is not reasonable to require international business to merge operating companies with headquarter companies just for the sake of qualifying for treaty benefits.

8. **PPT.** The various technical examples provided on the operation of the PPT rule foreshadow the difficulty taxpayers will have in proving the requisite facts to prevent denial of treaty benefits. As a result, it will be virtually impossible for most arm's length parties to determine whether reduced withholding rates may apply under a particular treaty. It is important to continue to monitor progress in this area – as the final report on BEPS Action 6 in September 2015 will likely recommend significant changes to the tax treaties. AmCham expresses the hope that countries will ensure that any future actions taken in this area will foster an environment in which businesses can thrive and compete in the global economy.

AmCham continues to encourage a focus on substance in the examples for the PPT. We suggest that if two tax authorities have differing views, there should be a *prima facie* assumption that it is not reasonable to conclude that obtaining treaty benefits was one of the principal purposes.

* * *

The Tax Committee of AmCham appreciates the opportunity to provide comments to the Revised Discussion Draft. We reiterate our support for rules that clarify the granting of treaty benefits that do not unreasonably interfere with past, present or future legitimate commercial business decisions.

Should you desire, we are available to discuss our comments and suggestions at your convenience in more detail at a location of your choice.

Yours Sincerely,

<signed> <signed>

Patrick Mikkelsen Arjan van der Linde
*Executive Director* *Chairman Tax Committee*
To: Marlies de Ruiter, Head, Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA

CC: The Ministers of charge of Tax in Belgium, Denmark, Finland, France, Germany, Ireland, Luxembourg, the Netherlands, Sweden, Turkey and the United Kingdom;
The Council of the European Union;
The European Commission;
The European Parliament

Re: Revised discussion draft Base Erosion Profit Shifting (‘BEPS’) Action 6: Prevent Treaty Abuse

Dear Ms de Ruiter,

We write on behalf of end investors, globally, who entrust us to invest their assets so that they can achieve their financial goals. As CEOs of large European asset managers, we support the international community’s attempt to curb aggressive tax planning but remain concerned that many of the BEPS Action Plans (namely Actions 2, 3, 4, 5, 6, 7 and 15) will have unintended consequences. Such unintended consequences will reduce investment choice and returns for end investors, as investment funds become less attractive and hence reduce capital flows to investment projects, companies and governments. This runs counter to the BEPS objectives set out in the 2014 Explanatory Statement which states “A key focus of this work is to eliminate double non-taxation. However, in doing so, new rules should not result in double taxation, unwarranted compliance burdens or restrictions to legitimate cross-border activity.”

In view of the limited time available, we comment here only upon the impact for non-CIV funds of the proposals in the revised discussion draft on Action 6 issued on May 22, 2015, aimed at preventing tax treaty abuse. In particular, the Action 6 proposals will set an unrealistically high bar for non-CIV funds to qualify for tax treaty access, which is an essential tool to enable them to deliver a tax-neutral outcome (compared to direct investment in the same assets).

A number of possible solutions (both short and longer term) regarding tax treaty access for non-CIVS have been suggested by the asset management industry in the course of prior consultations. Unfortunately, these suggestions have not been developed into a simplified, short-term solution, nor have any proposals emerged for a robust longer-term framework. Some tax authorities appear to believe that such simplified, short-term solutions present unacceptable opportunities for treaty-shopping/deferral; and that they had no mandate within the BEPS project to design a comprehensive end-to-end framework. The end result runs counter to the framework for the BEPS project (and the OECD’s basic principles) in that it will severely restrict legitimate cross-border investment. As CEOs of large European asset managers, we support the aims of the BEPS project to eliminate double non-taxation_and to achieve this without inflicting unintended adverse tax outcomes on bona fide cross-border investment.
If these dual objectives are not met, investors in non-CIV funds will be faced with huge uncertainty – funds face tax authority challenge if they do not pay the “fair amount of tax”, but no framework exists to define what this might be. As an industry, we believe this will have a chilling effect upon pooled investment, where certainty is particularly important. Non-CIV funds include funds investing in real assets such as infrastructure and real estate as well as funds investing in SMEs (venture capital funds and private equity funds). The effect of BEPS will be to undermine other initiatives such as the OECD Institutional Investors and Long Term Investment project and European Union initiatives, such as the Capital Markets Union, The European Fund for Strategic Investment and the European Long Term Investing Fund.

In the area of CIVs, progress has been made on ensuring that CIVs are not inappropriately impacted by Action 6 since the release of the first draft in April 2014. This was helped by the previous work undertaken by the governments and stakeholders which resulted in the OECD 2010 CIV Report which recognised the economic importance of CIVs, their right to treaty entitlements and mechanisms to facilitate treaty access for CIVs. No such body of work exists on the question on treaty entitlements for non-CIV funds and this has hampered viable solutions being included in Action 6 dealing with non-CIV funds and giving the required certainty.

Recommendation

Paragraph 24 of the revised discussion draft suggests that work might continue to explore solutions to issues related to the treaty entitlement of non-CIV funds. We believe it is essential that the countries participating in the BEPS project request the OECD to create a working group specifically to engage with the asset management industry to develop workable solutions (along the lines of the framework and output achieved in the OECD 2010 CIV Report). We further believe that it will be necessary to consider the impact of the BEPS Actions on non-CIV funds on a holistic basis, rather than Action by Action. We are committed to actively participate in this working group to develop workable solutions and to work with Governments in addressing any legitimate concerns around treaty shopping and other issues. We believe without such a working group between Governments and industry non-CIV funds will be left inadvertently impacted by Action 6.

We stand ready to assist this working group in what we believe will be a complex project, but one that is crucial to the future of alternative fund management globally.

Yours Sincerely,

Aberdeen Asset Management PLC
Andrew Laing
Deputy CEO

J.P. Morgan Asset Management
Mike O’Brien
CEO of Investment Management EMEA

Allianz Global Investors GmbH
Elizabeth Corley
Global CEO

M&G Securities Limited
Grant Speirs
Group Finance Director

APG Asset Management
Eduard van Gelderen
CEO and member of Executive Board of APG

PFA Pension
Allan Polack
Group CEO
BlackRock
David Blumer
Head of Europe, Middle East and Africa

Capital Group Companies Global
Hamish Forsyth
President - Europe

Fidelity Worldwide Investment
Jon Skillman
Managing Director, Continental Europe

Robeco
Roderick Munsters
CEO

State Street Global Advisors
Michael Karpik
Head of Europe, Middle East & Africa

UBS Global Asset Management
Martin Thommen
Head of UBS Funds
June 16, 2015

VIA E-MAIL

Ms. Marlies de Ruiter
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Centre for Tax Policy & Administration
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Re: Comments on Discussion Draft on BEPS Action 6: Preventing Treaty Abuse

Dear Ms. de Ruiter:

This letter is submitted on behalf of the members of the Association of Global Custodians ("AGC" or "Association") to provide you with comments in respect of the OECD Revised Discussion Draft: Preventing Treaty Abuse, issued on 22 May 2015 (the “Discussion Draft”) pursuant to Action 6 of the BEPS Action Plan.

As you know AGC members have been keenly following (and in some cases actively participating in) the work of the Organisation for Economic Co-Operation and Development ("OECD") for many years on various key tax developments and welcome the opportunity to provide comments to you on the third and final Discussion Draft.

The Association is an informal group of 11 member banks that provide securities safekeeping and asset serving functions to cross-border institutional investors worldwide including investment funds, pension funds, and insurance companies.

In providing global custody services, AGC members routinely seek appropriate tax treaty withholding tax relief on behalf of custody clients. The members typically collectively process millions of such relief claims each year, affecting substantial amounts of cross-border portfolio investment flows in and out of countries worldwide. A significant portion of the income for which the members process treaty relief claims is income received by institutional investors. As such, the AGC members experience on a daily basis the costs, inefficiencies, and excessive withholding that arises when the procedures for claiming lawful relief are unduly burdensome or complicated for the investors involved, or when the...
standards for entitlement to treaty relief are too unclear or complicated to effectively accommodate treaty relief claims, whether at source or by refund.

The Association notes on page 1 that the OECD wish for comments to be kept as short as possible and we have endeavored to adhere to that request. Our comments are attached in the Annex.

Sincerely yours on behalf of the Association,

Mary C. Bennett
Baker & McKenzie LLP
Counsel to the Association

Annex
AGC comments on the 22 May 2015 Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse

General Comments on Discussion Draft

The over-arching concern the Association has in connection with Action 6 is that there is still no substantive detail around how the testing of a Limitation on Benefits (LOB) or Principal Purpose Test (PPT) will work procedurally for cross-border investors claiming their due entitlements. Based on the Revised Discussion Draft (RDD) there appear to be three possible outcomes in testing under Action 6:

1) A Limitations on Benefit (LOB) accompanied by a Principal Purpose Test (PPT)
2) An LOB accompanied by an anti-conduit rule
3) A stand-alone PPT

We are also concerned that the final version of the Model provisions and related Commentary are due to be finalized by September 2015 without industry input into how operationally the various outcomes will be implemented for cross-border investors. We also note that there are a number of open items yet to be discussed at the Working Party meeting in June 2015 of which the outcome will not be known until the finalization of the model provisions in September 2015. In particular, we acknowledge the comments in the RDD that further work is required on exploring solutions to issues related to the treaty entitlement of non-CIV funds. However, the omission of appropriate solutions dealing with the non-CIV funds and the risk of finalization of Action 6 without appropriately dealing with this issue with the direct participation of relevant stakeholders is a cause of serious concern. We urge the OECD and the governments as a matter of urgency to work with the relevant industry stakeholders to devise workable solutions ensuring non-CIV funds are not denied treaty entitlements, while addressing concerns highlighted in the RDD around treaty shopping and deferral of recognition of income.

The Association very much welcomes the comments in the (RDD) around Collective Investment Vehicles (CIVs) noting that a single approach is not the way to address these vehicles in the practical application of obtaining treaty benefits. Each CIV will have its own specific fact pattern and having the flexibility and the worked examples in the 2010 CIV Report to stand behind (and be adopted by Governments into tax treaties) will almost certainly assist Governments, Investors and Service Providers gaining more comfort on a practical basis.

That being said, we have some concern about how the solutions from the 2010 CIV Report can be accommodated through the proposed multilateral instrument contemplated by Action 15, and we are also concerned about how those solutions would interact with a decision by a State to incorporate a PPT provision in its treaties, whether alone or in conjunction with one of those solutions as part of an accompanying LOB provision. The Association continues to be seriously concerned about the lack of clarity around the application of the PPT to cross-border institutional investors, and we were very disappointed that the RDD did not take the opportunity to provide more guidance on that, instead continuing to rely exclusively on one narrow example regarding an investment fund which raises as many questions as it answers. It will be critical to the stability of the cross-border
portfolio investment markets for there to be much greater clarity around the substantive and procedural application of the PPT simultaneously with its introduction into treaties.

In addition, we wish to stress the importance of ensuring that the “alternative simplified LOB” which is to be offered as a possible provision to combine with a PPT includes a paragraph 2(f) (i.e., a specific provision identifying the CIVs that will be treated as “qualified persons”). We note that the descriptive LOB article set out in the Annex to the RDD includes a paragraph 2(f), but since no corresponding paragraph appears in the sample alternative simplified LOB set out at paragraph 3 of the RDD, we want to make sure the version ultimately included in the Commentary does include the necessary language.

While the Association welcomes the RDD’s confirmation that the Working Party 1 delegates “agreed … that the implementation of the recommendations of the TRACE project was important for the practical application of” the conclusions around the 2010 CIV Report, the Association notes that such an agreement at the Working Party level falls far short of the commitment needed by Governments to actually move forward with implementation of the TRACE regime simultaneously with the introduction of any treaty changes based on the outcome of Action 6. If the restrictions contemplated by Action 6 are introduced across a wide number of treaties in the near term (e.g., through the multilateral instrument contemplated by Action 15) without a simultaneous introduction of the procedural mechanisms contemplated by the TRACE Implementation Package to clarify and guarantee how those changes will be implemented in practice, the Association foresees a period of widespread and serious disruption to legitimate treaty claims across the international markets, with correspondingly detrimental effects on cross-border investment. Accordingly, the Association urges the OECD in the strongest possible terms to ensure that any country intending to move forward with introducing the Action 6 restrictions into its treaty network formally commit to simultaneous adoption of the TRACE regime, particularly in light of the pertinent information OECD Member Countries will receive under the OECD Common Reporting Standard, which we expect to be in force prior to the Action 6 recommendations being adopted.

**New Developments in the RDD**

The Association observes that there are new recommendations being made to Action 6 as a direct result of proposed changes to the US model income tax convention. These are:

- Rule relating to Special Tax Regimes
- Partial Treaty termination
- Restrictions on the trade or business test

The Association notes that when the OECD Model provisions and Commentary are finalized in September 2015, and if these recommendations are adopted, clear procedural guidance of how this will fit into a multilateral instrument will need to be made available. The Association further notes that great care will be needed in drafting any provision aimed at addressing Special Tax Regimes to ensure that it does not operate to inappropriately deny benefits to either State’s CIVs or other legitimate institutional investors, including pension funds. We anticipate that this drafting could be difficult to achieve in the context of a
proposal potentially to be included in a multilateral instrument, and we question whether there is adequate time to properly consider this new recommendation at such a late stage in the process.

The Association fully understands the aim of the OECD in introducing a multilateral instrument by December 2016 to combat perceived treaty abuses. However, as a result, the Association can envisage more bilateral agreements (i.e. moving away from the multilateral route) being introduced by Governments, thus meaning more divergence in rules in testing treaty eligibility in an already difficult environment for genuine cross-border investors.

Comments on Previous Issues

The Association has the following comments on the RDD’s treatment of issues previously addressed in our comment letter of January 9, 2015, the contents of which we still stand behind.

Issue #2 -- Non-CIV funds: application of the LOB and treaty entitlement

We welcome the RDD’s confirmation that there will be a change to the Model Tax Convention to confirm that a pension fund should be considered to be a resident of the State in which it is constituted regardless of whether it benefits from a limited or complete exemption from taxation in that State. We further welcome the RDD’s confirmation that consideration will be given at WP1’s meeting this month to add further Commentary guidance on the application of the LOB and PPT provisions to non-CIV funds, and that further work to explore solutions to issues related to the treaty entitlement of non-CIV funds might continue between September 2015 and December 2016.

That being said, the Association notes that these are issues of great importance and significant complexity, requiring a full understanding of the different types of non-CIVs, their characteristics, and the types of procedural requirements they could reasonably be expected to satisfy to guarantee their legitimate entitlement to treaty relief. Our January 9, 2015 comment letter expressed particular concern about these issues in relation to pension funds. We therefore urge the OECD, as a matter of highest priority, to lay out a transparent process for identifying solutions to these problems, with the direct participation of relevant stakeholders and with effective consultation, beginning no later than September 2015. We further urge the OECD to ensure that any country intending to introduce the Action 6 recommendations into its treaty work formally commit to simultaneously adopt the solutions so identified.

We also note that under Issue #4 (Alternative LOB provisions for EU countries), the RDD notes the possibility of introducing a new derivative benefits safe harbor for pension funds which would allow a fund to qualify for benefits provided that more than 90 percent of its beneficial interests are held by individuals who are residents of the fund’s State or a third State with a comprehensive treaty with the source State, and provided further that the fund, if it were a resident of such third State, would be entitled to the same source State relief as applies under its own treaty with the source State. While we appreciate the apparent intention to preserve treaty benefits in such cases, we note that: 
• the availability of this safe harbor will be meaningless unless there is a clear and workable procedure for a pension fund to establish its entitlement to this provision; and
• treaty tests which have required a pension fund to establish its hypothetical entitlement to exemption under the domestic law of another country (presumably a constituent element of establishing satisfaction with the “same rate” test) have proven notoriously difficult to apply in practice, and a better approach here would be to deem the claimant pension fund to be an entity that would qualify as a pension fund under the equivalent beneficiary’s treaty and then enquire whether that treaty provides the same withholding tax relief on dividends and interest as the fund’s actual treaty does.

**Issue #6 -- Issues related to the derivative benefit provision**

The Association is pleased the RDD indicates that favorable consideration is still being given to including a derivative benefits provision, strongly urges the OECD to move forward with including such a provision without regard to the outcome of the deliberations on the new proposals on special tax regimes and subsequent domestic law changes, and references its comment above about the applicability of a derivative benefits provision to pension funds.

**Issue #12 -- Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level**

The Association was disappointed that the RDD included such a weak response to the comments urging greater procedural safeguards around the application of the PPT. As indicated in our January 2015 comments, we believe there should be a minimum standard of procedural process around the application of the PPT, and that the minimum standard should include high level panel review of any proposed denial of benefits under the provision and a timely ruling process to obtain certainty about the provision’s application. These safeguards remain particularly critical for cross-border portfolio investors in light of the continuing lack of clarity as to the substantive interpretation of the PPT in their circumstances.

**Issue #16 -- Drafting of the alternative “conduit-PPT rule”**

Finally, the Association believes it is important to confirm that the alternative “conduit-PPT rule” will not operate to deny benefits to a CIV that is a “qualified person” under the LOB (or simplified alternative LOB) provision simply because the CIV distributes its income to its investors. We suggest that a statement be added to the Commentary to provide that confirmation.
OECD DISCUSSION DRAFT ON BEPS ACTION 6 – Treaty shopping
AIC Submission

Introduction

The Association of Investment Companies (AIC) represents some 340 closed-ended investment companies with assets under management of over £130 billion. Investment companies have their shares admitted to trading on public stock markets. The AIC’s members are predominantly listed on the main market of the London Stock Exchange. Some are also quoted on the Channel Islands Securities Exchange.

The AIC’s members include UK investment trusts, Venture Capital Trusts, UK REITs and non-EU companies.

Our non-EU members are primarily Channel Islands domiciled. The AIC represents 64 closed-ended investment companies in Guernsey and 20 in Jersey. A number of Channel Islands investment companies were established in the past because, depending on the underlying asset class of the portfolio, UK collective investment vehicles did not achieve tax neutrality compared to direct investment or imposed an unnecessary compliance burden. Some Channel Island property investment companies have recently moved their tax residence to the UK and become UK REITs.

The AIC is concerned at the potential impact that the OECD discussion draft on BEPS Action 6 on treaty shopping may have on investment companies.

Benefits of Collective Investment Vehicles

The benefit of investment companies as collective investment vehicles (CIVs) for savings is well recognised. They offer:

- the expertise and knowledge of a professional fund manager who will manage the portfolio on the investors’ behalf;
- diversification which can help to reduce and manage risk within an investment portfolio;
- access to different asset classes that the investor may not otherwise be able to access such as property, private equity and infrastructure assets;
- access to different geographical sectors that the investor might not otherwise be able to access;
- the benefits of economies of scale even if small amounts are invested.

Importance of Collective Investment Vehicles and treaty access

The importance of CIVs is such that most countries have a tax system that provides for neutrality between direct investments and investment through a collective investment vehicle.
International diversification of investment portfolios has become increasingly more significant. The OECD in its 2010 paper “The granting of treaty benefits with respect to the income of collective investment vehicles” found that over 25% of all equity assets held by US CIVs were issued by non-US companies at that time. Also, about 30% of the assets of UK CIVs were invested outside the UK.

As more investments are made cross-border in order to gain access to a wider pool of investments and to hedge currency and market risk, the question of treaty access is increasingly important. CIVs represent a key source of investment capital. It is essential that capital invested through CIVs is available for cross border investment and the long term financing of economies.

Achieving tax neutrality between direct investment and an investment through a CIV in an international context is as important as achieving tax neutrality in a domestic context. Restricting the availability of treaty benefits to CIVs reduces investor returns from CIVs and undermines their viability as a savings and investment product.

The OECD acknowledges in its 2010 paper that governments have recognised the importance of CIVs as a complement to other savings vehicles in terms of facilitating retirement security. The 2010 paper continues that, in many countries, participants in defined contribution retirement plans invest primarily in CIVs.

**AIC recommendations**

The term “CIV” is defined in the 2010 paper as 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. Whilst investment trusts, VCTs and UK REITs are not authorised by the Financial Conduct Authority per se, there are extensive regulations surrounding the operation of the company and marketing and distribution of investment trust shares.

Investment companies marketed and/or managed in the European Union are Alternative Investment Funds (AIF). They must have an Alternative Investment Fund Manager (AIFM) which imposes various obligations on the company and brings them into the jurisdiction of the EU regulatory authorities.

Investment companies whose shares are admitted to trading on a regulated market in the EU comply with the Transparency Directive, the Prospectus Directive, the Alternative Investment Fund Managers Directive and the Consolidated Admissions and Reporting Directive. Companies that are listed on the UK are required to comply with Chapter 15 of the Listing Rules.

Further, investment companies incorporated in the UK adhere to a number of domestic regulatory requirements including company law (which includes provisions arising from EU company law directives) and the corporate governance code.

The AIC therefore considers that investment trust companies, VCTs and REITs are CIVs, as defined, and recommends that they are treated as such.
In any event, the AIC **recommends** that non-CIV funds should be able to obtain treaty access where such funds are widely held. Indeed the Revised Discussion Draft issued by the OECD on 22 May 2015 (RDD) states at paragraph 22 “As regards the broader question of treaty entitlement of non-CIV funds, the Working Party recognised the economic importance of these funds and the need to ensure that treaty benefits be granted where appropriate.”

The Limitation of Benefits (LOB) clause in the September 2014 OECD Report on ‘Preventing the Granting of Treaty Benefits in Inappropriate Circumstances’ contained a rule in Article 2(c)(ii) dealing with indirect ownership by a publicly traded company which required each intermediate owner to be a resident of either Contracting State. This wording was square bracketed and the Commentary indicated that some States considered that the requirement is unduly restrictive and preferred to omit. This restriction has not been included in the Simplified LOB clause in the RDD. The AIC agrees that the original wording is unduly restrictive and disproportionate and **recommends** that this restriction is not included in any future LOB clause as the focus should be on the ultimate beneficial owner.

The AIC **recommends** that the publicly traded condition is not required “throughout the taxable period” where a company becomes or ceases to be a publicly traded entity during a taxable period.

The LOB clause in the September 2014 OECD Report contained qualifications on the availability of treaty relief to publicly traded companies so that the location of the stock exchange on which the principal class of shares is primarily traded or the company’s principal place of management and control had to be in the Contracting State of which the company is resident. The Simplified LOB clause in the RDD does not contain such restrictions on the location of the recognised stock exchange and the AIC **recommends** that such restrictions are not reintroduced in the LOB clause as they are unduly restrictive. The AIC does support the introduction of provisions to deal with “dual-listed company arrangements.”

The RDD indicates that the US delegate on the Action 6 Working Party has made a proposal to exclude entities benefiting from a “special tax regime” from treaty relief which would add a new exclusion to the interest, royalties and other income articles. Whilst the proposed wording does contain limited safe harbours, the AIC **recommends** that the “special tax regime” is not adopted as it would lead to too much uncertainty.

The AIC **recommends** that the new proposal to partially terminate certain treaty provisions in the event of either contracting state providing an exemption from taxation to resident companies for substantially all foreign source income is not adopted as it would generate too much uncertainty.

The AIC is also concerned at the effect that the imposition of the principal purpose test (PPT), as proposed in Action Plan 6, will have on certain publicly traded investment companies. Some investment companies, in order to maximise the return to investors, will invest in certain jurisdictions via holding companies in a third party jurisdiction. To restrict treaty benefits to CIVs in such a situation will undermine the tax neutrality of CIVs and
threaten the viability as a savings and investment product. Given the importance of CIVs and their international diversification, the AIC recommends that the PPT should not apply to CIVs and other funds which are widely held.

June 2015

To discuss the issues raised in this paper please contact:

Janette Sawden, Taxation Advisor
janette.sawden@theaic.co.uk, 020 7282 5565
Dear Mrs. de Ruiter,

BDI* refers to the OECD Revised Discussion Draft “Prevent Treaty Abuse” issued on 22 May 2015. We would like to thank you for the possibility to provide our comments that allow us to engage with you on these important issues. We focus our feedback on the most fundamental issues with regard to the revised draft.

The primary objective of tax treaties is and should continue to be to facilitate cross-border trade through the allocation of taxing rights between countries and to provide for mechanisms to eliminate double-taxation.

Therefore, it is of major importance that anti-abuse rules are designed so that they have a minimum impact on genuine business operations. Consequently, we believe that perceived inappropriate behaviour is best addressed with specific and targeted anti-abuse provisions. In our view, both the proposed LOB provision and the PPT fail in this respect, since they are too general in nature and not limited to abusive situations.

We acknowledge that some improvements have been made since the last Draft, with some useful examples added. However, considering the added complexity and unpredictability that will follow if these proposals are implemented, we are concerned that, despite requests from numerous commentators, there is still not sufficient guidance in the Draft. In addition, several issues have been postponed by the Working Party until

* BDI (Federation of German Industries) is the umbrella organization of German industry and industry-related service providers. It speaks on behalf of 36 sector associations and represents over 100,000 large, medium-sized and small enterprises with more than eight million employees. A third of German gross domestic product (GDP) is generated by German industry and industry-related service.
its June meeting and new proposals such as the “special tax regime” have been introduced at a very late stage in the process.

We are not in favour of the combined approach of having both a LOB and a PPT in a tax treaty. Although the Draft suggests a simplified LOB, which would be preferable compared to the extensive one as suggested in previous Drafts, it would still leave companies with a lot of uncertainty as to the outcome, since after having passed the simplified LOB, they would be confronted with a very subjective PPT.

The Principal Purpose Test (PPT) is too wide and vague. This would allow tax authorities a very broad discretion to challenge the availability of treaty benefits and be therefore open to ambiguity and misinterpretation. In addition we fail to see how there could be more than one principal purpose. In our view, the test should naturally focus on the principal purpose of the arrangement or transaction. Also, the various technical examples provided on the working of the PPT rule effectively show the difficulty that taxpayers will have in proving the requisite facts to prevent denial of treaty benefits.

The LOB is still, despite numerous comments, overly restrictive and in some respects potentially in violation with EU law.

We strongly support a derivative benefit provision in the LOB. The derivate benefit provision would extend the granting of treaty benefits to entities that are controlled by entities that are resident of a third country and that would enjoy the same treaty benefits with the contracting state in question. In such situations, there is no incentive for treaty shopping.

At this late stage in the process, we object, however, to the proposal to introduce a new treaty provision on “special tax regimes”. We believe that issues relating to “special tax regimes” are best addressed through the OECD’s work on Harmful Tax Practices.

The revised Draft proposes in paragraph 32 that as long as a competent authority has properly exercised the discretion granted by the discretionary relief provision of the LOB rule, that provision has been complied with and it cannot, therefore, be argued that taxation is not in accordance with the provisions of the Convention. This seems to be intended to deny a taxpayer the possibility to invoke the mutual agreement procedure (MAP) regarding this decision. This seems imbalanced as MAP typically will involve both contracting states, whereas the residence country competent authority may not have been involved in a denied request under the discretionary relief provision.

To provide the necessary legal certainty to taxpayers regarding the tax treatment of their investments, it is crucial that (1) taxpayers have the possibility to get pre-clearance regarding the access to treaty benefits, (2) the proposals and proposed changes to the Commentary provide ample guidance on the application of both the proposed LOB and PPT rules, and finally (3) there should be unobstructed access to a mutual agreement procedure (MAP) and mandatory binding arbitration. If these three conditions are not met – which they are not presently – it will be virtually
impossible for most arm’s length parties to determine whether reduced withholding rates may apply under a certain treaty.

In view of the implications of introducing many of the new provisions mentioned in the Model Treaty, and considering the extensive input from commentators, we are concerned that many issues have not been addressed properly and that the Draft still lacks sufficient guidance in a number of areas. As currently drafted, we believe that the provisions could seriously undermine the certainty and predictability needed for investment decisions and also lead to an increase of double taxation cases. The effect would be very negative on investments, jobs and growth.

Please do not hesitate to contact us if you have any questions.

Sincerely,

Berthold Welling

Dr. Karoline Kampermann
This response is submitted by the BEPS Monitoring Group (BMG). The BMG is a group of experts on various aspects of international tax, set up by a number of civil society organizations which research and campaign for tax justice including the Global Alliance for Tax Justice, Red de Justicia Fiscal de America Latina y el Caribe, Tax Justice Network, Christian Aid, Action Aid, Oxfam, and Tax Research UK. This paper has not been approved in advance by these organizations, which do not necessarily accept every detail or specific point made here, but they support the work of the BMG and endorse its general perspectives.

This paper has been prepared by Jeffery Kadet and Sol Picciotto, with comments and input from Francis Weyzig.

We welcome this opportunity to comment on the Revised Discussion Draft (DD).

SUMMARY

A key test of whether the BEPS project can be a success is whether it will result in the inclusion of effective anti-abuse provisions in all tax treaties, not only prospectively, by formulating suitable provisions in the model treaty, but also more directly and quickly, by inclusion of such provisions in the proposed Multilateral Convention (MC), which aims to amend existing treaties.

The RDD proposes a ‘simplified’ limitation of benefits (LoB) provision, and as a minimum standard either (i) a combination of a principal purpose test (PPT) and an LoB provision, or (ii) a PPT provision alone, or (iii) an LoB rule plus some mechanism for dealing with conduit arrangements which are not already covered by other treaty provisions. However, the LoB provision is stated as only a bare outline with a direction to include whatever wording each pair of negotiating states can agree, while the full detailed wording of an LoB article is only in the Commentary, for use by states which prefer not to include a PPT provision.

This approach has exacerbated the concerns we expressed on the previous draft, that it would make it harder for small developing countries to conclude suitable treaties, and result in a kaleidoscope of different provisions, very likely leaving a continued scope for treaty shopping and increasing complexity for tax authorities as well as tax payers.

Furthermore, the RDD does not discuss how such provisions might be included in the MC, and the proposed ‘flexible’ format would make such inclusion difficult if not impossible.

Our comments also include a number of specific technical suggestions.

A. GENERAL COMMENTS

Technical and Policy Aspects

This is the third discussion draft under this Action, and we have been asked to keep comments as short as possible. This implies that they should be confined to specific technical points. However, it is essential in our view for technical points to be considered in the context of the wider policy issues. No doubt some of the participants are aware of these wider issues, but failing to make them explicit impoverishes the debate, and certainly excludes from participation many who do have an interest in those issues, but find it hard to understand the policy implications of the detailed technical proposals.

This Action aims to deal with the problem of treaty-shopping, i.e. taking advantage of the benefits of tax treaties by routing investments into a country through corporate or other legal entities formed in a jurisdiction which has a treaty with that country. Since tax treaties mainly
restrict the right to tax income or profits at source, treaties without effective anti-abuse rules damage countries which are either mainly capital-importing or have significant capital inflows. Thus, both developing countries and many developed countries are hurt by treaty shopping and have a strong interest in preventing it. However, developed countries that also have significant capital outflows will typically benefit from the restriction of taxation rights in source countries. For many developing countries, though, as some commentators have pointed out, concluding tax treaties makes little sense in tax terms. This is because without them such countries are free to take their own decisions on the most appropriate regime to apply to inbound investment, including making appropriate provisions to prevent genuine double taxation. Many developing countries are nevertheless persuaded to enter into such treaties, due to the perception that they help attract investments.

It is therefore very important that international bodies responsible for designing model treaties should ensure that such models include effective anti-abuse provisions, yet regrettably they have failed to do so. Those responsible for designing tax treaties have given higher priority to encouraging international investment than to ensuring effective taxation of income from such investment.

A key test of whether the BEPS project can be a success is therefore whether it will result in the inclusion of effective anti-abuse provisions in all tax treaties. This should be done prospectively, by formulating suitable provisions in the model treaty, but also more directly and quickly, by inclusion of such provisions in the proposed Multilateral Convention, which aims to override existing treaties to the extent that their provisions are unsuitable or inadequate. Hence, evaluation of the proposals under this Action should consider whether the rules they propose are appropriate for rapid implementation, especially by developing countries.

**The form proposed for anti-abuse provisions**

The report under Action 6 of September 2014 put forward two types of provision to deal with treaty-shopping:

(i) a principal purpose test (PPT), and

(ii) a more targeted limitation of benefits (LoB) provision with detailed definitions of the ‘qualified persons’ who should be entitled to treaty benefits.

It also proposed changes to the Preamble to make it clear that the purpose of tax treaties includes preventing evasion and avoidance, and discussed some other forms of treaty abuse, proposing specific provisions for dealing with some of them. It suggested (in para. 14) a minimum standard for treaties, which should include the general statement of purpose, plus either

(i) a combination of a PPT and an LoB provision, or

(ii) a PPT provision alone, or

(iii) an LoB rule plus some mechanism for dealing with conduit arrangements which are not already covered by other treaty provisions.

This minimum standard is now articulated, although not very clearly, in para. 1 of the draft Commentary to proposed Article X in the Annex of this report.

The Follow Up report of January 2015 put forward a number of further detailed questions for consultation on both the PPT and the LoB; and the present RDD presents the conclusions reached by Working Party 1 on most of these for further comment. A few matters remain to be dealt with at its meeting in June, although it is anticipated that some of the work (on the
treatment of collective investment vehicles) may extend beyond that, but ‘should in any event be concluded before the December 2016 deadline for the negotiation of the multilateral instrument that will implement the conclusions of the work on Action 6’ (RDD para. 24). This last reference is the only mention of the multilateral instrument in the RDD. Considering the importance that this multilateral instrument should play in this treaty abuse area, it is regrettable that this report focuses on the model treaty, and does not discuss how the proposed provisions might be dealt with in that instrument.

In our previous submissions on the proposals under this Action, as well as others, we have stressed the importance of achieving simplicity and clarity. On this Action we were specifically concerned that the proposals might leave a wide range of options for negotiation on a bilateral basis, which would (i) make it harder for small, especially developing countries to conclude suitable treaties, and (ii) result in a kaleidoscope of different provisions, very likely leaving a continued wide scope for treaty shopping.

We are disappointed that these concerns have not been addressed, indeed these revised proposals in some respects exacerbate the difficulties. In particular, although the RDD proposes a ‘simplified’ LoB provision, the actual draft treaty article it puts forward in the Annex consists of only a bare outline with a direction to include whatever wording each pair of negotiating states believe might be relevant to their particular relationship and individual needs. It is apparently intended to include the full detailed wording of an LoB article only in the Commentary, for use by states which prefer not to include a PPT provision.

Not only does this encourage significant variation in treaties, but there will be treaty negotiating teams from many countries which will have difficulty determining what inclusions in the LOB will be important and relevant for their respective countries. We believe that greater standardization would be beneficial for both tax authorities and taxpayers who do not have BEPS motivation. On the other hand, we fear that the greater variation that will result from this approach will continue to provide many opportunities for treaty-shopping.

Moreover, the RDD provides no explanation of whether or how an LoB provision might be included in the planned multilateral convention. An effective anti-abuse article is an essential element of this convention, since there are many treaties with developing countries which do not include any anti-abuse provision at all. Although some countries have begun to re-evaluate and renegotiate their treaties, this process would take time. Since the RDD does not propose an LoB provision in standard form, it seems that the multilateral convention might include only a PPT clause. Although this might be acceptable and indeed preferable for some countries, it begs the question of whether some leading OECD states, especially the United States, would be willing to accede to such a convention, in view of its strong policy preference for the LoB approach. Worst of all would be if the multilateral instrument did not include an immediately applicable provision against treaty shopping, but left it to parties to negotiate.

Regarding PPT provisions, we emphasize that these should be included in such a way that they apply to all treaty benefits. At present, if tax treaties include a main purpose test, such a provision is usually included with regard to selected treaty articles only, for example only articles 10 (Dividends), 11 (Interest) and 12 (Royalties). However, treaty abuse may also occur with regard to other treaty benefits, including the elimination of withholding tax on capital gains, under article 12 (Capital gains), or on management fees, as implied by article 21 (Other income). This is of particular relevance to developing countries, as evidenced by the new ActionAid report *An Extractive Affair.*
B. SPECIFIC COMMENTS

Part 1 - Alternative ‘Simplified’ LoB Rule and Presentation of the LoB Rule in the OECD Model

The full LOB provision as set out in the March 2014 BEPS Action 6 Discussion Draft included a base erosion test in Clause e) ii) of Paragraph 2. This base erosion test is missing from paragraph 2 of the simplified LOB rule set out in Paragraph 3 of the RDD.

We believe that the omission of this base erosion test from the simplified LOB rule creates a very big hole for back-to-back and other conduit arrangements through an unrelated person who will qualify as a ‘person other than an individual, if residents of that Contracting State that are qualified persons own, directly or indirectly, more than 50 per cent of the beneficial interests of the person’ under Paragraph 2.e) of the simplified LOB rule.

The explanation for this omission seems to be in paragraph 5, which states:

A number of delegates considered that this alternative version of the LOB rule would address different concerns raised by the LOB rule included in the Report on Action 6 and would provide a simpler way to address the most obvious cases of treaty-shopping, other cases being dealt with under the PPT. …

The idea is that the PPT would be used for conduit companies. While we agree that simpler rules will often be better, this will not be true at all for this situation.

Where there is reliance on a PPT that involves judgment, MNEs will continue to use structures that push the envelope to achieve BEPS objectives. They will rely on the audit lottery that will be highly skewed in their favour.

- Tax authorities will normally have to be examining a specific taxpayer during which time they must recognize that a structure being used is a potentially abusive conduit arrangement. Often, with an unrelated party masking the existence of a back-to-back arrangement, tax authorities will most often fail to recognize such structures.
- Tax authorities will have to gather all facts and circumstances regarding the structure and the participants. This is a difficult and time- and resource-consuming task.
- Tax authorities will have to analyze the information they have gathered and present a comprehensive case supporting the abusive nature of the structure. In addition, some countries may require a presentation of the case to a central authority that must clear any action taken when the PPT is applied.

With all this effort, there will be very few potentially abusive conduit and other similar structures pursued by tax authorities under PPT rules.

Where, however, there is a bright line rule for base erosion to prevent abusive back-to-back and other conduit arrangements, MNEs will not be able to push the envelope beyond the bright line. This bright line will set a minimum standard so that tax authorities will have no need to look for and spend considerable time and effort on applying the subjective PPT to highly abusive tax structures. The recent news that Amazon has decided to initiate reporting sales through branches of its Luxembourg operating sales company in some number of European countries into which it sells is clear proof of this.

For reasons expressed in the above General Comments section of this submission, we have recommended that this simplified approach be withdrawn with only the more comprehensive LOB being included. If this simplified LOB rule is retained, then the base erosion mechanism must be included in this simplified LOB.
If our suggestions are not accepted, there is clearly a need to deal more effectively with conduit and other structures where countries do choose this simplified LOB rule along with the PPT as a backup. We therefore suggest that the final recommendation include that countries adopting the simplified LOB approach along with the PPT (or a PPT alone) impose informational reporting for any conduit arrangements that do not meet some minimum base erosion test. The terms of such a test could mirror the base erosion rules in the full LOB rule.

Although there is a separate section in the Revised Discussion Draft covering intermediate ownership (Paragraph 46 that would amend Paragraph 2 e) of the draft simplified LOB rule), in our view this is an additional example where there must be clear requirements in the simplified LOB rule. The countries that would likely choose this simplified approach will be those most incapable of monitoring intermediate ownership and of challenging tax-motivated structures through only the principles of the PPT provision.

Part 2 – Issues Identified in the November 2014 Discussion Draft

2. Non-CIV funds: application of the LOB and treaty entitlement

We agree fully with the concerns expressed in Paragraph 24 and look forward to seeing what is drafted.

3. Commentary on the discretionary relief provision of the LOB rule

We reiterate that the discretionary relief provision of the LOB rule must be accompanied by a standard for public transparency. As paragraph 65 of the proposed changes to the Commentary notes, the paragraph on discretionary relief ‘grants broad discretion to the competent authority’. The possibility for discretionary relief could give rise to undue pressures on tax officials and create an enabling environment for corruption. Exchange of information on discretionary relief decisions among competent authorities would not help to create the necessary domestic checks and balances. To discourage corrupt practices, and to create more clarity for tax payers, the OECD should strongly recommend that tax authorities publicly disclose their decisions regarding requests for discretionary relief, including explanations of the decision. These could if necessary be anonymised. Various OECD countries, including the US, already have such a system in place for tax rulings in general.

4. Alternative LOB provisions for EU countries

Paragraph 40 involves an additional provision for pension funds under the LOB rule. We have no problem conceptually with this additional provision, but it certainly could be said that the difficulty of administratively trying to comply with the newly drafted 90% test where the 50% test cannot be met may well be insuperable for any pension fund that has more than five or ten members. We cringe at the information gathering and paperwork effort that would be necessary for any such fund of an MNE employer that includes employees in the fund from the many different countries in which it operates.

We are not aware of the extent of union based funds that include union members from multiple countries, but if there are any such vehicles, they would simply not have the resources for the information gathering and analysis to attempt meeting this 90% test.

Rather than forcing a 90% rate (or whatever rate the two contracting states agree to) when the basic 50% rule cannot be met, perhaps a better approach would be to allow treaty benefits under the LOB rule but only to the extent that a pension fund can demonstrate that its membership does qualify under Conditions A and B.

For example, if a pension fund can only show the two conditions are met for 40% of the fund members, then 40% of the relevant income would receive treaty benefits and 60% of the
income would be fully taxed under the domestic law of the source contracting state. This seems economically fairer and leaves the pension fund to decide how much effort to make to establish qualification for treaty benefits.

In order to avoid trying to micro-manage how pension funds should operate, if this suggested alternative approach is adopted, we suggest that there be no requirement for pension funds to track the treaty benefits to the qualifying fund members. Accordingly, funds could choose to either track such benefits causing qualifying members to receive higher benefits or benefit all fund members equally for any allowed treaty benefits.

6. Issues related to the derivative benefits provision

Given the intent of Proposal 1 to allow a source country to apply its domestic law when a taxpayer resident in the other contracting state is subject to a special tax regime in that state, this Proposal 1 should apply as well to provisions in the treaty governing business profits (including the definition of permanent establishment), dividends, and capital gains.

Regarding Proposal 2 (new general treaty rule intended to make a tax treaty responsive to certain future changes in a country’s domestic tax laws), since the domestic law changes contemplated must apply to substantially all foreign source income, the elimination of source country benefits must also be applied to the Article 5 definition of permanent establishment (PE). The source contracting state domestic definition should apply unless prior to the change the country of residence did not tax its residents on the income of foreign PEs.

Despite this change to Article 5, it seems sensible to leave Article 7 in place to have agreement between the contracting states on how income of the PE will be calculated. Of course, it should be made clear that the reference in Article 7 to a PE would be treated as a reference to a PE or whatever concept or term is used under domestic law (e.g. ‘Engaged in a Trade or Business in’ the country concerned).

10. Clarification of the ‘active business’ provision

Paragraph 72 amends Paragraph 3 of the LOB rule with subparagraph b) reading as follows. The one change is in bold.

If a resident of a Contracting State derives an item of income from a trade or business activity conducted by that resident in the other Contracting State, or derives an item of income arising in the other Contracting State from a related person, the conditions described in subparagraph a) of this paragraph shall be considered to be satisfied with respect to such item only if the trade or business activity carried on by the resident in the first-mentioned Contracting State is substantial in relation to the trade or business activity carried on by the resident or a related person in the other Contracting State. ... The added ‘a’ should be changed to read ‘the’ to clearly indicate that the related person from which the resident is receiving income is the same related person that is carrying on a trade or business in the other Contracting State. As the provision reads now, the related person from which the resident is receiving income could be a different related person from the related person that is carrying on a trade or business in the other Contracting State.

15. Whether some form of discretionary relief should be provided under the PPT rule

New paragraph 8 sets out a procedure under which certain reduced treaty benefits would be provided following a disallowance of treaty benefits under the PPT rule. The first sentence of the new paragraph reads as follows:

8. Where a benefit under this Convention is denied to a person under paragraph 7, the competent authority of the Contracting State that would otherwise have granted this
benefit shall nevertheless treat that person as being entitled to this benefit, or to
different benefits with respect to a specific item of income or capital, if such
competent authority, upon request from that person and after consideration of the
relevant facts and circumstances, determines that such benefits would have been
granted to that person in the absence of the transaction or arrangement referred to in
paragraph 7.

We are very concerned about this paragraph because it will have the counterproductive effect
of actually encouraging continued treaty abusive behaviour. This is because taxpayers will
see that they will be no worse off if their abusive treaty planning is disallowed than they
would have been had they not conducted the abusive planning. We recommend the following
amended wording for paragraph 8:

8. Where a benefit under this Convention is denied to a person under paragraph 7, the
competent authority of the Contracting State that would otherwise have granted this
benefit shall nevertheless consider treating that person as being entitled to this benefit,
or to different benefits with respect to a specific item of income or capital, if such
competent authority, upon request from that person and after consideration of the
relevant facts and circumstances, in its discretion, determines that such benefits
should be granted to that person on the basis that the transaction or arrangement
referred to in paragraph 7 had not occurred.

This new wording makes it clear that the decision to grant or not grant the relevant benefits is
at the discretion of the competent authority.

Discretion was discussed in paragraph 17 of the Commentary as follows:
The determination that benefits would have been granted in the absence of the
transaction or arrangement referred to in paragraph 7 and the determination of the
benefits that should be granted are matters that are left to the discretion of the
competent authority to which the request is made. The paragraph grants broad
discretion to the competent authority for the purposes of these determinations.

This ‘discretion’, though, is not discretion regarding whether to grant any benefits, but only
as to how the benefits will be calculated.

Appropriate changes to reflect this changed language in paragraph 8 should be made to
paragraph 16 in the Commentary. We suggest the following language for paragraph 16:

16. Paragraph 8 provides that where a person is denied a treaty benefit in accordance
with paragraph 7, the competent authority of the Contracting State that would
otherwise have granted this benefit shall nevertheless consider treating that person as
being entitled to this benefit, or to different benefits with respect to the relevant item
of income or capital, if such competent authority, upon request from that person and
after consideration of the relevant facts and circumstances, in its discretion,
determines that such benefits should be granted to that person on the basis that the
transaction or arrangement referred to in paragraph 7 had not occurred. In making his
determination, the competent authority may take into account all facts and
circumstances including the intentions of the person in entering into the transaction or
arrangement referred to in paragraph 7.

The newly drafted Commentary provides the following example:

18. The following example illustrates the application of the paragraph. Assume, for
example, that an individual who is a resident of State R and who owns shares in a
company resident of State S assigns the right to receive dividends declared by that
company to another company resident of State R which owns more than 10 per cent of the capital of the paying company for the principal purpose of obtaining the reduced rate of source taxation provided for in subparagraph a) of paragraph 2 of Article 10. In such a case, if it is determined that the benefit of that subparagraph should be denied pursuant to paragraph 7, the competent authority of State S shall, under paragraph 8, grant the benefit of the reduced rate provided for in subparagraph b) of paragraph 2 of Article 10 if it determines that such benefit would have been granted in the absence of the assignment to another company of the right to receive dividends.

To provide useful and appropriate guidance in light of the changed wording in paragraph 8, this example needs to be expanded, otherwise the message being provided to governments and taxpayers alike is very counterproductive and would only encourage BEPS behaviour.

We suggest the following amended language for Paragraph 18:

18. The following example illustrates the application of the paragraph. Assume, for example, that an individual who is a resident of State R and who owns shares in a company resident of State S assigns the right to receive dividends declared by that company to another company resident of State R which owns more than 10 per cent of the capital of the paying company. One of the principal purposes of making the assignment was obtaining the reduced rate of source taxation provided for in subparagraph a) of paragraph 2 of Article 10. In such a case, if it is determined that the benefit of that subparagraph should be denied pursuant to paragraph 7, the competent authority of State S shall, under paragraph 8, consider any request made by the individual that the competent authority grant the benefit of the reduced rate provided for in subparagraph b) of paragraph 2 of Article 10. Upon receiving such a request, the competent authority would examine all the facts and circumstances. In doing so, the competent authority would determine whether there were any compelling non-tax principal purposes that would have made the assignment worth executing even in the absence of the requested tax benefit (in this case the lower level of dividend withholding tax). If the competent authority determines that such compelling principal purposes exist, then it can choose to grant the benefit that would have been granted in the absence of the assignment to another company of the right to receive dividends. If the competent authority determines that no such compelling principal purposes exist, then no benefit would be granted under the treaty.

This amended wording makes clear that abusive arrangements will be treated in a manner that makes them worse off than if they had not conducted the abusive planning.

16. Drafting of the alternative ‘conduit-PPT rule’

Example C reads, in part:

TCO later realises that it can avoid the withholding tax on interest levied by State S by assigning the note to its wholly-owned subsidiary RCO, a resident of State R (the treaty between States R and S does not allow source taxation of interest in certain circumstances).

Such an assignment of an existing loan is at the extreme of black and white situations where a conduit arrangement exists. A somewhat more nuanced example would be more instructive and provide better guidance to tax authorities and taxpayers. Further the use of such an extreme black and white example give aggressive taxpayers the ability to argue that any arrangement that is not so black and white as Example C should qualify as not being a conduit.
The following amends Example C to attempt to provide such a more nuanced example.

Example C: TCO, a company resident of State T, which does not have a tax treaty with State S, wholly owns SCO, a company resident of State S, and RCO, a company resident of State R. All three companies conduct active businesses. SCO needs to raise 1,000,000 for use in its business. TCO is aware that the lack of a T-S tax treaty means that interest paid by SCO to TCO would be subject to State S's high level of withholding tax. To avoid this result by making use of a favourable R-S tax treaty which does not allow source taxation of interest in certain circumstances, TCO lends 1,100,000 to RCO under a note at 6 per cent interest and RCO lends 1,000,000 under a note to SCO a month later at 7 per cent.

The transaction in which TCO routed funds through a back-to-back loan through RCO to SCO constitutes a conduit arrangement because it was structured to eliminate the withholding tax that TCO would otherwise have paid to State S.

Example F involves what is clearly a back-to-back loan from a parent company to a subsidiary company through a group finance company. The regular business of the group finance subsidiary is to coordinate the financing of the parent company and all subsidiaries. The example makes clear that the group finance company conducts its group financing activities in an active manner through its own personnel.

Example F's conclusion includes:

Based on these facts and in the absence of other facts that would indicate that one of the principal purposes for these loans was the avoidance of withholding tax in State S, the loan from TCO to RCO and the loan from RCO to SCO do not constitute a conduit arrangement.

We believe that the conclusion for this Example F is incorrect and misleading. We suggest the following more nuanced conclusion:

In this example, RCO appears to be carrying on a real business performing substantive economic functions, using real assets and assuming real risks; it is also performing significant activities with respect to the transactions with TCO and SCO, which appear to be typical of RCO’s normal treasury business. RCO also appears to be bearing the interest rate and currency risk. Based on these facts, TCO intended and directed that its 15,000,000 in currency A lent to RCO would be on-lent by RCO to SCO in currency B with RCO managing the relevant interest rate and currency risks through forward contracts. As such, this constitutes a conduit arrangement. On the other hand, if TCO had transferred excess funds to RCO as a loan prior to any specific need by SCO, and RCO later lent required funds to SCO, then in the absence of other facts that would indicate that one of the principal purposes for these loans was the avoidance of withholding tax in State S, the loan from TCO to RCO and the loan from RCO to SCO do not constitute a conduit arrangement.

17. List of examples in the Commentary on the PPT rule

We believe that the examples added to Paragraph 14 are an excellent addition.

We suggest the following could be added at the end of Example H to provide further useful guidance:

On the other hand, if TCO supplied to RCO a substantial portion of the additional capital necessary for RCO's capitalization of SCO, and/or if this indirect ownership of
a subsidiary was an anomaly with respect to the TCO group's organizational structure, then Paragraph 7 would apply to these transactions.

19. The design and drafting of the rule applicable to permanent establishments located in third States

The bracketed 60% is simply too low to prevent BEPS focused structuring. We suggest that the bracketed amount be no less than 90%.

By using a low bracketed percentage such as 60%, the rules are merely giving a little guidance to aggressive MNEs and other taxpayers that they should continue to shift profits, ‘but please don’t be quite so greedy’.
Dear Marlies,

Please find below BIAC’s comments on the OECD Revised Discussion Draft on BEPS Action 6: Preventing Treaty Abuse, issued on 22 May 2015 (the “RDD”).

BIAC continues to support the BEPS project to target clear instances of abuse, including in relation to tax treaties, and welcomes the OECD’s work to improve international tax principles and to better align the taxation of profits with substance. However, to ensure that the project is successful, adequate time must be dedicated to developing rules – and refining their complexity – so that they can be objectively and consistently implemented, and consequently stand the test of time.

In relation to this last point, while we are supportive of any necessary changes to prevent Treaty abuse, we do feel it would be advantageous to governments as well as taxpayers to acknowledge that additional time is still needed before the project is “closed”. There are three reasons for this:

- Some important concerns stated in earlier BIAC comments, have yet to be fully addressed.
- There are new proposals appearing in the RDD for the first time, too late in this final phase for proper comment and consideration by business.
- Most importantly, several of the proposals currently allow for unilateral disallowance of treaty benefits by a single treaty partner. This seems inappropriate in a process that is meant to drive towards international consensus and practice, rather than unilateral action.

We hope that you find our comments useful. And, as always, we would also be happy to help in any way that we can to refine these proposals in order to renew the confidence of governments in the modern Tax Treaty system. Tax Treaties have played a critical role in facilitating cross-border trade and investment – and spurring growth and jobs – over more than 50 years, and anything that diminishes their effectiveness is a detriment to us all.

Sincerely,

Will Morris, Chair
BIAC Tax Committee
BIAC Consensus High-Level Observations on the Revised Discussion
Draft 22 May 2015 - 17 June 2015

Procedural

1. BIAC continues to support a common OECD framework to address Treaty Abuse issues. Treaties are principally designed to remove the barrier of double taxation to promote cross-border trade and investment. They are bilateral arrangements entered into by States to determine the agreed allocation of taxing rights. The unilateral denial of Treaty benefits based on subjective criteria should not only cause concern to taxpayers, but for governments too, as taxing rights may be unexpectedly usurped. The value of Treaties is significantly reduced if their application becomes less certain.

2. We recommend again, as a point of policy, that the OECD focus on aligning Treaty Abuse discussions with other BEPS actions, such as the work on Hybrid Mismatches. Many of the concerns identified in the RDD may fall away when other BEPS recommendations are adopted - allowing the Treaty Abuse work to focus on situations where Treaty benefits are claimed in inappropriate circumstances, rather than trying to use Treaties as a tool to tackle perceived avoidance, which should be addressed through domestic legislation.

3. The RDD addresses various concerns raised by Commentators. The RDD contains issues that broadly fall into three categories:

   a. No conclusion reached, to be discussed further at the June meeting of Working Party 1 (“WP1”);

   b. Conclusion proposed on way forward, but without addressing business issues raised; and

   c. New points, proposed for the first time.

In relation to category a), we would like to draw your attention to the previous detailed responses provided on 9 April 2014 and 9 January 2015, which we trust will be of assistance in preparing for the June meeting of WP1.

Regarding category b), we are concerned that the issues previously raised by BIAC have largely not been addressed. We appreciate that the OECD will have considered these issues, but the reasoning for not addressing those issues is largely unclear. There is also no clear indication as to how the OECD proposes to ensure that, as the proposals are implemented in practice, the Treaty benefits are still available, and genuine business concerns are fully addressed. Rather than repeat all of our concerns in detail, we have set out below the key issues, which we would urge the OECD to reconsider in the context of tackling avoidance through aligned domestic legislation, rather than using Tax Treaties as a tool for revenue raising. Using Treaties as a tool to generate additional tax, risks damaging international investment, and undermining the valuable work of the OECD over the recent years promoting cross-border trade and investment.

With respect to category c), we are alarmed that two significant proposals were included in the RDD, especially, since comments should be kept short and no public consultation will be held. We have commented further below on these two issues.
4. Overall, we have significant concerns about the direction of the various BEPS recommendations, including those made by Action 6. Those concerns relate to:
   a. coherence with other Action Items;
   b. the use of Treaties as a tool to raise revenue, when the perceived underlying avoidance is best addressed through domestic legislation;
   c. the lack of clarity over why business concerns have not been addressed; and
   d. the insertion of significant new proposals at such a late stage; and
   e. clarity as to how it is expected to allow flexibility for different intentions and aims of States, to be incorporated into a Multilateral Instrument.

Clarity, Certainty and Dispute resolution
5. Specifically, in relation to providing the necessary clarity and legal certainty of treatment for taxpayers’ investments, Action 6 should make it clear that taxpayers must have the opportunity to seek pre-clearance regarding access to treaty benefits.

6. Furthermore, there should be unobstructed access to a mutual agreement procedure (MAP) and mandatory binding arbitration, to ensure the Treaty is being applied to residents as intended by the relevant States when entering into the Treaty.

7. Finally, although we welcome the additional guidance offered by the RDD, we also request that the proposals (including proposed changes to the Commentary) provide further appropriately detailed examples, as guidance on the application of both the proposed LOB and PPT rules, where currently there remains significant lack of clarity.

8. As the proposals do not yet meet these three conditions, it will be extremely difficult to determine with an appropriate degree of certainty, whether reduced withholding rates may apply under a certain treaty.

Brief High-Level Comments on Specific Proposals
9. **Funds.** We welcome the proposals on CIVs. We note the non-CIV funds considerations are ongoing, and would draw your attention to our previous submissions on this topic.

10. **The current PPT test.** The Principal Purpose Test ("PPT") test ("one of the principal purposes") remains widely framed. Whilst we welcome the additional examples in the Commentary, and the recommendation to form an advisory panel, there remains a risk of misinterpretation or misapplication by tax authorities. Also, the various technical examples provided on the working of the PPT rule effectively show the difficulty that taxpayers will have in proving the requisite facts to prevent denial of treaty benefits. We continue to encourage a focus on substance. We would recommend that:
   a. if two tax authorities have differing views, there should be a *prima facie* assumption that it is *not* reasonable to conclude that obtaining treaty benefits was one of the principal purposes; and
   b. a clear recommendation should be made that disputes under the PPT rule will be rectified by mandatory arbitration. Currently, paragraph 82 of the RDD simply proposes to leave such considerations to work under Action 14.
11. **Publicly listed companies.** The issues highlighted in paragraph 63 of the RDD, and commented on in previous submissions, remain a concern. Whilst the OECD notes that listed entities are unlikely to be used for tax avoidance, no changes have been made to reflect that. Although the guidance provided in paragraph 67, as to what may be considered to constitute a recognised stock exchange, may be of assistance, it does not address the concerns outlined in paragraph 63. We recommend the simplified Limitation On Benefits (“LOB”) rule to be applied to publicly listed entities (as drafted in paragraph 3 of the RDD), and that any (extremely rare instances of) avoidance encountered are addressed through the PPT rule.

Paragraph 46, which primarily aims to address concerns on the simplified LOB, seems to result in denial of benefits unless the listed entity is resident in the same territory as the entity seeking Treaty benefits. This seems overly restrictive, and we would recommend withdrawing the changes proposed in paragraph 46. We note the OECD’s concern that a tax haven could be inserted in the ownership chain, but the changes proposed to paragraph 46 do not address this concern in cases where a publicly listed entity is resident in the same territory as the entity seeking Treaty benefits. In addition, such concerns over a tax haven being inserted should, in any case, be caught more appropriately by the PPT (or the “anti-conduit” version of the PPT). Therefore, paragraph 46 seems unnecessary and creates further restrictions on genuine business situations.

12. **Intermediary Companies.** The RDD notes that requiring every intermediary entity to be a resident of the contracting state was unduly restrictive. However, no position is taken on the issue, deferring this until the June meeting. We would draw attention to our previous submissions, with detailed worked examples, together with our specific observations in relation to Publicly Listed entities above. We strongly recommend that the requirement to consider all intermediary companies be removed as being unnecessary, time consuming, and overly restrictive.

13. **Active Business Test.** The RDD acknowledges previous comments regarding headquarters companies and holding companies. However, the RDD fails to address the issue either positively or negatively. The RDD also does not address situations of mixed active and investment income. We encourage clarification on both of these issues in a way that ensures treaty benefits will be granted to bona fide business activities. In particular, we are concerned over the possible inconsistency between the LOB and the PPT. Examples G and H provided in the Commentary to the PPT seem effectively to state that treaty benefits should be granted to companies that perform regional headquarters operations in one way or another. If this understanding is correct, it is counterintuitive for the LOB not to grant treaty benefits to a regional headquarters.

Finally, the RDD adds two new proposals to the deemed activities section. The first is the special tax regime (which is addressed in more detail below), and the second is that a connected party needs to be in the “same or similar” line of business. This requirement is ambiguous and unclear how it ties to the “in connection or incidental to” test that establishes the necessary relationships between the related businesses. The current Active Business test is longstanding and well understood. We would draw your attention to our previous detailed submissions on this topic.

14. **Derivative Benefits.** The RDD acknowledges the key comments presented to the OECD but again fails to address them. These issues remain of great concern to business, and we encourage the OECD to give them due consideration. We are happy to discuss the
comments already provided if that would be of assistance, in advance of the June WP1 meeting.

Of equally great concern, is the addition of two new concepts at such a late stage in the process:

a. The “special tax regime”; and

b. Changes to Treaty partner’s domestic law.

The “special tax regime” would apply if a person attracts special tax treatment (either through rate or tax base), with the proposed result that they should receive no derivative benefits. It is considered that States should assess such risks and special regimes before entering into a bilateral Treaty. We believe that issues relating to “special tax regimes” are best addressed through the OECD’s work on Harmful Tax Practices. We note too, that in relation to interest payments for example, in addition to potential disallowances as a result of Action 4, the proposals under Action 6 may create further restrictions, and this is once again effectively endorsing the use of Tax Treaties as a tool for revenue raising. Again, avoidance is best addressed through coordinated domestic legislation, and Treaties should remain focused on enhancing international trade by removing double taxation. We strongly recommend that this late addition be removed, and any concerns over such tax regimes be addressed more appropriately outside Action 6.

The second new addition would result in a unilateral and automatic denial of treaty benefits if there is a subsequent change in domestic legislation, exempting “substantially all” foreign source income. It is inappropriate to have automatic and unilateral denial of treaty benefits, which creates uncertainty for all taxpayers. It is not only undesirable, but in some States, such a trigger to remove intended Treaty benefits may require ratification. The preferred solution would be to renegotiate the Treaty where there is a concern over changes in domestic law of the Treaty partner.

15. **LOB Discretionary Relief.** The RDD notes in paragraph 28 some of the comments provided by business, but does not explain why disregarding those comments is consistent with the aim of Action 6. Clarification as to why those comments have not been addressed would be constructive, and would provide a better understanding on the future interpretation of the proposals. We draw your attention finally to our related comments in previous submissions.

The RDD proposes in paragraph 32 that as long as a competent authority has properly exercised the discretion granted by the discretionary relief provision of the LOB rule, that provision has been complied with and it cannot, therefore, be argued that taxation is not in accordance with the provisions of the Convention. This seems to be intended to deny a taxpayer the possibility to invoke MAP regarding this decision. This seems unfair as MAP typically will involve both contracting states, whereas the residence country competent authority may not have been involved in a denied request under the discretionary relief provision. We therefore request that the related changes in the Commentary on paragraph 5 of the LOB rule (i.e. paragraph 65) as proposed in paragraph 32 of the Draft, be reconsidered.

16. **Tie-breaker rule.** We note that the RDD highlights the key concerns that competent authorities should be obliged to determine the State of residency within a fixed timeframe and that failure to do so should result in MAP arbitration. The RDD reduces “required” to “encourages”; a “fixed timeframe” to “as quickly as possible”; and, by omission, appears to decline from according the protection of MAP arbitration. These are genuine – and growing
– business concerns over commercial structures, and we encourage the OECD to reconsider the above points, together with our previous submissions. Again, we advocate the continued use of the effective place of management tie-breaker.

17. We note again that there will be a significant increase on the resource requirement of Competent Authorities, and we have a concern over the responsiveness, clarity and certainty of treatment as a result. We recommend that increased reliance on Competent Authority procedures be backed by a corresponding increase in the availability of appropriately trained and experienced Tax Authority resources for such procedures. Enhanced dispute resolution mechanisms, including mandatory arbitration, should also be fully coordinated with, and addressed in, Action 14.
Dear Ms. de Ruiter,

Thank you for the possibility to submit comments on the revised discussion draft on Action 6 "Preventing the granting of treaty benefits in inappropriate circumstances" of the BEPS Action Plan (the "Discussion Draft"). As a tax law student from Leiden University, I am writing my thesis on the proposed LOB-clause in the Discussion Draft. By submitting my comments on the new discussion draft I hope to bring to the attention a few aspects which, in my view, require further attention before the release of the final report on BEPS Action point 6 in September 2015.

First, I would like to welcome the alternative simplified LOB rule and the direction that is taken by focusing on the underlying general principles of the different tests in the LOB rule, rather than focusing on the technical aspects of the LOB rule. The possibility for states to implement the simplified LOB rule in combination with the principle purpose test is a welcome development and should contribute to global implementation of the rule. A few issues I would like to point out are as follows.

1. Further attention to possible conflicts with EU law has to be paid. The revised discussion draft acknowledges that a lot of commentators expressed their concerns regarding the possible conflicts with EU law (p. 34), but in my opinion several conflicts do remain and need further guidance in the commentary for EU member states. The problem of the intermediate owner requirement is not explicitly solved, an aspect which needs further attention in the June 2015 meeting. If a Dutch NV (NV 1), listed at the AEX Stock Exchange, holds a US entity via Dutch BV2 and Dutch BV3, Dutch NV1 would be a qualified person and able to claim a reduction in withholding tax distributed on dividends paid from the US entity to Dutch BV 3. If the same Dutch NV1, holds a US entity via a Spanish entity and Dutch BV2, it would not be a qualified person, because of the intermediate owner requirement. In my opinion, this is a restriction of the freedom of establishment which cannot be justified.
2. Paragraph 2, subparagraph e of the simplified LOB rule, might be in breach with the fundamental freedoms of the European Union, and attention to this matter has to be paid. In my opinion it is in breach with the fundamental right of free movement that a Dutch individual who holds all of the shares in a Dutch BV, who in turn holds all of the shares in a US entity does qualify for a reduction of withholding tax on dividends distributed by the US entity to the Dutch BV, whereas the same Dutch BV controlled by a Spanish individual would not. As the European Court of Justice already ruled in the Open-Skies cases (i.e. C-466/98), this difference in treatment is unlawful. The ACT GLO case (C-374/04) does not allow for such a restriction, as the LOB rule in question was part of a dividend article which allocated taxing rights between member states in a coherent matter. The simplified LOB rule has an anti-treaty shopping purpose and does not affect the allocation of taxing rights, and should therefore comply with European Case Law on the subject of anti-abuse rules, such as formulated in the Cadbury Schweppes case (C-169/04). Further attention to this case law would be welcomed in the final report on action 6, in order to give guidance to EU member states who want to comply with the obligations resulting from their EU-membership.

3. The simplified LOB rule does not mention when the resident should be a qualified person in paragraph 1, where the ‘complex LOB rule’ mentions that a person needs to qualify at the time a benefit is granted. In my opinion this addition should also be added to the simplified LOB rule, as omitting this phrase leads to uncertainty. This issue is further discussed in paragraph 62, but leaving these issues to be dealt with by the competent authorities only leads to increased uncertainty.

I am looking forward to the release of the definitive rapport on action 6 in September 2015. I greatly welcome the approach taken in the new discussion draft and I hope further attention is paid to possible conflicts with EU law. As the LOB rule is mainly based on the US rule and thus on the underlying US treaty policy, it is helpful to develop generally accepted principles which form the underlying basis for the rule. In the BEPS context the LOB rule should function as an anti-abuse rule, where the US LOB rule basically allocates taxing rights based on economic nexus, which is a treaty policy a lot of states do not follow and - in my opinion - should not wish to follow.

Yours sincerely,

Tim Bijman
Student Tax Law at Leiden University, the Netherlands
Montreal, June 12 2015

Ms. Marlies De Ruiter,
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division
OECD/CTPA
Organisation for Economic Co-operation and Development
2, rue André Pascal
Paris, France
75116

Dear Ms. De Ruiter,

Re: Comments on the OECD Discussion Draft with respect to BEPS Action 6: Prevent treaty abuse ("Discussion Draft").

Please find below Bombardier’s response to the OECD’s Invitation to Comment on the Discussion Draft relating to Action 6 on preventing treaty abuse.

We welcome the opportunity to provide our experiences and share specific examples regarding this relevant issue. We would also welcome the opportunity to provide further insight on these issues at your request.

By way of background, Bombardier is the world’s largest manufacturer of both planes and trains. Looking far ahead while delivering today, Bombardier is evolving mobility worldwide by answering the call for more efficient, sustainable and enjoyable modes of transportation everywhere. Our vehicles, services and, most of all, our employees are what make us a global leader in transportation. Bombardier is headquartered in Montréal, Canada. Our shares are traded on the Toronto Stock Exchange (BBD) and we are listed on the Dow Jones Sustainability World and North America Indexes. In the fiscal year ended December 31, 2014, we generated aggregate gross revenues of $20 billion US.
Issue related to the LOB Provision

One very important item missing in the Discussion Draft is the consideration of substance/business activities of group companies located in the same jurisdiction. Very often, for legal, commercial or other business reasons, a multinational company organizes its legal structure in a way that not all the substance/business activities in a given jurisdiction are regrouped under the same legal entity. Same principle applies with regards to shareholdings in different foreign subsidiaries which are often owned and held by a distinct legal entity. Therefore, a given Holdco in a given jurisdiction should not be penalized if the substance in that given jurisdiction is owned/carried-on by distinct legal entities that are part of the same group, especially where such segregation of commercial activities and/or shareholdings is explained by non-tax reasons.

We hope the OECD will consider the above comments, which are aimed at helping the OECD, tax authorities and other stakeholders tailor the recommendations in development under Action 6 to the BEPS objectives targeted within the overall OECD project.

Best regards,

[Signature]

Pierre Lafontaine
Vice President, Taxation
Bombardier Inc.
Dear Sirs

Re: BVCA response to revised discussion draft on BEPS Action 6: Preventing treaty abuse

Introduction

I am writing to you on behalf of the British Private Equity and Venture Capital Association (the “BVCA”), which is the industry body and public policy advocate for the private equity and venture capital industry in the UK. With a membership of over 500 firms, the BVCA represents the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers. Our members have invested £30 billion in over 3,900 UK-based companies over the last five years. Companies backed by private equity and venture capital in the UK employ around 790,000 people and almost 90% of UK investments in 2013 were directed at small and medium-sized businesses.

The discussion draft

We are pleased that the discussion draft, the third issued so far in relation to Action 6, recognises the importance of non-CIV funds to the global economy. With this letter we have responded to each of the discussion drafts and also attended the meeting in January. It is clear from the discussion draft that significant effort is still required in order to finalise the work, highlighted by the fact that the discussion draft is not a consensus document. We remain committed to working with the OECD to provide insight into the private equity investment model, in order that the OECD can achieve its aims under Action 6 without doing disproportionate harm to the private equity funds market.

We remain concerned that if a workable solution cannot be found for the issues related to treaty access for non-CIV funds then it may well result in a reduction in i) returns for the investors in such funds; and ii) the availability of finance for businesses across the world. With pension funds being a key investor group and private equity contributing to the development of businesses, the detrimental impact on the real economy and individuals would be significant. With this in mind we note that the Working Party considers that the suggestions made by the BVCA and others in response to the previous discussion draft and also those made at the January meeting did not sufficiently take account of treaty shopping concerns. We understand that these concerns are twofold: i) that non-CIVs may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits and ii) that investors may defer recognition of income on which treaty benefits have been granted (which is, of course, not a treaty concern).

These two concerns are misplaced in the context of private equity funds for reasons explained previously and reiterated below. Should these concerns persist following the responses to the
current discussion draft then we would welcome an opportunity to discuss with the OECD the
course of their concerns and the reasons why previous responses – both in respect of explaining
why the concerns may be misplaced and also suggesting ways forward – have not been accepted,
as without this insight it is difficult to make proposals which the Working Party could accept.
Taking the two concerns separately:

**Non-CIVs may be used to provide treaty benefits to investors that are not themselves entitled to
treaty benefits**

- Private equity funds are closed ended investment vehicles formed for the purpose of
  investing in, broadly, unlisted securities in operating businesses. They are not formed for
  the purpose of delivering treaty benefits or any other form of tax avoidance. Indeed the
  constitutional documents of private equity funds prevent the manager from acting in a
  way which would favour one investor over another. However, that said, private equity
  funds do invest via intermediate holding companies but this is not purely for tax
  avoidance purposes. Instead, holding companies are used for a variety of commercial,
  legal and tax reasons including facilitating third party leverage, co-investment,
  management incentivisation, administrative convenience and consistency, and legal
  liability protection. In considering the location of such companies tax is of course
  considered, as it would be for any other business, but this does not mean that the use of a
  holding company indicates treaty abuse.

As set out in our January 2015 submission, the vast majority of investment into private
equity funds comes from investors who would generally be able to avail themselves of the
benefits of tax treaties entered into by their jurisdictions of residence, including pension
funds, sovereign wealth funds and high net worth individuals. Moreover, at present the
majority of investment in private equity funds is generally derived from jurisdictions with
wide treaty networks including the United States, the United Kingdom, Germany and
Canada.

- Private equity funds are subject to significant regulation as well as commercial and
  reputational pressure. They do not operate in an environment which would facilitate
  these arrangements to be marketed for the purpose of tax avoidance.

- As discussed in our January 2015 submission, the commercial and regulatory environment
  in which private equity funds operate means that in some respects they are no different
to CIV funds (in the sense that their managers are regulated and the funds are diversely
held); fund managers already comply with extensive requirements under anti-money
laundering and know your client procedures, and have extensive reporting obligations
under FATCA and similar regimes such as the Common Reporting Standard.

**Investors may defer recognition of income on which treaty benefits have been granted.**

- Private equity funds are generally structured both legally and commercially to ensure that
  cash from distributions and exit proceeds received by the fund is distributed to investors
  as soon as practically possible. Typically there are very limited circumstances in which a
  fund can re-invest proceeds from the disposal of an investment, and these will be defined
  in the fund documentation. There may be no ability to re-invest proceeds at all.
In addition to the protections afforded by the fund documentation, two related commercial features of private equity further highlight that funds are simply not designed to defer cash distribution. Firstly, investors will measure the performance of a fund (and allocate capital to subsequent funds) based on an internal rate of return calculation. Secondly, the carried interest model which incentivises the fund executives, is calculated on an internal rate of return basis. Together these are compelling reasons why a fund manager would not seek to defer the return of cash to investors.

Beyond the reasons above, the nature of the investors into private equity funds – being largely pension funds and similar institutions – means that investors do not need to leverage their investments. As a result they have no requirement for regular distributions with which to service debt.

Whether investors recognise income which is distributed to them is not within the control of the fund and should not be a relevant consideration in this discussion. It is not a treaty abuse issue. However, it is relevant to note that the vast majority of investment into private equity funds is ultimately sourced from pension funds, sovereign wealth funds and similar institutions which are typically exempt from tax, and for whom, therefore, deferral should not be a relevant concern.

**LOB and alternative simplified LOB**

The May discussion draft presents an alternative simplified LOB rule intended to be used in conjunction with the PPT. The alternative LOB rule includes an expanded derivative benefits provision which allows entitlement to treaty benefits to a non-qualified person whose direct or indirect owners are made up of more than 75% ‘equivalent beneficiaries’ (broadly individuals or entities who themselves would have access to the relevant treaty if participating in the relevant relationship directly).

While we welcome the broadening of the LOB concept, as currently drafted it does little to address our concerns around treaty access for non-CIV funds. Our fundamental concern is that the rules create a situation whereby it is no longer commercially sensible for a treaty qualified investor to make an investment through a private equity fund compared to making that same investment directly. Such a situation could well arise either where i) investing through a fund leads to that investor suffering foreign tax they would not otherwise have suffered, ii) there is uncertainty as to whether its share of investment returns should be subject to foreign tax or iii) where the investor’s share of fund running costs is large enough to offset the benefits of investing in a managed vehicle.

As discussed below, the structure of the simplified LOB rule along with inherent practical difficulties in determining whether it is applicable mean that as currently drafted there is a risk that each of i) to iii) above will be realised.

**Structure of the rule**

The strict ‘in or out’ nature of the expanded derivative benefits provision means that it is possible that a treaty qualified investor investing through a fund could suffer foreign tax on investment returns from an underlying asset by virtue of the fund being made up of 75% or less equivalent beneficiaries. If such an investor were eligible for treaty benefits on a direct investment in the
same asset then they are arguably putting themselves in a worse position by pooling capital through the fund to make that investment.

As it stands it would be difficult both from a constitutional and practical standpoint for the funds industry to solve this problem structurally by say segregating classes of investors into different vehicles depending upon their treaty status e.g. by grouping ‘good’ treaty investors in one vehicle and ‘bad’ treaty investors in another. Private equity funds often invest across a range of geographies and in a mix of assets (equity, loan notes, etc) potentially giving rise to numerous treaty qualification permutations across the investor base. In such a scenario there is no such thing as a ‘good’ treaty investor thus making it practically impossible for the fund manager to offer a product which gives investors any certainty that their foreign taxation position is in line with what it would have been had they invested directly, or indeed any degree of certainty on their foreign tax position generally.

**Practical issues**

The simplified LOB rule would create numerous practical challenges for private equity funds as explained below:

- Private equity funds typically have a wide investor base with many of the ultimate beneficiaries of returns participating in the fund through other fund or pooling vehicles.

- While private equity funds collect and retain information on entities which invest directly in the fund it will generally be unlikely that they will know about changes in the ultimate investor base of say a fund of fund investor (as they, rather than the private equity fund, will have to comply with the know your client and anti-money laundering obligations).

  Identifying the ultimate beneficial owners of interests in a private equity fund would require a level of inquiry which is beyond that required by other regimes which seek to identify beneficial owners of income (for example under FATCA a fund is generally not required to collect information on the beneficial owners of an investor fund). Further, it will be the case with many funds that their constitutional documents mean they have no legal right to request such information.

- For many funds even if it were possible to access the required information, the collection and analysis process would be an extremely costly task. Where these costs are passed on to investors it will increase the cost of pooling capital making investment in a fund less attractive.

We note the comment made during the OECD Webex of Monday 8 June that adoption of the TRACE package for CIV funds would go some way to addressing the issues around treaty access for non-CIV funds. We are concerned that the TRACE package was developed with no consideration given to non-CIV funds (as they were defined as being out of scope). Furthermore, a significant difference between the CIV and non-CIV fund markets is the role of the intermediaries which would operate the TRACE package in a CIV fund context; private equity funds do not commonly use intermediaries and to require them now to do so with no commercial benefit would increase costs and decrease returns for investors. It is not clear to us that this would be proportionate, given that no evidence of treaty abuse by non-CIV funds has been presented.
Given all of the above we reiterate the recommendation made in our January submission that private equity/non-CIV funds should be explicitly excluded from the LOB work under Action 6 such that their ability to access treaty benefits is not compromised. If this is unacceptable, then we recommend that further consideration is given to our alternative proposal that the definition of qualified person is expanded to include non-CIV funds meeting certain conditions which could be demonstrated by the fund manager using information already under their control, so as to not increase costs for investors. In the meantime we would request that the OECD makes a clear recommendation that treaty access for private equity funds is in principle to be maintained until the conclusion of the further work contemplated by paragraph 24 of the document.

PPT

The BVCA broadly supports the concept of a PPT as a workable approach to addressing treaty abuse concerns. However, the formulation of the draft PPT will exacerbate an existing barrier to international investment, being the lack of consistency between how individual jurisdictions apply treaty provisions in practice, a problem frequently encountered by private equity funds. This risk of inconsistency is further highlighted by the fact that the discussion draft is not, at this late stage, a consensus paper; treaty access is clearly a complex issue which invokes a range of different perspectives amongst stakeholders. Given that one of the objectives of the OECD is to promote consistency between jurisdictions we consider that an objective of the Action 6 work ought to be to minimise inconsistency, in the sense of minimising the likelihood of particular jurisdictions interpreting identical fact patterns in different ways. Providing examples in the commentary to the model treaty will not fully address this concern. We therefore reiterate our recommendation that the PPT is drafted so as to be a test of the (single) principal purpose of an arrangement. This, combined with appropriate commentary examples, would maximise consistency without defeating the aims of Action 6.

Notwithstanding the above we have set out two examples in the Appendix to this letter setting out our view of how the PPT, as currently drafted, could apply to common private equity holding structures.

Conclusion

Private equity funds are not vehicles for treaty shopping or any other form of tax avoidance. They exist solely to meet investor appetite for pooled investment in a particular class of asset. As noted in our previous submissions, such funds provide an important investment option for key institutions such as governments and pensions and play an important role in channelling capital to where it can most efficiently be deployed and in the global financial system generally. In order for such funds to remain available to investors it is vital that investing in a private equity fund does not worsen a participant’s treaty position (either in terms of tax suffered or simply uncertainty) in comparison with them making a direct investment and that the costs of investing in a fund are not prohibitively high. As set out above our concern is that the current drafting over the LOB and PPT rules creates uncertainty in this area.

Therefore while this representation is short the points made are fundamental to our principal goal which is to ensure that the asset class remains a viable proposition for investors. To this end we also endorse the views set forth by the Private Equity Growth Capital Council and the European
Private Equity and Venture Capital Association in their submissions in response to the discussion draft.

**Further work**

We welcome the commitment made in the discussion draft to explore solutions to the issues related to the treaty entitlement of non-CIV funds. We would welcome an opportunity to continue our engagement on this issue beyond September 2015 and to contribute to further working party discussions. We consider that further dialogue to identify the source and validity of the working party’s concerns about treaty abuse and income deferral for non-CIV funds would be constructive.

Yours faithfully,

David Nicolson  
Chairman of the BVCA Taxation Committee
Appendix

Example 1

A private equity fund is established with the intention of investing into a portfolio of unrelated trading businesses. Twenty investors of different types and treaty characteristics commit to providing capital to the fund, which will be managed by an entity subject to regulation under the Alternative Investment Fund Managers Directive. The fund is structured as a limited partnership, which due to its fiscal transparency is not resident in any state.

Bank finance is used to leverage the investors’ capital and make investments. The bank providing this finance requires that funds are lent into a group holding company in order to gain good security over the portfolio of assets. The fund must therefore establish a holding company for the investment portfolio into which the bank can lend and over which the bank can take security. The fund manager considers a range of potential jurisdictions for the holding company and as part of this process considers the legal regime, political stability, investor familiarity, flexibility to extract exit proceeds from piecemeal sales of the portfolio and tax considerations such as certainty around the taxation position of the holding company on disposal of its investments. The treaty position of each of the target entities is taken into account as part of the decision but this is one factor in a range of considerations.

In these circumstances, the set-up of the holding company is mostly driven by legal, commercial and tax reasons. Obtaining treaty benefits should thus not be considered as being one of the main purposes of the arrangements.

Example 2

A private equity fund also structured as a limited partnership, which due to its fiscal transparency is not resident in any state, intends to invest into a single trading business in a jurisdiction which imposes withholding tax on interest and dividend payments.

Through the information gathered in order to satisfy existing anti-money laundering and similar requirements at the inception of the fund, the fund manager is satisfied that a majority of the investors are likely to be entitled to treaty relief at source in respect of payments from the underlying investment.

Whilst the fund manager is not expecting significant ongoing interest and dividend flows from the investment (like most private equity funds the vast majority of returns will come via sale proceeds at exit) in structuring the acquisition the decision is made to acquire the investment through an entity located in a jurisdiction which has a favourable treaty with the target jurisdiction. The reason for this decision is to avoid imposing an administrative and potential cash flow burden upon the majority of the fund’s investors by requiring them to each make individual treaty claims with respect to interest and dividend payments from the investment. Were this to be required, there would be an additional administrative burden on the fund manager (which of course carries with it staff and cost implications), and the fund may be considered to be less desirable from an investor perspective, given the additional administration put upon the investors.
In these circumstances the set up of the holding company is driven by a desire to reduce the administrative burden for the majority of the fund’s investors and avoid investor relations difficulties for the fund manager. Potentially accessing treaty benefits for the small proportion of the investor base whose treaty position is uncertain is not a key driver behind the decision in comparison with managing the position for the majority of investors. Obtaining treaty benefits should thus not be considered as being one of the main purposes of the arrangements.
Dear Ms de Ruiter

**Revised discussion draft on BEPS Action 6: Preventing treaty abuse – BPF response**

**Introduction**

The British Property Federation (BPF) is the voice of property in the UK, representing businesses owning, managing and investing in property. This includes a broad range of businesses comprising commercial property developers and owners, financial institutions, corporate and local private landlords and those professions that support the industry.

We are pleased that the OECD acknowledges the economic importance of investment funds and we welcome the continued efforts to ensure that they are able to access treaty benefits where appropriate.

**Executive summary**

Investment into commercial real estate is critical for any economy. Such investment provides high quality accommodation in which businesses – from retailers to manufacturers, leisure centres to hospitals – can carry out their activities and allows them the flexibility to adapt and relocate as business economic conditions change.

Given its bulky and illiquid nature, it is common for investors to gain exposure through collective investment vehicles and joint venture arrangements. Such arrangements spread commercial risk among participants and give investors access to opportunities and expertise they would not have on their own.

These arrangements depend on entities within the investment structure being able to access treaty benefits in order that the ultimate investors are taxed as if they directly owned the underlying assets. If this ability were removed as a result of the OECD’s treaty abuse proposals, the impact on real estate and our built environment would be considerable. Cross-border investment flows into property would suffer greatly as investing into other jurisdictions becomes more expensive. This would be a very perverse outcome given that the purpose of double tax treaties is to facilitate cross-border investment and trade.

We therefore encourage the OECD to continue to consult with the investment management industry to develop a framework that protects against treaty abuse while at the same time ensuring that investment flows are not harmed.
Key points

- **Equivalent beneficiaries** – We welcome the reduction in the equivalent beneficiary threshold to 75% in the simplified LOB, which will be helpful for intermediaries in investment fund structures. At this stage, it would be helpful for the OECD to provide guidance on how the equivalent beneficiary rules should be implemented in practice, particularly regarding how taxpayers can evidence that their investors benefit from such status.

- **Non-CIVs** – We advocate a widely-held test for non-CIVs and would encourage the OECD to give further consideration to a test similar to the UK’s Genuine Diversity of Ownership test.

- **Protect against the abuse of more relaxed CIV and derivative benefit provisions.** This could be done by denying treaty access to funds which are ultimately more than 10% owned by a single non-equivalent beneficiary and their connected parties.

- **Simplified LOB** – We welcome the introduction of a simplified LOB. It is important that all tax treaties make it clear how CIVs are treated and to that end, we would encourage the OECD to incorporate sub-paragraph 2f (on collective investment vehicles) within the simplified LOB.

- **Encourage cross border investment** – A balance must be met between ensuring treaties are not easily abused and facilitating cross-border investment. A well functioning tax treaty regime is critical in ensuring that capital can flow efficiently to suitable investment opportunities.

Structure of this response

- Appendix 1: Full response
- Appendix 2: Examples of real estate investment structures
- Appendix 3: Non-CIV written examples for Commentary on the PPT rule

We would welcome the opportunity to discuss the contents of this letter in more detail. We remain at your disposal should you have any questions or require further details.

Yours sincerely

Rachel Kelly
Senior Policy Officer, British Property Federation
Email: Rkelly@bpf.org.uk
Tel: 0207 802 0115
Appendix 1: Full response

1. Issues related to the LOB rule

CIVs

We welcome the inclusion of clause 2(f) (in respect of collective investment vehicles) into the LOB clause in the annex of the discussion draft. We note that this same clause is not included in the new simplified LOB clause. We would urge the OECD to stress the importance to Governments of clarifying how CIVs are treated under treaties, and to that end we would suggest that clause 2(f) is included within the simplified LOB as well.

Equivalent beneficiaries

Reducing the equivalent beneficiary threshold to 75% within the simplified LOB will be helpful for intermediaries in investment fund structures. We would urge the OECD to provide clarity on what these rules will mean at a practical level before it is implemented. There are many fund structures where it may be difficult to identify the ultimate investors – particularly where units or shares are traded regularly or where there are several intermediary vehicles e.g. fund of fund structures. To that end, it would be useful to understand what evidence of ownership should be sufficient to provide comfort to tax authorities that investors in a fund structure are in fact equivalent beneficiaries.

Alternatively, it may be possible to establish at a multilateral level some sort of 'white list' of jurisdictions the residents of whom should generally be automatically considered equivalent beneficiaries. This approach would help to keep the administrative burden on taxpayers to a minimum.

Non-CIVs

The discussion draft notes that a number of commentators advocated an approach such as the UK’s “Genuine Diversity of Ownership” test; and indeed, this was reiterated at the public consultation in January. However, the discussion draft does not comment further on what the OECD’s views or concerns are regarding such an approach.

As noted in our previous submissions, we would encourage the OECD to make a “widely held” condition the most important factor in determining whether a fund should be entitled to treaty access. Where a fund is genuinely widely held, the risk that any individual investor (or small group of them) could influence the structure or investments of the fund to facilitate their own tax advantage is significantly mitigated. Therefore, we consider that the requirement for a fund to be “widely held” provides the greatest degree of protection against treaty abuse.

While we appreciate the commitment to find a solution for non-CIVs by December 2016; we would urge the OECD to find a solution as soon as possible in order to give as much advanced warning and certainty to the industry as possible.

Non-CIV avoidance safeguard

In order to further reduce the risk of non-CIV structures being used by non-treaty eligible investors, the OECD could consider introducing provisions that deny treaty benefits to any fund which is more than say, 10%, owned by a single non-equivalent beneficiary and their connected parties.
REITs and transparent entities

We welcome the OECD’s acknowledgement of the 2008 REIT report and intention to reference to the conclusions of this report, further to the June working group meeting. Transparent entities are also common in real estate investment structures and to that end, we welcome the helpful confirmation that treaty access for fiscally transparent entities will usually take place at the level of the investor.

2. Issues related to the PPT rule

Given that the LOB clause does not currently provide adequate double tax relief for all ‘Non-CIV’ funds, it is imperative that these funds are able to access double tax treaties where they can satisfy the PPT rules.

Examples

We are fully supportive of the OECD’s commitment to add one or more examples of non-CIV funds to the Commentary to the PPT rules. Indeed, it would be helpful to include both examples of structures that would and would not be eligible for treaty access. Appendix 2 sets out two illustrations of typical real estate investment structures and the activities that take place at each tier in the structure for your information. We would also be happy to assist in putting together written examples for the guidance – please let us know if that would be helpful.

Discretionary relief

There is a significant difference between the discretionary relief provisions under the LOB rule and the PPT rule. The PPT rule only denies tax relief if it is reasonable to conclude that tax avoidance is in point while the LOB discretionary relief provisions put the onus on the taxpayer to show that the obtaining of benefits under the treaty was not a principal purpose of the arrangement.

We would recommend that a consistent approach should be adopted for both the PPT and discretionary relief provision. We consider that the approach under the PPT rule is more appropriate and therefore it should be expressly stated that the PPT guidance is also relevant to the discretionary benefit rule.

Timeframe for clearances

Real estate investors require certainty regarding their eligibility for treaty access in order to determine the viability of investments and in order to price their fund units. To that end, we would encourage the OECD to recommend a deadline of no more than 30 days where advanced PPT clearances have been sought.

3. Encouraging cross border investment

Policymakers across Europe are currently considering ways to boost international investment and perhaps the most high-profile of these initiatives is the European Commission’s Capital Markets Union project. A well functioning tax treaty regime is critical in ensuring that capital can flow efficiently to suitable investment opportunities around the world and to that end, it would be very disappointing if the OECD’s treaty abuse recommendations resulted in cross-border investment becoming more expensive and difficult.
Not only would that be likely to result in a significant fall in the amount of capital invested in real estate and in our built environment, it would also limit investment choice in a way that would ultimately affect millions of pensioners and savers around the world. Dealing with treaty abuse is important, but so is facilitating investment, and we would urge the OECD to continue to work with the investment industry to develop a framework that protects against treaty abuse while at the same time ensuring that investment flows are not harmed.
Appendix 2a: Illustrative example of a widely held real estate investment structure

**Investors**
Investors invest via a fund to pool resources and achieve economies of scale, to spread risk and to access professional investment and portfolio management services.

**Master Feeder Fund**
This vehicle is usually a transparent entity. Investors like to invest in a transparent vehicle to ensure that they are taxed according to their individual tax attributes.

**Holding Company**
A holding company is required in order to consolidate all of the underlying real estate investments. The administration and financing of the property portfolio may also be carried out by the holding company.

Any double tax treaty claims applied for in respect of WHT suffered on the distributions received from the underlying investments are claimed by the holding company. This is an important function of the holding company as it is administratively simpler for one company to reclaim the WHT suffered, rather than each individual investor making a treaty claim. Individual investors may not have expertise to submit a treaty claim and it may not even be economically viable to do so on their portion of profits.

It is not uncommon for a local holding company to be used in the same jurisdiction as the investment, as illustrated with the investment in Country A.

**SPVs and investments**
Individual real estate assets are often directly owned by a special purpose vehicle or holding company, often (but not always) in the same country that the asset is located. This allows flexibility when selling the asset e.g. the ability to sell a proportion of the asset rather than the whole asset. It also allows for specific borrowing at the level of the asset if required.
Appendix 2b: Illustrative example of a joint venture real estate investment structure

The above is a relatively simple structure; JV arrangements can be far more structurally complicated. For example, investors may decide that further capital or expertise is required in respect of each of their investments. As a result, they may decide to invite a further JV partner to invest in that particular asset, as illustrated with the asset located in Country B. For every tier where further investors enter the structure, an additional holding company is typically introduced which adds further layers and complexity to the structure.

As with all real estate investment, rental income and gains made on the property are generally taxable in the location of the property. Hence, any further tax suffered by entities in the investment structure would constitute double or triple taxation on the same profits or earnings that are being repatriated to the ultimate investors.

**Investors**
Investors choose to invest together to benefit from the resources or skill set that the other joint venture partner brings to the arrangement. In this typical example, a pension fund or other professional institutional investor will bring the majority of the capital while the Property Company brings specific real estate industry expertise such as construction or development.

**JV investment vehicle**
JV’s can either be structured through partnerships (typically transparent) or corporate (opaque) or regulated fund vehicles (transparent) that just happen to have a small number of participants, albeit the institutional investors will ultimately be widely held.

**Holding Company**
A holding company is required in order to consolidate all of the underlying real estate investments. The administration and financing of the property portfolio may also be carried out by the holding company.

Where a second tier JV investor is introduced further down the structure, it is not uncommon for a local holding company to be used, as illustrated with the investment in Country B.

**SPVs and investments**
Individual real estate assets are often directly owned by a special purpose vehicle or holding company, often (but not always) in the same country that the asset is located. This allows flexibility when selling the asset e.g. the ability to sell a proportion of the asset rather than the whole asset. It also allows specific borrowing to be done at the level of the asset if required.
Submitted by email: taxtreaties@oecd.org


Through its members, BUSINESSEUROPE represents 20 million European small, medium and large companies. BUSINESSEUROPE’s members are 41 leading industrial and employers’ federations from 35 European countries, working together since 1958 to achieve growth and competitiveness in Europe.

BUSINESSEUROPE is pleased to provide comments prepared by the members of its Tax Policy Group, chaired by Krister Andersson, on the OECD Revised Discussion Draft entitled "BEPS Action 6: Prevent Treaty Abuse" (hereinafter referred to as the Draft).

General Comments

The initial and prime objective with tax treaties is and should continue to be to facilitate cross-border trade through the allocation of taxing rights between countries and to provide for mechanisms to eliminate double-taxation.

It is of utmost importance that anti-abuse rules are designed so that they have a minimum impact on genuine business operations. Consequently, we believe that perceived inappropriate behaviour is best addressed with specific and targeted anti-abuse provisions. In our view, both the proposed LOB provision and the PPT fail in this respect, since they are too general in nature and not limited to abusive situations.

We acknowledge that some improvements have been made since the last Draft, with some useful examples added. However, considering the added complexity and
unpredictability that will follow if these proposals are implemented, we are concerned that, despite requests from numerous commentators, there is still not sufficient guidance in the Draft. In addition, several issues have been postponed by the Working Party until its June meeting and new, and potentially far reaching, proposals such as the "special tax regime" have been introduced at a very late stage in the process.

The Principal Purpose Test (PPT) is too wide and vague. This would allow tax authorities a very broad discretion to challenge the availability of treaty benefits and be therefore open to ambiguity and misinterpretation.

In addition we fail to see how there could be more than one principal purpose. In our view, the test should naturally focus on the principal purpose of the arrangement or transaction.

Also, the various technical examples provided on the working of the PPT rule effectively show the difficulty that taxpayers will have in proving the requisite facts to prevent denial of treaty benefits.

The LOB is still, despite numerous comments, overly restrictive and in some respects potentially in violation with EU law.

To provide the necessary legal certainty to taxpayers regarding the tax treatment of their investments, it is crucial that (1) taxpayers have the possibility to get pre-clearance regarding the access to treaty benefits, (2) the proposals and proposed changes to the Commentary provide ample guidance on the application of both the proposed LOB and PPT rules, and finally (3) there should be unobstructed access to a mutual agreement procedure (MAP) and mandatory binding arbitration.

If these three conditions are not met – which they are not presently – it will be virtually impossible for most arm's length parties to determine whether reduced withholding rates may apply under a certain treaty.

Although the discretionary relief provisions under both the PPT and the LOB now both contain a requirement to consult the other contracting state before deciding, there is still no requirement for contracting states to consult each other before invoking the LOB or the PPT. A small improvement is made in that it is now recommended that senior level approval is obtained before making an adjustment. However, this still falls short compared to a requirement to consult – and preferably agree – before either contracting state invokes the LOB or PPT.

The new Discussion Draft proposes in paragraph 32 that as long as a competent authority has properly exercised the discretion granted by the discretionary relief provision of the LOB rule, that provision has been complied with and it cannot, therefore, be argued that taxation is not in accordance with the provisions of the Convention. We are concerned about this since the intention seems to be to deny a taxpayer the possibility to invoke the mutual agreement procedure (MAP) regarding this
decision.

We have limited our specific comments to some of the issues in the Draft.

**Part 1 – Alternative “Simplified” LOB rule and presentation of the LOB rule in the OECD Model**

BUSINESSEUROPE objects to the combined approach of having both a LOB and a PPT in a tax treaty. Although the Draft suggests a simplified LOB, which naturally is preferable compared to the extensive one as suggested in previous Drafts, it would still leave companies with a lot of uncertainty as to the outcome, since after having passed the simplified LOB, they would be confronted with a very subjective PPT.

**Part 2 – Issues identified in the November 2014 Discussion Draft**

3. **Commentary on the discretionary relief provision of the LOB rule**

BUSINESSEUROPE welcomes the proposal in paragraph 32 of the Draft that the competent authority should process a request for discretionary relief expeditiously.

4. **Alternative LOB provisions for EU countries**

As stated in our previous comments, BUSINESSEUROPE believes that the LOB rule needs to be adapted to reflect EU law requirements. We therefore would like to repeat our concerns in relation to the prohibition of non-resident intermediaries in the ownership tests.

5. **Requirement that each intermediate owner be a resident of either Contracting State**

We refer to our previous comments that the LOB rule should focus on the ultimate beneficial owner and not intermediate companies.

6. **Issues related to the derivative benefit provision**

We strongly support a derivative benefit provision in the LOB. The derivative benefit provision would extend the granting of treaty benefits to entities that are controlled by entities that are resident of a third country and that would enjoy the same treaty benefits with the contracting state in question. In such situations, there is no incentive for treaty shopping.
At this latest stage in the process, we object, however, to the proposal to introduce a new treaty provision on "special tax regimes". Whilst this proposal is included in the discussion on derivative benefits, it potentially represents a more fundamental change to the application of treaties which warrants proper consultation not afforded by the current process. This is an issue which should be addressed through the project on harmful tax practices.

7. clarification of the 'active business' provision

We agree with the Working Party that there should be clarification on the active business provision, but note that the Discussion Draft – specifically paragraph 71 – does not provide such.

B. Issues related to the PPT rule

12. Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level

BUSINESSEUROPE is in favour of such a requirement in order to prevent excessive use of the PPT and welcomes the proposal in paragraph 79 of the Draft.

13. Whether the application of the PPT rule should be excluded from the issues with respect to which the arbitration provision of paragraph 5 of Article 25 is applicable

BUSINESSEUROPE strongly recommends that the application of the PPT should be under mandatory arbitration. Introducing a substantive provision such as the PPT without the possibility of mutual agreement procedures or arbitration is not acceptable. Consequently, we are pleased that the OECD has decided not to endorse the minority view according to which the application of the PPT rule should be excluded from the arbitration mechanism.

15. Whether some form of discretionary relief should be provided under the PPT rule

BUSINESSEUROPE is supportive of having a discretionagary relief provision under the PPT rule and welcomes the proposal in paragraph 90 of the Draft.
16. Drafting of the alternative “conduit-PPT rule”

We appreciate the fact that the OECD has adhered to the criticism regarding the definition of the term “conduit arrangement” and we are positive to the proposed examples in paragraph 94 regarding the interpretation of such arrangements.

C. Other issues

19. The design and drafting of the rule applicable to permanent establishments located in third States

As stated in our previous comments, we question the necessity of a provision like this in the Model Treaty. This topic may be of interest in relation to some countries and should naturally be carefully considered before entering into a treaty with such a country. At any rate, those situations could be solved bilaterally.

Concluding Remarks

The introduction of provisions like the proposed LOB and PPT will undoubtedly induce further uncertainty into the Model Treaty and make treaty application even more difficult. The LOB still seems overly restrictive and runs the risk of having a very negative impact on genuine business operations.

Whereas the LOB provision may be considered technically complex, it leaves less room for subjective and arbitrary assessments. The PPT on the other hand takes the opposite approach and does not provide much guidance with respect to when the treaty benefits will be granted. The subjective nature of the PPT opens a door for tax administrations to disqualify taxpayers from treaty benefits where that tax administration finds it appropriate.

In view of the implications of introducing these new provisions in the Model Treaty, and considering the extensive input from commentators, we are disappointed that many issues have not been addressed properly and that the Draft still lacks sufficient guidance in a number of areas. As currently drafted, BUSINESSEUROPE believes that the provisions could seriously undermine the certainty and predictability needed for investment decisions and also lead to an increase of double taxation cases. The effect would be very negative on investments, jobs and growth.

On behalf of the BUSINESSEUROPE Tax Policy Group

Yours sincerely,
James Watson
Director
Economics Department
CBI RESPONSE TO THE OECD PUBLIC REVISED DISCUSSION DRAFT ON BEPS ACTION 6: PREVENT TREATY ABUSE

1. The CBI is pleased to provide comment on the OECD’s revised Discussion Draft on Action 6: Prevent Treaty Abuse.

2. As the UK’s leading business organisation, the CBI speaks for some 190,000 businesses that together employ around a third of the private sector workforce, covering the full spectrum of business interests both by sector and by size.

3. The CBI continues to support the BEPS programme to update international tax rules to reflect modern business practice, tackle abusive tax structures and target the incidence of double non-taxation. However, we are concerned that if complexity and uncertainty are not avoided, the outcome will be an increase of double taxation and resulting legal disputes, which could have a substantial and negative impact on cross border trade and investment, but also on tax administrations with limited resources.

Overview Comments

4. The CBI remains concerned that at this late stage, the revised discussion draft is still not a consensus document and that there seems to be an increasing level of divergence in the proposals – which we assume will then play out in the inconsistent implementation of the rules – especially in relation to the limitation of benefits (LOB) provisions which is less likely to be capable of implementation through the multi-lateral instrument.

5. We do request that when the final recommendations are submitted in September, a focus is given on how the provisions will be implemented and business is able to comply. If the proposals become impractical and companies which should be capable of claiming treaty benefits end up not being able to do so either through a technicality in the rules, or through being unable to meet the compliance burden of proving eligibility, this will then undermine the whole purpose of the global treaty network which is to facilitate cross border trade.

6. The CBI and other business groups raised genuine commercial concerns on a number of issues. Whilst many of these have been acknowledged, very few have been taken into account and some have been disregarded (and in some cases no reason for discarding has been provided). We would like to see more affirmative action in addressing business concerns, or at least provide an explanation as to why they were rejected/could not be addressed so that business has a greater understanding of the interpretation of treaties going forward to increase certainty of treatment.
Detailed Comments

Part I – Alternative simplified LOB Rule

7. The CBI welcomes the inclusion of a simplified LOB model clause to be used where countries wish to have protection of both a LOB and PPT (which we hope should be very limited as there should be no policy reason to test the ownership of a recipient if the purpose of the payment/transaction/arrangement has been tested and determined not to be abusive for treaty purposes). Whilst it is offered to be used only in conjunction with the PPT, there are many features of the simplified LOB which could/should be replicated in the main LOB to be used in conjunction with the anti-conduit rule which would still provide sufficient protection against treaty abuse.

8. With respect to paragraph 2 of the simplified LOB, the provisions should be extended to include the standard clause on 2 f) covering CIV’s and any additional wording which may be agreed for non-CIV funds. As the simplified model is supposed to be wider ranging that the full version (as it is a back up to the PPT), there seems no policy reason why the scope of qualified person should be restricted compared to the full version.

Part II – Issues identified in the November 2014 discussion draft

CIV Funds

9. The CBI welcomes the confirmation that the conclusions of the 2010 report should be respected. However, we do recommend that the square brackets round paragraph 2(f) in the final September report on Action 6 be removed in the final version to ensure that this should be recognised as a standard paragraph for the minimum standard (of course countries can negotiate tighter provisions if they so wish in bilateral discussion).

Non-CIV Funds

10. The CBI welcomes the acknowledgement of the economic importance of the non-CIV fund market as a source of funding for companies and the need for these funds to be granted access to treaties where appropriate. There are 3 broad approaches outlined in the paper, which we comment on below:

- New treaty provisions in relation to hybrid entities. It is acknowledged that these provisions will be helpful for some CIV fund structures where the whole structure is transparent. However, this will not always be the case and there are a number of reasons why a corporate platform or structure may be appropriate or required commercially.

- Derivative benefit clause. See further comments below, but the usefulness to non-CIV funds will depend on how restrictive the derivative benefits clause is. If the 95% requirement is lowered, the 7 or fewer investor requirement is eliminated and the requirement for all intermediate holding companies to be in a treaty state or be an equivalent beneficiary is again eliminated in line with our recommendations (and is therefore drafted for the main LOB in line with paragraph 3 of the simplified model), then the derivative benefits provisions would provide a significant improvement for non-CIV’s. However a derivative benefits clause in line with the final recommendations in the September 2014 report would be overly restrictive and therefore be of limited use.

- Providing a definition of a non-CIV fund that could be a qualifying person. In our submission to the first revised discussion draft submitted to the OECD in January, we supported the BVCA proposals for a “qualifying fund” that could be developed to provide treaty access whilst providing safeguards for treaty abuse. The proposals outlined were not a final proposition, but an outline of criteria that may be considered in consultation with the industry. If it is felt that these do not fully address the treaty abuse concerns (of deferring the recognition of income and gaining access to non-treaty investors) then we would encourage direct engagement between the OECD Working Group and the relevant industry groups to find a compromise which works both commercially whilst providing protection against BEPS behaviours. Due to the potential limitations of the hybrid rules and a
narrow derivative benefits clause, we do recommend that the qualified persons definition is pursued and welcome the extra time that the OECD are prepared to give themselves to getting this right.

11. We would stress, however, that it is not just arrangements that might be more generally regarded as “funds” that appear to fall within the category of non-CIV Funds. There will be many other arrangements, such as securitisation arrangements and other companies which are used for repackaging securities to produce an alternative instrument for investors to invest in. These arrangements reduce the cost of funds to businesses throughout the world, and are typically motivated by non-tax factors. Such entities need to be able to claim treaty benefits, otherwise the natural consequences will be to increase the cost of finance, or reduce its availability.

12. We welcome the clarification regarding the status of the taxation of pension funds, and look forward to seeing a workable provision following the June meeting. We would however caution regarding the criteria for beneficiaries of the pension fund. Whilst there is generally a requirement on occupational pension funds for the beneficiaries to be resident at the time of the contributions (and therefore unlikely to be a tax avoidance motive), there is generally no such controls and monitoring of individuals when it comes to making pension payments and therefore pension funds may have genuine concerns regarding the practical application of applying for treaty benefits.

**Discretionary Relief (LOB)**

13. We have no new comments to make in respect of these provisions.

**LOB for EU Countries**

14. We have no new comments to make in respect of the publically listed provisions.

15. In relation to the pension fund proposal outlined in paragraph 40, we would recommend the following:

- The [90 per cent] is either left as X% for countries to decide or is reduced in line with the derivative benefits simplified proposal of 75% (it is important to bear in mind that this is a minimum standard and countries are free to negotiate narrower provisions if they so wish).
- 2 ii) B) As noted in respect of the derivative benefits provision, we would welcome a review to see if this could be amended from a cliff edge provision to just limiting the benefit to the amount which would have been charged if the non-resident had received the money direct.

**Requirement that each intermediate company be a resident of either contracting state**

16. We have outlined in our previous submissions (May 2014 and January 2015) on this BEPS Action plan a number of commercial (non-tax planning – some even tax increasing) structures which this LOB provision would prevent treaty benefits from being claimed. In our view, this is too restrictive – especially for a minimum standard.

17. Outlined in paragraph 44 of the revised discussion draft is the concern that the intermediate owner requirement is required to prevent the imposition of a tax haven to which income is derived through a base-eroding payment. It is by no means obvious what this structure is and it is of concern that no detail is provided regarding this structure to enable commentators who may wish for this clause to be removed, to provide suitable alternatives that may address the risk in mind whilst safeguarding the commercial structures which are caught by the imposition of this clause.

18. In reviewing the potential risk of a base eroding payment to a tax haven (as outlined in paragraph 44), we have undertaken the following analysis and have not understood why a risk can still be in point:

- After the other BEPS Action Plans have been implemented (especially Actions 2 on hybrids and 8-10 on transfer pricing), would the base-eroding payment still be deductible? (If not, there is no requirement to address this risk in this action as well).
- Even if it is still deductible, if the payment is made to the tax haven directly, then the tax haven
would not be a resident of the contracting state and therefore the treaty would not be in point anyway.

- If the payment is made to a treaty resident, but is then on-paid to the tax haven, then this is exactly the risk that the anti-conduit provision is designed to catch (and there may also be possibilities depending on the structure/contracts to say the treaty resident is also not the beneficial owner). If there are deficiencies in the anti-conduit rules, we would recommend they are addressed in those provisions so there should be no need for this restrictive clause to protect such a structure.

- If the payment is made to a PE in a tax haven, then this is the structure the triangulation provisions are designed to prevent.

Whilst we do understand the need for protection to ensure that payments made directly or indirectly to non-treaty countries do not somehow obtain treaty benefits, we do not understand how such a payment can be made in a manner which treaty benefits can be claimed with the other provisions contained within the proposals in BEPS Action 6. As this clause does prevent treaty benefits to cases where (from a policy perspective) there should be no objection, we do request that it is eliminated from the final proposals.

If the risk is actually the payment to a company benefiting from a special tax regime, please see our comments below (paragraph 24 of this letter). If another risk really does exist, we do request that the risk is articulated in detail and the business community is consulted to see if an alternative approach can be determined that has less impact on commercial structures.

19. We would note that whilst allowing treaty benefits where there are equivalent beneficiaries in addition to just entities in the contracting states would be a significant improvement (and certainly we would recommend this over the original proposed requirement of such entities being resident only in contracting states), we would still consider such a requirement to be an unnecessary burden and restriction to gaining treaty benefits.

Issues related to the derivative benefits provision

20. There should be no doubt that a form of derivative benefits clause should be included within a minimum standard proposal (no square brackets, or doubts in commentary/guidance). There would seem no policy reason for applying a treaty shopping provision when the ultimate owners would have been entitled to exactly the same benefits if they had invested in the asset/received the payment directly.

21. We would recommend that paragraph 4(a) of the LOB proposals outlined in the September recommendations is replaced with paragraph 3 of the simplified LOB outlined on page 5 of this revised discussion draft. Whilst we have outlined our detailed reasons in prior submissions, we have outlined the high level arguments again below:

- The 95% holding requirement is arbitrary and is significantly higher than the other LOB provisions such as the listed company test. As a compromise between a sensible compliance burden and preventing abuse, we recommended this was lowered to 75% for the minimum standard treaty (which of course allows countries to negotiate a higher level if they deem necessary for their local market). The 75% is in line with the simplified LOB. If 75% can not be agreed, we would recommend that no fixed % is stated and is then left for countries to negotiate freely when entering into bilateral negotiations.

- Having only 7 or fewer investors would seem to run contrary to the rationale for allowing the publicly quoted and CIV test. The more investors a company has, the least likely it is that arrangements can be structured to meet all tax planning requirements.

- There should be no requirement for intermediate holding companies to be resident in the contracting state. The residence of intermediate holding companies bears no relevance to the taxation of the receiving entity in its own state or has any relevance on other key concepts such as
residence, beneficial ownership. As outlined in respect of similar provisions in the publically quoted company test in paragraph 18 above, the protection provided by the other clauses in the LOB, anti-conduit and other treaty provisions being proposed under BEPS Action 6, there would seem to be no obvious risk of the facilitation of base eroding payments to non-treaty jurisdictions.

22. Whilst the concerns of business were noted in the revised discussion draft, no proposals were put forward to deal with these – or reasons provided as to why the concerns could not be addressed. In fact, further restrictions have actually been proposed (see below). The final recommendation is a minimum standard and not a recommended best practice or absolute solution. We would like to see business concerns addressed in the final recommendation and preferably in the manner outlined in the paragraph above.

23. As noted above, new proposals have been put forward which would restrict the application of the tax treaty further – supposedly as a trade-off for allowing a derivative benefits clause. For all the reasons outlined above, in our prior submissions and submissions of other business commentators such as BIAC, there should be no question of a properly functioning derivative benefits clause being omitted from a minimum standard, and certainly not as a trade-off for further restrictions.

24. Notwithstanding the above, we would comment that proposal 1 (provisions relating to special tax regimes) is not an issue which should be considered as part of BEPS Action 6. We would strongly recommend that the entitlement to treaty benefits for special tax regimes should be included within the work of BEPS Action 5 (harmful tax practices) where the suitability of such regimes are being considered. As a general rule, we do not believe that there should be any restriction of treaty benefits for any tax regime that is not considered harmful under BEPS Action 5. Even if a regime is harmful under BEPS Action 5, it should then be for tax authorities to negotiate whether treaty benefits are appropriate (as is currently the case). There should not be a standard provision within this BEPS Action plan covering special tax regimes.

25. With respect to proposal 2 – whilst we would make a general point that this is much less benign than proposal 1, it does seem to go beyond what is necessary to address the risk and therefore creates uncertainty if countries do change their tax rules. We would suggest that the most appropriate solution to such a risk would be for countries to renegotiate the treaty. If there is a concern regarding the monitoring of all treaty partners tax regimes, maybe a compromise would be to include a notification requirement for a treaty partner to inform other treaty partners of tax regime changes such that there could be no doubt of such changes being hidden or not disclosed. It would then be up to the other country to initiate treaty changes through normal channels.

26. The concern from business regarding the cliff-edge effect has been noted in the discussion draft, but no indication as to whether any amendments will be considered to address this anomaly. If the purpose of the LOB is to eliminate treaty shopping, it would seem proportionate to address the issue through imposing the rate that the ultimate investors would have been subject to absence any intermediary, rather than imposing a full domestic rate (if interposing an intermediary increases the withholding rate, it is unlikely to have been inserted for tax treaty-shopping purposes).

Dual-listed companies
27. We welcome the proposed changes outlined paragraph 58.

Timing Issues
28. We note that the proposals from business will not be taken forward with regard to timing. We would request however that such a situation where the only reason the publically traded test has been failed is due to the technicality of accounting periods not ending when the company first lists or de-lists, this should be a situation that would be looked upon favourably in applying for discretionary relief.

Publically listed entities
29. We have no further comments in relation to this section.
Clarification of the Active Business Condition

30. Whilst the discussion draft acknowledges the comments made in respect of holding companies and headquarter companies, there is no confirmation as to whether any action will be taken to address these concerns, or explanations as to why not. This is not satisfactory. The distinction made between holding companies and trading companies for the qualification to entitlement under the treaty is not reflective of today's business environment where regional HQ operations often have significant substance and carry on active and important business functions through highly qualified employees. Alternatively, absent there being a "HQ test", we believe a holding or a headquarters operation and any connected persons in the treaty country of residence which are in the same or a similar line of business their activities should be aggregated in applying this qualification.

31. Including specific proposals within the LOB would ensure greater consistency with the PPT. Examples G & H would indicate that such entities would be entitled to treaty benefits where the contracting states agreed to use the PPT to address treaty shopping.

32. We note the additional proposals from the US relating to special tax regimes. As noted above in relation to the derivative benefits, any such rules should be considered under Action 5, and any appropriate restriction should only apply to the extent a tax regime is considered harmful in the final recommendations under Action 5.

Principle Purpose Test

33. Whilst the additional guidance provided in the guidance notes is helpful, we would recommend that more examples are provided. The examples given show the complexity and uncertainty in applying the test and therefore there could still be more examples. We would therefore recommend that each of the situations addressed in the LOB (e.g. CIV’s, non-CIV’s, pension funds etc) are all covered in the examples of the PPT.

34. We continue to encourage a focus on substance in the examples for the PPT. We would recommend that if two tax authorities have differing views, there should be a prima facie assumption that it is not reasonable to conclude that obtaining treaty benefits was one of the principal purposes.

Treaty residence tie-breaker

35. We have no new comments on this section

Third country PE’s

36. We note the revised provisions in relation to third country PE’s. We would request that in addition to the [60%] test, an equivalent beneficiary type test is also included so that if the PE is located in a territory and under the treaty between the company making the payment and the territory of the PE an equivalent (or reduced) rate would have applied, then the rate that would have applied under the treaty with the PE territory shall be the maximum rate that can be applied by the source state.

Interaction between domestic law and tax treaties

37. We have no new comments on this section

38. We trust that you will find the above comments helpful in understanding the potential impact of the proposals outlined in the Discussion Draft. We remain committed to ensuring that each BEPS Action achieves its stated goals, whilst ensuring that genuine business transactions are not unduly impacted.

39. We remain at your disposal should you wish to discuss the issues we have raised in this paper in more detail. Please contact neil.anthony@cbi.org.uk for more information.
17 June 2015

Dear Ms de Ruiter

Re: New discussion draft on BEPS Action 6 (Prevent Treaty Abuse)

The revised discussion draft sets out an alternative simplified LOB rule for use in conjunction with a principle purpose test. This simplified LOB rule bases qualification for treaty benefits on a series of alternative tests focused on “qualifying persons” status or ownership by qualified persons, active conduct of a trade and discretionary relief. We acknowledge that the simplified LOB provision may be more practical for the purposes of dealing with the BEPS challenge of treaty abuse; however the primary problem with LOB continues to be a serious concern for us. To restate our position, LOB provisions are fundamentally biased in favour of larger countries and economies. In contrast, for companies resident in jurisdictions with a small economy which are more reliant on an international investor base, it will be disproportionately more difficult to be a qualifying person under the LOB provision. Countries like Ireland which depend on foreign investment will face much more restrictive conditions compared to larger economies because LOB by its very nature, grants treaty access based on where the majority of investors are resident.

In the following, we take a number of key issues from the revised discussion draft for further consideration by the OECD.
Issues relating to the LOB provision

3. Commentary on the discretionary relief provision of the Limitation on Benefits (LOB) rule

In response to concerns raised on the approach to the management of LOB, the redrafted discussion document proposes to provide more guidance on the factors that a competent authority should take into account when considering a discretionary relief request and that authorities should process discretionary relief requests as quickly as possible. However, these measures fail to address the core problems we identified in our submission of 8 January 2015. To restate the difficulties as identified by our members, the suggested approach places considerable discretion on Revenue Authorities to act as gatekeepers for access to treaty benefits and will hamper cross-border commercial projects by virtue of the uncertainty created by a discretionary LOB.

4. Alternative LOB provisions for EU countries

The Revised Discussion Draft acknowledges that serious concerns were raised that the proposed LOB provision, as presented in the September 2014 Report, needed to be adapted to reflect European Union (EU) law requirements. However, the Working Party has decided not to make changes to the LOB provision, and instead allow the inclusion of alternatives in the Commentary or changes to the model provision to deal with EU law issues.

This is a disappointing development. It is untenable to restructure the Treaty framework fundamentals without reference to the binding agreements entered into by the 28 EU Member States which guarantee freedom of establishment, along with free movement of capital, persons and services. The Introduction to the Model Tax Convention states (at page 12, 8th edition 2010) that “it is scarcely necessary to stress the importance of removing the obstacles that double taxation presents to the development of economic relations between countries”. Alternative LOB provisions for EU countries should be introduced to remove the obstacle of double taxation.

8. Timing issues related to the various provisions of the LOB rule

The Revised Discussion Draft acknowledges that timing issues are dealt with differently under the various provisions of the LOB rule proposed in the September 2014 Report. Therefore it is unsatisfactory that the Working party has decided not to modify the LOB rule for the purposes of addressing potential conflicts or inconsistencies and instead further promotes use of discretion by the competent authorities involved to settle issues arising.

10. Clarification of the “active business” provision

The Revised Discussion Draft agrees that the Commentary on the “active business” provision of the LOB rule needs to explain further the meaning of a “business” to deal with situations where for example a company may carry out two trades. Again we call for Commentary on the matter to clearly state that business support activities can qualify as an active business. This would help
mitigate the difficulties encountered by taxpayers in smaller markets whose workforce is engaged in substantial managerial and operational activities in connection with support services, but where there are limited sales of the group's actual products and services by virtue of the small market size.

**Issues related to the Principle Purpose Test rule**

11. Application of the PPT rule where benefits are obtained under different treaties

The Revised Discussion Draft includes additional examples F,G,H and I for insertion of paragraph 14 of the proposed commentary on the PPT rule. While these are helpful in providing more specific examples of the factors that would be relevant in evaluating whether the PPT would be satisfied or not, we remain concerned that the PPT rule will give rise to a greater incidence of cross-border treaty disputes. Currently treaty disputes are typically resolved in accordance with the domestic procedures applicable in the country seeking to apply the charge to tax. Resolution in these instances is not straightforward, and the complexity of the current Action 6 proposals will not help.

Given some of the challenges that we foresee in the application of the PPT to the diverse scale and types of economies and business entities that will seek to apply these examples, we suggest that it is made clear in the commentary in paragraph 14 that it is not necessary that a particular transaction or commercial arrangement precisely fit within one of the examples in order for it to be considered to pass the PPT. Instead, it should be clearly stated that the examples provide illustrations of the determining factors which should be considered relevant in evaluating whether the test is satisfied or not.

For example the ownership of the company should not be relevant to the analysis of the business activities. In this regard, perhaps it could be expressly stated that, for example, if a privately held company were to carry on activities outlined in examples G and H that this should not preclude the application or relevance of the examples cited in the commentary.

Moreover, it should be made clear that if some of the background facts listed in either of those examples, e.g. in example G there is a reference to the country being a member of a regional grouping which may not be the case for businesses head quartered in smaller economies, did not exist, but that a significant number of the determining factors mentioned in either or both of examples G and H to locate in a particular State existed, that the PPT would equally be satisfied in such circumstances.
You may wish to note that this response is from a representative body. The Consultative Committee of Accountancy Bodies – Ireland is the representative committee for the main accountancy bodies in Ireland. It comprises Chartered Accountants Ireland, the Association of Chartered Certified Accountants, the Institute of Certified Public Accountants in Ireland, and the Chartered Institute of Management Accountants, which represent a combined membership of some 40,000 accountants. Brian Keegan, Director of Taxation at Chartered Accountants Ireland (brian.keegan@charteredaccountants.ie, +353 1 6377 347) may be contacted if any further details in relation to this letter are required.

Yours sincerely

Paul Dillon, Chairman, CCAB-I Tax Committee
Opinion Statement FC 11/2015
on the revised OECD Discussion Draft
on Preventing Tax Treaty Abuse (BEPS Action 6)

Prepared by the CFE and AOTCA
Submitted to the OECD
in June 2015

The CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Its functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe. The CFE is registered in the EU Transparency Register (no. 3543183647-05).

AOTCA (The Asia-Oceania Tax Consultants’ Association) was founded in 1992 by 10 tax professionals’ bodies located in the Asian and Oceanic regions. It has expanded to embrace 20 leading organizations from 16 countries/regions.

AOTCA and CFE unite almost 500,000 individual tax professionals in 37 countries (19 OECD member states).
Introduction


Please note that this is a preliminary version and while it has been agreed by AOTCA and CFE, there may still be changes in detail. The final version will be made available in the course of June 2015 on the CFE website.

We will be pleased to answer any questions you may have concerning CFE’s and AOTCA’s comments. For further information, please contact Piergiorgio Valente, Chairman of the CFE Fiscal Committee, or Rudolf Reibel, Fiscal and Professional Affairs Officer of the CFE, at brusselsoffice@cfe-eutax.org.

CFE’s and AOTCA’s observations

We welcome the OECD’s readiness to consider the stakeholder comments received in its follow-up work on certain BEPS Actions and the commitment to provide further examples.

The proposed simplified LOB (Limitation On Benefits rule) is a considerable improvement which appears much better fit-for-purpose than the detailed LOB. It also seems more likely that countries will adopt the simplified LOB.

We would nevertheless like to underline remaining concerns relating to the uncertainty that both the LOB or PPT (Principle Purpose Test) rules may cause, as well as on the increase of the difficulties in their application. Further guidance is needed and the OECD should not rush to release a proposal/deliverable within this Action, if certainty and clarity on the new proposed recommendations are not ensured.

On the PPT, we note that none of the concerns for small countries that have been raised has been addressed. We believe that the Commentary should contain an example to highlight that the PPT should not fail merely because a countries’ treaty network was one of a number of reasons for locating there. A similar example could be added to the commentary on the discretionary relief section of the LOB.

Discretionary relief section of the LOB

As noted in the Discussion Draft, both the PPT rule and the discretionary relief provision of the LOB rule include a test based on whether one of the principal purposes is the obtaining of benefits under a tax treaty. Our concerns with the possible application of the PPT on smaller economies are equally applicable to the discretionary relief section of the LOB. More examples should be added.

Derivative Benefits Provision

We consider that both proposals contained in § 53 increase uncertainty and lack clear guidance and should therefore be revisited:

2. [http://www.cfe-eutax.org/node/4094](http://www.cfe-eutax.org/node/4094)
§ 53 Proposal 1:

The new proposal on “special tax regimes” looks potentially very broad, there is very little time to consider it and there is no guidance. In our opinion, issues relating to “special tax regimes” should be addressed in the context of the OECD work on Harmful Tax Practices, and not within Action 6.

§ 53 Proposal 2:

This proposal for a new general treaty rule intended to make a tax treaty responsive to certain future changes in a country’s domestic tax laws increases the level of uncertainty for taxpayers. For the sake of clarity and certainty, the concerns that this proposal intends to address could be easily safeguarded through a simple renegotiation of the Treaty.

Active Business Test

We note that the substantiality test for dealings with connected parties is still included. This requirement impacts small countries disproportionately. While it seems obvious that an active business in a small country requires a smaller workforce than an active business in a large country, smaller member countries (e.g. Ireland) in practice have made the experience that the Active Business Test as contained in US tax treaties is difficult to meet. We are concerned that such challenges will be magnified if adopted across multiple jurisdictions.

We suggest that the OECD proposals are amended so that it is clear that business support activities (where the workforce in the smaller economy conducts substantial managerial and operational activities over those support services) can qualify as an active business even where those activities are provided for the benefit of related group parties and where there are no or limited sales of the relevant Group's products / services in the small country concerned.

In addition, an appropriately designed "safe harbour test" should be included.

Combination of Simplified LOB and PPT

While the simplified LOB is welcome, we note that the Discussion Draft proposes that it should only be used in conjunction with a PPT. However, the combination of both tests will result in increased uncertainty for international businesses as to their entitlement to the benefits of double tax treaties and the application of the treaty provisions to their business activities.

The option should be available for treaties to adopt the simplified LOB without requiring a PPT to also be included.

PPT rule and Dispute Resolution Mechanisms

§ 80 – 82 summarise the discussions held on “Whether the application of the PPT rule should be excluded from the issues with respect to which the arbitration provision of paragraph 5 of Article 25 is applicable”: We welcome the fact that the OECD appears to agree on the essentiality of subjecting the application of the PPT rule to MAP/arbitration (so as to ensure certainty). Disputes arisen in connection with the PPT rule should be solved through mandatory arbitration resulting in a legally binding outcome.
Application of the new treaty tie-breaker rule

§ 99-102 Proposal: The term “expeditiously” in the provision “The competent authorities to which a request for determination of residence is made under paragraph 3 should deal with it expeditiously and should communicate their response to the taxpayer as soon as possible” should be defined. A fixed time-frame would be welcome, so as to ensure certainty.
Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division  
Organisation for Economic Cooperation and Development  
2 rue André-Pascal  
75775, Paris, Cedex 16  
France  
Submitted by email: taxtreaties@oecd.org

June 17, 2015

Ref: OECD DISCUSSION DRAFT: Prevent Treaty Abuse (BEPS Action 6)

Dear Mrs. de Ruiter:

The Brazilian National Confederation of Industry (Confederação Nacional da Indústria - CNI) thanks the OECD for the opportunity to provide comments on its Revised Discussion Draft on Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances) of the Base Erosion and Profit Shifting (BEPS) Action Plan issued 22 May 2015 (the “New Discussion Draft”) and takes the opportunity to offer broader comments on Action 6 so as to provide adequate context. The comments offered by CNI in the attached report focuses on technical and policy issues which are particularly sensitive to Brazilian Industry yet which are relevant to all nations.

CNI is the largest and highest-level representation of industry in Brazil with a mission to promote a favorable business environment, enhance competitiveness and promote sustainable development. CNI represents 27 state federations of industry, over 700,000 manufacturing companies and 2,000 sectorial associations, encompassing issues such as economic policy, infrastructure, environment, SME development, labor relations, and international negotiations. CNI develops an active process of dialogue and influence with the National Congress and the Executive. With the Judiciary, the organization has the power to propose measures to ensure that laws are empowered by the Constitution in any respect that affects the industry’s interest. CNI also operates a vast high quality network of professional qualification, education, management training and promotion of entrepreneurship through three entities it oversees: the National Industrial Training Service (SENAI), the Industrial Social Service (SESI) and the Euvaldo Lodi Institute (IEL).

CNI will remain engaged in the BEPS Project and hopes to contribute further with the OECD and the G20 in the discussion of this and all other Action items.
Comments on OECD/G20 BEPS Project – Action 6: Prevent Treaty Abuse

Brazilian-headquartered multinational enterprises (MNEs) that are members of CNI have significantly expanded their global presence and footprint in the recent past, and operate complex global value chains with massive presence in Europe, Asia, Africa and the Middle East, and North America, and substantial trade across such regions. The potential ramifications from the proposed changes under the BEPS Project might differ in different areas of the world as, we fear, different nations will tend to interpret or enforce the proposed changes according to their national tax policies and traditions.

Similarly, the Brazilian Tax Authorities might interpret and enforce the new standards also according to their own views and tradition, particularly as it pertains to the Law of Double Taxation Conventions, which increases costs and complexity for both Brazilian Multinationals doing business abroad as well as Foreign Multinationals doing business in Brazil.

We offer our comments in this report using the following structure:

I. General Commentary on the Proposed Changes under Action 6;
II. Enforcement and Interpretation Issues Affecting Industry within Brazil;
III. Enforcement and Interpretation Issues Affecting Brazilian Industry in China, India, and in Developing Countries;
IV. Enforcement and Interpretation Issues Affecting Brazilian Industry in Europe and North America.

1 The author of this report is Mr. Romero J.S. Tavares, Esq., International Tax Policy Advisor to CNI, Head of the Centro de Estudos em Tributação Internacional, Researcher (DIBT/Ph.D.) and Lecturer at the Institut für Österreichisches und Internationales Steuerrecht of Wirtschaftsuniversität Wien (Institute for Austrian and International Tax Law of the Vienna University of Economics and Business). The author can be reached at romero.tavares@wu.ac.at. This report was independently reviewed by the officers of Multinational Enterprises that are members of CNI.
I. General Commentary on the Proposed Changes under Action 6

Brazil remains as a significant exporter of commodities, and also of diverse manufactured goods, and Brazilian MNEs that expanded globally represent very diverse sectors of industry (e.g., oil and gas, mining, steel, food and beverage, aviation, engineering services, etc.). The expansion of Brazilian MNEs occurred most markedly in the last two decades, a period during which international tax concepts and standards were well established, tried and tested by MNEs that originated in the U.S. and in Western Europe.

Accordingly, Brazilian MNEs concluded many substantial acquisitions of US and EU MNEs in the last two decades, and/or have established substantial presence and regional or global management “operational hubs” in EU countries. Such EU countries provide significant non-tax efficiencies (e.g., significant pool of skilled labor, greater access to capital markets, geographic proximity to supply and/or demand markets, robust infrastructure, low sovereign risk, etc.), as well as significant tax efficiencies related to a wider and stable network of tax treaties and to the functioning of the EU itself (as compared to Brazil’s very limited and often misinterpreted or “unstable” network of bilateral treaties).

Brazilian Industry relies on the stability and coherence of concepts derived from the OECD Model Convention (and the OECD Commentary), through EU and US subsidiaries of Brazilian MNEs. Such reliance and stability is, therefore, a critical factor that enables massive foreign direct investment (FDI) by Brazilian MNEs worldwide (as well as significant Brazilian exports and related international trade). Certain treaty concepts are of particular importance to Brazilian Industry (e.g. Articles 5, 7, and 9 of the OECD MC). Some of the proposals discussed under Action 6 can affect bona fide arrangements that do benefit from treaty rights derived from these provisions, particularly if countries interpret and apply such “anti-abuse” proposals incoherently.

The OECD reports under Action 6 that “treaty abuse” and “in particular treaty shopping” are key sources of BEPS concerns. Nonetheless, it seems to underestimate the problem of how “treaty abuse” might be understood by different countries, in spite of its attempt to define it in the reports. It also emphasizes that tax treaties “are not intended to be used to generate double non-taxation”, yet, again, different countries might interpret “double non-taxation” differently, and most importantly it is not entirely clear whether a
more broadly defined outcome of “non-taxation” can indeed be an acceptable result of treaty application, provided non-artificial arrangements are observed.

In setting forth recommendations related to treaty shopping, the OECD introduces a three-pronged approach which would mean significant alterations to the tax treaties currently in force (through Action 15), as well as to the Model Convention and to future bilateral treaties. The approach would include:

- First: a change to the title and preamble of the treaties to emphasize that the Contracting States enter into a treaty intend to avoid creating opportunities for “double non-taxation” or “reduced taxation through tax evasion or avoidance”, including through “treaty shopping arrangements”;

- Second: introduction of a specific anti-abuse rule (SAAR) in the treaties based on the “limitation-on-benefits” (LOB) provision that is used by the United States in its tax treaties;

- Third: a more general anti-abuse rule (GAAR), which would also limit situations that could escape the LOB SAAR, namely a “principal purposes test” (PPT).

In some sections of the 2014 Deliverable, the OECD quite appropriately refers to “treaty abuse” and “treaty shopping” in a fairly precise manner, as it systematically advances a concerted effort through multiple initiatives (and under multiple Actions of the BEPS Project) to curb legal structures that absolutely lack economic substance and “functionality”. Wholly artificial or empty “cash boxes”, “IP boxes”, and other forms of “PO Box” entities are simply no longer acceptable (irrespective of their financial capital and legal stance) – if they have ever been. Treaty entitlement is thus conditioned to “substance” and economic functionality (e.g., activities that contribute to value creation, active trade or business, etc.). Accordingly, under the G20 BEPS Project Mandate the OECD clearly and quite appropriately understands that “No or low taxation is not per se a cause of concern, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it.”2 Companies should therefore not be seen to be abusing Treaty benefits where a genuine business is set up, one of the implications of which is a preferable Treaty being available.

This approach would be supported by Brazilian Industry. If the OECD establishes a “minimum standard” of common enforcement and interpretation of tax treaties which does not protect wholly artificial arrangements (or artificial arrangements with consequences that are not intended by both Contracting States in a bilateral treaty), the OECD would reduce potential instances of conflicting interpretation and reduce incoherent practices between countries.

However, the BEPS reports often use the terms “abuse” and “avoidance” somewhat interchangeably and seem to broaden the scope of the G20 Mandate. If the intent of the OECD is to curb “abuse” (and “avoidance in the sense of abuse”, i.e. wholly artificial transactions that may be deemed legitimate in certain jurisdictions), such intent would be very much supported by Brazilian Industry as it “levels the playing field” and allows companies with good corporate governance (such as those that have securities publicly traded in the Brazilian capital markets and/or that are partly funded by the development banks and agencies) not to be at a disadvantage vis-à-vis competitors from around the world that may be “more aggressive”. In some of the passages of the report, however, the use of the term “avoidance” may be interpreted quite broadly and can exacerbate the mandate of the BEPS project, and in fact penalize arrangements that have economic substance, that are not artificial, yet that result in a tax burden “hypothetically lower” as compared to what, unilaterally and subjectively, some tax administrators might prefer. “No or low taxation” in these non-artificial arrangements should not be addressed or limited under the BEPS Project.

That is, in setting out a “principal purpose test”, under a new preamble limiting “avoidance” or “non-taxation”, and allowing domestic laws to limit the application of treaties in situations of “treaty abuse” and “treaty shopping” that are to be defined under domestic laws (in cases where local authorities understand that treaties are used to circumvent the application of local laws), the OECD seems to undertake a perilous approach. This approach not only deviates from the G20 mandate but could undermine the Law of Double Taxation Conventions, and be particularly harmful in Brazil and to Brazilian companies.

As different countries are likely to define “treaty abuse” and “treaty shopping” differently under domestic anti-abuse laws and through domestic enforcement practices, the risk is that countries (particularly those that are
not OECD Members) might unilaterally deny the application of a tax treaty through allegations of abuse and through unilateral interpretation of what constitutes abuse, causing unilateral treaty overrides, which significantly adds risk to (and diminishes) foreign direct investment.

Thus, it is absolutely essential that any such “principal purpose test” or general anti-avoidance rule (or practice derived from a new title and preamble) limiting the application of a bilateral tax treaty and denying treaty entitlement should only be applicable through Binding Mutual Agreement Procedures (with Arbitration), an improvement which is far from consensus under Action 14, particularly as it pertains to non-OECD Members. That is, treaty entitlement or treaty benefits could only be denied by one country under such general rules if the other country also deems a situation to be abusive, using a common standard to be consistently developed by the OECD through Action 14 of the BEPS Project and corresponding Commentary to a new Model Convention to be presented by the OECD upon conclusion of the Project; as such one treaty partner would not be permitted to unilaterally override the treaty by inconsistently and unilaterally interpreting what constitutes “treaty abuse”.

Furthermore, as briefly noted above, the OECD typically defines double non-taxation as an exploitation of incoherence (i.e., obtained through artificiality or abuse, or through harmful or opaque tax regimes), and such definition should not be equivalent to a broader “subject-to-tax” standard (as evidenced by the passage from the BEPS Action Plan quoted above). That is, if a payment is deductible in one jurisdiction and not taxable in another due to incoherent characterization or artificial construct, or if the same payment is deducted twice and only taxable once due to such incoherence or artificiality (such as described under Project BEPS Action 2, Neutralising the Effects of Hybrid Mismatch Arrangements), it seems rather clear that such incoherence or artificiality would create unintended results of double non-taxation. It is such incoherence of treatment, artificiality and unintended results that are the object of G20 mandate under the BEPS Project. If, instead, one country, in the exercise of its sovereignty and tax jurisdiction, decides to apply a low rate of corporate income tax (e.g., Ireland’s 12.5%) or even to exempt certain items income (without faltering into a “harmful tax practice”), irrespective of the “deductibility” of such income in another state, such result should not be seen to constitute “treaty abuse” or “hybridity” or “BEPS”, and instead should simply represent the exercise of a
sovereign taxing right\textsuperscript{3}, provided the required level of substance (for treaty entitlement) is there.

Treaty entitlement to residents that comply with an LOB provision, for example, can result in “low taxation” or even “non-taxation” of foreign-source income (be it through the application of tax treaties or otherwise). However, such result could be unilaterally misinterpreted as “abusive double non-taxation” by countries that might differ in their understanding of the Law of Double Taxation Conventions, and of the BEPS Project Mandate.

The LOB SAAR limits treaty entitlements to “residents” that pass certain tests which aim to identify whether such subjective entitlement to the treaty is justified by sufficient “economic allegiance” in the claimed residence state. Resident individuals and Contracting States (including subdivisions and wholly-owned entities) are by default qualified persons, however, legal entities that are not wholly-owned by the States need to meet intricate economic substance tests related to capital funding and ownership (or an alternative “active trade or business” test). These tests and \textit{bona fide} exceptions are far from perfect, and can fail to capture genuine business structures particularly within highly integrated multinational enterprises (or related to complex financial products). Nonetheless, such tests can be improved, and represent the “state-of-the-art” in terms of curbing treaty abuse through a reliable framework and under the rule of law. The 2014 Deliverable explores this rule as part of its “three-pronged” approach, and the November 2014 and May 2015 discussion drafts continue to advance the discussion of the LOB provision.

**Brazilian Industry is not opposed to the adoption of an LOB provision that complies with EU Law and that is consistent with US standards.** The LOB SAAR, in spite of its own practical issues and inherent complexity, is a useful policy to curb artificial arrangements, as it has been tried and tested by the United States with such purpose, and it seems to meet the policy objectives of the BEPS Project. To the extent that treaty entitlement (residence) is granted in light of the LOB SAAR, however, having a PPT GAAR or broader title/preamble language that defers to domestic laws and unilateral interpretation, permitting a unilateral definition of treaty abuse, \textit{is the recipe for treaty overrides and would undermine the international tax system built by the OECD} and adversely impact international trade and FDI, particularly vis-à-vis non-OECD countries (of the

\textsuperscript{3} That is separate and apart from any considerations under EU Law (e.g., “state aid”).
G20 and beyond), which seems to the contrary to the entire rationale of the joint OECD/G20 BEPS initiative.

Additional Comments on the New Discussion Draft of May 22, 2015

In the new discussion draft released wherein additional comments are requested, and to which this position document is addressed, and in the vast majority of comments submitted to the OECD on the prior discussion draft, we see many of the same issues and concerns discussed herein. Some of the issues that concern Brazilian Industry, and about which we offer our comments, are as follows:

- The “simplified LOB rule” suggested in Part 1 of the 2015 discussion draft, or the comprehensive rule illustrated in the 2014 Deliverable (which replicated the US Model provision of 2006), or the comprehensive rule included in the current OECD Commentary under Article 1, would be equally supported by Brazilian Industry, if such LOB provision is not adopted in combination with any form of unilateral PPT rule and with changes in the preamble and title of the treaties;

- Brazilian Industry supports the proposed changes to the Commentary suggested with respect to the discretionary relief provision of the LOB rule (Part 2, A, 3, item 32, p. 11-12 of the 2015 discussion draft);

- Brazilian Industry supports the development and adoption of an alternative LOB provision that is compatible with EU Law (e.g. Part 2, A, 4-7) and that not only addresses Art. X pars. 1 and 2 but also the “active trade or business” test of par.3;

- Brazilian Industry is not supportive of the deletion of the historical Commentary under Article 1 (Part 2, C, 20, 111, p.41) as these sections provide a rationale for anti-abuse rules that might be coherent with the object and purpose of the OECD Model Convention.
II. Enforcement and Interpretation Issues Affecting Industry within Brazil

(a) Outbound FDI – Brazilian MNEs Foreign Source Income

The Brazilian Tax Authority (and in particular its divisions engaged in Enforcement and Litigation, as opposed to policy design and international affairs) and the Office of the Federal Tax Attorney of the Ministry of Finance seem to have a very unique view of treaty entitlement and treaty interpretation. Such view seems to be contrary to traditional international standards and practices of the OECD, and also to a certain extent conflicting with the new – stricter – standards that are currently being designed under the BEPS Project.

The enforcement and litigation stance of the Brazilian Authorities is that treaty entitlements should always be regarded in first-tier, horizontal, group structures. That is, any indirect ownership of enterprises, however active, should be disregarded and all invested entities should be deconsolidated and deemed directly held by a Brazilian resident parent. That is irrespective of any substance tests or other bona fide indicators of economic allegiance that would otherwise justify treaty entitlement to lower-tier entities. That is so even in cases of uncontrolled subsidiaries, and of ownership chains of entities with active and undistributed (reinvested) foreign source income. To make matters worse, Brazil has a rather limited network of bilateral treaties, which does not – at all – cover the jurisdictions where Brazilian MNEs are engaged in active trade or business.

As such, consider the following structure: a Brazilian MNE BRACo, wholly owns a subsidiary (ActiveSub1) resident in State X, a country with which Brazil has a tax treaty in force. ActiveSub1, in turn, wholly owns another subsidiary (ActiveSub2) located in a State Y with which Brazil does not have a tax treaty in force, and ActiveSub1 also operates a Permanent Establishment (PE) in State Y. Yet, State X and State Y do have a tax treaty in force. Assume both subsidiaries would meet the “active trade or business” LOB test under the X-Y Treaty and are engaged in the same global value chain, and that if Brazil had a treaty with Country Y with an
LOB test, ActiveSub2 too would meet the “active trade or business” test and be entitled to benefits under that hypothetical treaty.

This structure can be depicted as follows:

That is, ActiveSub1 earns “business profits” in State X and in State Y, and is entitled to benefits with respect to such income effectively earned in State X and in State Y. Accordingly Brazil should refrain from taxing the active and reinvested business profits of ActiveSub1 whether or not earned within State X or State Y.

ActiveSub2 would earn and reinvest its own business profits within State Y. Yet, ActiveSub1’s investment in ActiveSub2 represents an income-producing asset of ActiveSub1, whilst both entities develop functions and economic activities that are connected and that form parts of the same active trade or business conducted within X and Y.

At present, the Brazilian enforcement and litigation authorities would seek to limit the application of the treaty between Brazil and Country X to income earned by ActiveSub1 only within Country X, and would thus seek to tax the profits earned by ActiveSub1 through its Permanent Establishment in Country Y. Their allegation is that extending the treaty
protection to the income earned by ActiveSub1 in Country Y through its unincorporated PE would be equivalent to “treaty abuse”. Or to use the language of Action 6, they would consider the extension of the Brazil-X treaty to income earned by ActiveSub1, a resident of X, through a PE in Country Y an “inappropriate circumstance” and hence deny ActiveSub1 entitlement to the Brazil-X treaty.

Similarly, the Brazilian enforcement and litigation authorities would disregard the corporate residence status of ActiveSub1 and its subjective entitlement to the X-Y treaty, disregard its ownership of ActiveSub2, and disregard the joint active trade or business of ActiveSub1 and ActiveSub2, and instead regard ActiveSub1 and ActiveSub2 as if all entities were “fiscally transparent” from a Brazilian perspective, as if they were unincorporated branches of BRCo. And thus the Brazilian enforcement and litigation authorities would seek to subject the active and undistributed business profits of ActiveSub2 to current taxation in Brazil as “business profits” of BRCo. These authorities would deem that the application of the Brazil-X Treaty to the fact pattern above would be necessarily “treaty abuse” and constitute “treaty shopping”, or using the Action 6 language, any indirect ownership would be, by default, an “inappropriate circumstance” that would characterize treaty application as abusive.

Furthermore, the Brazilian enforcement and litigation authorities seem to view any instances of low corporate tax rates (or any granting of exemptions) to active trade or business as equivalent to harmful tax competition, contrary to the view of the OECD, even broader than the definition of “special tax regimes” considered under subparagraph “c” of the active trade or business test of the LOB clause. Therefore, in the fact pattern above, if the corporate income tax rates of Countries X and Y are lower than the Brazilian rate of 34%, any untaxed (or tax-deferred) income would be viewed by such Brazilian authorities as evidence of “double non-taxation”, hence justifying the imposition of the Brazilian tax on active business profits retained and reinvested by foreign corporate subsidiaries.

This situation is already quite unfortunate as it stands, as it imposes a significant burden on Brazilian MNEs and is cause for massive litigation in Brazil, and as it significantly deviates from international tax law standards and practices before and after BEPS. It is a cost and thus a barrier to
outbound FDI by Brazilian MNEs, and accordingly a deterrent to global trade and global welfare.

Having an LOB provision in the treaties, as a specific anti-abuse rule applied by Competent Authority, might actually enhance the situation of Brazilian MNEs with genuine active business structures such as the one depicted hereinabove, with multiple and interrelated layers of ownership and operational activities that also permit access to broader treaty networks, in fact patterns that are viewed favorably by the OECD, that foster FDI, global trade, and global welfare. However, having a broader and general anti-abuse rule that can be interpreted as an authorization for local authorities to unilaterally and selectively deny treaty benefits in such ownership structures, based upon their own interpretation of what kind of “avoidance” might constitute “abuse”, and hence it might reinforce the current practices of the Brazilian enforcement and litigation authorities in their practices which represent treaty overrides that are inconsistent with the OECD interpretation of international tax law before and after BEPS.

(b) Inbound FDI – Brazilian-Source Income of Foreign Investors

Should the Brazilian enforcement and litigation authorities succeed in their interpretation that treaties should be applied horizontally and in de-consolidation for outbound FDI, it would be logical that they could attempt to look through inbound investment structures into Brazil, and deny treaty benefits to “treaty intermediaries” for investments or transaction flows into Brazil.

At the present time there is little incentive to pursue such interpretation as the Brazilian domestic rates of withholding tax substantially match what is permitted in the tax treaties. Nonetheless, such rates may increase (e.g., to 25%) and particularly with the revision of PE standards, and with respect to the taxation of services and intangibles imported into Brazil, it is quite possible that treaty entitlement post BEPS could significantly limit Brazil’s taxing rights. Therefore, given Brazil’s limited treaty network, non-Brazilian MNEs would naturally arrange their affairs so as to benefit from the treaties that Brazil does have in force and, accordingly, the genuine use (not abuse) of treaty intermediaries might become quite relevant post BEPS for several OECD Members that sell into Brazil or otherwise earn income from Brazil.
It is therefore critical to condition any denial by Brazil of treaty benefits under BEPS-related GAARs (title and preamble, and/or principal purposes test) to Mutual Agreement Procedures, and to have such GAARs guided by common OECD standards as opposed to domestic law and practices.

III. Enforcement and Interpretation Issues Affecting Brazilian Industry in China, India, and in Developing Countries

A similar stance may be adopted by other “source jurisdictions”. Suppose that Country Y in our example above are jurisdictions with which Brazil does not have a tax treaty in force and that generally impose high withholding taxation under domestic laws. Should these countries adopt a broader GAAR stance under domestic laws, similar to Brazil’s, withholding taxes imposed abroad on revenues earned by Brazilian MNEs could increase significantly (reducing also the tax revenues earned by the Brazilian Federal Government). Assume, furthermore, that Country X would be the Netherlands, that Country Y would be the United States, and another active subsidiary (Activesub3) would be wholly owned in a Country Z: China or India. The illustration would be as follows:
It is notorious that China and India have aggressive Transfer Pricing practices and equally aggressive policy interests with regard to the reform of Transfer Pricing rules under Actions 8, 9 and 10, and also of PE rules under Action 7. Many developing countries could follow in their footsteps post BEPS and adopt not only UN-recommended practices but more aggressive, subjective, and unilateral post BEPS measures to assess the existence of PEs and the allocation of profits out of Brazil and into such PEs.

Protecting BRCo’s interests through the US-China Treaty, using to Mutual Agreement Procedures between the US and China if potential disputes under Article 5, 7 or Article 9 arise, might result in greater limitations on China’s taxing rights as compared to a direct dispute between Brazil and China (or India for that matter). China would therefore have an incentive to disregard the ownership structure noted above, similar to the stance adopted by the Brazilian Authorities, and deny entitlement to the US-China treaty. In fact, access to another treaty network may be in the interest of the Brazilian tax authorities to the extent that a lower effective rate of Chinese corporate and withholding taxes (in light of the proper application of Articles 5, 7 and 9 for example) would also result in greater tax revenues in Brazil (be it under current anti-deferral rules or upon future distribution out of China).

Here the stance of Brazilian authorities, looking to deny treaty benefits for indirect ownership structures, and joining forces with China and India to permit the unilateral interpretation of “treaty abuse” through treaty and local GAARs, could significantly “backfire”. It could not only harm Brazilian MNEs doing business in developing countries, in China, and in India, but also hurt the Brazilian Treasury.

Also from this stance, it is imperative for the OECD to condition any denial of treaty benefits (e.g., by any country into which Brazilian MNEs indirectly invest) under BEPS-related GAARs (title and preable, and/or principal purposes test) to Mutual Agreement Procedures with Binding Arbitration, and to have such GAARs guided by common OECD standards as opposed to domestic law and practices.
IV. Enforcement and Interpretation Issues Affecting Brazilian Industry in Europe and North America

Similar to the issues discussed under item III above, suppose Country X in our original example is indeed one of the few with which Brazil has a tax treaty in force, and that Country Y is either the United States or Germany, or another European jurisdiction with which Brazil does not have a tax treaty in force. This situation could be depicted as follows:

Having a new LOB provision included in all treaties through Action 15 would likely provide a “safe harbor” to secure entitlement to both treaties in such a structure. However, if greater leeway is granted for Brazil and other countries to interpret “treaty abuse” extensively under domestic laws (through the application of the PPT rule or through a broad interpretation of the change in preamble), and if Brazil’s isolationist stance becomes more widely adopted worldwide (and thus significantly harming German or U.S. investment or sales into Brazil and other countries) it is conceivable that even developed nations such as Germany or the U.S. could “reciprocate”, and attempt to deny treaty entitlement to the intermediary holding entity above, seeking to ultimately impose higher source-taxation on a Brazilian ownership chain given that in the absence of a tax treaty. In reality, this issue might not materialize within the EU (under fundamental freedoms and principles of EU law), but could ultimately occur in the US or other non-EU
“source-countries”, if dividend withholding taxes (or equivalent) taxes are material and would be “avoided” through the structure noted above.

In this sense, and to the extent the LOB tests are met, the interposed country’s Competent Authority (in our example, the Netherlands) would be the only party positioned to dispute the enlarged taxing rights claimed by the source-country (e.g., the US) under a PPT or BEPS-related GAARs. Here too it would be in the best interest of Brazilian Industry (and of the Netherlands and the OECD), for the OECD to condition any denial of treaty benefits (e.g., by any country into which Brazilian MNEs indirectly invest) under BEPS-related GAARs (title and preamble, and/or principal purposes test) to Mutual Agreement Procedures with Binding Arbitration, and to have such GAARs guided by common OECD standards as opposed to domestic law and practices.
Dear Ms de Ruiter

Revised discussion draft on BEPS Action 6: Preventing treaty abuse

We are grateful for the opportunity to comment on this important aspect of the OECD’s work.

CREFC Europe is the voice of the commercial real estate (CRE) finance industry in Europe, representing banks, insurers, fund managers and others providing or intermediating the provision of debt to real estate businesses, as well as advisers, consultants and others with a stake in this sector. We seek to promote transparency and liquidity in CRE finance markets by developing and disseminating best practice and engaging with regulators and policymakers, so that our industry can flourish while playing its part in supporting the real estate sector and the wider economy and delivering returns to investors.

We would generally reiterate the points we made in previous submissions on this BEPS work stream (on 9 January 2015, 9 April 2014 and, jointly with other European real estate industry associations, on 23 May 2014). We are also aware of submissions from INREV1 and the BPF2 in response to the current consultation, and generally agree with their comments.

Our broad support for the OECD’s policy aims in relation to preventing treaty abuse is qualified by our concerns – shared with INREV and the BPF – regarding the need to find workable solutions for collective investment vehicles in our sector, both CIVs and non-CIVs.

CRE and, by extension, CRE debt are large and relatively illiquid asset classes which especially lend themselves to collective investment, including by institutional and other large-scale investors. If international capital is to continue to support investment in the built environment around the world, it is vital that investors who deploy capital collectively have effective access to a treaty network that gives them the same tax treatment that they would have had for individual direct investment.

We have the following specific comments.

• We welcome the introduction of a simplified LOB. It would be helpful to incorporate clause 2(f) from the Annex (certain collective investment vehicles) within the simplified LOB. We also welcome the reduction in the equivalent beneficiary threshold to 75% in the simplified LOB, and would suggest applying it for intermediaries in investment fund structures too. Practical guidance regarding implementation of the equivalent beneficiary rules, in particular covering evidential questions, would be very useful.

• We believe that a pragmatic solution is needed to allow non-CIV collective investment vehicles to benefit from treaties in appropriate circumstances. One way to ensure that only appropriate entities benefit would be to use a diverse ownership test. Further protection against abuse might take the form of denial of treaty benefits to funds which are ultimately more than, say, 10% owned by a single non-equivalent beneficiary (and its connected parties).

1 INREV is the European Association for Investors in Non-listed Real Estate Vehicles.
2 The BPF is the British Property Federation.
We have read and generally support the submissions of the BPF and INREV in response to the current proposal. We hope that the OECD will continue to listen and respond to legitimate concerns around ensuring that the baby is not thrown out with the bathwater. Bona fide cross-border collective investment in real estate and real estate debt quite properly needs to be able to rely on tax treaties, and should not be stymied by an anti-abuse initiative really aimed at quite different behaviours.

Yours sincerely

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The Confederation of Swedish Enterprise is Sweden's largest business federation representing 49 member organizations and 60 000 member companies in Sweden, equivalent to more than 90 per cent of the private sector.

The Confederation of Swedish Enterprise is pleased to provide comments on the OECD Revised Discussion Draft entitled “BEPS Action 6: Prevent Treaty Abuse” 22 May 2015 – 17 June 2015 (hereinafter referred to as the Draft).

General Comments

The initial and prime objective with tax treaties is and should continue to be to facilitate cross-border trade through the allocation of taxing rights between countries and to provide for mechanisms to eliminate double-taxation.

It is of utmost importance that anti-abuse rules are designed so that they have a minimum impact on genuine business operations. Consequently, we believe that perceived inappropriate behaviour is best addressed with specific and targeted anti-abuse provisions. In our view, both the proposed LOB provision and the PPT fail in this respect, since they are too general in nature and not limited to abusive situations.

We acknowledge that some improvements have been made since the last Draft, with some useful examples added. However, considering the added complexity and unpredictability that will follow if these proposals are implemented, we are concerned that, despite requests from numerous commentators, there is still not sufficient guidance in the Draft. In addition, several issues have been postponed by the Working Party until its June meeting and new, and potentially far reaching, proposals such as the “special tax regime” have been introduced at a very late stage in the process.
The Principal Purpose Test (PPT) is too wide and vague and open for ambiguity and misinterpretation. In addition we fail to see how there could be more than one principal purpose. In our view, the test should naturally focus on the principal purpose of the arrangement or transaction.

Furthermore, the technical examples provided on the working of the PPT rule effectively show the difficulty that taxpayers will have in proving the requisite facts to prevent denial of treaty benefits.

In order to provide the necessary legal certainty to taxpayers regarding the tax treatment of their investments, it is crucial that (1) taxpayers have the possibility to get pre-clearance regarding the access to treaty benefits, (2) the proposals and proposed changes to the Commentary provide ample guidance on the application of both the proposed LOB and PPT rules, and finally (3) there should be unobstructed access to a mutual agreement procedure (MAP) and mandatory binding arbitration.

If these three conditions are not met – which they presently are not – it will be virtually impossible for most arm’s length parties to determine whether reduced withholding rates may apply under a certain treaty.

The LOB is still, despite numerous comments, overly restrictive and in some respects potentially in violation with EU law.

We have limited our comments to some of the issues in the Draft.

**Part 1 – Alternative “Simplified” LOB rule and presentation of the LOB rule in the OECD Model**

The Confederation of Swedish Enterprise strongly objects to the combined approach of having both a LOB and a PPT in a tax treaty. Although the Draft suggests a simplified LOB, which naturally is preferable compared to the extensive one as suggested in previous Drafts, it would still leave companies with a lot of uncertainty as to the outcome, since after having passed the simplified LOB, they would be confronted with a very subjective PPT.

**Part 2 – Issues identified in the November 2014 Discussion Draft**

3. **Commentary on the discretionary relief provision of the LOB rule**

The Confederation of Swedish Enterprise welcomes the proposal in paragraph 32 of the Draft that the competent authority should process a request for discretionary relief expeditiously.
4. Alternative LOB provisions for EU countries

As stated in our previous comments, the Confederation of Swedish Enterprise believes that the LOB rule needs to be adapted to reflect EU law requirements. We therefore would like to repeat our concerns in relation to the prohibition of non-resident intermediaries in the ownership tests.

5. Requirement that each intermediate owner be a resident of either Contracting State

We refer to our previous comments that the LOB rule should focus on the ultimate beneficial owner and not intermediate companies.

6. Issues related to the derivative benefit provision

As stated in earlier comments, we strongly support a derivative benefit provision in the LOB. The derivate benefit provision would extend the granting of treaty benefits to entities that are controlled by entities that are resident of a third country and that would enjoy the same treaty benefits with the contracting state in question. In such situations, there is no incentive for treaty shopping.

At this late stage in the process, we strongly object, however, to the proposal to introduce a new treaty provision on “special tax regimes”. This is an issue which should be addressed through the project on harmful tax practices.

7. clarification of the ‘active business’ provision

We agree with the Working Party that there should be clarification on the active business provision, but note that the Draft – specifically paragraph 71 – does not provide such.

B. Issues related to the PPT rule

12. Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level

The Confederation of Swedish Enterprise is in favour of such a requirement in order to prevent excessive use of the PPT and welcomes the proposal in paragraph 79 of the Draft.

13. Whether the application of the PPT rule should be excluded from the issues with respect to which the arbitration provision of paragraph 5 of Article 25 is applicable

As stated in our previous comments, the Confederation of Swedish Enterprise strongly recommends that the application of the PPT should be under mandatory
arbitration. Introducing a substantive provision such as the PPT without the possibility of mutual agreement procedures or arbitration is not acceptable. Consequently, we are pleased that the OECD has decided not to endorse the minority view according to which the application of the PPT rule should be excluded from the arbitration mechanism.

15. Whether some form of discretionary relief should be provided under the PPT rule

The Confederation of Swedish Enterprise is supportive of having a discretionary relief provision under the PPT rule and welcomes the proposal in paragraph 90 of the Draft.

16. Drafting of the alternative “conduit-PPT rule”

We commend the OECD for adhering to the criticism regarding the definition of the term “conduit arrangement” and we are positive to the proposed examples in paragraph 94 regarding the interpretation of such arrangements.

C. Other issues

19. The design and drafting of the rule applicable to permanent establishments located in third States

As stated in our previous comments, we question the necessity of a provision like this in the Model Treaty. This topic may be of interest in relation to some countries and should naturally be carefully considered before entering into a treaty with such a country. At any rate, those situations could be solved bilaterally.

Concluding remarks

Introducing provisions like the proposed LOB and PPT will undoubtedly induce further uncertainty into the Model Treaty and make treaty application even more difficult. The LOB still seems overly restrictive and runs the risk of having a very negative impact on genuine business operations.

Whereas the LOB provision may be considered technically complex, it leaves less room for subjective and arbitrary assessments. The PPT on the other hand takes the opposite approach and does not provide much guidance with respect to when the treaty benefits will be granted. The subjective nature of the PPT opens a door for tax administrations to disqualify taxpayers from treaty benefits where that tax administration finds it appropriate.

In view of the implications of introducing these new provisions in the Model Treaty, and considering the extensive input from commentators, we are disappointed that many issues have not been addressed properly and that the Draft still lacks sufficient guidance in a number of areas. As currently drafted, the Confederation of Swedish Enterprise believes that the provisions could seriously undermine the
certainty and predictability needed for investment decisions and also lead to an increase of double taxation cases. The effect would be very negative on investments, jobs and growth.

On behalf of the Confederation of Swedish Enterprise

June 15, 2015

Krister Andersson
Head of the Tax Policy Department
Dear Marlies,

Revised Discussion Draft on BEPS Action 6: Prevent treaty abuse

Thank you for the opportunity to comment on the Revised Discussion Draft – ‘Prevent treaty abuse’, released on 22 May 2015. Our comments are made from the perspective of the UK.

We note the work done by the Working Party since the release of the Discussion Draft – ‘Preventing the granting of treaty benefits in inappropriate circumstances’, and the need for comments on this revised discussion draft to be kept as short as possible. Our comments are set out below.

1. **Holding companies and the ‘active business’ requirement** – we understand that comments on this issue received following publication of the first discussion document on Treaty Abuse have been considered and that some delegates objected to changes that would substantially broaden the definition of what constitutes the active conduct of a business. We consider this issue to be of sufficient significance that we do wish to raise our concerns once again. The use of regional holding companies, which often have a significant presence in their country of residence, is common and we feel that such holding companies should be entitled to access treaty benefits in a straightforward manner.

2. **Intermediate owners** - although the simplified LOB does permit indirect ownership, the provisions remain restrictive, which the revised discussion draft states is felt to be necessary to prevent base-eroding payments to be made to an intermediate company in a tax haven. However we consider these provisions to be unduly restrictive and likely to restrict commerce unnecessarily. Payments made to an intermediate company which take the form of dividends, are not tax deductible in the vast majority of jurisdictions and will not, therefore erode the tax base of the company making the payments. In addition, other anti-avoidance measures could apply. For example, holding companies in the chain could have controlled foreign company rules which tax the income of low taxed subsidiaries. It could be the case that changes to the ‘derivative benefit’ test could alleviate problems in this area.

3. **Collective Investment Vehicles (CIVs)** - we support the intention of the revised discussion draft that the recommendations of the TRACE project be incorporated into the LOB proposals. We do believe, however, that the interpretation and implementation of these recommendations is vitally important and that it would be better to be more prescriptive about the way in which the Working Party see these
recommendations being implemented.

4. **Pension funds and other non-CIV funds** – although the Working Party have recognised that pension funds should be considered a resident of the State in which they are constituted, regardless of whether they benefit from a limited or complete exemption from taxation in that State. We do not believe that treaty shopping is an area of significant concern in relation to commercial pension funds and the proposed compliance obligations regarding the residence of pension beneficiaries are likely to be too onerous for many widely-held funds. This is information which pension funds may not need to otherwise track and it would be helpful if the compliance burden were to be kept as low as possible.

5. **“Special tax regimes”** – we assume that if these provisions were to be introduced there would be accompanying commentary. In particular:
   a. The meaning of ‘substantial activity’ in respect of financing income;
   b. The application of the exemption in respect of ‘legislation regulation or administrative practice’ to double tax treaties which include these new provisions.

If you wish to discuss any of the points raised in this letter, please do not hesitate to contact either me (bdodwell@deloitte.co.uk), or Simon Cooper (sjcooper@deloitte.co.uk)

Yours sincerely

W J I Dodwell
Deloitte LLP
Ms Marlies de RUITER
Head Tax Treaties, Transfer Pricing and Financial Transactions Division
Centre for Tax Policy and Administration
OECD
Email: taxtreaties@oecd.org

Subject: EBF Comments on the OECD Revised Discussion Draft on BEPS Action 6: Preventing Treaty Abuse

Dear Mrs de Ruiter,

We welcome the opportunity to respond to the OECD’s revised discussion draft regarding BEPS action 6: prevent treaty abuse dated 22 May 2015 (the “Revised Discussion Draft”). In this context, we would like to reiterate our commitment to contribute constructively to the BEPS action plan, in the expectation that the final outcome will deliver fair, certain, sustainable and principled rules.

The present submission follows on from our precedent submission lodged in January 2015 in relation to the discussion draft regarding Action 6 released by the OECD on 21 November 2014.

We have previously highlighted our serious concerns that Action 6, when seen as a whole, potentially conflicts with the principles of the EU Internal Market enshrined in EU treaties, which are binding for a large number of the member countries of the OECD. These concerns arise because a significant proportion of entities carrying out legitimate cross-border activities within the European Union – the world’s largest single market, with transparent rules and regulations – would be denied the benefits, either partially or entirely, from tax treaties on the basis of the ownership of their shares. As indicated in our preceding submission and by reference to a consistent record of decisions from the Court of Justice of the European Union, the prohibition of non-resident intermediaries in the ownership tests set forth in the contemplated Limitation On Benefits (LOB) provisions would trigger in many cases undue discriminations under EU law. In this context, we acknowledge the proposals made in the Revised Discussion Draft pertaining to alternative LOB provisions for EU countries. We are, however, very disappointed that the said proposals are limited to the publicly-listed entity and pension fund exceptions of the contemplated LOB rule, thus leaving similar concerns raised in respect of other entities unaddressed.

Predictable and manageable rules are essential when it comes to determine whether treaty relief is available. Overly prescriptive requirements or provisions based on subjective assessments would indeed risk undermining the usefulness of tax treaty networks. In this respect, we acknowledge the proposal for an alternative “simplified” LOB rule in the Revised Discussion Draft, which provides additional clarity vis-à-vis the LOB provisions foreseen in the preceding discussion draft. In the meantime, we are concerned that the revised wording on both LOB and Principal Purpose Test (PPT) at Article X(5) and X(7) respectively would still grant very broad discretion to competent tax authorities, an outcome that is at risk of paving the way to subjective, and therefore unpredictable, interpretations on the part of tax authorities. In this respect, we reiterate the concerns raised in our preceding submission and evoke consistent case law of the Court of Justice of the European Union according to which anti-abuse measures that are too vague or unspecific in their terms do not meet the proportionality requirement under EU law.

In addition to greater uncertainty with respect to ordinary commercial transactions, we are concerned that the contemplated LOB and PPT provisions might exacerbate a tendency in the approach of tax authorities globally towards the application of more onerous information and evidential requirements.

1 SIAT case (C-318/10, para. 58) and ITELCAR case (C-282/12, para. 44).
at the time of the claim for treaty relief. One consequence is that this may result in a significant
decrease in the ability of investors to receive treaty relief at source, since the only way in which banks
acting on the customer’s behalf to satisfy the information requested would be via a reclaim process.
Proposals leading to a reduced relief at source system contradict to our view the objectives of the
Treaty Relief and Compliance Enhancement (TRACE) system, another tax-related project undertaken
by the OECD, which is aimed at moving towards a “relief at source system”. Whilst TRACE and BEPS
projects have different objectives, we are disappointed that presently there has not been greater
consideration of how TRACE might allow tax authorities to mitigate some of the concerns around
potential treaty abuse whilst providing business with increased certainty in relation to cross border
investment.

In the light of the above considerations and with reference to our prior comments regarding Action 6,
we formulate the following recommendations:

- We urge the European Union and the OECD Member States that are also Member States of
  the European Union to ensure that Action 6 will be implemented among EU Member States in
  conformity with EU law. Uncertainty risks undermining the usefulness of tax treaty networks
  in the context of the EU internal market would significantly impede cross-border trade and
  investment among EU Member states and might at the end of the day seriously interfere with
  the objectives of a Capital Markets Union. In this context, a good starting point would be the
  revised, simplified LOB clause set forth in the Revised Discussion Draft, subject to our
  additional recommendations below.

- The prohibition of non-resident intermediaries in the ownership tests currently foreseen in
  the LOB provisions of the Revised Discussion Draft would certainly conflict with EU law. Still in
  the context of the European Union, we therefore suggest expanding the list of shareholders to
  include shareholders of the Member States of the European Union and the European
  Economic Area.

- Where there is no treaty abuse, swift administrative clearance should be granted. In this
  context, we recommend to consider a pre-clearance process under which treaty benefits
  would be granted if the Competent Authority does not affirmatively deny them within a given
  (relatively short) time frame.

- We encourage the OECD to take greater consideration of how TRACE might allow tax
  authorities to mitigate some of the concerns around potential treaty abuse whilst providing
  business with increased certainty in relation to cross border investment. A transparent and
  predictable relief at source mechanism is certainly in the interest of tax authorities, cross
  border investors and businesses alike as it provides greater certainty around the granting of
  treaty benefits and reduces operational costs associated with reclaim processes for all parties.

- All in all, the application of LOB provisions based on objective characteristics of the party
  seeking treaty benefits should be privileged for the purpose of implementing Action 6. A
  combined application of LOB and PPT provisions on a general basis bears the risk of a
  multiplication of uncertainties and disproportionate burden of proof on the part of taxpayers.
  In this context, we recommend to make clear that the application of the PTT test, should its
  recourse be envisaged, is not intended to undercut the LOB provisions but is directed to
  clearly artificial and tax abusive arrangements.

Yours sincerely,

Wim Mijs
European Business Initiative on Taxation (EBIT)

Comments on the OECD's Revised Discussion Draft on BEPS ACTION 6 on Preventing Treaty Abuse
EBIT welcomes this opportunity to provide comments to the OECD on the Revised Discussion Draft on “BEPS Action 6 Preventing Treaty Abuse” (hereinafter “the Discussion Draft”). We refer to EBIT Members’ previous comments submitted to you on 9 April 2014 and 9 January 2015, which commented more extensively on the Action 6 proposals, many of which remain relevant. The comments in this note focus on the main concerns we have with the Discussion Draft.

- EBIT Members generally support the OECD’s work on preventing Treaty Abuse, but urges the Working Group to ensure that the proposals to mitigate any BEPS concerns around treaty abuse are in line with the fundamentals of international tax treaty policy, continue to promote bilateral trade and investment, and provide access to tax treaties to their intended beneficiaries. Last but not least, the OECD’s proposals should be targeted, proportionate, and even-handed.

PART 1 – ALTERNATIVE “SIMPLIFIED” LOB RULE AND PRESENTATION OF THE LOB RULE IN THE OECD MODEL

- EBIT Members welcome the introduction of the concept of a simplified limitation of benefits (LOB) article. We note that the proposed Entitlement to Benefits article (ETB) was strongly inspired by the most recent US LOB rule and is seemingly introduced for US domestic policy concerns. We also note that a new US Model Income Tax Convention is being developed which includes revisions to the LOB. In our view having these evolving US centred rules and proposals in a new OECD Model Convention, or in a multilateral convention, is not helpful. EBIT strongly believes that such domestic policy concerns should be addressed under domestic law, however, and not through treaties.

- We are particularly concerned that the proposals in the Discussion Draft appear to prescribe a combination of the use of the proposed simplified LOB to treaties with a principal purpose test (PPT) test, i.e. the simplified LOB would only be available to the limited number of treaties where both treaty partners agree to this combined test. EBIT Members note, however, that the LOB rule and the PPT rule are targeting distinct treaty shopping issues, respectively, eligibility of treaty residents for treaty benefits and targeting abuse of treaties by eligible treaty residents, which must therefore not be combined, especially given countries’ prerogative to choose to apply either a LOB rule or a PPT rule. We strongly urge the OECD to propose the simplified version and to allow bilateral treaty partners to customise a treaty LOB provision as deemed appropriate.

PART 2 – ISSUES IDENTIFIED IN THE NOVEMBER 2014 DISCUSSION DRAFT

A. ISSUES RELATED TO THE LOB PROVISION

3. Commentary on the discretionary relief provision of the LOB rule

- In EBIT’s view, the Discussion Draft imposes new standards rather than adds further clarification of the existing standards. The objective tests for eligibility for treaty benefits deny...
access to the treaty to treaty residents that are not treaty shopping. We note the proposed additional requirement in new paragraph 63 that in order to be granted treaty benefits a claimant must establish, to the satisfaction of the competent authority of the State from which benefits are being sought, that there were clear non-tax business reasons for its formation, acquisition, or maintenance and for the conduct of its operations in the other Contracting State. In practice this is in many instances not at all a straightforward process, however. On the contrary. For instance, one EBIT Member has had an application for discretionary relief with a tax administration for two and a half years, in a case where the facts were quite straightforward. EBIT Members are concerned that this new additional requirement is unnecessary and inappropriate, especially given the already broad discretion tax administrations have in determining whether to grant benefits. Also, situations where a taxpayer had no interest in the relevant treaty at the time of establishing residency in the treaty jurisdiction, could be caught by the proposed provision.

- We understand that there is currently no consensus view on Action Item 6. The reference in the proposed new paragraph 64 of the Discussion Draft that the discretionary grant process in all the BEPS-44 countries “should be handled expeditiously” is not helpful. EBIT urges the OECD to include a hard time limit of 6 months in its proposals for finalisation of applications for discretionary relief by competent authorities. Ensuring the appropriate application of anti-abuse provisions such as the discretionary relief provision of the LOB risks otherwise depending too heavily on competent tax authorities’ levels of technical expertise and notions of “reasonable behaviour”.

5. Requirement that each intermediate owner be a resident of either Contracting State

- EBIT Members are concerned that the Discussion Draft proposes to deny treaty benefits to subsidiary companies which have an intermediate owner that is not a resident of either Contracting State. We are concerned that this proposal is not compatible with today’s legitimate international business models and reality whereby it is commonplace that subsidiaries have an intermediate owner in a third jurisdiction, as a consequence of international acquisition or regional structuring choices. We also wish to note that subsidiaries, under most tests, will already have to meet a base erosion test, so adding another test is pointless, but it will mean an unwelcome additional compliance burden for multinational business.

6. Issues related to the derivative benefits provision

- We welcome the Working Party considering the proposed language regarding pension funds but are concerned at the proposed introduction of the exclusion of special regimes and the partial treaty abrogation rule with no discussion or proper consultation at this late stage of the BEPS process. The term ‘special tax regime’ is for instance broadly defined which could create considerable uncertainty for business. EBIT recommends that any concerns over ‘special tax regimes’ should be addressed as part of Action 5 (harmful tax practices).

7. Provisions dealing with “dual-listed company arrangements”

- EBIT Members welcome the requirement for competent authorities to deal with requests regarding dual residence “expeditiously” - but here again - we believe it is important to add a concrete timeline. Our suggested wording is: “The competent authorities to which a request for determination of residence is made under paragraph 3 should deal with it within 6 months, unless there are exceptional circumstances preventing this, and should communicate their response to the taxpayer as soon as possible.”

10. Clarification of the “active business” provision

- EBIT does not believe that the active business test is really clarified. We note that in almost all US tax treaties with an LOB, the business activities in the residence country of an affiliate can be
attributed to the resident company claiming the treaty benefits. The Discussion Draft states that the Delegate for the United States has proposed that the attribution rule should not apply if the claimant itself is not conducting business in the residence jurisdiction. We strongly believe that once the business nexus to the jurisdiction is established, the taxpayer should not be deprived of the treaty benefit if the taxpayer chooses a local organisation involving multiple entities. The proposal from the Delegate for the United States is not helpful as it would force businesses to arrange their operations in such a way as to have the operating company hold the shares rather than the holding company.

B. ISSUES RELATED TO THE PPT RULE

14. Aligning the parts of the Commentary on the PPT rule and of the Commentary on the LOB discretionary relief provision that deal with the principal purposes test

- EBIT Members welcome the inclusion of concrete examples to try to provide further clarity around the concept of “principal purpose” as used in the Discussion Draft. The examples provided give only very limited guidance and clarification, however, because they are very straightforward and do not cover complex situations. We urge the OECD to add further examples which could be based on some of the suggestions which have been made by stakeholders earlier on in this public consultation process.

- With regard to the alignment of the standards under the discretionary grant procedure in the LOB article with the standards applied to the PPT, we refer to our earlier comments aimed at ensuring an even-handed and equitable approach to the discretionary grant (or denial) of treaty benefits.

- EBIT recommends to replace the last sentence of proposed paragraph 63.1, to ensure that information requests by tax authorities are sufficiently targeted and offer some protection to taxpayers, with: “All evidence relevant to the determination of a principal purpose must be provided to the competent authority in order to enable it to determine whether this is the case.”

C. OTHER ISSUES

19. The design and drafting of the rule applicable to permanent establishments located in third States

- EBIT urges the OECD to reinstate paragraph f): excepting royalty income from the rule if the royalties are earned with respect to intangible property produced or developed by the enterprise through the permanent establishment. From an EU law perspective, the Cadbury Schweppes case would suggest that taxing rights on an arm’s length profit earned by activities undertaken in the jurisdiction of the PE should remain with the source country, irrespective of the effective rate of tax.

- EBIT trusts that the above comments are helpful and will be taken into account by the OECD in finalising its work in this area, and EBIT is always happy to discuss with the OECD.

Yours sincerely,

European Business Initiative on Taxation – June 2015

For further information on EBIT, please contact the EBIT Secretariat via Bob van der Made, Tel: +31 6 130 96 296; Email: bob.van.der.made@nl.pwc.com).

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Dear Mrs. de Ruiter,

REVISED DISCUSSION DRAFT – FOLLOW UP WORK ON BEPS ACTION 6: PREVENT TREATY ABUSE - 22 MAY 2015

EFAMA\(^1\) welcomes the opportunity to comment on the Revised Discussion Draft "BEPS Action 6: Prevent Treaty Abuse" issued on 22 May 2015.

1. Part 2.A.1.: Collective Investment Vehicles ("CIV")

EFAMA welcomes the recognition of the importance of ensuring CIV treaty entitlement is retained. We support that the conclusions of the 2010 CIV Report are appropriate in the context of dealing with the application of any limitation on benefits ("LOB") clause.

EFAMA also welcomes the Simplified LOB approach, to the extent that it results in a less subjective outcome than widespread primary reliance on principal purpose tests ("PPT"). The Simplified approach should facilitate the more effective application of such LOB rules for international business generally. We agree that, as intended, the Simplified LOB is likely mean many more source countries preferring the LOB approach. For funds that are primarily sold mainly in just one home or domestic market, demonstrating that most investors are primarily entitled, or at least equivalent beneficiaries, may be quite easy.

Many funds are however much more widely distributed, and Luxembourg or Irish domiciled funds are routinely distributed beyond Europe to Asia and Latin America, with any one fund often achieving

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\(^1\) EFAMA is the representative association for the European investment management industry. EFAMA represents through its 26 member associations and 63 corporate members almost EUR 19 trillion in assets under management of which EUR 12.7 trillion managed by 55,600 investment funds at end March 2015. Just over 29,300 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 26,300 funds composed of AIFs (Alternative Investment Funds). For more information about EFAMA, please visit [www.efama.org](http://www.efama.org)
substantial sales in 25-30 countries. In such circumstances, demonstrating compliance with an “equivalent beneficiary” test is less straightforward. Retail funds are typically held through distributors and would only have information about those distributors as legal owners (as opposed to beneficial owners). FATCA and Common Reporting Standard (“CRS”) require the financial services industry to enhance the documentation of investors, but even these significant initiatives work on the core principle that each financial institution only sees the next institution in the chain, and only rarely require look-through to the end beneficial investor. So, even a fully CRS compliant fund would not know the treaty entitlement of its end investors.

TRACE, by contrast, is designed to improve efficiency for claiming treaty benefits for investors. The BEPS Action 6 Revised Discussion Draft acknowledges the role of the TRACE project in the practical application of the CIV Report recommendations. We are supportive of early TRACE implementation, but are concerned that in practice implementation may be quite protracted and will not in all cases ensure treaty entitlement of CIVs.

In sum, wider adoption of an LOB approach means more cases where the lack of data about underlying beneficial owners is problematic, and while TRACE is a potential solution for certain distribution structures of CIVs in some countries, it may not be workable for CIVs in all countries or may not be in place for some years. We therefore believe the commentary to the Multilateral Instrument should encourage governments to adopt:

- A purposive approach to applying the 2010 Report\(^2\), and constructive use of the Clause 2(f) proposed in the OECD Report dated 16 September 2014\(^3\), to ensure CIVs are protected even in cases where LOB approaches are practically difficult;

- "Administrative flexibility", such that any analysis of the “equivalent beneficiary” test should be based on available data on a best efforts basis. For example, where a CIV’s units are distributed through intermediaries, it should explicitly be permitted that the jurisdiction of the intermediary is taken as the country of residence of the investors on whose behalf the intermediary has invested. Another example is where a CIV has obtained authorization by financial market authorities in order to be distributed in specific countries, it should explicitly be permitted that the CIV’s units are deemed to be held by residents of those countries where the units are distributed; and in addition,

- Fast track adoption of TRACE.

2. Part 2.A.2: Non-CIV

Unlike CIVs, non-CIV funds are not sold to the public, and although some might be widely held, determining ownership is typically less difficult than for widely held and widely distributed CIVs. The Simplified LOB approach, with a suitably drafted equivalent beneficiaries’ provision, might be an appropriate determinant of treaty access.

Non-CIV funds provide vital source of capital to companies, particularly to small and medium businesses, infrastructure projects, property development and other essential economic activities. They are formed for the purpose of providing access to investment opportunities for a variety of


\(^3\) Preventing the Granting of Treaty Benefits in Inappropriate Circumstances – OECD – 16 September 2014
investors, typically institutionally investors representing pension funds and insurers. We welcome the proposal to include examples of non-CIV funds in the commentary on the application of the PPT rule, and we hope the examples reflect the true purpose of the vast majority of non-CIV funds. For the purpose of clarity, we also believe that the examples could also illustrate situations where non-CIV funds are used for treaty shopping purposes.

We believe that an appropriately applied LOB rule, along with suitably targeted examples of non-CIV funds in the Commentary should mitigate concerns that non-CIV funds can be used to provide treaty benefits to investors that are not themselves treaty entitled.

However, if there remain concerns about inappropriate access to treaties through non-CIV funds, one additional safeguard would be to deny treaty benefits for non-CIV funds where a single investor (along with its related parties) that is not treaty entitled, or an equivalent beneficiary, holds over 10% of the economic interest in the fund. This would provide even greater surety that it cannot be used for treaty shopping purposes.

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) 2513 3969.

Kind regards,

Peter De Proft
Director General
Comments on revised discussion draft on Action 6: Prevent Treaty Abuse

EPRA has taken note of the OECD’s invitation to submit comments on the revised discussion draft on Action 6 of the BEPS Action Plan, dated May 22, 2015. In line with our previous submissions from April 9, 2014, May 23, 2014, and March 9, 2015, and in accordance with the views expressed by other organisations representing Real Estate Investment Trusts (REITs), including the National Association of Real Estate Investment Trusts (NAREIT), EPRA’s comments are related to the following:

Limitation on Benefits Provision (LOB)

EPRA welcomes the approach taken by the Working Party on Tax Conventions and Related Questions to address the concerns of the REIT industry. In particular, the Working Party’s decision to further discuss the inclusion of a specific reference to the conclusions of the 2008 REIT Report, as stipulated under paragraph 20, is a welcome development.

In accordance with the OECD report on “Tax Treaty Issues Related to REITs”, REITs, as well as persons wholly-owned by REITs, can be considered qualified persons for purposes of the limitation-on-benefits (LOB) rule. In order to ensure that access to tax treaty benefits is not denied to many bona fides REITs, the suggested reference to this report should be included in the footnote to the first part of paragraph 31 of the Commentary on subparagraph 2 f) of the LOB rule included in paragraph 16 of the Report on Action 6. EPRA encourages the Working Party to retain the proposed wording below, with particular clarification to the point underlined. EPRA believe that such clarification would account for the various REIT regimes across the EU (as well as worldwide). EPRA would also welcome further prominence be given to this proposal by placing it in the main body of the text, rather than as a footnote:

31. As indicated in the footnote to subparagraph f), whether a specific rule concerning collective investment vehicles (CIVs) should be included in paragraph 2, and, if so, how that rule should be drafted, will depend on how the Convention applies to CIVs and on the treatment and use of CIVs in each Contracting State.\(^1\) \textit{Whilst no such rule will be needed with respect to an entity that would otherwise constitute a “qualified person” under other parts of paragraph 2}, a specific rule will frequently be needed since a CIV may not be entitled to treaty benefits under either the other provisions of paragraph 2 or \textit{under paragraph 3}, because, in many cases ...

\[^{1}\text{Footnote 1}\] See also paragraphs 67.1 to 67.7 of the Commentary on Article 10 and the report “Tax Treaty Issues Related to REITs” which deal with the treaty entitlement of Real Estate Investment Trusts (REITs), which should also be applicable to persons wholly-owned by REITs. With respect to the application of the definition of “resident of a Contracting State” to REITs, see paragraphs 8-9 of the report “Tax Treaty Issues Related to REITs”.
Nevertheless, it would be important to add an additional sentence to the aforementioned footnote, noting that “a specific rule concerning CIVs would not be relevant to the application of paragraph 2 to those REITs that would be qualified persons under other subparagraphs of such paragraph. This would provide a REIT-specific illustration of the general point made in the Commentary.

Principal Purpose Test Provision

In relation to the proposed Principal Purpose Test (PPT) provision, paragraphs 97 of the revised discussion draft states that the Working Party agreed to include four new examples in paragraph 14 of the proposed Commentary on the PPT rule. The new examples listed under paragraph 98 do not include investment vehicles. However, paragraph 25 states that the Working Party intends to further discuss adding one or more examples on non-CIVs to the Commentary on the PPT rule. EPRA therefore encourages the Working Party to add a REIT specific example (which EPRA is willing to provide) to paragraph 14 of the Commentary during its meeting in June.

New treaty provisions on “special tax regimes”

Under paragraph 53, the OECD invites comments on a proposal made by the US Treasury delegate to the Working Party for a new provision on “special tax regimes.” The revised discussion draft indicates that it was concluded that a decision on this proposal would need to be reached at the June meeting and would take into account the comments that will be received.

Under the proposed special tax regime provision, withholding tax reductions on interest, royalties and other income would be denied if the income is subject to a special tax regime in the residence country. Special tax regime is defined as anything providing a preferential effective tax rate to an item of income through reductions in the tax rate or the tax base. A series of exclusions from treatment as a special tax regime is set forth in the provision, including an exclusion for any legislation, regulation or administrative practice:

vii) that facilitates investment in widely-held entities that hold real property (immovable property), a diversified portfolio of securities, or any combination thereof, and that are subject to investor-protection regulation in the Contracting State in which the investment entity is established;

This exclusion is conditioned on the entity being subject to investor-protection regulation, which is the same condition that is part of the CIV definition. The inclusion of such a condition would mean that
REITs would not qualify for this exclusion from the definition of special tax regime, if REITs would be considered to meet the basic definition.

In line with the position expressed by NAREIT, EPRA requests that, if the Working Party includes the special tax regime provision in its recommendations, the Commentary language accompanying it should explicitly state that European REIT regimes qualify for the exclusion for legislation that facilitates investment in widely-held entities that hold real property.

About EPRA

EPRA is the voice of the publicly traded European real estate sector: it is the representative association for commercial property companies that are quoted on the public stock exchanges of Europe and other exchanges around the world. With more than 200 active members, EPRA represents over EUR 350 billion of real estate.

EPRA’s membership also includes the institutional investors such as pension funds and insurance companies that invest in, or have an interest in investing in real estate indirectly via these listed property companies. Through the provision of better information to investors, improvement of the general operating environment, diffusion of best practices and the cohesion and strengthening of the industry, EPRA works to encourage greater investment in listed real estate companies in Europe with long-term and stable income producing assets.
On behalf of the Public Affairs Executive (PAE) of the EUROPEAN PRIVATE EQUITY AND VENTURE CAPITAL INDUSTRY

17 June 2015

To Organisation for Economic Co-operation and Development (OECD)

Re Consultation on Public Discussion Draft BEPS Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances.

Introduction:

The Public Affairs Executive (PAE) of the European Private Equity and Venture Capital industry is pleased to provide its comments on the third public discussion draft released by the OECD on Action 6 (“the Consultation Document”).

We write on behalf of the representative national and supranational European private equity (including venture capital) bodies. Our members cover the whole industry, from the institutional investors who provide the capital for investment to the private equity firms who invest the capital in European companies at all stages of their development.

Summary of Main Points:

- Existing due diligence procedures (such as the requirements under FATCA and Anti-Money Laundering legislation) already offer an efficient means of ensuring that private equity funds are not used to provide treaty benefits to investors who are not themselves entitled to treaty benefits.

- Deferring distributions from the private equity fund would have an adverse impact on investors’ management of their funding risk and negatively impact the internal rate of return of the fund. There is therefore a strong commercial imperative inherent in private equity fund models to distribute quickly.

- During its life-cycle, it is impossible for the private equity fund to take into account the tax status of each of its ultimate investors when the fund manager decides the structuring of the fund’s investments.

- The intermediate holding company structures used by private equity funds should not disadvantage such funds in their tax treatment as the structure

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1 The term “private equity” is used in this paper to refer to all segments of the industry, including venture capital. The term “venture capital” is used in specific contexts where there are issues that relate particularly to this segment.
is not designed to facilitate tax avoidance. Rather, they serve to prevent the tax distortion and barriers to investment that exist under the current laws, due to the lack of global harmonisation of the treatment of entities used in fund structures and for other non-tax reasons.

- A private equity fund as such cannot be used to defer recognition of income. The OECD’s concern for investors in non-CIVs is thus a separate question of investors and their tax status in their respective locations. The debate should not be misconstrued in the framework of the treaty benefits of fund structures.

- We believe that further work could, however, be undertaken on the creation of an additional category of qualified person, to include the concept of a ‘qualified fund’, provided this were tailored and appropriate to the private equity industry, based on existing reporting requirements.

- We agree with the conclusions of the Working Party that it should continue to explore solutions to issues related to the treaty entitlement of non-CIV funds and their holding companies. In this light, we would like to see the creation of a specific OECD Working Group dedicated to examining solutions to non-CIVs which will continue work beyond the current deadline of September 2015 for Action 6 under the BEPS project.

**How Private Equity Operates in Practice:**

In our response to the previous discussion draft, we provided an overview of what private equity is, as requested by the OECD. We also provided some brief information as to how private equity operates in practice, explaining who the institutional investors that invest into private equity funds are, the typical sectors into which private equity funds invest, and the average time-periods for the lifecycle of private equity funds and holding of portfolio companies by the fund. In this paper, we would like to provide a concrete example of how a private equity fund works in practice.

Private equity *firms* are often global in nature, having offices in numerous major cities throughout the world. When a private equity firm is considering where it will establish a fund, this choice is mainly made on the basis of criteria such as the residence of the management team and the ability of the structure to be suitable for, and acceptable to the majority of the international investor base. In the EU, given the new European regulatory framework under the Alternative Investment Fund Managers Directive (AIFMD), most management teams prefer to market European funds which are Alternative Investment Funds (AIFs).
If a private equity firm decides to establish a fund in France for example, there are various legal requirements under both French law and EU law which must be adhered to. French private equity structures are usually FPCIs or FPSs that can have legal personality. These structures are not in the scope of French income tax or corporate tax and as a result, they are not considered as tax resident entities and cannot automatically benefit from the tax treaties which other Member States have signed with France.

Before admitting an investor into the fund, the fund must comply with several specific due diligence procedures regarding the status of the potential investor. Pursuant to Articles L. 561-2 et seq. of the French Monetary and Financial Code (Code Monétaire et Financier), which implements domestic provisions on the fight against money laundering and the financing of terrorism, a fund manager must:

- assess the risks of money laundering and financing of terrorism; and
- verify, as far as possible, the identity of each investor and the effective beneficial owner of the investment in the private equity fund.

Each investor must complete an anti-money laundering and anti-financing of terrorism questionnaire and provide all necessary information including: constitutive documentation in respect of such investor; a declaration made by the investor in relation to the determination of the nature and the provenance of any funds invested; an annual report; a certificate of incorporation or registration; (where applicable) a copy of any relevant passports or identity documentation; a list of effective beneficial owners; and a declaration and supporting evidence regarding the residence of any effective beneficial owners.

In addition, there is voluntary action around the world to implement multilateral tax information exchange between countries, so as to deal effectively with tax evasion. This started with the introduction of US rules under the Foreign Accounts Tax Compliance Act (FATCA), aimed at tackling tax avoidance by US taxpayers. Further efforts to increase tax information exchange are continuing, both at EU level (such as amendments to the Directive on Administrative Cooperation) and at global level (such as the OECD Common Reporting Standard).

These existing due diligence procedures on the status of a private equity fund’s direct and indirect investors, carried out to the greatest extent possible by the private equity fund upon the creation of the fund and before acceptance of the subscription of an investor, already offer an efficient means of ensuring that private equity funds are not used to provide treaty benefits to investors who are
not themselves entitled to treaty benefits (this being the first general concern regarding non-CIVs raised by the OECD Working Party).

The financial business model of a private equity fund relies on a strong principle of alignment of interest of investors and the fund manager since the management team always invest a significant amount alongside the investors (between 1% and 3% of the size of the fund) and in addition, can obtain a percentage of 20% of capital gains of the fund (carried interest) after a minimum rate of return received by the investors (“preferred return”).

Furthermore, it is important for investors to be able to manage cash flows effectively, which also impacts the ability to better manage the funding risk of their investment. In this regard, deferring distributions would not be helpful to investors and it would negatively impact the internal rate of return (the ‘IRR’) they achieve. There is therefore a strong investor imperative to distribute quickly.

The result of this financial model is that the fund manager will make its best efforts to ensure that the fund distributes to its investors as soon as practical the amounts received from investments. In any case, as private equity fund structures are most often tax transparent and many investors are tax exempt, any deferral of distributions would not necessarily result in any tax deferral. This financial business model is relevant to the second general concern raised by the OECD Working Party.

Generally speaking, private equity funds make equity investments and debt investments. The normal exit is to sell their equity and debt investments after five years or more. In addition, the investment by the fund is usually made with third-party debt financing (e.g. mezzanine debt, senior bank debt). In such a context, a private equity fund cannot make investments without creating an interposed wholly-owned holding company in order to make its investments and also to locate the mezzanine debt and the senior bank debt.

During its life-cycle, it is impossible for the private equity fund to take into account the tax status of each of its ultimate investors when the fund manager decides the structuring of the fund’s investments, as to do so would create significant conflict of interest issues given the different tax situations of investors. In addition, there is no universal rule on the tax transparency of a private equity fund. As a result, the investee countries may refuse (i) to recognise the tax transparency of a fund that is established in another country.

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2 The fund must pay a fixed priority return (around 7 or 8%) on contributions of investors that have not been yet repaid.

3 For more information on who the investors into private equity funds are, please see pages 3 & 4 of our Response to the 2nd OECD Consultation Document on Action 6 which was submitted in January 2015.
and (ii) the tax residence of the fund as it is not subject to tax. This has the effect of denying treaty relief to treaty eligible investors.

For these reasons, the private equity fund is expected to invest through one or more wholly-owned holding companies. There is no doubt that these holding companies have a real business substance because they are the financial pillars of the investment made by the fund. In order to benefit from the protection of tax treaties, a private equity fund generally arranges the governance within the holding companies so that the decision that these companies make are taken locally at their level. In addition, to strengthen the limited liability of investors in the fund (which is a key criterion for the investors), it is advised to have a strict distinction between the management of the fund localised at the level of the fund manager.

Although some of the above requirements imposed on the fund and fund manager may be specific to French law as per this example, equivalent rules are found across the EU and indeed beyond. Therefore while the specifics of a private equity fund’s operations may differ from country to country, the essence of the fund’s activities generally remains the same. This is due to natural harmonisation of rules as investors who invest their money across borders feel more protected when the differences between regulatory environments are minimised.

As can be seen, the above example shows that private equity funds, being closed-ended and unleveraged, use intermediary holding company structures and channel capital from institutional investors to the real economy. Contrary to some other vehicles which are classed as non-CIVs throughout the rest of the world, there is business substance in these intermediary holding structures and they perform valuable functions.

The LOB test presents two threats to these investments made by the private equity community. The first is the compliance burden. As set out above private equity funds devote time and resources to carry out due diligence on their beneficial owners and have invested significantly in systems to comply with FATCA and to be CRS-ready. But these existing regimes (the anti-money laundering rules, FATCA and CRS) adopt a pragmatic approach in balancing the burden placed on financial institutions against the risks which the regimes are intended to mitigate. For example, if an investor in a private equity fund is itself FATCA-compliant, the private equity fund does not need to make any further report in relation to it. Similarly, the focus of most national anti-money laundering laws is on identifying those beneficial owners with a stake of 25% or more. As set out in our previous submissions, satisfying the LOB test would be significantly more onerous for a widely held non-CIV fund than complying with these existing regimes.
The second and more critical concern (as set out in the examples in our previous submission) is that a private equity fund using a structure such as the one just described would face double taxation due to the inability of the fund and/or its holding structure(s) to satisfy the LOB test.4

We have also previously provided examples of how the proposed Principle Purpose Test (PPT) is too wide and is likely to be implemented inconsistently across BEPS participant jurisdictions.5 We believe that the PPT rule should be re-drafted to apply only in cases where it is determined that “the principal purpose” of an arrangement is to obtain tax treaty benefits, rather than being “one of the principal purposes”.

**Use of Intermediary Structures by Private Equity:**

As can be seen in the example described above of a private equity fund domiciled in France, private equity funds usually use holding companies to acquire portfolio companies. The legitimate use of intermediaries for investment funds is acknowledged in the OECD 2010 Report: “CIVs thus act as both issuers of securities and investors in securities. As a result, there may be layers of intermediaries both below the CIV (i.e. between the issuer of the security in which the CIV is invested and the CIV), and above the CIV (i.e. between the CIV and the beneficial owner of the interests in the CIV). In many cases, those intermediaries will not be located in the country in which the issuer is located and may not be located in the country in which the investor is located.”6

The OECD 2010 Report acknowledges the difficulty for CIVs in identifying the ultimate investors in the fund: “[t]he difficulty in tracing of course also is compounded by the fact that interests in CIVs frequently are held through layers of intermediaries. In those cases, the CIV’s records will show the names of the intermediaries through which the investors hold their interests in the CIV, rather than the names of the investors themselves.”7

The intermediate holding company structures used by private equity funds should not disadvantage such funds in their tax treatment as the structure is not

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4 Please see pages 6 & 7 of our Response to the 1st OECD Consultation Document on Action 6 which was submitted in April 2014.

5 Please see pages 17 & 18 of our Response to the 2nd OECD Consultation Document on Action 6 which was submitted in January 2015.


7 ibid, pp7
designed to facilitate tax avoidance. Rather, they serve to prevent the tax distortion and barriers to investment that exist under the current laws, due to the lack of global harmonisation of the treatment of entities used in fund structures and for other non-tax reasons to meet the needs of investors. They allow a fund to invest in an asset on the same level as other investors in that asset. They can facilitate access to tax treaty provisions for investors in the fund without those investors having to make treaty claims individually. They can also provide practical benefits such as allowing participation in shareholder meetings and votes, and making the conclusion of contracts more straightforward.

Tax Status of Investors:

As can be seen from the example described above of a private equity fund domiciled in France, the specific tax status of many ultimate investors is something that the fund is unable to control or influence and, in many cases, ascertain due to investors investing via funds of funds and other indirect methods. The Consultation Document states that future work in this area should address two general concerns: firstly that non-CIVs may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits, and secondly, that investors may defer recognition of income on which treaty benefits have been granted.

In our view, it is misaligned to conflate these two concerns with the tax treaty eligibility of fund structures. As can be seen in the example, as soon as the fund divests the assets, that return on capital will be distributed to the investors in the fund. Thus, a private equity fund as such cannot be used to defer recognition of income.

At this point, the taxation of those returns in the hands of the investors is an issue which is beyond the reach of the fund manager. It would be illogical, in our view, to penalize those non-CIVs which perform a legitimate capital-channeling function simply because there is a potential that the investors into those funds may not be fully tax compliant on a standalone basis in their particular jurisdictions. As demonstrated in the example described above, this potential is significantly mitigated by the fund manager’s due diligence requirements. Rather, we believe the OECD should focus on fund structures having a wide investor base - as explained in our previous response - and as such identify those funds which are not structured for treaty shopping purposes.

Although a significant percentage of investors in certain fund structures are entitled to relief in their own right by making a claim through a double tax treaty if they were a direct investor, administratively it is far more efficient that
they receive the correct return in the first place without having to resort to treaty claims. This is especially so if the investor is tax exempt like most pension funds. In this case, the tax levied becomes a de facto cost as there is no tax levied in the investor’s home jurisdiction against which this tax can be offset. This is also an issue where withholding tax is applied to interest income and dividends or more importantly capital gains tax is levied on non-resident investors.

Should the fund manager take on the role of processing tax reclaims on behalf of investors, then it will still involve increased resources and costs, thereby reducing returns. It will also mean that there could be a significant delay in some investors receiving all the proceeds due to them as the processing of repayment claims by tax authorities can be slow (sometimes taking years, rather than days). Without an intermediary holding company, funds could also be exposing their investors to local tax filing requirements, which is not the aim of Action 6 nor the BEPS project overall. Even where all the investors are entitled to relief in their own right, inconsistencies in the tax treatment of commonly used fund entities can still create barriers to obtaining relief in practice.

**Importance of Private Equity in Financing the Real Economy:**

We are pleased to see that the Consultation Document states that the Working Party “recognised the economic importance of these funds and the need to ensure that treaty benefits be granted where appropriate.” Indeed, the economic importance of private equity & venture capital funds must not be overlooked. The recent publication of the Capital Markets Union Green Paper by the European Commission is illustrative in this regard. The goal of the Capital Markets Union (CMU) is to reduce the reliance on bank financing, unlock investment in Europe’s companies and infrastructure, thereby creating a true single market for capital for all 28 Member States in the EU, and in so doing create jobs and growth.

The European Commission explains why they are pursuing their goal of creating a CMU, pointing out that if European venture capital markets were as deep as the US, “as much as €90 billion of funds would have been available to finance companies between 2008 and 2013.” According to the CMU Green Paper, “private equity and venture capital play an important role in the European

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10 ibid, pp 2
economy.”11 The Green Paper then specifically asks “[h]ow can the EU further develop private equity and venture capital as an alternative source of finance for the economy?”12

We note that the OECD Working Party has agreed that pension funds should be considered to be a resident of the State in which it is constituted regardless of whether it benefits from a limited or complete exemption from taxation in that State. Pension funds are important investors into private equity funds. The previous Action 6 Consultation Document was correct therefore when it stated that “pension funds, like sovereign wealth funds, are often among the institutional investors that invest in alternative funds and private equity funds and these may be established in third countries”.13

Indeed, 32% of capital which is invested into private equity funds comes from pension funds.14 In 2014, the total investment into European private equity funds from pension funds amounted to just over €14 billion.15 Echoing similar statements from European institutions, the 2014 OECD Report on Institutional Investors and Long-term Investment correctly identified that pension funds are increasingly investing in private equity funds, not just on a European basis but indeed globally.16

Solutions & Way Forward:

Although the Consultation Document judges that “most suggestions included in the comments received did not sufficiently take account of treaty-shopping concerns”, the basis for this conclusion (i.e. the tax status of investors themselves) is a consideration which is not factored in as part of the fund structuring. Rather, this is a separate question of investors and their tax status in their respective locations. The debate should not be misconstrued in the framework of the treaty benefits of fund structures.

Despite the OECD’s concerns, we believe that further work could, however, be undertaken on the creation of an additional category of qualified person, to

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11 ibid, pp 17.
12 ibid, pp 19.
13 The previous discussion draft, Follow Up Work on BEPS Action 6: Preventing Treaty Abuse, November 2014, pp 6
14 Further information can be found in the EVCA Yearbook - 2014 European Private Equity Activity: Statistics on Fundraising, Investments & Divestments, May 2015.
15 Ibid, pp 15.
include the concept of a ‘qualified fund’, provided this were tailored and appropriate to the private equity industry, based on existing reporting requirements and not on TRACE which is inappropriate for our industry. We do not consider that any solution based on the principles of the TRACE project could be a practical solution for private equity funds. If the OECD feels that there is insufficient time to properly deal with such negotiations then we would ask that non-CIV funds are carved-out of the current proposals and the status quo maintained until such time as treaty entitlement for private equity funds can be properly addressed.

With this document, we have now responded to all three consultations which the OECD has issued on Action 6. As can be seen, we are committed to continued engagement with the OECD and to give further explanation and information on how private equity operates in order to allow the OECD to achieve its goals of designing rules to stop base erosion and profit shifting, while still allowing investment funds to continue their important task of channelling capital to the real economy.

We are more than willing to further engage with the OECD on this issue, and if necessary become more closely involved in the work in this area. We agree with the conclusions of the Working Party that it should continue to explore solutions to issues related to the treaty entitlement of non-CIV funds and their holding companies. In this light, we would like to see the creation of a specific OECD Working Group dedicated to examining solutions to non-CIVs which will continue work beyond the current deadline of September 2015 for Action 6 under the BEPS project.

**Conclusion:**

Private equity funds are not in the business of treaty shopping. They pursue a genuine business purpose, i.e. the co-investment arrangement or pooling of capital to make investments into companies. As long as different countries’ interpretations of what constitutes a permanent establishment are not harmonised across the globe, tax treaty access will remain crucial in order to achieve tax neutrality for funds, and to avoid double or even triple taxation in genuine bona fide investment structures.

In the context of the Consultation Document, private equity funds, irrespective of shape or form, typically raise and invest funds internationally and it is imperative that the location as well as the structure chosen for the fund is tax neutral for the investors. In other words, the co-investment or pooling of the investments via the fund entity should not trigger *additional* tax for investors when compared with a
situation in which the investors invest directly in those companies. This is a general principle for structuring funds which is not unique to private equity.

Contact

Thank you in advance for taking our comments into account as part of the consultation process. We would be more than happy to further discuss any of the comments made in this paper.

For further information, please contact Danny O’ Connell at the European Private Equity & Venture Capital Association (EVCA).

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The Public Affairs Executive (PAE) consists of representatives from the venture capital, mid-market and large buyout parts of the private equity industry, as well as institutional investors and representatives of national private equity associations (NVCAs). The PAE represents the views of this industry in EU-level public affairs and aims to improve the understanding of its activities and its importance for the European economy.

About EVCA

The EVCA is the voice of European private equity.

Our membership covers the full range of private equity activity, from early-stage capital to the largest private equity firms, investors such as pension funds, insurance companies, fund-of-funds and family offices and associate members from related professions. We represent 650 member firms and 500 affiliate members.

The EVCA shapes the future direction of the industry, while promoting it to stakeholders such as entrepreneurs, business owners and employee representatives.

We explain private equity to the public and help shape public policy, so that our members can conduct their business effectively.

The EVCA is responsible for the industry’s professional standards, demanding accountability, good governance and transparency from our members and spreading best practice through our training courses.

We have the facts when it comes to European private equity, thanks to our trusted and authoritative research and analysis.

The EVCA has 25 dedicated staff working in Brussels to make sure that our industry is heard.
17 June 2015

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Comments on Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse

Dear Ms. De Ruiter:

EY appreciates the opportunity to submit these comments to the OECD on the revised discussion draft on BEPS Action 6: Prevent Treaty Abuse released on 22 May 2015 (Revised Discussion Draft). These comments build on our 9 January 2015 comment submission on the earlier Action 6 discussion draft released on 21 November 2014. Our focus with these comments is on the need to ensure that efforts to protect against the grant of tax treaty benefits in inappropriate circumstances do not interfere with the grant of such benefits in appropriate circumstances.

As the OECD requested, this submission is relatively brief, and it focuses in particular on new proposals included in the Revised Discussion Draft.

Alternative Simplified Limitation on Benefits Provision

The Revised Discussion Draft includes an alternative limitation on benefits (LOB) provision that is a simplified version of the LOB provision included in the September 2014 Report on Action 6. This simplified LOB provision is described as being intended for use in combination with a principal purpose test (PPT) provision.

The concept of a simplified LOB provision is a welcome one. However, the statement that such a provision is intended to be used in combination with a PPT provision seems overly prescriptive.
This provision would be a new tool for countries to use in addressing the potential for treaty shopping. Its application would be relatively straightforward, which is an important consideration, particularly for countries where such provisions have not been used before. We believe that countries should be free to choose to use the LOB provision that is most appropriate to their own circumstances, whether in combination with a PPT provision or in combination with an anti-conduit mechanism. Similarly, countries should be free to use some elements from the simplified LOB provision and some from the “full” LOB provision if they consider such a combination to best suit their needs.

The Revised Discussion Draft further states that “the non-application of the simplified LOB in a given case should not be interpreted in any way as suggesting that the PPT would not be applicable in that case.” This statement reflects the OECD’s view that satisfaction of the objective tests of the LOB provision should not be determinative of qualification under the more subjective approach of the PPT provision. Nevertheless, we believe that the presence of facts that result in satisfaction of such objective tests could properly be considered to be a relevant and positive factor in the PPT analysis. We urge the OECD to include in the final report on Action 6 an affirmative statement regarding this connection between the LOB provision (both the simplified LOB and the “full” LOB) and the PPT provision when such provisions are used in combination.

Treaty Entitlement of Collective Investment Vehicles (CIVs)

The Revised Discussion Draft reflects support for the conclusions of the OECD’s 2010 Report on treaty benefits with respect to CIVs, including the need for flexibility in approaches in light of the variations in structures, investor bases and investment policies found across the range of CIVs. We welcome this decision not to specify a single approach to the treaty entitlement of CIVs.

The Revised Discussion Draft also notes that proper implementation of the TRACE project’s recommendations with respect to compliance approaches is essential to make any approach to treaty entitlement of CIVs operational. In this regard, we urge the OECD to make clear in the final report on Action 6 that adoption of the TRACE recommendations is an integral element of any provision with respect to the treaty entitlement of CIVs.

Treaty Entitlement of Non-CIVs

The Revised Discussion Draft includes a proposal for explicit confirmation of the conclusions with respect to the treaty entitlement and resident status of real estate investment trusts (REITs)
that are reflected in the OECD’s 2008 Report on REITs. It also includes a proposal that the resident status of pension funds should not be affected by the partial or full tax exemption of such funds. Both of these proposals are to be further considered by the Working Party at its meeting later this month. We welcome these proposals and urge that they be incorporated in the final report on Action 6.

In addition, the Revised Discussion Draft indicates agreement in the Working Party to continue to explore approaches for treaty entitlement of non-CIV funds, noting that the work in this area might continue after the September 2015 adoption of the final report on Action 6. We appreciate the OECD’s commitment to working on these important issues and to devoting the time necessary to develop solutions. We encourage the OECD to bring to this work a consultative approach and to seek input from the industry, including all the various industry sectors, in order to ensure that operational issues are fully considered and that the solutions developed are practical and workable. Until this work is completed, we urge that the OECD make clear that any new provisions restricting treaty access should not adversely affect non-CIVs.

Derivative Benefits Provision and Relaxation of Restrictions on Intermediate Entities

The Revised Discussion Draft reflects the Working Party’s continuing consideration of the addition of a derivative benefits test to the LOB provision. Also reflected is the continued consideration of whether the restrictions on intermediate entities for purposes of ownership based tests in the LOB provision could be relaxed. Both of these issues are critically important in the context of modern global businesses that conduct activity involving multiple entities and multiple countries. The inclusion of a derivative benefits test that allows consideration of comparable benefits is essential to the functioning of an LOB provision. Such a rule would reflect the commercial realities and global nature of business today. In addition, the relaxation of proposed restrictions on intermediate owners under a derivative benefits test and other ownership based tests also is essential and would similarly reflect modern business structures.

Active Trade or Business

The Revised Discussion Draft includes a proposed modifications to the active trade or business test in the LOB provision that are to be considered further at the Working Party’s meeting later this month. One proposed modification would limit the ability to take into account activities conducted by connected persons to situations where such persons are engaged in the same or a similar line of business as the resident to which the LOB provision is being applied. Global businesses often have activities divided among multiple entities for regulatory, management or
commercial reasons. It is appropriate that the activities of one group entity be attributed to an affiliated group entity for purposes of determining whether there is sufficient business connection to a country to dispel any concern about treaty shopping. We are concerned that introduction of a same or similar line of business requirement with respect to this aggregation rule would create significant uncertainty for businesses. We urge the OECD not to include such a requirement in the final report on Action 6. Moreover, if such a requirement were to be added to the active trade or business test, we urge the OECD to include detailed commentary explaining and illustrating when lines of business would be considered to be the same or similar.

More generally with respect to the active trade or business test, we urge the OECD to add an illustrative example making clear that in analyzing whether a holding company would be considered to satisfy the active trade or business test, the aggregation rule would apply to allow the activities of a connected management company to be taken into account. We also request the OECD to clarify that the exclusion of “the business of making or managing investments” from the active trade or business test under the LOB provision would be limited to passive investment businesses and would not apply where the investor takes an active role in the business of the investee. Further, we ask the OECD to incorporate guidance that recognizes the circumstances of smaller countries and focuses on the characteristics of the business functions conducted rather than merely the quantity of such functions.

PPT Provision

We continue to be concerned that the proposed PPT provision is overly vague and would add excessive uncertainty with respect to access to treaty benefits by introducing a subjective standard that would be difficult to evaluate and administer in practice because it is dependent on the intent of the taxpayer. Such uncertainty would interfere with the proper functioning of tax treaties and with appropriate access to the intended benefits of tax treaties.

We urge the OECD to incorporate into any PPT provision a more objective approach for taxpayers to demonstrate that they satisfy the provision. As discussed in our January submission, such an approach could include, for example, a derivative benefits type test and an active business type test. Where these tests are satisfied, the PPT should not be considered to apply to deny treaty benefits.

Special Tax Regimes

The Revised Discussion Draft includes a proposal for a new treaty provision that would deny certain treaty benefits in the case of income that is subject to a special tax regime. This proposal
is discussed in the context of the potential for inclusion of a derivative benefits rule in the proposed LOB and is described as addressing some of the concerns about such inclusion. We appreciate the OECD’s continued work on developing approaches that would facilitate the addition of a derivative benefits rule. However, we believe that development of recommendations regarding the substance and reach of any special tax regime provision properly should be done in connection with the OECD’s work on BEPS Action 5 on harmful tax practices. Addressing such matters with respect to the special tax regime concept under Action 5 would ensure greater consistency with the approach to the consideration of other favorable tax regimes being addressed in the work under Action 5.

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If you have questions or would like further information on any of the points discussed above, please contact Barbara Angus (barbara.angus@ey.com), Arlene Fitzpatrick (arlene.fitzpatrick@ey.com), Jim Tobin (james.tobin@ey.com) or me (alex.postma@eyg.ey.com).

Yours sincerely
On behalf of EY

Alex Postma
Dear Ms de Ruiter,

Response from FTI Consulting to the OECD Revised Discussion Draft on BEPS Action 6 (‘the RDD’):

We welcome this opportunity to comment on the OECD’s revised discussion draft (RDD) under BEPS Action 6 Prevent Treaty Abuse, published on 22 May 2015.

We agree to have our comments posted on the OECD website.

We would like to thank you for the opportunity to comment on the discussion draft and hope our comments are helpful.

Yours sincerely,

Marvin Rust

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Marlies de Ruiter,
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By email: mailto:taxtreaties@oecd.org

16 June 2015
1. Introduction

The Revised Discussion Draft (‘RDD’) includes a simplified Limitation on Benefits (LOB) Article for inclusion in the OECD Model Income Tax Convention and provides ‘conclusions and proposals’ on 20 targeted issues. Most of the proposals are in response to public comment but the RDD also contains new proposals. Some proposals aim to restrict access to treaty benefits with respect to income that may be subject to preferential tax treatment.

FTI Consulting’s (‘FTI’s’) view, as with all the work being undertaken in relation to the BEPS project, is that it is also essential for the OECD to continue to promote the cost effective use of taxpayers’ and tax administrations’ resources for improved compliance and enforcement processes. Whilst it is clearly vital that tax treaties are not abused it is important that genuine commercial activities are not curtailed by onerous administrative burdens. FTI hopes that when the Working Party meets to produce a final version of the Report on Action 6 that it will give emphasis to this point.

2. General Comments

We recognise that this is the third discussion draft and so have kept our comments to a minimum. Where we have not commented it may be taken that we are content with what is proposed.

3. Specific Comments

ISSUES RELATED TO THE LOB RULE

3.1 Collective investment vehicles (CIVs); application of the LOB and treaty entitlement

The RDD concludes that since there was general support for the conclusions of the 2010 CIV Report concerning the treaty entitlement of CIVs, and since the LOB rule dealt with applying the LOB to CIVs in a way that reflected the 2010 CIV Report’s conclusions, additional changes to address these issues are unnecessary. The RDD notes that implementing the Treaty Relief and Compliance Enhancement (TRACE) project’s recommendations was important for the practical application of these conclusions.

FTI is concerned that simply referring to the CIV report and expecting TRACE to provide practical solutions is unduly optimistic. Treaty entitlement for funds has been left open and it is uncertain whether TRACE will ultimately succeed. Notwithstanding the Working Party’s conclusion FTI would like to see firmer guidance being given in the final document.
3.2 Non-CIV funds; application of the LOB and treaty entitlement

The RDD states that a pension fund should be considered to be a resident of the state in which it is constituted regardless of whether it benefits from a limited or complete exemption from taxation in that state. This is a welcome approach. As a result, the OECD agreed to consider, at its June meeting, a proposal for changes to the OECD model tax convention that would ensure that outcome.

Separately, the RDD does not drop the requirement that a pension fund is a qualifying person only if at least 50% of all beneficiaries are resident in either contracting state, but adds an alternative means of qualifying. This alternative test is met if more than 90% of the beneficiaries are resident of either contracting state, or are residents of another state (third state) if those individuals are entitled to the benefits of a tax treaty between that the third state and the source state and would be entitled to the same or lower rate of tax on dividends and interest under a tax treaty between the source state and the third state as would apply if the individual were a resident of the same state as the pension fund.

Where a pension fund has thousands of beneficiaries it may have great difficulty in determining whether 90% of its beneficiaries meet the alternative test. Thus, FTI feel that such difficulties could make this alternative impractical for such funds and would urge the Working Party to consider these practical difficulties at their June meeting and to reflect that concern in their final report.

On the broader question of the treaty entitlement of non-CIV funds, the Working Party recognised the economic importance of non-CIVs and the need to ensure the granting of treaty benefits where appropriate. It noted, however, that most suggestions included in the comments did not sufficiently take account of treaty-shopping concerns.

The RDD at paragraph 24 sets out the ground that the Working Party intends to cover at its June meeting; this includes adding a specific provision on non-CIVs in the LOB rule and adding one or more examples on non-CIVs to the Commentary on the PPT. Whilst FTI accepts that treaty shopping may be a concern of some jurisdictions with a minority of non-CIVs it urges the Working Party to give sufficient emphasis to the economic importance to non-CIVs in its final report.

3.3 Commentary on the discretionary relief provisions of the LOB rule

The RDD states that more guidance should be provided about the factors that a competent authority should take into account when considering a discretionary relief request. It thus sets out revised changes to the Commentary on the paragraph of the LOB rule. The RDD also notes that the competent authority that receives a discretionary relief request should process that request expeditiously. FTI think that it would be useful if a time limit could be suggested in the revised Article e.g. 3 months.

The purpose of the provisions under discussion is to prevent treaty abuse; i.e. treaty shopping. But, rather than adding additional guidance on how to consider whether the principal purpose of a transaction is treaty shopping the proposal as it stands seems to further restrict when discretionary relief may be granted, e.g. “clear non-tax business reasons,” a substantial relationship to the residence state, and that granting benefits is not otherwise contrary to the
Convention’s purposes. Given that the test is intended as a safety net for companies that are not treaty shopping and thus vests broad discretion to the Competent Authority, FTI believe that these additional restrictions are counter productive in achieving the objective of the provision.

3.4 Alternative LOB provisions for EU countries

It seems to FTI that the suggested changes to the LOB rule to deal with pension funds will give rise to the same practical problems as those described at 3.2 above. Thus, FTI similarly urges the Working Party to consider these practical difficulties at their June meeting.

3.5 Requirement that each intermediate owner be a resident of either Contracting State

The November 2014 Draft included a requirement in the subsidiary of public company test, the ownership-base erosion test, and the derivative benefits test that each intermediate owner be a resident of either contracting state (or, in the case of derivative benefits, an equivalent beneficiary). The draft indicated that further work was required in order to determine whether and how the requirement could be relaxed without creating opportunities for treaty shopping. The RDD observes that when the Working Party discussed this issue in March 2015 it was explained that the purpose of the intermediate resident requirement is to prevent the interposition of a company in a tax haven to which base-eroding payments could be made. FTI note that it is intended that the Working Party will further discuss the intermediate resident requirement in June and tie that in with the derivative benefits and equivalent beneficiary provisions.

FTI is concerned that the application of the rule as it stands may result in ineligibility for treaty benefits where no treaty shopping is present so we hope that the Working Group will be able to relax the rule in its final report.

3.6 Issues related to the derivative benefits provisions - special tax regimes and changes to a country’s domestic tax laws (partial treaty termination)

During the discussion of issues raised by the derivative benefits provision, we note that the Working Party discussed two proposals concerning possible changes to the OECD Model that would deal with special tax regimes and that would make a tax treaty responsive to certain future changes in a country’s domestic tax laws. It was argued that these proposals could address some of the objections to the addition of a derivative benefits provision in the LOB rule.

- Firstly, new provisions would be added to articles 11 (Interest), 12 (Royalties), and 21 (Other Income) providing that payments of such income are not eligible for treaty benefits if beneficially owned by a person subject to a special tax regime. A ‘special tax regime’ would be defined as any legislation, regulation, or administrative practice that provides a preferential effective rate of taxation, unless one of several exceptions apply.

- Secondly, a new rule which provides that if, at any time after the treaty signing, either contracting state provides an exemption from taxation to resident companies for substantially all foreign source income, the provisions of treaty articles 10 (Dividends),
11 (Interest), 12 (Royalties), and 21 (Other Income) may cease to have effect with regard to those articles.

FTI have the following comments:

- The denial of treaty benefits when the income is subject to a preferential tax regime is likely to lead to significant uncertainty for business. Whilst the issue of “special tax regimes” is one that understandably concerns states, FTI believes that it is a matter that is best left to bi-lateral negotiations.

- Whilst replacing a foreign tax credit system with an exemption system is a major change for a treaty partner to undertake, automatic partial termination seems to be a measure that could raise legislative issues in some countries. FTI thinks that this is something that needs to be carefully considered in the Working Party’s discussions.

ISSUES RELATED TO THE PRINCIPAL PURPOSE TEST (‘PPT’) RULE

3.7 Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level

FTI believes that the additional Commentary is helpful and that such an approach is to be encouraged as it will provide some certainty to business

3.8 Aligning the parts of the Commentary on the PPT rule and of the Commentary on the LOB discretionary relief provision that deal with the principal purposes test

FTI note that some delegates did not agree that there should be any alignment or equation between the PPT rule and the discretionary relief provision. These delegates do not support the inclusion of a PPT provision and note that the two concepts were developed separately with no intention to equate the two. Therefore, these delegates will not find any PPT guidance relevant for purposes of the determination of discretionary relief under an LOB provision. FTI find that difference of approach disappointing but, in those circumstances accept that the change in the commentary to the LOB rule seems to be the best that can be achieved.

3.9 Drafting of the alternative “conduit-PPT rule”

FTI note that when the Working Party discussed this issue at its March 2015 meetings, it was argued that the alternative definition of “conduit arrangements” suggested in paragraph 15 of the proposed Commentary raised some technical difficulties and, in particular, that the “all or substantially all” threshold was problematic. It was therefore decided that the relevant part of the Commentary should simply focus on general principles and include examples of transactions that an anti-conduit rule should address. Delegates also agreed with the commentators who suggested that the examples found in the exchange of letters between the United States and the United Kingdom were useful and should be included in the Commentary.
FTI finds both this approach and examples used useful.

OTHER ISSUES

3.10 Proposed Commentary on the interaction between tax treaties and domestic anti-abuse rules

FTI broadly shares the concerns outlined at paragraph 109 of the RDD and hopes that the final report will reflect those concerns.

4. Conclusion

As indicated earlier FTI’s view is that it is essential for the OECD to continue to promote the cost effective use of taxpayers’ and tax administrations’ resources for improved compliance and enforcement processes. FTI believes that much of what has been proposed in the RPP is helpful and constructive but, as will have been noted, has significant reservations in some areas and it hopes that the final report will adequately deal with those issues.

Thank you again for the opportunity to share our ideas and concerns.

To: Marlies de Ruiter, Head, Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA

Following comments received on previous discussion drafts the OECD released its revised draft of the public discussion on ‘BEPS Action 6: Prevent Treaty Abuse’ on 22 May 2015 with comments invited by 17 June 2015.

The comments provided below are prepared by the author as representative of Gazprom Marketing & Trading Ltd.

Introduction

The intention to continue with the Limitation of Benefits (“LOB”) provision and amendments to the residency tie-breaker clause still continue to cause us the most concern. Despite the majority of public comments expressing a variety of concerns over both provisions it is disappointing that the OECD wish to continue with their introduction. We welcome the step towards simplification of the LOB but feel these proposals should be dropped entirely. The introduction of additional proposals concerning limitation of benefits within the income Articles will, in its current form, lead to significant uncertainty for most taxpayers.

LOB provision

The majority of the public comments did not support the introduction of this provision so the proposed simplified approach to LOB is a welcome step. However, we feel that the inclusion of an LOB clause in any form is an unnecessary step that will create a considerable compliance burden for companies. It is particularly complicated to apply with companies often having to rely on reaching agreements with competent authorities which may take many years to settle. As a result, adopting this clause on a mandatory basis can create uncertainty and complexities for legitimate companies claiming treaty benefits.

Tie-breaker rule for determining the treaty residence of dual-resident persons

We are disappointed that the majority of comments objecting to a change to the long standing ‘effective management’ tie-breaker for dual residence have been ignored in favour of the new provision. Whilst the OECD has intended to address concerns over uncertainty, unpredictability and the risks of double taxation including commentary wording encouraging competent authorities to address requests under the provision as quickly as possible it is still felt that the proposed wording is not workable in practice. Mutual agreement procedures are outside of the control of the OECD and are likely to take considerable time to resolve, if indeed they are ever resolved at all. The current
wording should be kept with the commentary strengthened around what effective management means to address those rare situations of companies introducing dual resident companies for tax avoidance purposes.

**Derivative Benefits provisions**

We also note that the OECD proposes to add new provisions to the Interest, Royalties and Other Income Articles providing that payments of such income are not eligible for treaty benefits if beneficially owned by a person subject to a special tax regime. Such provisions are likely to lead to considerable uncertainty and compliance costs for businesses that are not seeking to avoid tax as they seek to interpret these rules and analyse the impact on their businesses. Moreover, the second proposal to turn off treaty benefits to income if certain changes to a country’s domestic law are made in future is similarly unhelpful. Existing domestic-anti abuse legislation is already able to deny treaty benefits for taxpayers and if a treaty GAAR is also pursued then there should be enough scope to restrict any tax avoidance through the use of these treaty Articles. Ultimately the test of whether a payment is “acceptable” for tax purposes should primarily be aimed at the payer. If the payments are commercial, reasonable and arms length then the identity of the payee is somewhat irrelevant.

**Conclusion**

Whilst the OECD have moved to address some of the concerns over LOB and Principle Purpose Test (“PPT”) provisions by proposing a simplified LOB provision to be used in combination with the PPT we feel the introduction of specific provisions is unnecessary and unpopular – such provisions are already available to States and we feel that it is no coincidence that they have very rarely been adopted. The new tie-breaker rules on residency were also almost unanimously rejected in public comments yet proposals still remain to alter these provisions.

On the whole these new rules will impact all businesses in the attempt to target a small number of tax avoiders where existing legislation should already address such issues. Whilst the provisions are intended to address the issue of treaty abuse, the main impact of the majority of such provisions will be to create uncertainty and compliance costs for both tax payers and competent authorities.

These comments have been prepared by:

**Tim Branston - Director of Global Taxation**
Gazprom Marketing & Trading Ltd
20 Triton Street
London, NW1 3BF

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Dear Ms. de Ruiter,

We are writing in connection with the OECD’s invitation to comment on its Revised Discussion Draft “BEPS Action 6: Prevent Treaty Abuse”, released May 22, 2015 (the “RDD”). We greatly appreciate the OECD’s consideration of the issues raised in the letter of January 9, 2015 and its accompanying report submitted by the Canadian parties to this letter, the letter of January 9, 2015 submitted by the Dutch parties and the letter of January 9, 2015 submitted by the Australasian Parties. The parties to this letter, representing some of the largest global pension funds, share the same views and concerns as regards the content of the RDD, which is of great importance to pension funds worldwide, and have therefore decided to provide you with joint comments and observations.

We view the contents of the RDD as constructive and positive in making progress in addressing some of our initial concerns. However, we continue to have significant concerns regarding the potential for inadvertent, material adverse tax consequences for pension and government-related funds arising from the recommendations on Action 6 and we will briefly outline them below.

The RDD indicates the OECD will continue work on certain areas of interest to us. We are keen to work with the OECD to further explore solutions that take into account our concerns and

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1 Referred to herein as the “Canadian Submission”, the “Dutch Submission” and the “Australasian Submission” respectively, and collectively, as our “Submissions”.

2 Notably, the RDD refers to further work to be performed regarding: (i) pension funds being explicitly recognized as residents for tax treaty purposes (paragraph 21, page 9), and (ii) the granting of benefits to non-CIVs and the related implications for new rules regarding “special tax regimes” (paragraph 52, page 17). In addition, any future work by the OECD on a reciprocal exemption from source taxation for pension funds is of great interest to us.
particular circumstances while also addressing national governments’ concerns about base erosion and profit-shifting behaviours. In that connection, we would appreciate a description of the process that will be undertaken to perform that additional work on the identified work streams and specifically how we as stakeholders can participate.

Recognition of pension funds as tax treaty residents

We welcome the OECD’s endorsement of the explicit recognition of pension funds as tax treaty residents regardless of their taxation in their home countries and the related planned update to the OECD Model Tax Convention (the “Model Tax Convention”).

There is considerable diversity in the legal and organizational nature of pension funds around the world. It is important that the pension fund definition adopted by the planned revision to the Model Tax Convention be properly designed so as to appropriately capture the diverse range of such organizations. Our Submissions provide suggested definitions for the OECD that could achieve the intended objective of giving these types of organizations and their wholly-owned subsidiaries clearer access to tax treaty benefits. We further suggest that the definition of a pension fund for the purpose of the residence article in the Model Tax Convention be harmonized with that used for other provisions dealing with pension funds within the Model Tax Convention and elsewhere. We also recommend that this provision be considered for inclusion as part of the BEPS Multilateral Instrument Action. We welcome the opportunity to work with the OECD on the development of suitable language for inclusion in this definition.

Reciprocal exemption from source country taxation for pension funds

We are pleased with the OECD’s interest in exploring a reciprocal exemption from source taxation for pension funds as raised in the questions contained in its Public Discussion Draft “Follow up Work on BEPS Action 6: Preventing Treaty Abuse”, released November 21, 2014.

However, the RDD does not make any recommendations on the matter or set out any specific steps to further examine the merits of such exemption. This is an issue of critical and growing importance to the global pension fund community. Near-term action on the matter is both desirable and appropriate, notably to avoid double taxation. This has particular urgency given the potential collateral impact on pension funds’ ability to claim tax treaty benefits as a result of certain Action 6 recommendations.

Further work on this matter would support the OECD’s core objective of fostering economic growth through cross-border trade and investment and we are eager to assist the OECD in carrying out this work. Please advise us on how we can participate in advancing this important initiative.

3 Formed in the same country and regulated under the same statute as its ultimate parent. Similar accommodation of wholly-owned subsidiaries in the Simplified LOB rule, the main LOB rule and the “special tax regimes” rules is also appropriate.

4 Such as the proposed exclusion for pension funds in the definition of “special tax regimes” at page 17 of the RDD.

5 The RDD indicates at page 9 that the change to the Model Tax Convention regarding pension funds will be considered at the June 2015 meeting of Working Party 1. We would be interested in understanding how we might participate in this process.

6 For further details, please see paragraphs 23 to 43 of the Canadian Submission, in particular regarding the compelling policy rationale for such an exemption, including notably the avoidance of double taxation and paragraph 4 of the Dutch Submission.
Treaty benefits for non-CIVs

Our Submissions outlined non-tax reasons why pension funds make investments through non-CIVs. It also emphasized the need for mechanisms to ensure that pension funds would not be penalized by a higher tax burden when investments are made, for commercial reasons, through non-CIVs instead of being made directly.

The RDD does address some mechanisms that appear to have been intended to provide narrow relief through, for example, limited potential discretionary relief and a derivative benefits provision. However, these provisions remain, at best, very limited in scope and very uncertain in their adoption and application.

For instance, the necessity to request resolution through competent authority intervention may be impractical given the generally limited relevant resources available by national tax authorities. Furthermore, the derivative benefits provision may not, in practice, provide relief for pension funds investing through an intermediary entity, since not all of the investors may qualify as an “equivalent beneficiary”. Investors in non-CIVs as well as other investment vehicles are often pooled together for commercial reasons (as described in our Submissions) and we would like to emphasize again that pension funds will have little or no influence on the other investors with which they are pooled together.

As a consequence, we remain deeply concerned about the potential for an inappropriate and punitive tax outcome associated with investment through non-CIVs. For instance, with respect to the principal purpose test, we strongly believe that the absence of a lower withholding tax rate through investment in a non-CIV than that which would have applied through direct investment should be regarded as evidence that no treaty abuse has taken place7.

Further consideration of a ‘look-through’ rule or additional guidance on circumstances where tax treaty benefits might be appropriately granted to non-CIVs or its investors would be warranted. The TRACE project may be helpful in this respect, however, it does not address the underlying question of qualification and treaty entitlement of non-CIVs (and CIVs) as such and the timeline for the implementation of TRACE extends beyond the Action 6 delivery date. We are therefore interested in participating in the process for identifying potential solutions.

The OECD has historically advanced the interests of cross-border investment through the encouragement of appropriate national, bilateral and multilateral tax policies. Further work on the affirmative recognition of pension funds as tax treaty residents, the development of a reciprocal exemption from source country taxation and shielding pension fund beneficiaries from double taxation would be consistent with this tradition and reinforce the OECD’s considerable thought leadership on cross-border investment matters.

7 We find especially troubling the statement at page 11 of the RDD that the absence of a lower withholding tax rate “would not, in itself, be sufficient to establish that the conditions for granting the discretionary relief are met”. We acknowledge national governments’ concerns about multinational enterprises potentially achieving tax deferral and a better than tax-neutral outcome, however this would not generally arise with respect to pension fund investors in non-CIVs, as pension funds generally benefit from a limited or full income tax exemption in their State of residence.
We, of course, wish to contribute to identifying workable solutions and would gladly provide you with further input.

Sincerely,

[Signed]
Jacquelyn Colville
Chief Financial Officer
Alberta Investment Management Corporation

[Signed]
Evert-Jan Spoelder
Senior tax counsel
APG Asset Management

[Signed]
David Woodward
Senior Vice President, Finance
British Columbia Investment Management Corporation

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Steve Bossé
Senior Director, Tax
Caisse de dépôt et placement du Québec

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Kristina Fanjoy
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Canada Pension Plan Investment Board

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John Payne
Head of Tax
New Zealand Superannuation Fund

Serena Lefort
Managing Director, Head of Tax
OMERS Administration Corporation

Hersh Joshi
Vice President, Taxation
Ontario Teachers’ Pension Plan Board

Niels Krook
Head of Tax
PGGM Investments

Jean-François Ratté
Vice President, Taxation
Public Sector Pension Investment Board

Jonathan Gilmore
Head of Tax
Universities Superannuation Scheme (USS)

Vince Quagliata
Head of Tax
QIC
Marlies de Ruiter  
Head, Tax Treaties,  
Transfer Pricing and Financial Transactions Division,  
OECD/CTPA  
2 Rue Andre Pascal  
75775 Paris Cedex 16  
FRANCE  

17 June 2015  

Dear Ms. de Ruiter,  

OECD Revised Discussion Draft – BEPS Action 6: Prevent Treaty Abuse  

Grant Thornton International Ltd, with input from certain of its member firms, welcomes the opportunity to comment on the OECD Revised Discussion Draft entitled BEPS Action 6: Prevent Treaty Abuse, issued on 22 May 2015.  

Our observations and detailed comments are set out below. We have confined our comments to areas of the Revised Discussion Draft where we still have concerns about the OECD’s proposals and followed the numbering of this document.  

PART 2 – ISSUES IDENTIFIED IN THE NOVEMBER 2014 DISCUSSION DRAFT  

A. Issues related to the LOB provision  

1. Collective investment vehicles: application of the LOB and treaty entitlement  

The revised discussion draft notes that due to the general support for the conclusions of the 2010 CIV Report and the fact that subparagraph 2(f) of the LOB rule effectively reflects the conclusions of the CIV Report, there was no need for further changes to the Report on Action 6.  

The revised discussion draft also notes that the application of the recommendations of the TRACE project is critical for the application of the conclusions of the CIV Report.  

Comment  

We note that references to subparagraph 2(f) in the Revised Discussion Draft relate to the LOB rule in Section A of the OECD Report on Action 6 and also to the LOB rule in the Annex of the Revised Discussion Draft.  

We consider that the operation of an LOB rule to CIVs would be administratively onerous and would restrict and limit the ease with which CIVs invest and operate across borders. We welcome the exclusion of CIVs from the LOB provisions (as incorporated in subparagraph 2(f)) and would also welcome further commentary on the issues surrounding the application of any LOB rule to CIVs to be clarified and included in the Commentary to the Model Convention.  

In the meantime, there would need to be widespread implementation amongst OECD member countries of the recommendations of the 2010 CIV Report and the TRACE package before the application of LOB rule
to CIVs. Therefore, a "grandfathering" provision in the latest proposed text is necessary to achieve this effect.

2. Non-CIV funds: application of the LOB and treaty entitlement

The Revised Discussion Draft introduces a specific reference to the conclusions of the 2008 REIT Report in the Commentary to subparagraph 2(f) of the LOB rule and recognises that pension funds should be considered to be a 'resident' of the State in which it is constituted regardless of whether it benefits from a limited or complete exemption from taxation in that State. However, there has been minimal progress in addressing the issues and consequences of subjecting non-CIVs to an LOB rule. Although solutions to resolve issues surrounding the treaty entitlement of non-CIVs will be explored and work on addressing these issues and arriving at a solution will continue after the September 2015 deadline for the adoption of the final report on Action 6, there are concerns that this work would not be completed before the December 2016 deadline for the negotiation of the multilateral instrument that will implement the conclusions of Action 6.

Comment

Although the Discussion Draft did not ask for comments with respect to REITS, we welcome the inclusion of the footnote in the Commentary which references the 2008 REIT Report. The inclusion of the reference provides greater certainty for the wider REIT industry.

We consider that this is an unfortunate outcome. It also gives rise to additional uncertainties and is yet another indication that the BEPS project may not be concluded in entirety before the end of 2015. Non-CIVs play an important role as investors in capital markets and any denial of treaty benefits to non-CIVs could have adverse implications to cross-border trade and investment. Whilst the importance of investment funds is recognised in the Revised Discussion Draft, neither the extent to which the LOB rule could impact non-CIVs nor possible solutions of ways to ensure treaty benefits may be granted to non-CIVs have been considered. Issues and concerns raised in relation to the application of an LOB rule to securitisation vehicles and the securitisation industry have also not been addressed.

We also note that aside from confirmation that pension funds may be considered to be 'residents' of a Contracting State, guidance and commentary on the actual application of an LOB rule to pension funds has also not been provided in the Revised Discussion Draft.

3. Commentary on the discretionary relief provision of the LOB rule

In order to provide clarity and further guidance, the Revised Discussion Draft replaces paragraphs 63 to 65 of the proposed changes to the Commentary on paragraph 5 of the LOB rule.

Comment

As a general comment, we welcome the decision to provide further guidance on the factors that should be taken into account by tax authorities in considering requests for discretionary relief. The specific requirement that a competent authority should process a request for relief expeditiously is useful but it would be more helpful if it prescribed a clear time limit, for example three months from the date of the request, so that this matter is not open to further interpretation or delay.

4. Alternative LOB provisions for EU countries

The Revised Discussion Draft states that no changes will be made to the model provisions included in the Report in order to specifically address critical EU law issues at hand. Notwithstanding this, the Working Party agreed that such issues should be addressed generically (so as to avoid giving preferential treatment to EU/EEA residents) in the Commentary. We also note that revised wording has been proposed to allow greater foreign participation in a pension fund that constitutes a "qualified person".
Whilst we recognise the OECDs concerns about preferential treatment, we are disappointed that specific guidance on the LOB rule will not be provided in the Commentary, especially in light of the Papillon (C-418-07) and RBS (C-311/97) cases.

We welcome the changes concerning the ownership of pension funds though we believe that obtaining the information needed to meet the alternative thresholds is likely to prove onerous in practice with the proposed 90% threshold being prohibitively high.

6. Issues related to the derivative benefits provision

The Revised Discussion Draft states that various issues are unresolved and need to be addressed before a decision can be reached on the manner in which a derivative benefits test would operate. The Revised Discussion Draft includes new treaty provisions on "special tax regimes" including a definition of a "special tax regime" and new provisions for Articles 11, 12 and 21 of the OECD Model Tax Convention.

We consider that the inclusion of specific definitions in relation to "special tax regimes" and the modification of Articles 11, 12 and 31 of the OECD Model Tax Convention would further complicate the operation of the derivative benefits provision and would confuse the underlying objective of Action 6.

The granting of treaty benefits to entities that are considered to be subjected to a "special tax regime" should not, in itself, be considered to be "abusive" within the context of Action 6. We consider that issues surrounding special tax regimes should be dealt with by Contracting States through bilateral negotiations and where appropriate, the renegotiation of double tax conventions. We also consider that it would be more appropriate to address the issue of "special tax regimes" under Action 5 of BEPS and through the OECD's continuing work on harmful tax practices. We consider that the other mechanisms of Action 6 (such as the LOB and PPT rules) appropriately capture the use of conduit entities and arrangements, even where those conduit entities or arrangements may be subject to a special tax regime.

Additionally, we note the September 2014 deliverable on Action 5 included a review of specific tax regimes in a number of OECD member and associate countries and concluded that many of these regimes were not harmful. Therefore, the inclusion of "special" tax regime provisions does not appear consistent with the broader conclusions of the work on harmful tax practices. There should be a carve-out for regimes which the OECD considers are not harmful while the new proposed rule should only be adopted in cases where the activities benefiting from the relevant tax regime do not have sufficient substance.

B. Issues related to the PPT rule

11. Application of the PPT rule where benefits are obtained under different treaties

The Revised Discussion Draft states that it was agreed by Working Party 1 that no changes to the Commentary was required.

We welcome the OECDs decision not to amend the wording of the PPT rule itself. As noted in our letter dated 9 January 2015, an amendment to the rule would have resulted in a lack of clarity as to when the rule should and should not apply.

Nonetheless, in that same letter, we urged the OECD to amend the draft Commentary to clarify the operation of the rule with respect to regional hub structures. Such structures are used for example where the UK or other EU territory is used as a holding location for European subsidiaries (where the ultimate parent is outside the EU), or where the US is used as a holding jurisdiction for the Americas, or Australia is used as a holding jurisdiction for the Asia-Pacific region.
12. Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT is only applied after approval at a senior level

The Revised Discussion Draft proposes amendments to the Commentary on the PPT rule. The proposed amendments indicate that countries establish their own administrative process so as to ensure that the PPT is only applied after approval at a senior level.

Comment

We welcome the OECDs proposal for individual countries to establish their administrative processes for the purposes of restricting the application of the PPT rule. However, to maintain consistency with the OECD's latest proposals for the discretionary relief rule we consider it essential that such processes should have as uniform a timeframe as possible, or at least that a competent authority should be encouraged to consider individual cases on a timely basis.

If you would like to discuss any of these points in more detail then please contact either myself or Martin Lambert, Partner, Grant Thornton UK LLP (martin.lambert@uk.gt.com).

Yours sincerely

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MEMORANDUM

To : OECD, Mrs. M. de Ruiter, Head TT, TP and FTD
From : Mr A.P. Berkhout / Prof. Mr B.P. Honnebier
Re : Comments revised draft May 22, 2015 Action point 6:
- Non-conduit example: ‘Leasing of ICS-equipment e.g. aircraft between unrelated parties’

Date : 16 juni 2015
CC: Gomez & Bikker Law Offices

OECD / CTPA
Attn. Mrs. M. de Ruiter,
Head Tax treaties, Transfer Pricing and Financial Transactions Division
Paris

Amsterdam, June 16, 2015

Subject: non-conduit example: leasing of ICS - equipment e.g. aircraft between unrelated parties

Dear Mrs. de Ruiter,

Herewith our comments – in cooperation with Prof. B.P. Honnebier of Gomez & Bikker Law Offices - regarding the new discussion draft on Action 6 of the BEPS action plan (prevent treaty abuse) dated May 22, 2015.

Please add the attached example regarding ‘leasing of ICS-equipment e.g. aircraft between unrelated parties’ that should not be considered to be a conduit arrangement for that purpose.

A prime example of relevant private law treaties in the field of leasing of mobile equipment is the Convention on International Interests in Mobile Equipment (CIME) and the Aircraft Equipment Protocol (AEP), also referred to as Cape Town Convention 2001 (CTC). These treaties are historically supported by the OECD guidelines and LASU (large aircraft sector understanding), 2007 ASU (aircraft sector understanding) on export credit financing support, which is nowadays also arranged for by the so-called “Cape Town” discount on the lease rentals for leases which are structured via CTC member States. This is because the CTC gives the banks, financiers and owners, lessors extensive international protection against the (financial) problems of defaulting or insolvent operators, lessees of aircraft, aircraft engines and helicopters in these jurisdictions.

After entering into force and the required ratification by countries of also the Protocols regarding Railway Rolling Stock and Space Objects, substantial (CTC protection) advantages will also apply for lessors, banks, financiers and owners such mobile equipment.

Best regards,

Nexia Horlings Tax Advisors

mr. A.P. Berkhout
Non-conduit Example: leasing of ICS – equipment e.g. aircraft between unrelated parties:

RCO is a publicly traded company resident of State R, active in the business of Industrial, Commercial and Scientific (ICS) - equipment leasing. In particular, it leases aircraft and aircraft engines to commercial operators around the world.

SCO is an aircraft operator e.g. airline and is resident in State S. SCO buys several aircraft from an aircraft manufacturer while it cannot finance the purchases itself. Therefore, SCO sells the aircraft to RCO as a part of a sale - lease - back transaction. However, RCO also has to finance the purchase of the specific aircraft.

For a long time, RCO has undertaken most of its banking and aircraft financing activities with TCO, a bank resident of State T. This is because of the sophisticated banking system of this country. Moreover, in State T certain aviation related private law treaties (aircraft secured interests law), aviation safety law and investment protection treaties apply which make the financing and leasing of ICS – equipment e.g. aircraft more cost efficient.

State T has a tax treaty for avoidance of double taxation with State R and with State S. State R does not have a tax treaty with State S.

According to its usual finance practice the aircraft are financed by RCO with TCO under at arm's length conditions and subsequently (finance) leased by RCO to a certain (orphan) Lease in - Lease Out company (SPV) in State T, which (finance) sub-leases the commercial equipment to SCO. The legal reasons for this kind of financial structure are generally to strengthen the ownership rights of the lessor RCO and the secured interests of its financier the bank TCO. The operator of the aircraft SCO pays (finance) lease rentals to the SPV in State T. SPV keeps an at arm's length spread with the (finance) lease rentals it receives and pays the remainder as (finance) lease rentals to RCO.

This example refers to a normal commercial structure where RCO, TCO, SPV and SCO carry on real economic activities in States R, T and S respectively. In the facts presented above, RCO, TCO, SPV and SCO are unrelated. It is clear that the arrangements between lessor RCO, bank TCO, lease entity SPV and the operator SCO have been put in place to strengthen the financial interests of the lessor and the bank by the application of the national law and international treaties in State T. Based on the specific facts, the arrangement between RCO, TCO, SPV and SCO does not constitute a conduit arrangement.
June 17, 2015

Ms. Marlies de Ruiter
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Organisation for Economic Co-operation and Development
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France
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Re: Comments on Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse

Dear Ms. de Ruiter:

The International Alliance for Principled Taxation (IAPT or Alliance) is a group of major multinational corporations based throughout the world, and representing business sectors as diverse as consumer products, media, telecommunications, oilfield services, transportation, computer technology, energy, pharmaceuticals, beverages, software, IT systems, publishing, and electronics. The group’s purpose is to promote the development and application of international tax rules and policies based on principles

1 The current membership of the IAPT is made up of the following companies: Adobe Systems, Inc.; Anheuser-Busch InBev NV/SA; A.P. Møller-Mærsk A/S; AstraZeneca plc; Baker Hughes, Inc.; Chevron Corporation; Cisco Systems, Inc.; The Coca-Cola Company; Exxon Mobil Corporation; Hewlett-Packard Company; Johnson Controls, Inc.; Juniper Networks, Inc.; Microsoft Corporation; Procter & Gamble Co.; RELX Group plc; Repsol S.A.; TE Connectivity, Ltd.; Thomson Reuters Corporation; Transocean Ltd.; Tupperware Brands Corporation; and Vodafone Group plc.
designed to prevent double taxation and to provide predictable treatment to businesses operating internationally.

The Alliance appreciates the opportunity to provide input to the OECD with respect to its Revised Discussion Draft on BEPS Action 6, Prevent Treaty Abuse released on May 22, 2015. Our comments are set forth in the Annex to this letter.

The Alliance would be pleased to respond to any questions or to provide further input as the work of the OECD on this item continues.

Sincerely yours on behalf of the Alliance,

Mary C. Bennett
Baker & McKenzie LLP
Counsel to the Alliance

Annex: Comments on the May 22, 2015 Revised Discussion Draft
ANNEX

INTERNATIONAL ALLIANCE FOR PRINCIPLED TAXATION

COMMENTS ON MAY 22, 2015 REVISED DISCUSSION DRAFT ON BEPS ACTION 6,
PREVENT TREATY ABUSE

JUNE 17, 2015
IAPT Comments on the May 22, 2015 Revised Discussion Draft on BEPS Action 6, Prevent Treaty Abuse

1. Executive Summary

1. We appreciate that some prior comments have been taken into account, but we have both continuing concerns about the way some previously identified issues were dealt with and new concerns about some new proposals. We also find it difficult to provide complete comments given how many issues are deferred for decision until the June 2015 Working Party 1 (WP1) meeting or later.

2. The alternative simplified LOB provision would be a welcome proposal as a standalone provision, but when combined with a principal purpose test (PPT) provision it (like the more detailed LOB) would simply lead to uncertainty and complexity and would act as a barrier to cross-border trade and investment. In order to improve upon the proposal, we suggest:

   - Allowing the alternative simplified LOB (coupled with an anti-conduit provision) to satisfy the minimum standard for addressing treaty abuse, without being coupled with a PPT provision;

   - If the provision is combined with the PPT:

     - Including text in the Model itself to clarify the interaction between the PPT and LOB determinations;
     - Including text in the Commentary to describe the narrower scope of permissible PPT inquiries in cases where the LOB is satisfied;

   - Ensuring that any alternative simplified LOB provision that is ultimately incorporated into the Commentary will include all the elements constituting the main features of an LOB described in the proposed Model text found in the Annex to the RDD; and

   - Omitting (or at least clarifying) the language in the discretionary relief paragraph in the version of the alternative simplified LOB which appears at paragraph 3 of the RDD which says that the competent authority who receives the request shall make its determination “in accordance with its domestic law or administrative practice”.

3. Regarding the Commentary on the LOB discretionary relief provision (Issue #3), we recommend deletion of the new proposed language which refers to a standard (i.e., “clear non-tax business reasons”) not grounded in the language of the Model text itself (i.e., which refers to not having as a principal purpose obtaining benefits under the Convention) and reinstatement of the language from the September 2014 Report which tracked the Model standard.
4. Regarding the proposed derivative benefits safe harbor for pension funds as a response to the question of alternative LOB provisions for EU countries (Issue #4), we suggest inclusion of language to confirm that a pension fund would not fail to qualify for that safe harbor simply because it did not meet all of the technical requirements applicable to pension funds established in the countries of residence of its participants where those pension funds were entitled to equivalent benefits from the source State. We also stress the importance of arriving at workable solutions to the procedural mechanisms for pension funds to claim treaty relief before any new restrictions are imposed on them under Action 6.

5. Regarding the requirement that each intermediate owner be a resident of a Contracting State (Issue #5), we reiterate the critical importance of removing these restrictions in order to make the various safe harbors available as a practical matter to the types of totally non-abusive and extremely common ownership structures found in MNEs worldwide, and we would urge the OECD to remove the restrictions without regard to how the discussion on the new proposals (on special tax regimes and subsequent changes in law) comes out.

6. Regarding the issues related to derivative benefits provisions (Issue #6), we similarly reiterate the critical importance of including such provisions, without regard to how the discussion on the new proposals comes out.

7. While we understand the principle behind the proposed provision denying certain benefits to income subject to a special tax regime, we believe that the provision would raise many difficult issues of interpretation in practice (examples of which we identify), and that the OECD should therefore study the issue further before deciding whether or how to incorporate such a concept into the Model.

8. Notwithstanding our strong encouragement to the OECD to defer a decision on whether to include the proposed special tax regime provision until there has been further opportunity to study it, if the OECD decides to go ahead with the provision, we suggest that it be amended to include the condition that it would be triggered only after the source State provides public notification that a regime triggers its application.

9. Similarly, regarding the proposal to deny the benefits of Article 10, 11, 12, and 21 where a Contracting State has made certain changes to its domestic law after concluding a treaty, we believe significant interpretive issues may arise (examples of which we identify), and we suggest the OECD further analyze and clarify this proposal before deciding whether to incorporate it into the Model. If the proposal is incorporated into the Model, we suggest that it not apply to benefits under Article 10.

10. Regarding the clarification of the “active business” provision (Issue #10), we recommend against adopting the proposed changes to the active business test described at paragraph 72 of the RDD, for reasons we outline in detail.

11. Regarding the list of examples in the Commentary on the PPT rule (Issue #17), we recommend clarification of the extent to which the inquiries suggested by the examples would remain appropriate if the PPT was accompanied by an LOB provision which had been satisfied, and we further suggest
clarification of the new Example I (i.e., to indicate to what benefits and persons the PPT is being applied in the example).

12. Regarding the design and drafting of the rule applicable to permanent establishments located in third States (Issue #19), we question the policy rationale for the proposed deletion of subparagraph (f) on royalty payments. We support some of the suggested changes described at paragraph 106 of the RDD (i.e., that the disallowance rule should not apply to cases where the source State has a treaty in force with the PE State and the effective tax rate on the PE is at least 60% of the rate of tax in the PE State, and that the application of the rule should be subject to some form of discretionary relief).

13. Regarding the proposed Commentary on the interaction between treaties and domestic anti-abuse rules, we would:

- Note that the existing Commentary paragraphs 7 to 12 and 20 to 22.2 contain a very important and long-standing summary of the interaction between tax treaties and domestic anti-abuse rules, so that any amendment to those paragraphs must be very carefully undertaken to preserve the validity of the conclusions reflected there; and

- Caution once again that any new domestic anti-abuse rules designed to address other BEPS Action Items would prevail over treaties only per the description in the proposed Commentary (i.e., where they are specifically allowed in the treaty, where the treaty benefit refers to domestic law for its application, or where they are consistent with the PPT / Commentary).

2. **General comments on the Revised Discussion Draft (RDD)**

14. We appreciate the opportunity to comment on this RDD and also appreciate the fact that some of our prior comments were taken into account in a number of respects.

15. We note, however, that it is difficult to comment on some topics because the RDD indicates decisions on firm proposals will not be made until June or later. This is particularly true for new proposals appearing for the first time in this RDD. Our comments are therefore based on what we understand to be potential provisions to be included in the Model and Commentary.

16. With respect to the issues that were identified in the November 2014 Discussion Draft, we are for the most part commenting only on those issues that are of most concern to our members and on which we have not previously commented. Where there are issues of concern on which we have previously commented, we are not repeating those comments here, but our previously submitted views still stand.²

² Those comments relate, *inter alia*, to the need for greater clarification as to the application of the LOB discretionary relief rule and for alignment between that rule and the PPT rule, the need for a flexible approach to determining the timing of qualifying for
3. **Alternative simplified LOB rule**

17. We appreciate that some attention was paid to the suggestion to have a less detailed, less restrictive LOB provision, and the version of a more simplified LOB found at paragraph 3 of the RDD is a good example of what such a provision might look like.

18. That said, proposing such a provision exclusively for use in conjunction with a PPT provision, and leaving the recommendation for a detailed, restrictive LOB in place for standalone use, is not responsive to the concerns expressed by commentators, notwithstanding the apparent desire on the part of delegates to be so. Where a PPT coexists with an LOB provision in a treaty, more attention must be paid to clearly defining the scope of the challenges that can be based on the PPT (or, more particularly, the scope of the challenges that should not be allowed) than in the case where the PPT standing alone must carry all the weight of addressing treaty shopping concerns.

19. If the respective scope of the two rules is not properly delineated where they coexist, the presence of the LOB in a treaty will merely serve as an additional barrier to cross-border trade and investment, not as a means of providing greater certainty to taxpayers or governments. We are concerned that the delegates may be underestimating the importance of guaranteeing that proper delineation.

20. We appreciate that some effort has been made in proposed paragraph 5 of the Commentary on the new Article X (Entitlement to Benefits) to suggest that the PPT should not be used to re-litigate the successful satisfaction of objective criteria that have been set by particular elements of the LOB test, but we are concerned that the passing reference to this concept in the Commentary is inadequate to address this fundamental concern. While we appreciate that proposed new examples have been added to the existing examples in the Commentary on the PPT provision, we are concerned that the examples do not include any discussion of whether the RCO in the examples is otherwise eligible for benefits under an LOB provision in the same treaty. Where that is the case, the examples could inject uncertainty by focusing on characteristics that have already been analyzed and found allowable under the LOB (e.g. the fact that RCO has a third country owner, or that it is deriving income connected with or incidental to its active conduct of a business), and by introducing new questions about the legitimacy of those characteristics (e.g., questions about whether there is an adequate commercial basis to justify RCO’s third country ownership or its receipt of income connected with or incidental to its active conduct of a business).

21. **Suggestion.** We suggest that the concept referenced at paragraph 5 of the proposed Commentary be specifically included in the text of any treaty that includes both a PPT provision and an LOB.
provision; this could be achieved by adding language along the following lines to paragraph 7 of the new Article X: “Where, however, a person is entitled to one or more benefits of this Convention by virtue of being a qualified person as defined in paragraph 2 or by virtue of meeting the requirements of paragraph 3 or 4, this paragraph shall not have the effect of denying such benefit or benefits to such person on the basis of any characteristics of such person or such person’s ownership or activities that have been taken into account in determining such person’s entitlement to benefits under those respective paragraphs.”

22. Suggestion. We further suggest that the Commentary specifically state that the range of grounds for challenging treaty benefits under a PPT provision will be narrower where that provision applies alongside an LOB test in the same treaty, for the reasons just explained.

23. We find it difficult to comment on the contents of the alternative simplified LOB because we cannot determine from the RDD exactly what those contents will be. Paragraph 3 of the RDD contains the text of one version of an alternative simplified LOB which is described as having triggered the discussion of the concept at WP1. The Annex to the RDD contains the proposal for adding a new “Article [X] (Entitlement to Benefits)” to the Model Tax Convention, the text of which is merely a description of the main features of what an LOB provision should have. Those main features do not fully correspond to the text of the alternative simplified LOB found at paragraph 3 of the RDD (e.g., the latter does not include safe harbors for charities, pension funds, or CIVs).

24. Suggestion. We assume that any alternative simplified LOB provision that is ultimately incorporated into the Commentary will include all the elements constituting the main features of an LOB described in the proposed Model text, but it would useful for that to be confirmed.

25. Suggestion. We note that the discretionary relief paragraph in the version of the alternative simplified LOB which appears at paragraph 3 of the RDD says that the competent authority who receives the request shall make its determination “in accordance with its domestic law or administrative practice”. It is not clear to us what is intended by that additional language, which does not appear in the corresponding discretionary relief paragraph found in the detailed LOB set out in the September 2014 Action 6 Report. It would be useful to have a clarification of the meaning of that language and confirmation that it would not operate to alter the substantive standard reflected in the provision and its Commentary or the basic procedural guarantees intended by the provision (e.g., that the competent authority consider the relevant facts and circumstances before reaching a decision, that it consider each request on its own merits, that it process the request expeditiously, and that it consult with the competent authority of the other Contracting State before rejecting a request).

26. Our understanding based upon the proposed Commentary found in the Annex to the RDD is that the OECD intends the Commentary to say that a State which does not include the PPT “should adopt” the detailed version of the other paragraphs of the proposed Article [X], rather than the alternative simplified version of those paragraphs. As we have previously commented, we do not believe the detailed version of the LOB which has been under consideration has been adequately analyzed by participating countries to justify its endorsement in the OECD Commentary. That detailed version, in our view, is much too
restrictive on certain points, and we believe Contracting States should have the right to decide between using the detailed or the alternative simplified version, without regard to whether they have adopted the PPT or not.

4. **Issues identified in the November 2014 discussion draft related to the LOB provision**

4.1 **Issue #3: Commentary on LOB discretionary relief provision**

27. The proposed changes to the Commentary on the LOB discretionary relief provision (and some of the pre-existing sentences) do not align with the standard laid out in the provision itself for granting discretionary relief. That standard looks to whether “the establishment, acquisition or maintenance of the resident and the conduct of its operations did not have as one of its principal purposes the obtaining of benefits under this Convention”. Accordingly, the relevant inquiry is whether or not the purpose of obtaining treaty benefits was one of the principal purposes.

28. By contrast, the first sentence of proposed paragraph 63 of the Commentary would require a person to show that there were “clear non-tax business reasons” for its formation, acquisition or maintenance and for the conduct of its operations. This would expand the relevant inquiry beyond the standard authorized by the treaty provision to take into account potential tax considerations unrelated to the obtaining of treaty benefits; as such, the proposed Commentary would not be a faithful interpretation of the treaty text itself.

29. **Suggestion.** We recommend reinstatement of the prior version of that sentence from the September 2014 Report, which more closely tracked the treaty standard.

30. **Suggestion.** We also recommend deletion of the sentence later in that paragraph that refers to “non-tax business reasons”.

31. We note that the new proposed text would require a person to show that it has a “substantial” relationship to its State of residence (rather than a “sufficient” one). There is no definition of the term “substantial” in this context, and we struggle to find any basis in the treaty text for requiring a “substantial” relationship.

32. **Suggestion.** Accordingly, we recommend deletion of that new and unfounded requirement.

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3 For similar reasons, we would recommend deleting from proposed new Example G in the Commentary on the PPT rule (see paragraph 98 of the RDD) the caveat as to whether one of the reasons for establishing a holding company in State R was tax purposes unrelated to tax benefits under the Convention, as that caveat has no grounding in the text of the PPT rule.
4.2 Issue #4: Alternative LOB provisions for EU countries

33. We appreciate the decision to address certain issues in the Commentary in generic fashion in order to address particular issues that arise under EU law.

34. With respect to pension funds, we appreciate the good intentions behind the proposal to add a derivative benefits safe harbor for them. In cases, however, where the relevant treaties provide an exemption from source State tax for dividends and interest received by pension funds resident in the respective countries, we anticipate that some questions could arise as to whether a pension fund established in one country (Country A) would be entitled, under the provisions of another country’s (Country B’s) treaty with the source State (Country C), to the same exemption as it could obtain under its own country’s treaty with the source State.

35. A question could arise, for example, as to whether a Country A pension fund would meet the definition of a “pension fund” under the treaty between Countries B and C and whether the characteristics of the Country A pension fund would have to be such as to meet all the requirements for treatment as a pension fund under the domestic laws of Country B.

36. **Suggestion.** We suggest that such a detailed inquiry would not be appropriate, and that it would therefore be useful to include a sentence along the following lines in the Commentary: “For purposes of subparagraph 2(d)(ii)(B), where the relevant treaties whose benefits are being compared both provide an exemption from dividend or interest taxation in the source State for pension funds, the pension fund otherwise entitled to such exemption from the source State under the treaty between the source State and the pension fund’s State of residence shall also be considered entitled to such exemption under the treaty between the source State and that third State.”

37. We note, too, that the inclusion of this derivative benefits safe harbor for pension funds is unlikely as a practical matter to achieve the desired results of guaranteeing treaty benefits in the cases described in the provision unless effective solutions are found to the kinds of unreasonable administrative hurdles some tax authorities are creating in their application of treaty anti-abuse rules to pension funds.

38. We therefore welcome the OECD’s commitment at paragraph 24 of the RDD to try to find appropriate solutions to these issues between September 2015 and December 2016.

4.3 Issue #5 (Requirement that each intermediate owner be a resident of either Contracting State)

39. We note that the RDD says the resolution of the question of whether to restrict the residency of intermediate owners under various paragraphs of the LOB is likely to depend upon outcome of new proposals described below on “special tax regimes” and subsequent changes to domestic law. We would simply refer to our prior comments regarding the critical importance of removing these restrictions in order to make the various safe harbors available as a practical matter to the types of totally non-abusive
and extremely common ownership structures found in MNEs worldwide, and we would urge the OECD to remove the restrictions without regard to how the discussion on the new proposals comes out.

4.4 Issue #6: Issues related to derivative benefits provision

40. As indicated in our previous comments, we believe a derivative benefits provision is critical to the proper functioning of an LOB provision, and we encourage the OECD to include a derivative benefits provision without regard to whether the LOB also includes the recent US proposals for provisions on “special tax regimes” and “subsequent changes in domestic law”. While we comment on each of these proposals below, we note that the concerns they appear designed to address (i.e. relating to the possibility that features of a country’s tax system could create the risk of double non-taxation) are also concerns the September Report recommended countries consider in deciding whether to enter into treaties in the first place, and appropriate consideration of those concerns at that stage could obviate the need for special provisions.

New proposal on “special tax regimes”

41. Regarding the proposal to deny the benefits of Articles 11, 12, and 21 to income subject to a “special tax regime”, such a provision should not be applicable for payments to unrelated parties, in part because it would be too much of an obligation to place on the payor/withholding agent to determine whether a special tax regime applied to the payee’s payment.

42. The term “special tax regime” is very broadly defined, and the term “preferential effective rate of taxation” is not defined at all, with the result that significant uncertainty could arise as to the application of the provision. For example:

- Would a regime for the amortization of intangibles constitute a “special tax regime” on the grounds that it provides for a reduction of the tax base and might disproportionately benefit royalties?
- What about a research tax credit?
- What is meant by “financing income” in relation to the statement that the term “special tax regime” with regard to financing income includes notional interest deductions?
- Is the reference to “other income” in the proposed carve-out for any regime that “does not disproportionately benefit interest, royalties or other income” intended to refer to income that falls under Article 21?
- Since the category of income covered by Article 21 is defined in the Model by reference to income that is not covered by other treaty articles (i.e., it is a negative definition), how could one determine whether a domestic law regime disproportionately benefits such income?
• Is the question of whether a regime disproportionately benefits interest, royalties or other income to be determined generically or by reference to the particular taxpayer involved?

• Is there any materiality threshold involved in determining whether an effective rate of taxation is “preferential”?

• Does the special tax regime have to apply to the payment in question in order for this provision to apply?

43. **Suggestion.** While we understand the principle behind the proposed provision denying certain benefits to income subject to a special tax regime, we believe that the provision would raise many difficult issues of interpretation in practice and that the OECD should therefore study the issue further before deciding whether or how to incorporate such a concept into the Model.

44. **Suggestion.** Notwithstanding our strong encouragement to the OECD to defer a decision on whether to include the proposed special tax regime provision until there has been further opportunity to study it, if the OECD decides to go ahead with the provision, we suggest that it be amended to include the condition that it would be triggered only after the source State provides public notification that a regime triggers its application. This would help to address the concern that the scope of its application is very uncertain as currently drafted and explained. We understand that this would require the source State to be aware of the regimes in question, but that concern should be addressed by the fact that the residence State has the obligation to notify the source State (under Article 2(4) of the Model) about significant changes in its domestic law relevant to the treaty and will also have the obligation under Action 5 to provide information to the residence State about rulings on preferential tax treatment given to residents of the residence State.

**New proposal on subsequent changes in domestic law**

45. Regarding the proposal to deny the benefits of Article 10, 11, 12, and 21 where a Contracting State has made certain subsequent changes to its domestic law, we believe significant interpretive issues may arise as to whether a Contracting State’s change in law results in “an exemption from taxation … for substantially all foreign source income (including interest and royalties)”. For example, if foreign source income is taxable, but only when remitted, is the regime covered by the proposed provision?

46. Since dividends are frequently exempted even under a “normal” territorial regime, we question whether it makes sense to call off treaty benefits for dividends on the grounds that the country has introduced a broader than normal territorial regime.

47. **Suggestion.** We suggest the OECD further analyze and clarify this proposal before deciding whether to incorporate it into the Model.

48. **Suggestion.** We further suggest that if this proposal is incorporated into the Model, it not apply to benefits under Article 10.
4.5 Issue #10: Clarification of the “active business” provision

49. **Suggestion.** We recommend against adopting the proposed changes to the active business test described at paragraph 72 of the RDD.

50. In paragraph 3(b) of the LOB rule, which relates to the application of the so-called “substantiality” test to an item of income derived by a resident of a Contracting State from the conduct of a trade or business conducted by that resident itself in the source State or by a person related to that resident, the existing language looks to whether the residence State business is substantial in relation to the source State business conducted by the resident or “the” related person. The proposal would change “the” related person to “a” related person. No explanation is given for this change, and it does not seem to make any sense, since the relevant comparison should be between the residence State business and the source State business from which the income is derived. The proposed change could have the effect of either allowing benefits inappropriately (e.g., by looking to a small source State business conducted by “a” related person which had no connection to the income item in question) or denying benefits inappropriately (e.g., by looking to a large source State business conducted by “a” related person which had no connection to the income item in question).

51. The first proposed change to paragraph 3(c) of the LOB rule would prevent a resident of a Contracting State from being deemed to conduct the business activities conducted in that State by related persons where the resident is subject to a special tax regime in that State.

52. **Suggestion.** For the reasons outlined above regarding the need for further study of the earlier special tax regime proposal, we recommend that the OECD not adopt this change until it has had more time to study the special tax regime concept and to decide whether it is appropriate to include it in the Model.

53. We also question the policy rationale for relying upon the special tax regime concept to prevent attribution of business activities in this context, given that the more general special tax regime test would not apply to deny benefits.

54. For example, suppose a resident company of a Contracting State was engaged in manufacturing activities which benefited from a special tax regime in that State. Suppose further that it had a sister company resident in that State and engaged in distribution activities in that State with respect to the goods it manufactured. Finally, suppose the first company derived dividends from a subsidiary in the source State which was engaged in manufacturing and distributing the same line of goods there. The basic special tax regime rule would not apply to deny source State benefits with respect to those dividends, since they are not base-eroding and that rule applies only to Articles 11, 12, and 21. If the first company conducted the residence State distribution activities directly, it would be entitled to benefits under the active business test for those dividends from the source State, assuming that its combined manufacturing and distribution business was substantial in relation to the business of the source State subsidiary. What
possible justification could there be for denying the first company the ability to take into account the distribution activities of its sister company for purposes of applying the substantiality test?

55.  The second proposed change to paragraph 3(c) of the LOB rule would prevent a resident of a Contracting State from being deemed to conduct the business activities conducted in that State by a related person unless the resident and the related person “are engaged in the same or a similar line of business”.

56.  **Suggestion.** We believe that this change is inadvisable and should be abandoned, as it would result in arbitrary distinctions depending upon whether a group’s activities in a State are conducted through one or multiple companies, a circumstance which is likely to be based on commercial considerations having nothing to do with the availability of treaty benefits.

57.  For example, suppose a multinational group has a significant operating business structure in Country A which is headed by a Country A holding company. The holding company, which is not itself engaged in the active conduct of a business, has several wholly owned Country A subsidiaries engaged in the active conduct of the group’s business in Country A. The holding company also has a wholly owned subsidiary in Country B which is engaged in the active conduct of the group’s same business in Country B.

58.  Under the proposed change, dividends paid by the Country B subsidiary to the Country A holding company would not be eligible for benefits under the active business test because the Country A holding company is not directly engaged in the active conduct of a business and because its lack of an active business would render it ineligible to take into account the active business operations of its wholly owned Country A subsidiaries.

59.  We submit this would arbitrarily and inappropriately deny the application of the active business test.

60.  We note that if the business activities conducted by the operating subsidiaries in Country A were not activities that formed part of or were not complementary to the business activities generating the income from Country B, attributing those activities to the Country A holding company would not help it to satisfy the requirements of the active business test.

5.  **Issues identified in the November 2014 discussion draft related to the PPT rule**

5.1  **Issue #17: List of examples in the Commentary on the PPT rule**

61.  **Suggestion.** For the reasons outlined in Section 3 above regarding the alternative simplified LOB rule, we recommend that the examples to be included in the Commentary relating to the PPT rule all indicate whether the applicable treaty in the example has an LOB provision in addition to the PPT rule, and whether if it does the RCO in the example satisfies the LOB provision; we further recommend that the OECD consider whether the analysis in the examples should be refined if the relevant treaty has an LOB provision which the RCO satisfies.
62. With respect to proposed new Example I, it is not clear to us what the relevant treaty benefits are, or who the relevant treaty claimants are, to which the PPT rule is being applied (e.g., is it with respect to royalties paid to the rights holders? Service fees paid to SCO or RCO?)

63. **Suggestion.** We suggest that this example be clarified to indicate to what benefits and persons the PPT rule is being applied.

6. **Other issues**

6.1 **Issue #19: The design and drafting of the rule applicable to permanent establishments located in third States**

64. We question the policy rationale for deleting subparagraph (f), regarding the exception for royalties received as compensation for the use of, or the right to use, intangible property produced or developed by the enterprise through the permanent establishment. In such circumstances, it seems appropriate to us that the PE should derive the royalties in question and should be regarded as having a substantial enough connection to those royalties to be able to qualify for treaty benefits on them, without regard to the rate of tax imposed by the PE State.

65. **Suggestion.** We would support the suggestion made in paragraph 106 of the RDD that the disallowance rule should not apply to cases where the source State has a treaty in force with the PE State and the effective tax rate on the PE is at least 60% of the rate of tax in the PE State.

66. **Suggestion.** We would also support the suggestion that the application of the rule should be subject to some form of discretionary relief.

6.2 **Issue #20: Proposed Commentary on the interaction between tax treaties and domestic anti-abuse rules**

67. **Suggestion.** We note that the RDD does not provide any indication of WP1’s response to the various concerns of Commentators referenced at paragraph 109 of the RDD. We suggest that the final version of the Commentary take those concerns into account and make the changes suggested by the commentators to address them.

68. We note further that the RDD does not propose any final Commentary to address this general topic but instead says that:

- “The proposed Commentary will need to be reviewed in June in order to decide whether any recommendations resulting from the work on Actions 2, 3, 4, and 8-10 raise treaty issues not already addressed in the Model”; and

- Paragraphs 7 to 12 and 20 to 22.2 of the existing Commentary on Article 1 “would need to be amended in order to avoid any overlap with the changes to the Commentary proposed in paragraph 49 of the Report whilst clarifying that the conclusions already reflected in these
paragraphs concerning the interactions between treaties and domestic anti-abuse rules remain valid”.

69. In this connection, we would:

- Note that the existing Commentary paragraphs 7 to 12 and 20 to 22.2 contain a very important and long-standing summary of the interaction between tax treaties and domestic anti-abuse rules, so that any amendment to those paragraphs must be very carefully undertaken to preserve the validity of the conclusions reflected there; and

- Caution once again that any new domestic anti-abuse rules designed to address other BEPS Action Items would prevail over treaties only per the description in the proposed Commentary (i.e., where they are specifically allowed in the treaty, where the treaty benefit refers to domestic law for its application, or where they are consistent with the PPT / Commentary).
PREVENT TREATY ABUSE: OECD PUBLIC DISCUSSION DRAFT

ICAEW welcomes the opportunity to comment on the public discussion draft Prevent Treaty Abuse published by OECD on 2 May 2015.

This response of 17 June 2015 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty’s Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

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Appendix 1
ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW’s regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 144,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
INTRODUCTION

1. We welcome the opportunity to comment on the public discussion draft Prevent Treaty Abuse published by OECD on 22 May 2015.

2. We submitted responses to two earlier discussion drafts on this same topic, namely TAXREP 3/15 in January 2015 and TAXREP 18/14 in April 2014.

GENERAL COMMENTS

3. We believe that the main response to potential treaty abuse should be by using an LOB or a GAAR based on a PPT (principal purpose test).

4. We are concerned that the current discussion draft ties the use of the simplified LOB to treaties which combine it with a principal purpose test (PPT) test, which means it would only be available to the limited number of treaties where both treaty partners agree to this combined test.

5. The LOB and the PPT are directed to distinct treaty shopping issues – eligibility of treaty residents for treaty benefits in the case of the LOB and combatting abusive use of treaties by eligible treaty residents in the case of the PPT. These independent standards should not be confused.

6. Some countries will prefer to deal with anti-abuse through a PPT and others may consider a more targeted anti-abuse rule the best avenue. That choice should not dictate whether a simplified LOB is used. We believe the OECD should opt for the simplified version, leaving it to bilateral negotiation to tailor a treaty LOB to the needs of the treaty partners.

7. We are also concerned about proposals for partial treaty termination if there are changes to the tax regime in one of the contracting parties ie an exemption from taxation to resident companies for substantially all foreign source income. This could, for instance, turn off the provisions of the particular treaty in relation to Article 10 (dividends), Article 11 (interest), Article 12 (Royalties) and Article 21 (other income). We believe it should be up to the contracting parties to introduce such a provision, in relation to their own bilateral treaty, and not include such a provision at the Model Convention level.

8. The new proposal for an alternative “simplified” LOB rule also has the potential to leave the treaty entitlement of a significant number of bona fide residents to be determined under the competent authority procedure if they don’t fit into any of the simplified categories of qualified persons.

9. This approach would most obviously disadvantage institutional investors (including those pension funds and charities which are specifically treated as treaty residents under the US model treaty and would stand to benefit under the model LOB article included in the OECD’s September 2014 Action 6 report “Preventing the granting of treaty benefits in inappropriate circumstances”). Not only would they face substantial delay in the determination of their treaty entitlement but it would also make it impracticable for any treaty relief to be granted at source. There would be a significant increase in the number of claims for refunds of tax withheld at source in excess of the treaty rate, which is likely to prolong the delays in obtaining refunds that bona fide claimants currently experience and to increase the amount of tax at source that cannot be reclaimed in practice because the source state does not provide a cost effective refund procedure.
10. For the first time, and at the very end of the BEPS process, the discussion draft introduces two new proposals viz exclusion with relation to special regimes and partial treaty termination that would reflect fundamental changes in treaty policy. A major shortcoming of the BEPS process is the truncated time period allowed to address complex, untested principles. Neither time nor the request for brevity allows us to properly critique the rules proposed in the discussion draft for these novel concepts that can have a major impact on entitlement to treaty benefits and the viability of a tax treaty. Determining how these rules would work, the definitional standards to be applied, the appropriateness of the "remedy" and the local constitutionality of the partial termination proposal on which we have commented briefly above in paragraph 8 are among the more obvious issues that should be vetted in a careful, deliberative process. The BEPS process has been an iterative process where new rules are aired, stakeholders respond, revisions are proposed and further input is provided by stakeholders before the end product is produced. We urge that the final report on Action 6 should not attempt to formulate rules that could be faulty and could be embedded in the Model or the multilateral convention, making hastily developed decisions difficult to reverse. Rather, it would be appropriate to set forth general principles for further consideration and development in a deliberative manner.

SPECIFIC COMMENTS

Item 18 – application of the new treaty tie-breaker rule
11. We believe there should be a maximum time limit for resolution of dual residence issues via the competent authority route and we suggest that this should be fixed at 6 months.
APPENDIX 1

ICAEW TAX FACULTY’S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

4. Easy to collect and to calculate: a person’s tax liability should be easy to calculate and straightforward and cheap to collect.

5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

Comments to the OECD Revised Discussion Draft BEPS Action 6 “Prevent Treaty Abuse”

The International Chamber of Commerce (ICC), as the world business organization speaking with authority on behalf of enterprises from all sectors in every part of the world, welcomes the opportunity to provide comments on the Revised Discussion Draft (RDD) regarding BEPS Action 6: Prevent Treaty Abuse. ICC is fully supportive of the aim of preventing the abuse of tax treaties through both treaty provisions and domestic law anti-abuse rules. However, ICC has already highlighted its serious concerns that Action 6 is focusing only on combating treaty abuse without due regard for the fact that the vast majority of potential beneficiaries of income tax treaties do not engage in abusive practices and, in many cases could be deprived of the certainty and predictability that is the fundamental goal of tax treaties and which is essential to facilitate cross-border investment. This misfocus is compounded in the RDD, by introducing new rules (such as the “special tax regime”), which is better addressed under the Harmful Tax Practices workstream. Introducing these late proposals and by allowing tax authorities a route to deny treaty benefits in circumstances where the benefits should apply – rather than addressing the underlying concerns through domestic legislation – there is a risk of creating further uncertainty and undermining the valuable work the OECD has achieved.

ICC notes that there are many complex issues in the BEPS action plan which require time and due diligence to fully consider the holistic implications of all the proposed changes. The OECD has made substantial progress and has the opportunity to make significant changes to the international tax scene. However, as ICC has previously underlined, failure to take the time necessary to consider the integration of all the actions, will result in faulty rules which will create difficulties for businesses – significantly hampering cross border trade and economic growth – and which would take years for governments to correct. The impact on the global economy and the prospect of developing countries is not to be underestimated.

ICC is aware that it is very challenging to reach full consensus in the given timeframe of the OECD/BEPS project. However, the lack of time for appropriate consideration is apparent from the RDD. Other than some further examples in relation to the Principal Purpose Test (PPT), and some progress in relation to Funds, the RDD offers very limited new guidance on the important issues that should be resolved. Many of the fundamental concerns raised by business have regrettably not been adequately addressed. Furthermore, ICC notes the introduction of new rules into Action 6 (such as the “special tax regime” referred to above) at the last breath of Action 6, while no Public Consultation is available to raise concerns adequately. ICC strongly believes that Working Party 1 should take more time to consider – and address – business concerns more rigorously, as well as ensuring an outcome that is coherent with BEPS actions overall.

Given the relatively little progress since the January 2015 Discussion Draft, it seems appropriate to reference prior comments provided by ICC1 (April 2014 and January 2015). ICC notes that there may be merit in returning to Action 6 discussions towards the conclusion of the OECD/BEPS project when other deliverables will be in a more final state.

As previously noted, paragraph 6 of the 2014 Deliverable states: “When examining the model treaty provisions included in this report, it is also important to note that these are model provisions that need to be adapted to the specificities of individual States and the circumstances

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of the negotiation of bilateral conventions.” ICC strongly agrees with this statement. However, ICC understands that the OECD intends to implement the guidance through the negotiation and adoption of a multilateral instrument. This is inconsistent with the OECD’s own recognition of the need to adapt approaches to account for different circumstances. This conflict may prove difficult to resolve. The drive to create a multilateral instrument may lead to trying to resolve on a multilateral basis issues that can only effectively be resolved on a bilateral basis. ICC believes that much of the complexity and the unresolved issues in the RDD reflect this tension. It would be constructive if the OECD could comment on how it expects to deliver Action 6 through a multilateral instrument. In the absence of such comment, it remains ICC’s view, that given the constraints of the process, it will be impossible to resolve all of these issues, and the model provisions should focus on outlining the key elements without prescribing the details that will need to be worked through in bilateral negotiations between States.

- ICC recommends that the OECD provides a clear mandate for countries to adhere to when seeking to deny treaty benefits. The fundamental aim of tax treaties must remain promoting international trade and investment through establishing rules that provide the greatest degree of certainty and predictability for bona fide beneficiaries of tax treaties. Rules that create subjectivity and uncertainty are to be avoided;
- In order to increase certainty and coherence with other BEPS activities, ICC recommends Working Party 1 takes time to consider the deep concerns expressed already by business, and form a consistent and aligned international approach;
- To enhance certainty, ICC suggests that the OECD would consider a pre-clearance process under which treaty benefits are granted if the Competent Authority does not affirmatively deny them within a given (relatively short) time frame.
- ICC recommends reducing and simplifying the overly restrictive prescriptive requirements in the proposed Limitation on Benefits (LOB) clauses – a good starting point is the simplified LOB in paragraph 3 of the RDD. This provides a clear minimum standard and the details will be worked bilaterally using guidance from the existing Model;
- In line with such simplification, with providing clarity, certainty and with ensuring the various Actions under BEPS address concerns appropriately, ICC recommends removal of the new “special tax regime” and treaty response to certain future changes in a country’s domestic law clauses. These have been introduced with insufficient time for either business or OECD members to consider their implications adequately, including the ramifications of permitting unilateral disapplication of treaty benefits.
- ICC continues to recommend focusing on substance and is concerned that the current principal purpose test (PPT) remains widely framed. Therefore, even with the additional examples in the Commentary, there is a risk of misinterpretation or misapplication by tax authorities.
- The clearest possible guidance, with further examples, ought to be provided in order to create as much clarity and certainty as possible in what is a highly subjective area. While ICC supports the proposal for countries to set up a form of advisory panel, any conclusion to disapply treaty benefits should be bilateral, and in the case of disagreement a mandatory arbitration process should follow.
- ICC recommends to make clear that the application of the PPT test – particularly if it applies in combination with a LOB test – is not intended to undercut the LOB provisions, but directed towards conduit financing or clearly artificial and tax abusive arrangements.
The International Chamber of Commerce (ICC)
Commission on Taxation

ICC is the world business organization, whose mission is to promote open trade and investment and help business meet the challenges and opportunities of an increasingly integrated world economy. Founded in 1919, and with interests spanning every sector of private enterprise, ICC’s global network comprises over 6 million companies, chambers of commerce and business associations in more than 130 countries. ICC members work through national committees in their countries to address business concerns and convey ICC views to their respective governments.

The fundamental mission of ICC is to promote open international trade and investment and help business meet the challenges and opportunities of globalization. ICC conveys international business views and priorities through active engagement with the United Nations, the World Trade Organization, the Organisation for Economic Co-operation and Development (OECD), the G20 and other intergovernmental forums.

The ICC Commission on Taxation promotes transparent and non-discriminatory treatment of foreign investment and earnings that eliminates tax obstacles to cross-border trade and investment. The Commission is composed of more than 150 tax experts from companies and business associations in approximately 40 countries from different regions of the world and all economic sectors. It analyses developments in international fiscal policy and legislation and puts forward business views on government and intergovernmental projects affecting taxation. Observers include representatives of the International Fiscal Association (IFA), International Bar Association (IBA), Business and Industry Advisory Committee to the OECD (BIAC), Business Europe and the United Nations Committee of Experts on International Cooperation in Tax Matters.
Dear Marlies:

ICI Global\(^1\) on behalf of our collective investment vehicle (CIV)\(^2\) industry members, appreciates greatly that the Base Erosion and Profit Shifting (BEPS) Action 6 Revised Discussion Draft\(^3\) reflects concerns we raised in our January submission\(^4\) and during the March public consultation. In support of your entirely-reasonable request to keep comments “as short as possible,” we note seven here and discuss below only the last one. Specifically:

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\(^1\) The international arm of the Investment Company Institute, ICI Global serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US$19.6 trillion. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC.

\(^2\) A CIV is defined for this purpose consistently with the OECD’s Report entitled “The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles” (the “CIV Report”). Specifically, CIVs are defined as “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.” CIV Report, page 3, paragraph 4. Funds that are not treated as CIVs in the CIV Report (and that are not addressed in our comments) include “investments through private equity funds, hedge funds or trust or other entities that do not fall within the [Report’s] definition of CIV.” Id.


• we appreciate greatly Working Party 1’s support for the conclusions of the 2010 CIV Report\(^5\) concerning CIV treaty entitlement;

• we support strongly the adoption of an equivalent beneficiary standard for treaty eligibility in any limitation on benefit (LOB) clause and, more specifically, one that applies the same percentage otherwise used in an LOB clause;

• we appreciate greatly Working Party 1’s agreement that implementing the Treaty Relief and Compliance Enhancement (TRACE)\(^6\) project’s recommendations is important for the practical application of the CIV Report’s conclusions;

• we urge Working Party 1 to adopt the expansion (in paragraph 40) of the LOB rule pension fund exception and provide a reasonably-low equivalent beneficiary percentage (reflecting the fact that the typical pension fund is not engaged in “treaty abuse”);

• we support fully the well-considered exceptions from the proposed definition of “special tax regime” for domestic tax rules applicable to investment pools such as pension funds (subparagraph vi) and CIVs (subparagraph vii);

• we support enhancing the effectiveness of dispute resolution mechanisms by, among other things, expanding the availability of mandatory binding arbitration; and

• we urge that the Commentary include one more example of the Principal Purpose Test (PPT) rule’s potential application to CIVs.

Our only suggestion for which additional explanation is provided herein involves the PPT rule’s potential application to CIVs. We appreciate greatly, as noted in our January comments and during the March public consultation, Example D (on pages 72-73) of the BEPS Action 6 2014 Deliverable.\(^7\) We submit, however, that the PPT rule relief provided by this example is too limited – particularly in the context of any treaty that has been crafted based upon the CIV Report’s recommendations. Specifically, if two countries examine how each country’s resident CIVs are organized, operated, taxed, and distributed, and then agree that CIVs with these characteristics are treaty eligible, the two countries have agreed that these CIVs are not treaty shopping vehicles. In this context, the PPT clearly should not be applied unilaterally by one of


the countries to deny the carefully-considered, treaty-negotiated relief provided to the other country’s CIVs. An example to this effect would be most welcome by those CIVs that cannot establish with sufficient ease that they satisfy the requirements included in Example D.

* * *

Please feel free to contact me (at lawson@ici.org or 001-202-326-5832) at your convenience if you would like to discuss this issue further or if we can provide you with any additional information. My colleagues Karen Gibian (at kgibian@ici.org or 001-202-371-5432) and Ryan Lovin (at ryan.lovin@ici.org or 001-202-326-5826) also may be called upon for assistance.

Sincerely,

Keith Lawson
Deputy General Counsel – Tax Law

cc: taxtreaties@oecd.org
Dear Ms. de Ruiter

BEPS Revised Discussion Draft Action 6: Prevent Treaty Abuse

The IDSA welcomes the opportunity to comment on the BEPS Revised Discussion Draft on Action 6: Prevent Treaty Abuse, issued on 22 May 2015 (the “Revised Action 6 Discussion Draft”).

In our previous response to the 21 November Discussion Draft “Follow-up Work on BEPS Action 6 (Prevent Treaty Above)”, dated January 9, 2015 [and attached, for reference, as an Appendix, to this letter], we outlined the importance of the role of the securitisation industry as an alternative to bank funding and its role in filling the “bank funding gap”. We also outlined the importance of treaty access to the securitisations industry and that treaty access in the area of securitisation had so far been overlooked in the Action 6 workstream.

We acknowledge that the Working Paper has heard these concerns through comments included in paragraph 22 of the Revised Action 6 Discussion Draft “…the Working Paper recognised the importance of [non-CIV] funds and the need to ensure treaty benefits be granted where appropriate. It also noted, however, that most suggestions included in the comments received did not sufficiently take account of treaty-shopping concerns.”

And paragraph 24 “The Working Party agreed that it should continue to explore solutions to issues related to the treaty entitlement of non-CIV funds that would address two general concerns that governments have about granting treaty benefits with respect to non-CIVs: that non-CIVs may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits and that investors may defer recognition of income on which treaty benefits have been granted. Possible options that the Working Party intends to further discuss at its June meeting include adding a specific provision on non-CIVs in the LOB rule and adding one or more examples on non-CIVs to the Commentary on the PPT rule.”
Recommend continuance of work on Action 6 and application to non-CIVS post September 2015 deadline

We note the comments of the Working Party in paragraph 24 of the Revised Action 6 Discussion Draft “…that work on [options to add a specific provision on non-CIVs in the LOB rule and adding one or more examples on non-CIVs to the Commentary on the PPT rule] and other options might continue after the September 2015 adoption of the final report on Action 6 but should in any event be completed before the December 2016 deadline for the negotiation of the multilateral instrument that will implement the conclusions of the work on Action 6.”

We would strongly advocate that this approach be followed. As outlined in our previous submission a securitisation company in any jurisdiction will likely fail the base erosion test contained with the proposed “detailed” LOB since it may not be in a position to identify who its bondholders are. Thus a securitisation company may ultimately never be in a position to demonstrate that it satisfies the LOB test other than through applying for discretionary relief under paragraph 5 of the proposed LOB. This may be the case even though its bondholders may be institutional investors in OECD member states. Applying for discretionary relief under paragraph 5 is not a viable option. It would be time-consuming, costly and likely to lead to inconsistent results between different jurisdictions; in addition to the harm the uncertainty would cause the securitisation industry as a whole.

Therefore, the IDSA considers that the only available solution for the securitisation industry, under the current Treaty-Abuse proposals, is to satisfy the “standalone” PPT rule. Securitisations are generally effected for bona fide commercial purposes and not for the purposes of tax avoidance or treaty abuse. For this reason, IDSA considers that securitisation vehicles should qualify for treaty benefits under any PPT rules. It is therefore critical for the securitisation industry, that the PPT rule and related commentary and examples are “fit for purpose” and are clear on how the PPT should operate in practice and apply to the securitisations industry. The Working Party has indirectly acknowledged this in paragraph 24 where it states its intention to discuss adding one or more examples on non-CIVs to the PPT rule. We have drafted an example specific to the securitisation industry for inclusion in the PPT commentary below.

Furthermore, while the inclusion of an LOB test is vehemently not the preferred approach of IDSA, IDSA considers that the only available solution under the LOB approach is to develop a separate category of “qualified person” to apply to “cross-border” securitisation companies/vehicles which will make it clear when a securitisation vehicle will be treated as satisfying the “detailed” LOB. Further work should also be undertaken to ensure that the Derivative Benefits provision in the “Simplified” LOB is appropriate for the securitisations industry (e.g. through consideration of testing dates, minimum ownership threshold, etc.)

In order to ensure such provisions are properly drafted and take account of the concerns of all parties further consultation and study (along the lines of the 2010 CIV Report) for each of the industries in the non-CIV area will be required. In particular, should the LOB route be adopted, the practical and logistical challenges of trying to identify the investors and bondholders in securitisation structures will have to be given further thought – CIVs are further along this road due to the TRACE
project and the extension of such a system or the development of something similar to non-CIVs will require further thought and consultation. In this regard we recommend that the Working Paper continues to work on the application of this work stream to the non-CIVs/ securitisation industry post September 2015.

1. Example for inclusion in commentary to PPT rule of application of PPT rule to securitisation vehicle

In response to the Working Party’s request under paragraph 24 of the Revised Action 6 Discussion Draft, the ISDA proposes that the example outlined below be included in the commentary to the PPT rule. The PPT rule is especially important to the Securitisation Industry given that a securitisation company will, under current practices never be in a position to demonstrate that it satisfies the LOB rule based on the current drafts of the “detailed” and “simplified” LOB rules. Thus given the importance of the PPT rule to the securitisation industry and the importance of access to a tax treaty network to the securitisation industry, the commentary on the interpretation of the PPT should acknowledge that it is legitimate to recognise that an important consideration in deciding to locate and establish a business in a jurisdiction is the existence of a good tax treaty network and the benefits it affords. The commentary should make explicit, at a minimum through the provision of clear examples, that this can be especially the case for smaller economies (where some of the wider business related benefits available in larger economies are not present) and where there are strong fundamental commercial reasons supporting the underlying business transaction and parties have flexibility to determine where to locate the business.

“BankCo is a bank established in State Q. BankCo wishes to raise new capital and de-risk its balance sheet and has identified a pool of loans which it has originated and that can be sold to raise the capital it requires. BankCo establishes RCo, a securitisation company resident in State R. RCo has only nominal share capital which is held by an independent share trustee on trust for charitable purposes in order to ensure RCo, as the securitisation company, is “bankruptcy remote” which is an appropriate commercial characteristic for the success of the securitisation transaction. RCo raises debt finance by issuing bonds to investors in the capital markets. The bonds are widely held by investors and are listed on a recognised stock exchange. BankCo also retained an interest in RCo. RCo uses the proceeds of the bond issuance to acquire the portfolio of loans from BankCo. The loans are owed by debtors located in a number of jurisdictions. Specifically 15% of RCo’s portfolio is held in receivables of SMEs resident in State S, in respect of which RCo receives regular interest payments. Under the tax convention between State R and State S, the withholding tax rate on interest is reduced from 30% to 10%.

BankCo’s decision to establish RCo in State R is driven by State R’s securitisation legislation, established credentials as a location for establishing securitisation companies, skilled and knowledgeable labour force and professional services market, membership of a regional grouping and the comprehensive double taxation treaty network of State R, including its tax treaty with State S, which provides a reduced rate of withholding tax on interest. Furthermore, it is likely that a majority of investors in RCo are pension funds and other financial institutions located in OECD member states. Investors’ decisions to invest in RCo are
not driven by any particular investment made by RCo and RCo’s investment strategy is not driven by the tax position of investors. RCo is taxed in State R on income earned and is entitled to a full deduction for interest payments made to investors.

In this example, merely reviewing the effects of State R’s tax treaty with State S on interest payments by the SME debtors in State S to RCo, or the fact that State R has a comprehensive double tax treaty network, would not enable a conclusion to be drawn about the purpose for the establishment of RCo by BankCo. The intent of tax treaties is to provide benefits to encourage cross-border investment and, therefore, in order to determine whether or not paragraph 7 applies to an investment, it is necessary to consider the context in which the investment is made. RCo was established as a result of a genuine commercial decision made and implemented by BankCo and provided RCo’s business is properly conducted in State R through, for example, the making of decisions necessary for the conduct of its business by skilled personnel with the knowledge and experience appropriate to make such decisions and assume real risks, it would not be reasonable to deny the benefit of the State R / State S tax convention to RCo.”

2. **Sample approach for specific provision to deal with securitisation vehicles in “detailed” LOB**

As noted above the LOB approach is not the preferred approach of IDSA for trying to manage treaty-abuse concerns for the securitisations industry. For the reasons outlined above, a securitisation company will generally not be in a position to establish whether it satisfies an LOB test. Further securitisations are generally effected for bona fide commercial purposes and not for the avoidance of tax avoidance or treaty abuse. Thus IDSA believes that securitisation companies should start from the premise that they are entitled to treaty benefits rather than having to prove that to be the case. However in the interest of addressing the Working Party’s concerns as noted in paragraph 22 and trying to come up with an LOB that might work for the securitisations industry we propose that a separate category of “qualified person” be included in the LOB clause to deal with securitisation companies.

The OECD papers recognise that there are parallels between the issues arising for CIVs from the proposed LOB rules and the issues affecting non-CIVs. For these reasons we believe that non-CIV securitisation companies should be afforded similar treatment as is currently being contemplated for CIVs – taking account of the Working Party’s comments in paragraphs 22 and 24 of the Revised Action 6 Discussion Draft that any modifications to the LOB for non-CIVs needs to take account of treaty shopping concerns. In this regard IDSA propose the inclusion of a specific paragraph, a new paragraph 2(g), to apply to “cross-border” securitisation vehicles which is largely based off the proposed subparagraph 2(e) for privately held companies but adjusted to take account of issues identified as arising for CIVs and would heavily rely on the drafted commentary proposed for CIVs with appropriate adjustments for the securitisation industry/ non-CIVs. As noted above, further thought and consultation with industry will be required between all parties in order to get any such provision right and also make it practically implementable from an industry perspective. As noted previously, currently there is no system whereby a securitisation company can identify who are its bondholders and thus could not currently demonstrate that it satisfied the proposed LOB test below.
Finally, IDSA would like to highlight that any LOB should not undermine the rights of freedom of establishment and free movement of capital between Member States of the European Union. These principles are enshrined in European law. IDSA considers that the LOB, as currently proposed, could potentially undermine these rights and be incompatible with European law. For example, under the proposed LOB, a securitisation vehicle established in a Member State of the European Union would be entitled to tax treaty access where its bondholders are all tax resident in that same Member State. However, that same securitisation vehicle would likely not be entitled to treaty access where it: (i) was established in a different Member State; or (ii) raised capital from bondholders that were tax resident in a different Member State. This approach has the effect of allowing / denying tax treaty access on a discriminatory basis by reference to which Member State the securitisation vehicle is established in and / or has raised its capital from. The IDSA considers such an LOB approach could potentially be contrary to the freedoms guaranteed by European law.

3. Sample approach for specific provision to deal with securitisation vehicles in “simplified” LOB

While we acknowledge the revised “Derivative Benefits” test included in the “simplified” LOB, IDSA is concerned that given the wide investor base in securitisation transaction, the 75% ownership threshold would be difficult to substantiate in practice and a 50% threshold is more appropriate. Accordingly rather than trying to amend the Derivative Benefits test we would propose the inclusion of a special category of “qualified person” to deal with the securitisations industry.

4. Proposals re new treaty provisions on special tax regimes

*General comments*

IDSA was surprised to see an entirely new proposal for ‘special tax regimes’ introduced to Action 6. This new proposal comes at a very late stage in the consultation process. In IDSA’s view, this late proposal has the potential to undermine the public consultation process, which stakeholders have been engaged in since the commencement of Action 6. This is particularly true where stakeholders have been requested to make as few comments as possible on revised Action 6 proposals. In IDSA’s view, there are many technical tax issues that need to be dealt with in the ‘special tax regime’ proposal (mentioned below), though all of these are superseded by the requirement for proper consultation on the issues and time to allow stakeholders to properly consider the draft proposals. In this regard, IDSA suggests that no final decision should made on this proposal until 2016, after a full consultation has taken place.

*Difficulties with the ‘special tax regime’ proposal*

Although IDSA believes that stakeholders have not had sufficient time to consider the potential impact of the ‘special tax regime’ proposal, there are some general issues which may be highlighted at a high-level at this stage.

The ‘special tax regime’ proposal is a wholly subjective concept. There are no objective bench marks as to what a tax regime has to be compared with. In the absence of such objective criteria, taxpayers and tax authorities are likely to attempt to evaluate qualitative differences between their local and foreign tax regimes to decide if a foreign tax regime is ‘special’. Taxpayers and tax authorities will inevitably adopt conflicting positions with respect to the same foreign tax regime. A
taxpayer or tax authority (as the case may be) may consider a particular foreign tax regime to be ‘special’, though another taxpayer or tax authority may not. This will result in an inconsistent approach amongst taxpayers (including taxpayers in the same OECD jurisdiction) and an inconsistent approach amongst different OECD tax authorities, in each case with respect to the same taxpayer. In addition, taxpayers and tax authorities will have to decide for themselves what qualitative differences make a foreign tax regime ‘special’. Although it is not possible to foresee all of the differences that may be considered relevant, some obvious questions are whether a foreign tax regime could be ‘special’ compared to another tax regime simply because it has:

- different tax depreciation regimes;
- different rules for claiming specific tax deductions (eg, financing expenses); and
- local tax exemptions for items of income which may not be relevant to the particular item being considered for treaty benefits.

To decide if there are qualitative differences between tax regimes, taxpayers and tax authorities are likely to need detailed information about the taxpayer in the other jurisdiction. It is difficult to see how this (often commercially sensitive) information could be obtained in unrelated party transactions. In addition, the proposal also implicitly assumes perfect knowledge amongst taxpayers and tax authorities as to how all foreign tax regimes operate. In practice, this is an unrealistic assumption and implementing the special tax regime proposal would require taxpayers and tax authorities to obtain detailed information and advice as to how a particular foreign tax regime may apply to particular items of income. This is obviously an impractical and unworkable model.

Finally, OECD jurisdictions differ in the way their tax regimes are constructed. For example, some jurisdictions may have specific tax regimes for particular items of income, whereas others may have a comprehensive tax regime that applies generally, though with some specific provisions for particular items of income. How is a taxpayer or tax authority to determine whether a particular tax regime is special in each of these contexts?

**Scope is not clear**

IDSA also believes that the potential scope of the ‘special tax regime’ proposal is not clear. In particular, Action 6 proposes that treaty relief would only be denied if the taxpayer is subject to a special tax regime:

- “with respect to” interest, royalties or other income. It is not at all clear when a regime will be considered to apply “with respect to” any particular item of income. For example, would receipts of interest, royalties or other income have to be exempt from tax or subject to an entirely different tax regime than other items of income?
- that “disproportionately benefit interest, royalties or other income or any combination thereof”. Again, it is not clear what this means. Would the tax regime have to be a completely different tax regime that applies solely to these items of income?

Detailed explanations and commentary would be required to define the scope of the ‘special tax regime’ proposal to provide certainty for taxpayers and tax authorities. As mentioned above, some jurisdictions may have specific tax regimes for particular types of income, whereas others may have
a comprehensive tax regime that applies generally. It is not clear how the proposed scope of the ‘special tax regime’ proposal as described above could be applied in these different contexts.

Unclear how exclusions may work

Action 6 proposes that Contracting States will be permitted to carve particular local provisions out of the ‘special tax regime’ proposal. However, Action 6 proposes that this would only be possible if the relevant local provisions do not result in a low effective rate of taxation. It is not clear how any carve-out proposal could work in practice, as a special tax regime (by its very nature) is likely to result in a lower effective tax rate than usual.

EU law

The ECJ has already concluded (in Case C-318/10) that local tax rules that determine the tax treatment of a payment made in one EU Member State by reference to the characteristics of the tax system of another EU Member State are contrary to European law. In this regard, any proposal relating to special tax regimes could not be applied to tax treaties between EU Member States.

IDSA proposals

IDSA proposes that no final decision should be made on this special tax regime proposal until 2016, after a full consultation has taken place with stakeholders on the issues involved. However, if this proposal is to be advanced in its current form, IDSA has some recommendations as to how it might be improved.

1. Related parties; - The ‘special tax regime’ proposal should be limited to payments between related parties only. This is the proposed approach to be applied in the US model tax treaty. This reflects a more sensible approach as it is unlikely to require the taxpayer or tax authority to obtain detailed information about the recipient’s tax status (which, in an unrelated party context, is unlikely to be available).

2. Securitisation vehicles, together with other Non-CIV funds, should be carved-out of any special tax regime provision. This would allow Contracting States to decide for themselves whether securitisation vehicles should be subject to any limitations under applicable tax treaties. Any different approach would undermine existing proposals to treat Non-CIV funds in this way under proposed LOB provisions.

Yours faithfully,

GARY PALMER
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Irish Debt Securities Association
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Appendix


The IDSA welcomes this opportunity to provide comments on the 21 November Discussion Draft “Follow-up Work on BEPS Action 6 (Prevent Treaty Abuse)” as we believe the area of securitisation and treaty access has perhaps been somewhat overlooked so far in this work stream. We would be pleased to attend the Public Consultation Meeting on the 22 January 2015 for which we have requested registration and to make some of the points mentioned in this paper.

1. **Irish Debt Securities Association (“IDSA”)**

The Irish Debt Securities Association (“IDSA”) is an industry organisation established with the aim of promoting and developing the environment and infrastructure in Ireland to support the global structured finance, debt securities and the specialist securities industries. The IDSA promotes a responsible, sustainable and effective environment within which debt securities and other specialist securities can be used to facilitate transactions, to create investment products and to raise capital funding.

The membership of the IDSA includes corporate administrators, trustees, audit firms, legal advisors, listing agents, and other parties involved in the structuring and management of special purpose vehicles in Ireland. The IDSA works to promote high standards of professional conduct among industry service providers and to lead industry activity in developing and providing a world-leading environment for structured finance transactions and for the issuance of debt securities and other specialist securities.

2. **The role and importance of Securitisation.**

2.1 **Bank Funding Gap**

Economic growth in Europe and the rest of the world is low by historical standards. Growth requires investment and investment requires funding. There is a natural limit to the availability of equity finance and, in Europe in particular, debt finance is hugely important.

A survey published by Standard & Poor’s in May 2012, estimated that Europe will require an additional €1.6 trillion to €1.9 trillion to finance any kind of growth between 2012 and 2016. This only focuses on growth and does not include any long-term or replacement investment needed to maintain competitiveness. As such the conservative estimate is a minimum €4 trillion gap in funding for the European economy in the next 5 years. Unless this funding gap can be bridged, Europe faces the potential of a wasted decade from an economic standpoint. European banks will struggle to fill this funding gap without raising significant capital.

Of all the ways in which it is possible to open up financing channels from capital market investors to the mid-cap, SME and consumer borrowers, securitisation seems most capable. Securitisation has the characteristics that make it a versatile and powerful funding channel and the potential to be a key component of any attempt to bridge the European funding gap. This is not to suggest securitisation is the only such channel or could even aspire to being the sole way in which these borrowers obtain non-bank funding. However as a funding tool it is acknowledged that securitisation can contribute to a well-diversified funding base in terms of maturity, investor type and currency.
2.2 Deleveraging Banks

The deleveraging of European banks will be in the order of 7% of their balance sheet according to the IMF, conservatively estimated at US$2.6 trillion at the lower end or a top range of US$3.8 trillion. In accordance with the Basel III liquidity rules a further €600 billion of cash will be required to be held by European banks. These new capital and liquidity regulations will constrain the ability of European banks to fund the real economy to the order of €2.5 trillion. The ECB stress tests have put more focus on deleveraging the European banks to boost regulatory capital. One of the principal reasons is the need for European banks to deleverage due to new regulatory rules on capital in addition to increased liquidity requirements.

Traditionally Europe has had a great reliance on banks to provide funding to the economy than for example the United States. The ratios of securitised loans and corporate bonds to total financing volumes in Europe in 2011 was 19 per cent, compared to 64 per cent in the United States. It is clear that European banks need increasingly to securitise their assets. The transfer of credit risk away from the banking sector can be beneficial to the real economy and to monetary and financial stability.

The higher the price that can be achieved for bank assets (principally loans to customers), the less regulatory capital banks will have to raise. Accordingly, a strong securitisation market, particularly in Europe, would assist in deleveraging banks, freeing up regulatory capital and enabling banks to lend to business.

2.3 Alternatives to Bank Funding

If the banks cannot fill the funding gap, it has to be filled from somewhere and there are limited realistic options.

- First, the gap can be filled by the public sector. This is not realistic due to current fiscal consolidation.
- Secondly, the missing finance can simply continue to go missing, resulting in a low growth period extending for a number of years. This should not be an acceptable outcome for policymakers.
- Thirdly, all or some of the missing finance can be channelled to the real economy from non-governmental and non-bank sources: in other words from the capital markets. In some cases, private equity can fill the gap, but it is largely debt funded so it in turn depends on banks (unlikely in this environment) and the capital markets.

The use of securitisations and bond issuances to fund either direct lending to businesses or to acquire debt already advanced to businesses will be a key component of any successful attempt at bridging the funding gap and providing funding to businesses.

3. Basic Structure of a Securitisation

Most securitisations have a similar legal structure. A typical securitisation structure and transaction can be explained in the following way:

3.1 A bank/financial institution wishes to raise new capital and de-risk its balance sheet and has identified a pool of loans that it has originated that can be sold to raise the capital it requires.

3.2 A new securitisation vehicle is established (for example, in Ireland). The securitisation vehicle usually has only a nominal equity share capital.

3.3 The nominal equity share capital of the securitisation vehicle is held by an independent share trustee usually on trust for charitable purposes. This equity structure is designed to ensure that
the securitisation vehicle is ‘bankruptcy remote’, meaning that it is insulated from the insolvency risk of other parties to the securitisation (as it does not form part of any other party’s group of companies).

3.4 The securitisation vehicle raises debt financing by issuing bonds to investors (ie, bondholders) in the capital markets. Most (if not all) of these bondholders will be resident in a different jurisdiction than the securitisation vehicle, as securitisations generally involve cross-border investment.

3.5 The proceeds of the bonds are used by the securitisation vehicle to acquire loans (such as a portfolio of mortgage loans) from the bank/financial institution which ‘collateralise’ the bonds issued to bondholders. The proceeds of this sale represents new capital for the bank/financial institutions that can be used for new lending business. It also represents a de-risking of the loans from the bank/financial institution’s balance sheet.

3.6 The securitisation vehicle uses the returns received on the loans it has purchased from the bank/financial institution (i.e. repayments of principal and interest from borrowers) to pay interest and to repay principal to its bondholders as these payments fall due.

3.7 The bonds are commonly listed on a recognised stock exchange and held in global form by a common depositary on behalf of a clearing system (such as Euroclear or Clearstream). The presence of a clearing system in the ownership chain means that the securitisation vehicle may not know who the beneficial owner of its bonds are from time to time. In addition, bondholders may freely trade their positions in the bonds through the clearing system. Importantly, the bonds are not typically traded on the recognised stock exchange on which they may be listed, but are traded through the clearing systems in electronic form.

3.8 A diagram of a typical securitisation structure is as follows:

3.9 Commonly, bonds do not all have the same repayment priority and may be issued in senior and junior tranches. Usually, senior bonds have first claim on the proceeds of all the loans in the securitised pool. Junior bonds have a subordinated claim, meaning they get paid after the senior bonds. In short, this means that losses are “allocated” first to the junior bondholders who therefore take the greater risk.
3.10 Senior bonds can be ‘over collateralised’ and in this way it is possible to issue bonds that appeal to the most risk averse capital market investors. The junior bonds, which generally constitute a much smaller proportion of the overall securitisation pool, can be sold to other capital market investors who have greater risk appetite.

3.11 Bonds which are often rated and listed are subject to the kind of benchmarking that can attract global investors. As bonds are freely tradable they allow an investor to sell the bond before its maturity. In this way they offer the possibility of liquidity to the capital market investor whilst allowing long term funding for the securitisation vehicle.

3.12 Finally, most loans that are securitised are originated by a bank. After the securitisation, the bank usually continues to service the loans. The securitisation process allows the capital market investors to leverage off (and effectively pay) the institutions that have already created the infrastructure to advance loans.

4. Regulation of a Securitisation

In recent years, the EU and the United States have introduced regulation relating to the holding of a “retention piece” in securitisation transactions in order that certain regulated entities may invest in such structures. As mentioned above, securitisation transactions are usually funded by a number of different tranches of bonds with increasing levels of risk and return and decreasing ratings. For example, a securitisation vehicle will often issue A, B, C, D, E etc. bonds with the potential for increasing return (and risk) as they are more deeply subordinated. In many securitisations in order to comply with risk retention requirements a specified proportion of the lowest tranche, or of each tranche, of the capital structure (the retention piece) must be held by an “originator”, “sponsor” or “original lender” (usually the bank that advanced or originated the debt in the first place) for the life of the transaction. This is to prevent banks from securitising loans which are of poor quality and passing the risk of any default entirely onto investors in the bonds. In addition, securitisation vehicles are subject to reporting to the Central Banks of the European member states and onward to the European Central Bank pursuant to Regulation (EC) No 1075/2013 of the European Central Bank of 18 October 2013 concerning statistics on the assets and liabilities of financial vehicle corporation engaged in securitisation transactions (commonly known as the “FVC Regulation”). We have set out in the appendix a brief overview of the EU law regulating many securitisations in Europe.

5. Securitisation Tax Regimes

Most of the tax systems of the countries that have securitisation regimes work in fundamentally the same way. The securitisation company is subject to corporation tax on its income but obtains a deduction for its funding leaving behind a small profit spread in the company.

From a superficial level this could be viewed as base erosion. An apparently simple “solution” to this base erosion would be to tax the securitisation company (say in Ireland at 25%) and deny a deduction for payments out to investors. The payments out would be dividends to the investors who would benefit from a participation exemption in their local jurisdiction. Accordingly, the tax on the securitisation activity would default to the location of the securitisation vehicle. Clearly, this is not the correct outcome as evidenced by the fact that many jurisdictions have securitisation transactions legislation that adopts a wholly different approach.

In reality, the correct approach is that the payments out to the securitisation vehicle would be usually deductible in the source country and would be taxed wherever the investors are liable to tax. The investors in securitisation vehicles are generally large institutions such as insurance companies, banks, pension funds and investment funds. These are all subject to regulation and to a tax system in the jurisdiction in which they are located.

6. Action 6 Preventing Treaty Abuse
The initial Discussion Document, the September Report and the Follow Up work on BEPS Action 6 published on 21 November last contain a number of proposals designed to prevent treaty abuse. In particular two new anti-abuse tests are suggested viz

- Limitation on Benefits (LOB) rule and
- Principal Purposes Test (PPT)

We are concerned that these proposals may have unintended adverse consequences on an industry which is slowly recovering from the financial crisis and whose wellbeing could be important to global economic recovery. In addition the implicit favouring of securitisation vehicles which are owned by residents of the vehicle’s home country would in our view be discriminatory against small countries where, by definition, the choice of investments would be smaller and the available pool of investors would be diminished.

7. **Analysis under LOB**

A securitisation company in any jurisdiction would likely fail the base erosion test contained within the LOB. Bonds issued by securitisation companies are commonly listed on a recognised stock exchange and held through a clearing system. This means that, in almost all cases, a securitisation vehicle cannot establish who its bondholders may be at any time and what their tax residence status may be.

For this reason, ‘cross-border’ securitisation vehicles will not satisfy the base erosion test included in paragraph 2(e)(ii) of the draft LOB as it simply will not be in a position to confirm who its bondholders may be. In addition, a securitisation vehicle in any jurisdiction would equally be unable to benefit from the equivalent beneficiaries provision contained in paragraph 4 of the draft LOB for the same reasons.

In any event, in most securitisations it would be anticipated that a majority of the bonds issued may be held by residents of a jurisdiction other than where the securitisation vehicle is established. In many cases, bondholders will be tax resident in OECD member states and may be institutional investors, such as pension funds. In this regard, a securitisation vehicle in any jurisdiction would likely fail the base erosion test contained within paragraph 2(e)(ii) LOB even if it could establish the identity and tax residence status of its bondholders. This may be the case even though its bondholders may be institutional investors in OECD member states.

It seems that the only option available to such securitisation vehicles under the draft LOB would be to apply for discretionary relief under paragraph 5 of the draft LOB. However, this is not a viable option, it would be time-consuming, costly and is likely to lead to inconsistent results between different jurisdictions.

The IDSA considers that a better solution, if an LOB must be included in the Model Tax Convention, would be to treat ‘cross-border’ securitisation companies that issue bonds that are held through recognised clearing systems as a separate category of qualified person on the basis that they are not generally established for treaty abuse purposes and have many broader benefits for the financial system including more efficient allocation of capital, promoting more investment and growth, risk sharing and reducing dependence on the banking/financial sector.

Indeed, the proposed LOB includes a separate category of qualified person for publically traded entities. The commentary on this category of qualified person explains that the rationale for including this category is that ownership of such entities are generally widely held and, therefore, unlikely to be established for treaty shopping. The same rationale can be applied to securitisation companies (whether listed or held through a recognised clearing system) as effectively the various investors in securitisation companies are the holders of the economic interests in these entities (in the same
manner that shareholders are in publically traded companies). While some of these interests are legally structured as debt, rather than equity, the fact that a securitisation company is securitising a pool of assets rather than operating a trading business means that such investors more closely reassemble stock holders in a company (albeit some with a preferred interest) than the types of third-party financiers one might find in the case of debt-financed ‘traditional’ trading company.

Alternatively, if securitisation vehicles cannot be treated in this way, specific provisions should be included in the LOB outlining when ‘cross-border’ securitisation companies that issue bonds that are held through recognised clearing systems will be treated as satisfying the LOB. As currently drafted, it is not possible for such ‘cross-border’ securitisation vehicles to satisfy the LOB. Any proposal to separately deal with ‘cross-border’ securitisation vehicles in the LOB (other than including them as a separate category of qualified person) would require further consultation with industry.

Finally, IDSA would like to highlight that any LOB should not undermine the rights of freedom of establishment and free movement of capital between Member States of the European Union. These principles are enshrined in European law. IDSA considers that the LOB, as currently proposed, could potentially undermine these rights and be incompatible with European law. For example, under the proposed LOB, a securitisation vehicle established in a Member State of the European Union would be entitled to tax treaty access where its bondholders are all tax resident in that same Member State. However, that same securitisation vehicle would likely not be entitled to treaty access where it: (i) was established in a different Member State; or (ii) raised capital from bondholders that were tax resident in a different Member State. This approach has the effect of allowing / denying tax treaty access on a discriminatory basis by reference to which Member State the securitisation vehicle is established in and / or has raised its capital from. The IDSA considers such an LOB approach could potentially be contrary to the freedoms guaranteed by European law.

8. **Analysis under PPT**

The IDSA considers that the PPT is a better solution to tackle treaty abuse than the LOB.

Unlike the LOB, the PPT is focussed on arrangements that have as their principal purpose obtaining treaty benefits. Clearly, where the PPT applies, the LOB test can only have any material application in the cases where there is **no treaty abuse**. If this were not the case, the PPT would be failed and treaty benefits denied. Since BEPS action 6 is designated to prevent treaty abuse, the LOB should, by simple logic, not apply where a PPT applies.

Securitisations are generally effected for **bona fide** commercial purposes and not for the purposes of tax avoidance or treaty abuse. For this reason, the IDSA considers that securitisation vehicles should qualify for treaty benefits under any PPT. However, the PPT is subjective in nature and will require detailed commentary. Tax will always feature as a consideration in international dealings and investments. Accordingly, we would recommend that a **PPT only** is applied to securitisation vehicles in order to determine treaty access. We would also suggest that clear commentary is included to support this by the OECD. The commentary should state that securitisations that are in principle accepted as non-abusive unless there are unusual facts that would suggest otherwise. We would also suggest that the examples in the commentary be expanded to explicitly deal with the assessment of securitisation vehicles so as to demonstrate that the fact that choosing a jurisdiction for the establishment of the securitisation which has a tax treaty with the investment jurisdictions should not, in and of itself, be considered a reason to fail the PPT as long as there are other good commercial reasons for the securitisation vehicle to be based in that jurisdiction (and notwithstanding the fact that there might be other jurisdictions which offer similar economic benefits).

Tax authorities can take appropriate action if they discover that a particular securitisation is abusive or has occurred for tax planning reasons. Tax authorities have (or will shortly have) sufficient information gathering tools, including under mutual exchange of information, FATCA and CRS to determine whether there is a greater risk of tax treaty abuse. Securitisation vehicles are generally
financial institutions registered for FATCA purposes and we assume will be registered for CRS purposes. Accordingly, the payment flows from the securitisation vehicle to the bondholders will be capable of being tracked through the financial system to determine who the ultimate beneficial owner of those payments are. This information is not available to the securitisation vehicle or the banks and advisors involved. As a result, any securitisation effected for bona fide commercial purposes (as described above) should only have treaty benefits denied prospectively if the tax authorities discover information not available to the securitisation vehicle or the banks and advisors involved.

9. **Beneficial Ownership/Conduit**

Finally, the IDSA considers that a securitisation vehicle that is established for bona fide commercial purposes and not for the purposes of tax avoidance or treaty abuse should always be treated as being the beneficial owner of the interest it receives from underlying borrowers for tax treaty purposes, and should not be considered a conduit financing arrangement. The IDSA would also suggest that clear commentary is included to support this by the OECD.

10. **Conclusion**

We hope that policy-makers will recognise that securitisation has played and will continue to play a vital role in economic growth. These transactions are not abusive, so should not be adversely affected by the work on Treaty abuse. An over-reaction to the possibility of abuse would cause lasting economic damage by restricting securitisations and fragmenting the market into separate domestic securitisation markets. Such a policy would conflict with good economic policy and in particular, would cause EU law issues by restricting the single market.

Finally, and as mentioned we believe the area of securitisation and treaty access has perhaps been somewhat overlooked so far in this work stream and would be pleased to make ourselves available to meet with you in advance of any public session and/or to participate at the Public Consultation Meeting.

Yours faithfully,

GARY PALMER  
Chief Executive  
Irish Debt Securities Association  
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Appendix

1. **The implications of a transaction being a “Securitisation”**

The question is whether a transaction would be treated as a “securitisation” for purposes of Capital Requirements Regulation (Regulation 575/2013 EU) (the “CRR”). CRR and what the impact of that would be. The question is important for a number of reasons, including that, if the Transaction is a “securitisation” for CRR purposes, then:

(a) if an investor in any of the Notes (or in the case of an investment fund, its investment manager) is subject to regulation under CRR, the EU Alternative Investment Fund Managers Directive (“AIFMD”), the EU Directive on Undertakings for Collective Investment in Transferable Securities (UCITS) or the Solvency II Directive (prescribing capital requirements for insurance and reinsurance undertakings), then that investor will be subject to securitisation risk retention and due diligence requirements pursuant to Articles 405 and 406 of CRR, Article 17 of AIFMD (and related regulations), and eventually, corresponding legislation and rules for UCITS funds and for insurance and reinsurance undertakings;

(b) if the Seller is a credit institution or investment firm regulated under CRR, then that Seller will be subject to the requirements on credit granting criteria and disclosure set out in Articles 408 and 409 of CRR;

(c) if the Issuer or any related third party (defined as “the originator, arranger, sponsor, servicer or any other party that interacts with a credit rating agency on behalf of a rated entity ...”) solicits a credit rating from a credit rating agency (a “CRA”), then, under Articles 8c and 8d of the EU Credit Rating Agency Regulation as amended (the “CRA Regulation”), it must request two ratings from two independent CRAs, and must consider getting one such rating from a smaller CRA;

(d) if the Transaction is established after the effectiveness of regulatory technical standards implementing Article 8b of the CRA Regulation, then the issuer, the Seller and the sponsor of the programme will be required to post detailed information regarding the Transaction on a public website to be established by the European Securities and Markets Authority; and

(e) if the Loan is itself a securitisation, it is likely that the Transaction will be a “resecuritisation” as defined in CRR; in that case the Notes would be subject to higher capital requirements under CRR and unfavourable treatment under various other regulations.

2. **Features of a “securitisation”**

(a) CRR (in Article 4(1)(61)) defines “securitisation” as follows:

“securitisation” means a transaction or scheme, whereby the credit risk associated with an exposure or pool of exposures is tranched, having both of the following characteristics:

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme.
(b) The CRR definition is based on the definition of securitisation in the Basel II capital framework, which says in part (BCBS 128 paragraph 539):

A traditional securitisation is a structure where the cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures.

(c) The Basel text (cited above) adds the following to distinguish securitisation from certain other credit-tranched structures:

The stratified/tranched structures that characterise securitisations differ from ordinary senior/subordinated debt instruments in that junior securitisation tranches can absorb losses without interrupting contractual payments to more senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to the proceeds of liquidation.

(d) Questions often arise as to whether the CRR securitisation definition (as well as the Basel II definition and its counterparts in other jurisdictions) captures various kinds of transactions that include some element of credit risk tranching, obligations dependent on performance of underlying assets, or other elements typical of securitisation, but lack other elements or features typical of mainstream securitisation transactions.

(e) In a securitisation, subordinated tranches “absorb losses without interrupting payments to more senior tranches”, and so enhance the credit quality of the senior tranches. To the extent that junior tranches have more credit risk of the underlying assets, senior tranches have less credit risk.
Mexico City, June 17th, 2015

Via e-mail
taxtreaties@oecd.org
Ms. Marlies de Ruiter
Head of the Tax Treaties,
Transfer Pricing and Financial Transactions Division
OECD/CTPA

Dear Ms. De Ruiter,

On behalf of IFA Grupo Mexicano, A.C. (Mexican Branch of the International Fiscal Association) kindly find below the comments on the Revised Discussion Draft on Action 6 (Prevent treaty abuse) of the BEPS Action Plan and its Proposals on how to deal with the issues for Follow-up Work on the Report on the Action 6 mentioned.

Comments

Part 1.- Alternative “simplified” LOB rule and presentation of the LOB rule in the OECD Model

When analyzing the simplified LOB rule we realized that in the simplified version included in the Revised Discussion Draft, the considerations related to paragraph 4 of Article X (Entitlement of Benefits), related to the derivative benefits, are missing. We consider that this omission should be corrected in the final version.

Additionally, considering that the simplified LOB rule includes only the basic items of the LOB test, but it does not include a rule to consider the Pension funds, Charities and Collective Investment vehicles as qualified persons, we believe that it is important to establish a clear threshold for considering this kind of persons as qualified persons.
Finally, regarding the presentation of the LOB rule in the OECD Model Tax Convention, we agree with the structure illustrated in the Annex, which describes the main features of the LOB in the Articles of the OECD Model and presents the alternative formulations of each paragraph in the Commentary.

Part 2.- Issues identified in the November 2014 Discussion Draft

A. ISSUES RELATED TO THE LOB PROVISION

1.- Collective investment vehicles: application of the LOB and treaty entitlement

We believe that because the success of the implementation of the TRACE project has not yet been proved and that while there was a "general support" of the conclusions of the 2010 CIV Report concerning the treaty entitlement of CIVs, the current perspective drafted in the Revised Discussion Draft leaves open an uncertainty window just by the mere fact of referring to the CIV report and to the expectations about the TRACE project of providing practical solutions to the issue. In our point of view, this uncertainty should be reduced within the final version of the Report on Action 6 by the end of September, 2015.

2.- Non-CIV funds: application of the LOB and treaty entitlement

We believe that in spite of the inclusion of the new treaty provision on transparent entities in Part 2 of the Report on Action 2 (Neutralising the effects of hybrid mismatch arrangements) that has been made and that, according with the Revised Draft Discussion, only "some of the concerns" have been considered in the possible inclusion of a derivative benefits provisions in the LOB rule, such statement would not be enough to provide the certainty needed for either the global investors and the governments involved about the provisions and cases that they should apply on their non-CIV funds; and in consequence, we highly recommend to address this uncertainty.

What is more, the Revised Discussion Draft provides that all of the work on Action 6, would not be finished on the original final due date (September 2015) but in any event afterwards (new due date: before December 2016), increasing the uncertainty around this issue.
3.- Commentary on the discretionary relief provision of the LOB rule

Our point of view and in benefit of certainty, is that it would be important to specify the concepts: “clear non-tax business reasons”, ”a substantial relationship to its State of residence” and “expeditiously” for those companies that are not treaty shopping.

We do believe that it will be a challenge for the competent authorities to set the basis needed to ensure the procedures, timing and conditions between the Contracting States, however, any uncertainty and lack of definitions would prevent the aligning between the new provisions.

4.- Alternative LOB provisions for EU countries

The introduced alternative test would be met if more than 90% of the beneficiaries are resident of either Contracting State or another state; if those individuals are entitled to the benefits of a tax treaty between that other state and the state from which the benefits are claimed and finally; with respect to interest and dividends, they would be entitled to the same or lower rate of tax under a tax treaty between the source state and such other state as it would apply if the individual were a resident of the same state as the pension fund.

In this regard, we believe that the introduction of this alternative will likely translate in extra cost and complexity, specifically for those beneficiaries or participants that would not be retired in the residence state of their pension funds, considering the number of beneficiaries and locations of their participants. In consequence, we believe that it is recommendable to provide a proper guidance about the foreign participation in a pension fund or a qualified person.

5.- Requirement that each intermediate owner be a resident of either Contracting State.

Our point of view on this matter, is that this restriction is questionable and disproportionate, and that it would result in ineligibility for a treaty benefit where no treaty
shopping exists. Even more if the concerns about abuse will already be covered by the work on Action 3 on CFC Rules.

6.- Issues related to the derivative benefits provision

A. It is important to consider that, the Proposal 1("New Treaty provisions on “special tax regimes”") is pretty close to the proposal made by the US Treasury with respect to the new definition in Article 3, paragraph 1, l) named “special tax regimes”. However, in addition to the absence of a definition of the terms: “a preferential tax rate of taxation” and “a low effective rate of taxation”, included in the proposed paragraph X), there are certain issues to observe:

i. Exclusions:

The Proposal 1 takes a broad approach regarding the key features of a special tax regime, but, differently than the scope of the proposal made by the US Treasury (which is excluding any legislation, regulation or administrative practice that satisfies a substantial activity requirement with respect to Royalties), the Revised Discussion Draft is excluding from the definition of special tax regime: any legislation, regulation or administrative practice that satisfies a substantial activity requirement with respect to financing income (the term special tax regime includes notional interest deductions that are allowed without regard to liabilities for such interest) or those designed to prevent double taxation.

ii. New provisions and their scope of application:

The Revised Discussion Draft includes new provisions that would be added to Articles 11 (Interest), 12 (Royalties) and 21 (Other income) of the OECD Model that would deny treaty benefits with respect to interest, royalty payments or other income beneficially owned by residents benefiting from a special tax regime in their country of residence at any time during the taxable period in which such income was paid.
On the other side, the proposal made by the US Treasury about these provisions only would deny treaty benefits with respect to related party payments.

B. The Proposal 2 ("New general treaty rule intended to make a tax treaty responsive to certain future changes in a country’s domestic tax laws") is also similar to the proposal made by the US Treasury with respect to the tax treaty responsive to future changes that would trigger a special tax regime. However, we observed the following issues that would generate constitutional issues in certain jurisdictions:

i. The Revised Discussion Draft has established a new general rule that is considering that, at any time after the signing of the Convention, either Contracting State provides an exemption from taxation to resident companies or individuals for substantially all foreign source income (including interest and royalties), the provisions of Article 10 (Dividends), 11 (Interest), 12 (Royalties) and 21 (Other income) may cease to have effect for payments to companies / individuals resident of either Contracting State.

In addition, the difference between the Proposal 2 made in the Revised Discussion Draft versus the one issued by the US Treasury is that, for the OECD Model the partial treaty termination would only apply if a country provides an exemption from taxation; while the US Model proposal would also apply if there is a reduction on the tax rate below 15%.

We believe that, this turn off on the treaty provisions would raise constitutional issues in certain jurisdictions, due to the uncertainty about the notification process between the Contracting States. Furthermore, the OECD proposal includes just as an option, to notify the other treaty country of the change in domestic law, lacking the certainty of the application of this new general treaty rule.

**B. ISSUES RELATED TO THE PPT RULE**

12.- Inclusion in the Commentary of the suggestion that countries consider establishing some form of administrative process ensuring that the PPT rule is only applied after approval at a senior level
We would like to have a recommendation about the time frame in connection with said administrative process.

14.- Aligning the parts of the Commentary on the PPT rule and of the Commentary on the LOB discretionary relief provision that deal with the principal purposes test

In this regard, we would like to stress out that throughout the document the reference is “principal purpose test” and not “one of the principal purposes test”, which gives the idea that the test is, as we consider it should be, that treaty benefits will be denied only when the principal purpose of entering into a transaction is to benefit from a tax treaty unless in accordance with the object and purpose of the relevant provisions of the Convention, i.e.: an artificial arrangement, but not when only one of the principal purposes of entering into a transaction is to benefit from a tax treaty unless in accordance with the object and purpose of the relevant provisions of the Convention.

We know the name of the test “one of the principal purposes test rule” would be too long, but our point is that is different to state that “the principal purpose” of a transaction was to benefit from a tax treaty than to state that “one of the principal purposes” of a transaction was to benefit from a tax treaty.

On the other hand, there is no explanation of the changes to paragraph 63.1. of the Commentary, some of which are material.

Paragraph 63 used to make reference to “clear reasons, unrelated to the obtaining of treaty benefits, for its formation, acquisition, or maintenance and that any reasons, related to the obtaining of treaty benefits were clearly secondary to those unrelated reasons”, which recognized that obtaining treaty benefits could clearly be secondary to certain unrelated reasons.

The proposed paragraph 63 merely disregards that a taxpayer may enter into a given transaction and still consider secondarily, benefitting from a tax treaty as a tax reason for entering into said transaction.

Additionally, it is worth noting that the proposed paragraphs 63.1 and 63.2 of the Commentary on the discretionary relief provision of the LOB rule forget to make reference
to if “one of the principal purposes” of carrying out a transaction in a given way is the obtaining of tax treaty benefits then those treaty benefits should be denied, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.

On the other hand, we find too arbitrary to state in the proposed paragraph 63.1. that “It is not necessary to find conclusive proof of intent but the competent authority must be able to conclude, after an objective analysis of the relevant facts and circumstances, that none of the principal purposes for the establishment, acquisition or maintenance of the person and the conduct of its operations was to obtain benefits under the Convention” because it cannot be judged lightly and so arbitrarily; the consequences of denying tax treaty benefits when they should not be denied could be fatal.

We also believe that the burden of proof that one of the principal purposes of carrying out a certain transaction was to obtain tax treaty benefits unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention should lie with the competent authority, since there is no clear guidance as to what is considered to be “in accordance with the object and purpose of the relevant provisions of the Convention”.

15.- Whether some form of discretionary relief should be provided under the PPT rule

We would like to have a time frame of when will the competent authority determine that the benefits would have been granted to a person upon request to contribute to certainty.

We did not see that the proposed paragraphs 16-19 take on account the re-characterization of income or a transaction that a competent authority may make under domestic laws, for which the discretionary relief should also be provided. Plus, the discussion draft under revision mentions that it is adding paragraphs 16 to 24 but paragraphs 20-24 are missing in the revised discussion draft.
16.- Drafting of the alternative “conduit-PPT rule”

Our comments are on Example D, which although recognizes expressly that “seeking the benefits of the treaty between State R and S is clearly a factor in SCO’s decision” and that “it may even be a decisive factor, in the sense that, all else being equal, the availability of treaty benefits may swing the balance in favour of borrowing from RCO rather than from another lender”, concludes that “whether the obtaining of treaty benefits was one of the principal purposes of the transactions would have to be determined by reference to the particular facts and circumstances”.

We find that conclusion incongruent because it makes no reference to the requirement that the obtaining of treaty benefits be in accordance with the object and purpose of the relevant provisions of the Convention.

Regarding Example E, we believe it should conclude that there is no conduit arrangement, not because RCO has subsidiaries located around the world and because said subsidiaries carry out similar activities in countries which have treaties which offer similar or more favorable benefits, but because RCO is the holding company which natural role is to consolidate licenses from its subsidiaries and sublicense them to said subsidiaries.

Finally, as for Example F, our opinion is that the example should not reach said conclusion considering a given number of employees (50), but a sufficient and qualified number of employees to undertake a given activity, which in some cases might suffice to be 1, and this would still be a real business performing substantive economic functions, depending on the nature of the business.

17.- List of examples in the Commentary on the PPT rule

Example G admits that the decision to establish RCO as a regional company in State R, was made considering, among other factors, “the comprehensive double taxation treaty network of State R, including its tax treaties with the five States in which TCO owns subsidiaries, which all provide low withholding tax rates”.

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Notwithstanding this, the example concludes that “it would not be reasonable to deny the benefits of the treaties concluded between State R and the five States”. Although we agree with the conclusion, we believe it is confusing, since it does not make reference of the obtaining of the tax treaty benefits being in accordance with the object and purpose of the relevant provisions of the Convention.

C. Other issues

18.- Application of the new treaty tie-breaker rule

In this regard, we would like to have a specification of what “expeditiously” and “as soon as possible” mean in the proposed paragraph 24.2 in order to have certainty.

19.- The design and drafting of the rule applicable to permanent establishments located in third States

On this topic we have two comments:

a) Paragraph 105 of the discussion draft proposes deleting the specific exemption for royalties provided in subparagraph f) arguing that many situations that would have otherwise been covered by subparagraph f) would be dealt with by subparagraph e), however our concern is that not all of the circumstances of subparagraph f) will be dealt with but only “many” of them, which we believe is not enough.

b) About the proposed changes to the provision included in the paragraph 42 of the Report on Action 6, we think the effective rate of tax on the profits of the permanent establishment in the third jurisdiction should be compared to the effective tax rate of the Residence State, and not to “the general rate of company tax” as proposed.
The participation of IFA Grupo Mexicano, A.C. is made on its own behalf exclusively as an IFA Branch, and in no case in the name or on behalf of Central IFA or IFA as a whole.

We hope you find these comments interesting and useful. We remain yours for any questions or comments you may have.

Sincerely,

IFA Grupo Mexicano, A.C.
Subject: INREV’s response to OECD’s “Revised Discussion Draft BEPS Action 6: Prevent Treaty Abuse”

Dear Ms De Ruiter,


We hope again to provide a meaningful contribution to your work to support the development of a sound regulatory framework and remain available should you have any specific questions about the non-listed real estate fund industry.

Kind regards,

Matthias Thomas
Chief Executive INREV

Attachment:

Submitted via email: taxtreaties@oecd.org
About INREV: the voice of the European non-listed real estate investment industry

INREV is the European Association for Investors in Non-Listed Real Estate Vehicles. We provide guidance, research and information related to the development and harmonisation of professional standards, reporting guidelines and corporate governance within the non-listed property funds industry across Europe.

INREV currently has 368 members. Our member base includes institutional investors from around the globe including pension funds, insurance companies and sovereign wealth funds, as well as investment banks, fund managers, fund of funds managers and advisors representing all facets of investing into non-listed real estate vehicles in Europe.

Our fund manager members manage more than 500 European non-listed real estate investment funds, as well as joint ventures, club deals and separate accounts for institutional investors. INREV’s members represent almost all jurisdictions of the European Union’s internal market and a range of underlying long-term investment vehicle structures, both CIVs and other non-listed real estate investment vehicles, the vast majority of which are Alternative Investment Funds (“AIFs”) subject to regulation under the European Alternative Investment Fund Directive (“AIFMD”).

Comments regarding the Discussion Draft on Treaty Abuse

INREV welcomes the opportunity to comment on the recent OECD Revised Discussion Draft: BEPS Action 6: prevent treaty abuse (the “Revised Discussion Draft”). We are very pleased that the OECD seeks the view of the stakeholders in the investment management industry in order to find appropriate solutions for CIVs and non-CIVs in connection with the work on BEPS Action 6 – Treaty Abuse.

As we have previously stated, INREV shares the concerns of the G20 and the OECD that action is needed to effectively prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from the activities that generate it. INREV also supports a coordinated and comprehensive international approach to tackle these important issues.

INREV and other real estate associations have made submissions in response to the various BEPS Action 6 consultation drafts, noting that proposed measures could inadvertently have a significant negative impact on the future development of institutional real estate investment and institutional investment in related sectors such as infrastructure that generally use the same or very similar investment fund structures. The potential loss to the European economy of the benefits of investment in real estate and infrastructure funds, in terms of economic stimulation, job creation and growth, would be incalculable.

As we have argued in our previous submissions, the policy defined by the OECD in the 2010 CIV report should be upheld: the goal should be to put the investors in non-listed real estate vehicles in the same tax position that they would be if they invested directly in the underlying assets. In other words, there should be tax neutrality between direct investments and investments via a non-listed real estate fund or other investment vehicle, whether it is a CIV or a non-CIV.

In addition, we would again highlight that the various developments in the field of international transparency, including FATCA, CRS, EU Savings Directive, as well as the EU AIFM Directive, significantly mitigate the risk of non-listed real estate funds and other investment vehicles being used
for inappropriate reasons including tax avoidance; most of these vehicles are entities with regulatory reporting obligations under the recently enacted transparency and regulatory supervision regimes.

**Issues related to CIVs and the LOB rules**

INREV welcomes the inclusion of clause 2(f) regarding CIVs into the LOB clause in the annex of the discussion draft. However, we note that this same clause is not included in the new simplified LOB clause and we would suggest that clause 2(f) should be included within the simplified LOB as well.

Reducing the equivalent beneficiary threshold to 75% within the simplified LOB would also be helpful for intermediaries in investment fund structures. In addition, we would urge the OECD to provide clarity on what these rules will mean at a practical level before they are implemented. In particular, it would be useful to provide examples regarding what evidence of ownership should be sufficient to assure tax authorities that investors in a fund structure are in fact equivalent beneficiaries.

**Suggestions related to non-CIVs**

We note the statement in section 22 that most comments to the previous Public Discussion Draft did not sufficiently take into account the OECD’s treaty-shopping concerns and would like to make a suggestion regarding how to address the treaty shopping concerns for non-CIVs. We also note the CFA’s line of thinking and possible options for the upcoming June meeting mentioned in section 24 and support those efforts.

We would suggest that the OECD’s treaty shopping concerns for non-CIVs could be addressed by granting treaty benefits if one of the following conditions is fulfilled:

1. In its jurisdiction of residence, the non-CIV maintains an ‘active investment management business enterprise’ involved in the management of the non-CIV, similar to the ‘active business enterprise’ illustrations in Example H on page 35 of the Public Discussion Draft. As in these examples related to active business enterprises, with an increased substance level (constituting an ‘active investment management business enterprise’) it would generally not be reasonable to deny treaty benefits to non-CIVs (see further explanation below); or

2. The non-CIV maintains an adequate percentage of equivalent beneficiaries, directly or indirectly.

In order to reflect the diversity of non-CIV legal structures, this rule should apply to:

- non-CIVs that are internally or externally managed in the jurisdiction of residence; and
- directly or indirectly wholly owned entities, resident in the non-CIV jurisdiction (‘SPVs’).

Regarding the first condition, we acknowledge that Example H is written for a regional company held by a publicly-listed company, not for a non-CIV held by various investors. Nevertheless, they share several important characteristics:

- Both the regional company and the non-CIV are set up in an intermediate country for valid business reasons: in the case of a regional company, in a jurisdiction that neighbours group subsidiaries, therefore allowing the efficient provision of group services; and in the case of a
non-CIV, in a jurisdiction that has a robust regulatory environment and fund infrastructure, therefore allowing professional operation and distribution of non-CIVs while ensuring investor protection.

- As intermediate entities, both find themselves facing a similar tax treaty challenge: whether source income country governments will be willing to grant treaty benefits to them as an intermediate entity.

In practice, the legal structures of non-CIVs takes a wide variety of forms. Non-CIVs can be either internally or externally managed. Moreover, some non-CIVs tend to centralise their functions in a separate central fund management entity. In addition, investment structures of non-CIVs are typically comprised of one or more layers of wholly owned SPVs, both for legal, business operations or tax neutrality reasons. Against this background, any treaty benefit rule should embrace all these various legal structures. In order to do so without affecting the treaty shopping concern, the rule on granting treaty benefits to non-CIVs should refer to the jurisdiction instead of the legal entity. By referring to an active investment management business enterprise domiciled in the same jurisdiction as the SPV or non-CIV, the treaty benefit rule proposed above includes the various non-CIV legal structures within its scope while respecting the treaty shopping concern.

Acknowledging that a publicly-listed company and funds are different economic activities, our suggestion would require additional thought on a set of functions and circumstances which makes an ‘active investment management business enterprise’ comparable to the ‘active business enterprise’ in examples G and H.

We believe that the substance suggestion above would reflect current developments as investment managers more and more consolidate and centralise functions in regional operations, driven by various regulatory, commercial, tax, operational and capital requirements.

Further work and the costs of regulatory uncertainty

We would be pleased to discuss any of the issues and implications with the OECD and to assist in further work, as referred to above. We agree with the conclusions of the Working Party that it should continue to explore solutions to issues related to the treaty entitlement on non-CIV and hope that our suggestions offer a constructive contribution.

We join with other industry associations in urging the creation of a specific OECD Working Group dedicated to examining solutions to non-CIVs that will continue work beyond the current deadline of September 2015 for Action 6 under the BEPS project. Nevertheless, we would point out that the current regulatory uncertainty surrounding future eligibility of non-CIVs to the benefits of double tax treaties is already casting a long shadow.

Given the critically important contribution of institutional real estate investment in the real economy and its impact on economic growth and job creation, this uncertainty should be resolved as soon and clearly as possible. This should be achieved in a way that allows investors in unlisted real estate funds, which are primarily pension funds and insurance companies, to obtain tax certainty that is both non-discriminatory and avoids double and, in some cases even, triple taxation.

1 The same applies for a typical regional holding company; this may be addressed in further working out Example H.
Dear Ms de Ruiter

RE: OECD REVISED DISCUSSION DRAFT ON BEPS ACTION 6

The Investment Association\(^1\) welcomes the opportunity to comment on the BEPS Action 6 revised discussion draft. Once again, we are grateful to the OECD for recognising the particular concerns of the funds industry. Our comments follow below.

PART 1 – Simplified LOB rule and presentation of the LOB rule

We note that the description of the general elements of a simplified LOB rule on pages 4 and 5 are different from the LOB rule presented in Annex. The Annex includes sub-paragraph 2 f) (on collective investment vehicles) but this is not in the description of the simplified LOB rule in Part 1.

We believe that a clause 2 f) will be a critical feature of double tax treaties that incorporate an LOB clause (see comments to Part 2 below), and it is therefore vital that the model convention and accompanying commentary makes it clear that governments should provide clarity on how CIVs are treated under treaties, and in particular by incorporating a clause 2 f).

PART 2 – A.1. – Collective Investment Vehicles

We agree with the view that clause 2 f) provides a partial remedy to the concerns expressed by the funds industry about the application of LOBs to CIVs, and which are recognised in the Commentary to Article 1 of the Model Tax Convention.

\(^1\) The Investment Association (formerly the Investment Management Association) represents the asset management industry operating in the UK. Our Members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of around $5.4 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles.
The Commentary to Article 1 of the Model Tax Convention, based on the 2010 CIV report, describes the factors that negotiating countries should consider in granting treaty benefits to CIVs. As we have stated previously, we continue to believe that it is appropriate that a range of options should be available to governments, as described in the Commentary.

Nevertheless we have two remaining concerns about the presentation of clause 2 f) in the final BEPS 6 recommendation.

1. **The increased emphasis on LOB clauses as a means to counter treaty shopping will lead countries to want to deploy LOB tests for CIVs, either within the clause 2 f) or otherwise.**

2. **The presentation of clause 2 f) as an optional or exceptional feature impairs the negotiating position of countries for which CIVs are important.**

Currently many countries have predominantly domestic CIV regimes – ie funds are sold primarily to domestic investors. If bilateral negotiations can agree that this is a sufficient test to demonstrate eligibility, then meeting an LOB clause would not be problem and these countries could prefer not to incorporate a clause 2 f) as part of their treaty negotiations.

The ability to sell funds across borders allows investors access to a much broader range of financial products, and this is particularly important in countries that do not have developed financial markets. Equally it provides opportunities for cost saving that can be shared with investors who can benefit from cheaper access to financial products.

We believe that in the near future, cross border sales of funds will be the norm and not the exception and this is already evident in the EU where the UCITS Directive enables a single market for CIVs that are frequently sold across the EU. Similar schemes are being replicated by governments throughout the world in order to increase the availability of financial products to citizens, and facilitate cross border investment.

The application of LOB clauses to CIVs will inevitably result in increased administrative complexity, which in some cases will be insurmountable and result in incorrect denial of treaty benefits for investors in CIVs.

**Recommendations in relation to CIVs**

We believe that the increased prominence of LOB tests will result in increased scrutiny of how LOB clauses can apply to CIVs. Therefore we recommend that additional language should be incorporated in 6.30 of the Commentary on Article 1 of the MTC to further clarify the application of LOB where CIVs are distributed through intermediaries. The proposed language is as follows:

> For example, where units or shares of a CIV are distributed to investors in a treaty eligible third country through an intermediary based in that country, it would be appropriate to conclude that the owners of the shares or units sold through the intermediary are resident in that country.

We believe that this addition will provide significant clarification for many CIVs on how to apply the conditions of an LOB in a workable and proportionate manner.

We also recommend that the Commentary at 6.29-6.31 should be more explicitly replicated in the Commentary on the application of the LOB test.
We welcome the proposal to incorporate a clause 2 f) but we urge the OECD to emphasise the importance of this clause and to include it prominently as a recommended feature of LOB clauses, and that countries should be encouraged to provide clarification about which of their CIV products should be treated as qualified persons under a clause 2 f), regardless of whether or not CIVs in those countries are routinely sold across borders.

PART 2 – A.2. – Non-CIV funds

We concur with the view expressed in paragraph 23 of the revised discussion draft that the inclusions of a derivative benefits clause in the LOB rule could address some of the concerns regarding treaty entitlement of non-CIV funds. Non-CIV funds are not sold to the public, and although some might be widely held, it is less common for such funds to encounter significant problems in accessing information about who the ultimate beneficial investors are. Therefore we see no need to distinguish between non-CIV funds and other persons in determining treaty benefits, subject to the comments below on equivalent beneficiaries, and the PPT.

In common with CIVs, non-CIV funds are often sold to investors in multiple jurisdictions, who may be equivalent beneficiaries of treaties. An equivalent beneficiaries clause is therefore vital to ensure that investors are not deprived of treaty benefits simply by investing through collectivised funds (that are non-CIVs). Moreover, the design of the LOB rule should be effective in giving benefits to equivalent beneficiaries when applied to non-CIV structures as a whole, which may include more than one tier for various commercial reasons, such as to ring-fence liabilities or to manage guarantor agreements under finance facilities.

As we have described previously, non-CIV funds provide vital source of capital to companies, particularly to small and medium businesses, infrastructure projects, property development and other essential economic activities. The denial of treaty benefits to non-CIVs could have a significant impact on the availability of cross border capital investment.

As we have previously stated, we agree that the addition of examples of non-CIVs in the commentary on the PPT rule will be helpful. These can serve to illustrate cases where non-CIV funds are established only for the purpose of collectivising investment in important economic activities. We recommend that examples should also clearly illustrate cases where non-CIVs are established for the purpose of obtaining treaty benefits for investors that are otherwise not treaty entitled (and that should therefore fail a PPT condition).

We believe that a combination of a suitable LOB condition (with equivalent beneficiaries) and a PPT rule with suitable comprehensive illustrative examples, could provide the necessary clarity to investors in non-CIVs, and assurances to governments about the concerns expressed in relation to non-CIVs.

To address any residual concerns about the deferral of income, additional commentary could be provided on offshore fund reporting regimes. Many countries (including the UK and Germany) have enacted rules to prevent resident investors in offshore funds from benefitting from income deferral. Countries that have concerns about income deferral by investors in non-CIV funds could have regard to the existence of such rules in equivalent beneficiary jurisdictions in negotiating treaty entitlement of non-CIVs.
Finally, I would like to thank for the opportunity to comment on the discussion draft and we appreciate the considerable efforts that have been made to consider factors that are uniquely relevant to the funds industry. We hope to be able to continue to contribute to the consultation and I am available at your convenience to discuss anything in this letter at jorge.morley-smith@theinvestmentassociation.org or on +44 (0)20 7831 0898.

Yours sincerely

[Signature]

Jorge Morley-Smith
Director, Head of Tax

cc. Andrew Dawson – HM Revenue & Customs
    Tom Matthews – HM Revenue & Customs
    Mike Williams – HM Treasury
Dear Ms de Ruiter

BEPS Action 6: Prevent treaty abuse

The Investment Property Forum (IPF) welcomes the opportunity to comment on the OECD’s revised discussion draft.

About the IPF

The IPF is the leading UK property investment organisation for individual members, comprising a network of over 2,000 senior professionals drawn from across the property investment and finance market. The IPF is not a lobby organisation. Rather, its mission is to enhance the understanding and efficiency of property investment in all its forms (i.e. public, private, equity, debt and synthetic exposure), by both its members and other interested parties, including Government. We do this through undertaking research, running seminars/workshops and providing a forum for discussion and debate around the current topics affecting the market.

General comments

The IPF’s focus is primarily on large-scale commercial and ‘alternative’ property assets. Investment in these assets is essential for any economy. However, since these assets are large and relatively illiquid, many investors gain exposure to them through collective investment vehicles and joint ventures.

As we are concerned to ensure efficiency within the property investment market, we support the principle of putting the investors in property vehicles (whether a CIV or a non-CIV) in the same tax position that they would be if they invested directly in the underlying property assets.
Specific comments

CIVs and LOB clauses

We welcome the inclusion of clause 2(f) regarding CIVs into the limitation on benefits (LOB) clause in the annex to the discussion draft. It would help clarify how CIVs are to be treated if clause 2(f) was to be included within the simplified LOB clause as well.

The reduction in the equivalent beneficiary threshold to 75% in the simplified LOB is welcome. It would also be helpful, if the OECD could provide guidance as to how the equivalent beneficiary rules should be implemented in practice, particularly regarding the appropriate evidence of ownership to assure tax authorities that investors in a fund structure are in fact equivalent beneficiaries.

Non-CIVs

As the legal structures of non-CIVs take a wide variety of forms, we suggest that perhaps the OECD should consider making a ‘widely held’ condition a key determinant as to whether a fund should be entitled to treaty access.

REITs and transparent entities

We welcome the confirmation that treat access for fiscally transparent entities will usually take place at the ‘investor’ level.

Discretionary relief

We think that there should be consistency of approach between the discretionary relief provisions under the LOB rule and the principal purpose test (PPT) rule. The latter is probably more workable.

Cross border investment

Investors need to be able to access appropriate assets/vehicles across borders in as straightforward and efficient manner as possible. There is therefore a balance to be found between this requirement and ensuring that tax treaties are not easily abused.

Yours sincerely

Sue Forster
Chief Executive, Investment Property Forum
Direct Tel. No. +44 (0)20 7194 7922
Email: sforster@ipf.org.uk
RE: Revised discussion draft BEPS Action 6: Prevent Treaty Abuse

The Irish Funds Industry Association (“Irish Funds”) is the industry association for the international investment fund community in Ireland. Irish Funds represents custodians, administrators, managers, transfer agents and professional advisory firms. Ireland is a leading centre for the domicile and administration of collective investment vehicles, with industry companies providing services collective investment vehicles with assets totalling in excess of €3.8 trillion.

Irish Funds acknowledges the work done by the OECD to date. The revised discussion draft issued under Action 6 of the OECD’s Base Erosion and Profit Shifting (“BEPS”) project contains some welcome conclusions. In particular, we welcome the conclusions reached in respect of the application of the limitation on benefits (“LOB”) provision to collective investment vehicles (“CIVs”) and the recognition that the implementation of the Treaty Relief and Compliance Enhancement (“TRACE”) project is important. However, it also contains wholly new proposals and issues which require further consideration including the critical issue of the treaty entitlement of non-CIV funds. Irish Funds has the following comments on the revised discussion draft:

1 Alternative simplified LOB rule

CIVs should be included as a category of qualified person in paragraph 2 of the simplified LOB. We note that the category of collective investment vehicle is included in 2(f) of the presentation of the LOB in the OECD Model Tax Convention in the Annex to the revised discussion draft. However, an equivalent 2(f) is not included in paragraph 3 detailing the alternative “simplified” LOB. Please ensure the final version of the simplified
LOB includes the equivalent 2(f). Failure to do so will undermine the conclusions of the 2010 CIV Report and the progress made to date under Action 6 with regard to the entitlement of CIVs to claim treaty relief.

2 TRACE Implementation

Implementation of TRACE is critical. The option of granting of treaty relief for both CIVs and non-CIV funds on the basis of ‘equivalent beneficiaries’ either through the alternative simplified LOB or any final agreed derivative benefits provision would, in practice, be dependent on the TRACE project becoming operational. Therefore, we strongly believe that the implementation of TRACE project is not just ‘important’ (as mentioned in paragraph 14 of the discussion draft) but is unavoidably a necessary precursor to the application of the LOB rule to both CIV and non-CIV funds. The final report on Action 6 should reflect this key practical point.

In the absence of the broad implementation of TRACE, governments should be encouraged to adopt reasonable approaches under the 2010 CIV report and facilitate administratively feasible solutions in identifying ‘equivalent beneficiaries’ on a best efforts basis. The implementation of the recommendations of the 2010 CIV report without TRACE implementation should not create additional barriers to treaty entitlements.

3 Non-CIV funds

Non-CIV funds should be eligible for treaty benefits. The economic importance of non-CIV funds should be acknowledged in the Commentary on the Model Tax Convention. As acknowledged in the draft, countries should continue to extend treaty benefits to non-CIV funds in appropriate cases. It is important to appreciate that non-CIV funds are formed for important commercial reasons. We note the comments in the revised discussion draft that most of the suggestions included in the comments received on the November 2014 discussion draft did not sufficiently take into account treaty shopping concerns. We also note that work should continue on exploring solutions related to the treaty entitlement of non-CIV funds that would address the concerns that Governments have and such work might continue after September 2015 but be completed by December 2016.

In this regard, we urge Governments to give the OECD the mandate to establish a working group including the relevant industry stakeholders to explore solutions for inclusion in Action 6 dealing with the broad question of the treaty entitlement of non-CIV funds.

Deferral of income recognition is not a valid basis for denying treaty relief. Governments concerned about the use of non-CIV funds to defer income recognition should amend their domestic provisions to limit the ability of taxpayers to defer income
recognition. Many jurisdictions already have domestic rules to address income deferral through fund investments. Furthermore, significant work is being undertaken under BEPS Action 3 with a view to strengthening CFC rules and accordingly addressing regimes that permit income deferral. Seeking to address concerns about income deferral under the terms of the treaty itself (and Action 6) is wholly inappropriate and will cause new and inappropriate instances of double taxation.

**Derivative Benefits.** Non-CIV funds should be permitted to claim treaty relief where the ultimate investors are equivalent beneficiaries (as will usually be the case). In this regard, it is key that the ‘seven or fewer’ condition in the original proposed LOB be disapplied. There is no policy rationale for imposing this condition on non-CIV funds; it should not matter whether seven or, for example, 77 equivalent beneficiaries hold the defined ‘vote and value’ threshold. The OECD must recognise that governments adopting an over-zealous approach to addressing treaty shopping (either by restricting the definition of CIV or by limiting the type of non-CIV funds that can qualify for relief) will result in treaty benefits being denied in legitimate cases and cause economic damage to the OECD member states and their businesses.

**Tax Transparent Entities.** We note the observation in the revised discussion draft (paragraph 23) that the new treaty provision on transparent entities will be beneficial for non-CIV funds. CIVs, and non-CIV funds in the form of transparent entities (treated as fiscally transparent in the investors’ country of residence and in the country of domicile of the fund), are becoming more commonplace, particularly for institutional investors (e.g. pension funds). While the income of transparent entities may be treated as income for taxation purposes in country of residence of the investor (irrespective of where the fiscally transparent entity is domiciled) many challenges arise in the source jurisdictions on the effective application of treaty entitlements either through the recognition of the entity as fiscally transparent and/or administrative mechanisms processing the treaty entitlements for the underlying investors. We recommend that governments be strongly encouraged to recognise and facilitate the treaty entitlements for such investors in fiscally transparent entities.

It should be noted that the majority of non-CIV funds do not consist of transparent entities and, as a result, while important, it will not provide a broad solution to the issue of treaty entitlement of non-CIV funds.

4 **Special tax regimes provision**

It is very late in the process to introduce two entirely new proposals (the special tax regime and the ‘future changes’ provision) designed to deny treaty relief. The
inclusion of entirely new concepts at this late stage, with very limited guidance and
combined with a request to keep comments short is unreasonable. Stakeholders must be
afforded an adequate opportunity to reflect on the new proposals, along with draft
commentary outlining how it is anticipated the provisions should be applied. Therefore, this
aspect of Action 6 must be extended for review and comment until 2016.

The special tax regimes provision is unclear and lacking in objectivity. We would ask
what the ‘effective’ rate of taxation is for this purpose. Is it a comparison of the cash tax
paid in a particular year against the accounting profits recognised in that year, or another
method? What benchmark should be applied to determine when a taxpayer’s effective rate
of taxation is “preferential”? Should it be compared against effective rates of taxation in the
source state or in the state of residence? Or will the OECD seek to identify an
“appropriate” base case, if that is even possible? Is the regime contemplated by paragraph
(i) focused on specific exemptions for, say, foreign source interest receipts? Are taxpayers
that claim tax depreciation to be treated as benefiting from a special tax regime unless they
fall within one of the exclusions in paragraphs (i) to (viii)? (That would be a very
disproportionate result and would cause great concern.) What types of regime are
contemplated under paragraph (viii)? If a regime does not result in a low effective rate of
taxation, why would countries need to agree separately to exclude it under paragraph (viii)?

It is unclear how the provisions apply. Although included under the section dealing with
derivative benefits, it seems that the ‘special tax regimes’ provision and the ‘future changes’
provision could be applied to deny relief to taxpayers that qualify for treaty benefit under
other parts of the LOB. Clear commentary is required on how the draft provisions might
interact with other parts of the LOB.

Reference in paragraph (vii) to the type of assets an investment entity holds should be removed. Once an investment entity is widely held and subject to investor protection
regulation it should not be precluded from claiming treaty benefits by this special tax
regime. The type of assets in which it invests should not impact on its entitlement to treaty
access. As financial markets mature, investment funds are now investing in wider
categories of assets (e.g. traded commodities).

5 Examples in the commentary on the PPT

Additional examples involving CIVs should be included. As it stands only one of the
nine examples includes a CIV and it features a domestically distributed CIV. This is too
narrow an example. It should be amended so that it reflects a broader range of CIVs. We
have prepared additional examples (Schedule 1) to be considered for inclusion. In relation
to non-CIV funds, we note that further discussions will be undertaken this month and
beyond with a view to adding one or more examples on non-CIV funds to the Commentary on the PPT. Due to the broad spectrum of non-CIV funds, we would recommend the inclusion of a number of examples representative of the broad base of non-CIV funds.

**Taking a wide treaty network should not trigger the PPT.** We strongly urge that a clear statement is included in the Commentary that investment decisions which take into account the existence of tax benefits provided by a particular country’s tax convention network should not trigger the application of the PPT.

6 **Anti-conduit provision**

**CIVs should not be considered as conduit arrangements for the purposes of the treaty.** In the absence of a clear statement in the commentary confirming the position that a CIV distributing its income to its investors should not be considered a ‘conduit arrangement’, there remains a risk that a CIV that has satisfied the LOB would lose treaty benefit under an anti-conduit rule. This would undermine the position agreed and accepted on Action 6 in recognising the position of CIVs.

Yours sincerely,

Pat Lardner

Chief Executive
1 **Widely-held CIV**

RCo, a collective investment vehicle resident in State R, manages a diversified portfolio of assets. The interests in RCo are widely-held. RCo is subject to investor protection regulation in State R and is not taxed in State R on income or gains. The investors are resident all over the world and interests are frequently held through nominees (including investment banks and other brokers). RCo has limited visibility about who are its investors but is aware that the interests are marketed in OECD and G20 countries. RCo currently holds 15% of its portfolio in shares of companies resident in State S, in respect of which it receives annual dividends. Under the tax convention between State R and State S, the withholding tax rate on dividends is reduced from 30% to 10%.

RCo’s investment decisions take into account the existence of tax benefits provided under State R’s extensive tax convention network. Investors’ decisions to invest in RCo are not driven by any particular investment made by RCo and RCo’s investment strategy is not driven by the tax position of the investors.

In making its decision to invest in shares of companies resident in State S, RCo considered the existence of a benefit under the State R / State S tax convention with respect to dividends, but this alone would not be sufficient to trigger the application of paragraph 7. The intent of tax treaties is to provide benefits to encourage cross-border investment and, therefore, to determine whether or not paragraph 7 applies to an investment, it is necessary to consider the context in which the investment was made. In this example, unless RCo’s investment is part of an arrangement or relates to another transaction undertaken for a principal purpose of obtaining the benefit of the Convention, it would not be reasonable to deny the benefit of the State R / State S tax convention to RCo.

2 **Cross-border CIV**

RCo, a collective investment vehicle resident in State R, manages a diversified portfolio of assets. The interests in RCo are held by a relatively small number of investors all of whom are resident in State R or other jurisdictions that have agreed a tax convention with State S that provides for withholding tax on dividends to be reduced to at least 10%. RCo is subject to investor protection regulation in State R and is not taxed in State R on income or gains. RCo currently holds 15% of its portfolio in shares of companies resident in State S, in respect of which it receives annual dividends. Under the tax convention between State R and State S, the withholding tax rate on dividends is reduced from 30% to 10%.
RCo’s investment decisions take into account the existence of tax benefits provided under State R’s extensive tax convention network. Investors’ decisions to invest in RCo are not driven by any particular investment made by RCo and RCo’s investment strategy is not driven by the tax position of the investors.

In making its decision to invest in shares of companies resident in State S, RCo considered the existence of a benefit under the State R / State S tax convention with respect to dividends, but this alone would not be sufficient to trigger the application of paragraph 7. The intent of tax treaties is to provide benefits to encourage cross-border investment and, therefore, to determine whether or not paragraph 7 applies to an investment, it is necessary to consider the context in which the investment was made. In this example, unless RCo’s investment is part of an arrangement or relates to another transaction undertaken for a principal purpose of obtaining the benefit of the Convention, it would not be reasonable to deny the benefit of the State R / State S tax convention to RCo.
Irish Tax Institute

Response to OECD Discussion Draft:
BEPS Action 6
Preventing Treaty Abuse

June 2015
About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland’s AITI Chartered Tax Advisers (CTA) and is the only professional body exclusively dedicated to tax. Our members provide tax expertise to thousands of businesses and individuals in Ireland and internationally. In addition many hold senior roles within professional service firms, global companies, Government, Revenue and state bodies.

The Institute is the leading provider of tax qualifications in Ireland, educating the finest minds in tax and business for over thirty years. Our AITI Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice.

A respected body on tax policy and administration, the Institute engages at the most senior levels across Government, business and state organisations. Representing the views and expertise of its members, it plays an important role in the fiscal and tax administrative discussions and decisions in Ireland and in the EU.
The Irish Tax Institute welcomes the opportunity to comment on the revised Action 6 Discussion Draft published on 22 May 2015. As requested in the Discussion Draft, we have kept our comments as short as possible.

1. **Principal Purposes Test (PPT)**

The revised proposals require that a treaty include a PPT unless the more detailed version of the Limitation on Benefits (LOB) clause is included. Given the concerns previously expressed by many respondents about the detailed LOB, it is likely that many countries will opt to include a PPT in their tax treaties.

As highlighted in our January 2015 submission, we are concerned that businesses operating in a large country will find it much easier to conclude that they pass a PPT than businesses operating in a smaller country.

A company carrying out arrangements and transactions in a larger economy will find it easier to demonstrate the natural business advantages that arise from that economy, than a company in a smaller economy.

In this context, it is more likely that the positive benefits of access to the tax treaty to avoid double taxation in relation to the cross border transaction or business arrangements will be more evident in the case of the taxpayer based in the smaller economy. Smaller country businesses face considerable uncertainty as to whether they can ever pass the PPT test and actually may find it impossible to conclude with certainty that they do so.

The commentary on the interpretation of the PPT should acknowledge that it is legitimate to recognise that an important aspect in deciding to establish and continue to conduct business in a jurisdiction is the existence of a tax treaty and the benefits it affords. The commentary should make explicit that this can be especially the case for smaller economies where some of the wider business related benefits on offer in the case of larger economies are not present. Any evaluation of the purpose of an arrangement or transaction should take into account the relatively larger weight of importance that the existence of a treaty benefit is likely to present in this scenario.

Our concerns outlined above could be minimised by the addition of further examples in the commentary of the PPT.

We welcome the addition of further examples on the PPT into the commentary in the revised discussion draft although we note that the examples focus on situations where an entity is ultimately owned by a public company. Cross border trade is not conducted solely by entities which are members of publicly listed groups. This is likely to be the case for businesses based in smaller economies which may have less ready access to capital markets. Express acknowledgement in the commentary that the nature of the business transactions and activities which are cited in the examples could equally be carried on by groups which are privately held would be welcome.

The additional examples F,G,H and I for insertion in paragraph 14 of the proposed commentary on the PPT rule are helpful in providing more specific examples of the factors that would be relevant in evaluating whether the PPT test would be satisfied or not.

However, we would recommend that it be made clear in paragraph 14 of the proposed commentary that it is not necessary that a particular transaction or commercial arrangement precisely fit within one of the examples in order for it to be considered to pass the PPT test. Instead it should be clarified that the examples provide illustrations of the determining factors which should be considered as relevant in evaluating whether the test is satisfied or not. As noted above, for example, the precise ownership of the company (i.e. publicly listed group) cannot be taken as determinative. In this regard, perhaps it could be illustrated that, for example, if a privately held company or non-listed group (which may or
may not have diverse ownership) were to carry on activities outlined in examples G and H, these could be taken as examples of the type of activities capable of meeting the PPT.

It should be made clear that in reviewing the examples, the PPT test would equally be satisfied where a significant number of the determining factors listed in the examples did exist even if some of the background factors listed (e.g. in example G there is a reference to the country being a member of a regional grouping) did not exist in a particular fact pattern.

We would also welcome clarification (which perhaps may emerge when the final documents are prepared) that the PPT test remains a standalone test which contracting states can adopt without a LOB test (whether the detailed LOB or ‘simplified’ version).

2. Simplified LOB

We welcome the inclusion of a simplified LOB option which addresses many of the concerns previously highlighted with the LOB.

2.1 Active Business test

We note that within the active business test of the simplified LOB, the substantiality test for dealings with connected parties is included. As highlighted in our previous submissions, this requirement again impacts small countries disproportionately. Many small country operations that a reasonable person might think easily meets an Active Business test have, in practice, found it difficult to meet the Active Business test in US tax treaties. This simply illustrates the challenges that meeting this test presents and which will be magnified if adopted across multiple jurisdictions.

We suggest that the OECD proposals are amended to clarify that business support activities (where the workforce in the smaller economy conducts substantial managerial and operational activities over those support services) can qualify as an active business. This is even in circumstances where those activities are provided for the benefit of related group parties and where there are no or limited sales of the relevant Group’s products / services in the small country concerned.

In addition, an appropriately designed “safe harbour test” should be included. We included more detailed suggestions on this test in our previous submission on Action 6 in January 2015 and these are set out in Appendix 1.

2.2 Discretionary relief

As noted in the Discussion Draft, both the PPT rule and the discretionary relief provision of the LOB rule include a test based on whether one of the principal purposes is the obtaining of benefits under a tax treaty. Our concerns with the possible application of the PPT on smaller economies are equally applicable to the discretionary relief section of the LOB. For that reason, amendments to the commentary, similar to those outlined above regarding the PPT, should also be included in the commentary on the discretionary relief element of the LOB.

2.3 Combination of Simplified LOB and PPT

While the simplified LOB is welcome, we note that the Discussion Draft proposes it should only be used in conjunction with a PPT. As previously highlighted in our response to the original Action 6 Discussion Draft, the combination of both tests will result in increased uncertainty for international businesses as to their entitlement to the benefits of double tax treaties and the application of the treaty provisions to their business activities.
The option should be available for treaties to adopt the simplified LOB without requiring a PPT to also be included where contracting states can be satisfied that sufficient protections exist against treaty abuse measures e.g. within the domestic tax framework of the contracting states.

3. Detailed LOB

We note that there are no significant changes to the detailed LOB proposed in the revised Discussion Draft.

3.1 Special Tax Regime proposals

We note the new proposal to include in the LOB, the ability to deny treaty benefits where income has benefited from a “special tax regime”. While the proposal is designed to address concerns about having a derivative benefits clause, we understand that it is designed to operate to deny treaty benefit to any claimant, regardless of whether or not they are seeking to rely on the derivative benefits clause.

This proposal as worded appears to be very broad and there is very little guidance as to how it should be applied. Further guidance would be necessary and more time should be given to consider the proposal.
Some US treaties contain a “safe harbour” whereby substantiality is assumed if, in prior years, the asset value, gross income and payroll of the small country activity are, for example, at least 7.5% of the equivalent numbers in the US, and the average of the three ratios exceeds 10%. In practice the US safe harbour can be difficult to meet because of the US source of income rules outlined above.

Options for a fair safe harbour might include a mathematical safe harbour which is similar to the ones in some US treaties but:

(i) with clarification that the resident country activity includes all sales / services from the resident country entity to counterparties outside the country concerned. This clarification would be required for the purposes of the general substantiality test and any mathematical safe harbour; and

(ii) with adjustment for the relative size of the economies concerned.
Ms. Marlies de Ruiter  
Head of Tax Treaties, Transfer Pricing and Financial Transactions Division  
Centre for Tax Policy and Administration  
Organisation for Economic Cooperation and Development  

Accounting & Tax Committee  
Japan Foreign Trade Council, Inc.

Comments on Discussion draft on  
Action 6 (Prevent Treaty Abuse) of the BEPS Action Plan

The following are the comments of the Accounting & Tax Committee of the Japan Foreign Trade Council, Inc. (JFTC) in response to the invitation to public comments by the OECD regarding the “Revised discussion draft on BEPS Action 6: Preventing Treaty Abuse”.

The JFTC is a trade-industry association with Japanese trading companies and trading organizations as its core members. One of the main activities of JFTC's Accounting & Tax Committee is to submit specific policy proposals and requests concerning tax matters. Member companies of the JFTC Accounting & Tax Committee are listed at the end of this document.

<Overall Comments>
1. We support measures for denying the benefits of tax treaties to treaty shopping, and artificial transactions and arrangements aimed solely at securing the benefits of a tax treaty. We also support provisions explicitly stating that tax treaties are not intended for use in generating double non-taxation.

2. However, excessively strong anti-avoidance rules introduced into tax treaties and domestic laws may result in unfair treatment of substantive transactions and investments, which should be avoided. In the revised discussion draft, the model tax treaty has become more flexible due to the simplified LOB rule. However, the LOB rule and PPT rule are still used simultaneously and this may result in negative effects for taxpayers who should essentially enjoy the
benefits of a tax treaty.

3. In the examples of PPT, so-called “regional headquarters” and companies who provide investment management services to related companies do not contravene the treaty abuse if there are business reasons. However investment management work may not satisfy the conditions for being considered a qualified person for LOB. Consistency between the two rules is required. The examples of cases that present no problem as regards PPT, which emphasizes actual conditions should be listed under the “active business provision” in Paragraph 3 a), Article X of the model tax treaty of the LOB rule. In addition, it would be better for the regional headquarters and investment management companies to be clearly listed under “qualified person” stated in Paragraph 2, Article X.

4. Since the provisions of the definition of PPT are too wide, tax authorities may determine one of the principal purposes of an arrangement in an arbitrary manner without clear criteria or objective analysis, resulting in an excessively restricted application of the treaty. There is a concern that the expression “one of the principal purposes” contained in the examples of a Conduit Arrangement in Part 2-B-16 may leave room for the competent authorities to interpret these purposes at their discretion. In such cases, the treaty benefits may be disclaimed and double taxation may arise in spite of the existence of legitimate business purposes. Therefore, we request a clarification of the conditions in which treaty benefits would apply that goes beyond a simple recitation of examples. Also, the definition of “one of the principal purposes” is newly added in Paragraph 86 regarding the discretionary relief provision of the LOB rule. We request a clarification of the conditions for this case as well to avoid double taxation.

5. The revised discussion draft does not sufficiently reflect the comments of follow-up work, especially with regard to issues 5, 6, and 10, which are expected to be discussed at the meeting of Working Party 1 (hereinafter referred to as “WP1”) in June. Thus, we would like to request a re-publication of the revised discussion draft in July or later that would include the results of the meeting of WP1.
PART 1 – ALTERNATIVE “SIMPLIFIED” LOB RULE AND PRESENTATION OF THE LOB RULE IN THE OECD MODEL

➢ The alternative “simplified” LOB rule does not reflect Subparagraph 3.c which was proposed in Paragraph 16 of the Report on the Work on Action 6 (“Preventing the Granting of Treaty Benefits in Inappropriate Circumstances”) of the BEPS Action Plan (hereinafter “the Report”). Accordingly, the following sentence should be added to Subparagraph 4 of the rule.

“4. ... c) For purposes of applying this paragraph, activities conducted by persons connected to a person shall be deemed to be conducted by such person... (omitted)... In any case, a person shall be considered to be connected to another if, based on all the relevant facts and circumstances, one has control over the other or both are under the control of the same person or persons.”

PART 2 – ISSUES IDENTIFIED IN THE NOVEMBER 2014 DISCUSSION DRAFT

A. Issues related to the LOB provision

[Issue 3. Commentary on the discretionary relief provision of the LOB rule]

➢ In the commentary on the discretionary relief provision in Part 2-A-3, taxpayers are responsible for proving their legitimate business purposes and the substance of these to the competent authorities. In such conditions, we request that clear guidelines be provided by which the competent authorities will judge whether discretionary relief should be applied to taxpayers. We also request guidelines on how taxpayers can prove business purposes and substance to the competent authorities.

➢ We expect that there will be opportunities for discussions on how to deal with the likely increase in the number of requests to the competent authorities for giving relief in cases of inappropriate applications of LOB, along with discussions regarding the LOB rules. We are concerned that it might be difficult for the competent authorities to discuss relief after the LOB rules have been fixed in Action Plan 6.

[Issue 6. Issues related to the derivative provision]
We welcome the fact that the portion of shares possessed by equivalent beneficiaries, which was proposed to be at least 95 percent in the initial draft, has now been changed to 75 percent in the general elements of the LOB rule, which we believe reflects our comments.

On the other hand, one of the conditions for being considered an equivalent beneficiary states that the maximum tax rate between the source country and the third country should be at least equivalent to the maximum tax rate under the relevant treaty. Unless the condition above is satisfied, the said beneficiary will not be regarded as a derivative beneficiary and the domestic tax rate of the source country will be applied. This issue was raised in our previous public comments and has also appeared as a public comment on Paragraph 49. Since these comments have not yet been reflected as proposed, we would like to request a reconsideration of this point. As it stands, the proposed condition would yield an unreasonable outcome, given that the equivalent beneficiary provision is a type of bona fide provision. In such instances, therefore, the tax rate applied should be that of the tax treaty applied in a case where the ultimate beneficial owner has made an investment directly. As an example of this approach, this treatment is accepted in the technical explanations of the US-UK Tax Treaty and in court cases in certain states, and should be appended to the OECD Model Tax Convention.

“Special tax regimes” are defined in Article 3 of the model tax treaty and mentioned in the related articles 11, 12 and 21. Introduction of this special tax regime should be based on the premise that the derivative beneficiary provision will be included. In addition, consistency and overlap with other action plans must be carefully considered.

The definition of special tax regimes in Proposal 1 is vague and extensive (“including through reductions in the tax rate or the tax base”) and is likely to disturb sound economic activities. To preserve the original intent of single taxation, which is fundamental to the BEPS project, this definition should be revised to read “to generate stateless income or double non-taxation,” making it clearer and more specific.

In Proposal 2, it is proposed to include in the provision a sentence to the effect that related provisions will be ineffective if the other country
virtually exempts the foreign source income of residents from taxation after conclusion of the treaty. However, since the economic effect of any amendment made after the conclusion of the treaty is not related to transactions or investments made by taxpayers for the purpose of tax avoidance, this phrase should be deleted as it departs from the main point of preventing tax abuse. Additionally, when this clause is considered in light of the inclusion of a territorial taxation system in “iii) the purpose of excluding double taxation,” as one of the examples of cases where a special tax regime would not apply, the sentence makes judgments more uncertain and should therefore be deleted.

[Issue 10. Clarification of the “active business” provision]

1) Treatment of holding companies (management of investments)

- Following the raising of concerns by some delegates at the March 2015 meetings of WP1, we would like to express strong concerns regarding the automatic exclusion of “the business of making or managing investments for the resident’s own account” from the definition and scope of “active business.” If the resident’s business of making or managing investments involves substantive economic functions and the resident is actually engaged in real business including decision-making or management support which would enhance the investee’s enterprise value, such business should be considered as “active business.” This treatment is consistent with Example G in Paragraph 98, and it would not be reasonable for the tax treaty’s application regarding the business of making or managing investments to differ between the LOB and the PPT rules.

- Any decision on whether a certain business is conducted actively should be made based on all the relevant facts and circumstances. We are concerned that an automatic determination based on industrial categories might distort fair global competition.

- Considering the above, in relation to Subparagraph 3 a) of the LOB rules proposed in Paragraph 72, we suggest either deleting the sentence in parentheses, or revising it to read as follows: “(other than the passive activity of merely holding investments for the resident’s own account . . .”).

2) Cases where the same company carries on both investment and other active business

- In relation to Paragraph 71, it is quite usual for the same company to carry on several lines of business, and we believe that if these various lines of
business, including the active business, are related to one another and constitute a cohesive business operation, the company's activities as a whole should be considered as constituting the “active business.”

In the example below, RCO holds shares in SCO, in addition to its active business in State R. As the investment in SCO is part of the cohesive business activities of RCO, it is reasonable to determine that the overall activities of RCO as a whole constitute the active conduct of a trade or business.

Example 1  Case where the same company carries on trading and investment (The business of the companies differ, but they are related and inseparable)

- RCO, a company resident in State R, is a non-listed company. RCO is actively engaged in the business of trading natural resources with substantial economic substance, and located in State R, for non-tax business reasons such as the existence of a sophisticated commodity exchange, the availability of highly skilled personnel, a reliable legal system, and a business-friendly environment.

- In addition, RCO holds 100% shares in SCO, which is engaged in the exploration, development and production of natural resources under license in State S. RCO analyzes the status of the international market, the demands of its customers, and other economic considerations affecting natural resources, and develops a business strategy to enhance the RCO group’s enterprise value as a whole. Such a strategy includes determining the transaction flow, e.g. RCO purchases products from SCO and sells them to customers in State R or third countries or sells through a commodity exchange, or SCO sells to customers directly.

- As above, RCO’s management activities regarding its investment in SCO should be considered part of the RCO’s cohesive business operations integral to its trading business in natural resources.

Example 2  Case where the same company carries on infrastructure business and investment
(The companies form individual businesses in each country, but perform the same activity)

RCO, a company resident in State R, is a non-listed company. RCO is engaged in the infrastructure business in State R, with substantial economic substance.

In addition, RCO holds 100% shares in SCO, which is engaged in the infrastructure business in State S. RCO and SCO share relevant information and know-how regarding the infrastructure business, and collaborate to enhance the group’s overall enterprise value.

RCO’s management activities for its investment in SCO are considered to be part of the RCO’s cohesive business operations in the infrastructure business.

3) Level of assessment for the active business provision

- The active business test should be applied on a corporate group (consolidated) basis, rather than assessing the individual entity on a stand-alone basis. There are cases where legally separate entities need to be incorporated to carry on segregated business, for non-tax business reasons such as diversification and consolidation of business risks. In addition, in fields such as natural resources and infrastructure, in which the organization of project finance is key to the success of the business, third-party financial institutions often request incorporation of a legally separate entity on a project-by-project basis from the perspectives of bankruptcy remoteness or clear distinction of the secured assets. Nevertheless, even if the separated entities are incorporated for finance purposes, in many cases cohesive business operations or structures are implemented, e.g. through appointment of the same directors to each entity, for effective and efficient business operations, and concentration of know-how, etc.

- Taking into account the actual business practice of business fragmentation motivated purely by non-tax business reasons, when the active business provision is applied, we suggest adding criteria for determining whether a
corporate group is engaging in active business in the resident jurisdiction with reference to the entire corporate group, in addition to assessing individual entities on a stand-alone basis.

- From the same perspectives, in relation to Subparagraph 3. c) of the LOB rules proposed in Paragraph 72, we would like to suggest deleting the sentence that reads “only if...such other persons are engaged in the same or a similar line of business,” similar to Paragraph 16 of the Report, on the grounds that some relationship necessarily exists between the businesses of the resident and the connected party if the “connected party” conditions are met. Alternatively, we suggest adding the following sentence to the relevant Commentary.

“If business activities carried on by connected parties constitute complementary functions that are part of a cohesive business operation, for example where a resident and the connected party appoint the same director who designs the business strategy, manages the operations, and makes business decisions to enhance the enterprise value of both parties efficiently and effectively, both parties shall be considered to be engaged in the same or a similar line of business.”

4) Others
- We request guidelines on common procedures among all countries in applying treaty benefits following the introduction of the LOB provisions in the treaties so that tax payers are not subject to an excessive administrative burden.

B. Issues related to the PPT provision

[Issue 12. Inclusion in the Commentary of the suggestion that countries consider some form of administrative process ensuring that the PPT is only applied after senior approval]

- As the PPT rule grants tax authorities broad taxation powers and may restrict taxpayers’ use of treaty benefits, an explicit and strict administrative process should be established and implemented by the tax authorities when the PPT rule is introduced. On the other hand, we understand that administrative procedures and organizations relating to taxation differ in each country, making the adoption of a single approach difficult. In this regard, we would like to suggest revising the last sentence of the new Paragraph 14.1 of the Commentary (proposed in Paragraph 79)
as below.
“States **may wish** are required to establish a similar form of administrative process that would ensure that paragraph 7 is only applied after approval at a senior level within the administration in accordance with the administrative procedures and organization of each State.”

[Issue 16. Drafting of the alternative “conduct-PPT rule”]
- We welcome the fact that the explanation of the conduit-PPT rule has been changed to include concrete examples, since this will increase predictability for taxpayers. However, in Example D, it is stated that “If, however, RCO’s decision to lend to SCO was dependent on TCO providing a matching collateral deposit to secure the loan so that RCO would not have entered into the transaction on substantially the same terms in the absence of that deposit, the facts would indicate that TCO was indirectly lending to SCO by routing the loan through a bank of State R and, in that case, the transaction would constitute a conduit arrangement.” However, the comment to the effect that “RCO would not have entered into the transaction on substantially the same terms in the absence of that deposit” relates not to “one of principal purposes for a reduction of the tax,” but rather to a contract with a financial institution when carrying out appropriate financing as a group, such as expanding sources of external capital financing and ensuring stable liquidity. Also, since both internal and external deposits and guarantees of monetary liabilities are usual parts of group finance, this explanation in the revised discussion draft is a one-sided opinion. Thus, the sentences following “If, however, RCO’s decision” should be deleted.

[Issue 17. List of examples in the Commentary on the PPT rule]
- Example H refers to a case where TCO establishes RCO only in State R. On the other hand, as stated above, many MNE Groups fragment their business into several lines and incorporate separate entities for each business line in State R, as part of their business strategy and for risk management purposes. In this regard, we would like to suggest adding the following “Example H-2”, just after Example H.

**Example H-2:** In contrast with Example H, TCO fragments business in State R and establishes five subsidiaries in State R, namely R1CO, R2CO, R3CO, R4CO and R5CO, which carry on wholesaling, retailing, manufacturing, financing and domestic and international investments, respectively. The fragmentation R5CO undertakes the development of new
business activities in State S, and for that purpose, contributes equity capital and makes loans to SCO. The fragmentation of the business in State R derives purely from non-tax business reasons such as bankruptcy remoteness or simplification of the decision-making process and, even after the fragmentation, all business activities constitute complementary functions that are part of a cohesive business operation. The other facts and assumptions are same as in Example H.

In this example, the only difference with Example H is the fragmentation of the RCO business, which is carried on by five separate companies, based on clear non-tax business reasons. All the other assumptions are exactly the same as in Example H. Hence, R5CO’s financing of SCO through equity and loans should be considered part of RCO’s active conduct of a business in State R. In this regard, Paragraph 7 would not apply to these transactions, either.
Japan Foreign Trade Council, Inc.

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Comments on the Revised Discussion Draft on BEPS Action 6
(Prevent Treaty Abuse)


We consider it fair to deny treaty benefits to any transaction or arrangement made through an entity that has been established solely to obtain such benefits and has no business substance. At the same time, it is equally fair for any genuine economic activity to be entitled to treaty benefits, as we stated in our April 2014 comment letter.

The Revised Discussion Draft has apparently given consideration to taxpayers, especially by leaving the structure of a limitation-on-benefits (LOB) provision up to individual contracting states, thereby avoiding uniform application of the overly strict LOB rule, and by providing additional illustrative examples on the principal purposes test (PPT). However, attention should be paid to an increase of the administrative burden for taxpayers because multiple choices regarding the structure of a LOB provision and complication of the rule are two sides of the same coin. And as for the PPT, the term "one of the principal purposes" stated in paragraph 7 of Article X in the Revised Discussion Draft should be changed to "the principal purpose" in order to ensure that the scope of the PPT will not be unreasonably wide.

In the Revised Discussion Draft, the treatment of some of the matters of concern to Japanese companies remains unsettled, while new proposals have been presented. In view of these, our comments below focus on the two issues we consider particularly important: regional headquarters, and the derivative benefits provision and special tax regimes.
1. Regional Headquarters

The Revised Discussion Draft has enhanced the Commentary on the PPT rule, adding Examples G and H that demonstrate it is not reasonable to deny treaty benefits to a company managing certain intra-group services or undertaking business developing activities within the region. Of these two, Example G raises some concerns, primarily because what “a real business” and “substantive economic functions” mean may not be uniformly interpreted by countries. Nevertheless, it is clear that, in both examples, the companies in question have no intention of abusing the tax treaty and are engaged in the active conduct of a business. We thus welcome the conclusions that the PPT rule would not apply to either of them. Going forward, more illustrative examples should be provided to clarify that the PPT rule does not apply to a regional headquarters that holds shares in multiple subsidiaries thereunder.

As for the LOB rule, meanwhile, the September 2014 interim report on Action 6 entitled “Preventing the Granting of Treaty Benefits in Inappropriate Circumstances” contains two relevant statements. The one is that “the business of making or managing investments” is not treated as “the active conduct of a business,” laid down in subparagraph a) of paragraph 3 of Article X that is contained in the report’s paragraph 16. The other is that “a headquarters operation is in the business of managing investments,” set out in paragraph 48 of the report’s Commentary on the LOB Rule. As a result of these, the issue remains that regional headquarters may not be entitled to treaty benefits.

In respect to this issue, the Revised Discussion Draft only mentions in paragraph 70 that the pros and cons of the issue were discussed at the March 2015 meetings of Working Party 1, without referring to any conclusion thereon other than the comment in paragraph 71 which stated that the Working Party agreed that the Commentary on the “active business” provision should clarify the concept of “business”. From the perspective of consistency, though, given that the PPT rule does not apply to regional headquarters, under the LOB rule, regional headquarters should also be entitled to treaty benefits unless other facts indicate that it has been established solely for tax purposes.

There are some possible approaches to realize this. One is to recognize a regional headquarters operation as the active conduct of a business in subparagraph a) of paragraph 3 of Article X. A more desirable approach, however, is to recognize a regional headquarters itself as a qualified person under paragraph 2 of Article X without requiring an unduly strict condition, taking into account predictability to taxpayers.
2. Derivative Benefits Provision and Special Tax Regimes

We disagree with the proposal for special tax regimes that the Revised Discussion Draft presents in connection with the derivative benefits provision. What Action 6 aims for is the elimination of double non-taxation. Considering that aim, it would be overdone to resort to nullifying treaty benefits to entities that enjoy a preferential effective rate of taxation to income or profit on interest, royalties, and other income, so long as they are taxed accordingly.

Paragraphs 47 and 48 explain the proposal in the context of the interaction with Actions 5 (harmful tax practices) and 8 (intangibles). This suggests that the proposal has mainly stemmed from concerns over the transfer of intellectual property rights from the country of the head office to a lower-tax jurisdiction and the resultant granting of treaty benefits to base-eroding payments. However, such transfers of intellectual property rights, in particular wrongful ones, are expected to be deterred to a considerable extent by the rules pursuant to Action 5 and Actions 8 to 10, as well as Action 3 (CFC rules).

Tax treaties should, first and foremost, aspire to encourage economic exchange between the contracting states through the elimination of double taxation. It is not desirable for such treaties to institute measures that would overlap with measures taken under other Action items. Therefore, inserting new provisions into the articles of the OECD Model Tax Convention should be avoided, including those into Articles 3 (general definitions), 10 (dividends), 11 (interest), 12 (royalties), and 21 (other income). As for the derivative benefits provision, it is appropriate to be introduced as part of the LOB rule, without adopting the special tax regime rule.

Lastly, in the event that the number of tax treaties incorporating the LOB rule increases, the OECD will need to develop uniform guidelines on procedures for certificates of residence and other documentation in order to reduce the administrative burden on taxpayers and standardize enforcement by nations.

Sincerely,

Subcommittee on Taxation
KEIDANREN
Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division  
OECD/CTPA  

17 June 2015

By email: taxtreaties@oecd.org

Dear Ms de Ruiter

BEPS Action 6: Prevent Treaty Abuse (Revised discussion draft released on 22 May 2015 (the "Draft"))

We are writing to you further to our letters of 30 October 2014 and 7 January 2015 in relation to our concerns that the previous proposals in relation to Action 6 could deny Treaty benefits to debt funds (which, as in our earlier letters, we use in this letter to refer to debt funds, CLOs, securitisations and other special purpose entities established to advance or acquire loans to individual or corporate borrowers).

We are disappointed that our comments have not been taken into account in the Draft and we consider that those concerns remain relevant to the revised proposals in the Draft.

In our letter of 30 October 2014 we set out the reasons why we consider that Treaty benefits should be available to debt funds. Those reasons form the background to the comments on the Draft which are set out below, but, to maintain brevity, we do not repeat them here.

Our comments on the proposals in the Draft focus only on the treatment of debt funds. In short:

1. General comments on LOB Rules – We consider that, if the LOB Rule is implemented (in either the proposed simplified or full form), then it seems almost inevitable that many debt funds will be denied access to Treaty benefits.

In the case of, in particular, securitisations and other capital markets entities, we consider that this result would be directly contrary to the general consensus which has built up over the last few years that revitalising the securitisation market and creating greater ease of access to capital markets is critical to widening the sources of funding available to businesses, and to filling the "funding gap" that has resulted from bank deleveraging (particularly for SME financing). 1

Specifically, for debt funds issuing cleared notes (e.g. as part of a securitisation), it is simply not possible to identify the ultimate noteholders, as required by both the proposed simplified and full LOB Rule. Fundamental legal, regulatory and commercial changes to the way in which clearing operates in Europe would be needed in order to put issuers of cleared notes in a position where they could identify the holders of notes which they issued.

Identification is also difficult (albeit not in principle impossible) for debt funds that do not issue cleared notes, particularly given the fact that some debt fund investors are themselves funds or other intermediaries.

We note that FATCA and CRS were designed to avoid the necessity of tracing beneficial ownership to the ultimate beneficiary; disclosure and/or withholding takes place at the level of the last intermediary in the chain of payment/settlement and not (as Action 6 requires) at the level of the underlying borrower/issuer. This kind of "withholding agent" approach seems to us more practicable, fairer and less distortive than the LOB (given that it means all beneficial owners entitled to treaty relief would obtain it, and all beneficial owners not so entitled would not). However we appreciate that at this juncture so radical a change is unlikely to be considered by the Working Party.

We would, therefore, be most grateful if the Working Party could consider the question of how the LOB can be applied in practice, particularly in the context of cleared notes. Our preference would be for appropriate exemptions to be included in the LOB and simplified LOB; or alternatively for implementation to be delayed until practical details are resolved. However if the Working Party does not wish to do this, it would be helpful if the OECD could engage with a full range of stakeholders before finalising its proposals, given the implications for securitisations and capital markets.

(Alternatively it may of course be the case that the LOB will be adopted by so few OECD Members that it is of little practical relevance. However it seems to us that we (and the wider market) will have little visibility on the level of LOB adoption until it is too late to adapt systems and processes to deal with it.)

2. **Simplified LOB Rule** – As drafted, this would not assist debt funds. In most cases, they would simply not be eligible for Treaty relief.

Debt funds are unlikely to be "qualifying persons" themselves, and, as they cannot usually identify their owners, they will generally be unable to determine if they are entities in which the requisite beneficial ownership is held by qualifying persons or by equivalent beneficiaries. Indeed, as noted above, for debt funds issuing cleared notes (e.g. as part of a securitisation), it is simply not possible to identify the ultimate noteholders.

In most cases, debt funds will also be unable to meet the "active business" test. Unless Contracting States agree to extend the proposed excluded entities list, most debts funds are likely to fall within the "investment" carve out wording included in paragraph 4(a).
Accordingly, in order to benefit from Treaty relief, the only option available to many debt funds would be to obtain specific clearance. We are concerned that, without clear guidance on the circumstances in which clearance would be granted, there will be both uncertainty and a real risk that debt funds would not be treated in a consistent manner. As a result, reliance on the availability of discretionary relief would be commercially unacceptable to potential investors. Even if clearance could be obtained, there would often be delays before relief was granted. Unless the period of delay was reasonably certain in advance (and short), this is also likely to be commercially unacceptable to potential investors.

The effect would be to inhibit the access of residents of Contracting States (or at least those Contracting States that did not agree specific wording to cater for debt funds) to an increasingly important source of financing. This would put such entities at a significant disadvantage.

We therefore ask that, as a minimum, the Working Party consider:

(a) including guidance in the Commentary which makes it clear that in the case of debt funds, there is a presumption that clearance should be granted, which would be rebutted if the PPT is failed;

(b) following on from this (and to fully reflect EU principles of freedom of movement and establishment), amending any guidance along the lines of that set out in paragraph 32 of the Draft accordingly, and in particular, so that that wording relating to the position of entities with parents in third States is revised to deal with the position of investors in debt funds (and to reflect our proposal at (a)); and

(c) including guidance making it clear that requests for Treaty relief must be processed promptly (as reflected in the proposed guidance at paragraph 32 of the Draft), and in any event within the timetable outlined in that guidance.

It would also be helpful if specific guidance (including examples) relating to the application of the PPT to debt funds could be included in the Commentary.

3. Full LOB Rule – In our view it is helpful that the Working Party has concluded that it should continue to look at solutions to issues relating to the treaty entitlement of non-CIV funds.

We note the concerns raised at, in particular, paragraph 24 of the Draft. Our view is that those concerns are not really relevant to debt funds – in relation to which, broadly, the commercial aim is simply to make available debt funding to borrowers on a tax-neutral basis.

We consider it helpful that options to be discussed include adding a specific provision on non-CIV funds in the LOB Rule, and adding examples on non-CIV funds to the Commentary to the PPT rules, and we would urge the Working Party to proceed with both of these alternatives. We consider that, in relation to the second option (examples in Commentary) our comments at paragraph 2 are again relevant.
4. **Special Tax Regime** - Because of the importance of debt funds such as securitisations as a means of raising finance, a number of jurisdictions (such as the UK, Ireland, Luxembourg) have introduced special tax rules for securitisations. Broadly, those rules ensure that the SPVs used in such financings are subject to simplified tax rules, and bear no, or a nominal amount of tax. This means that the underlying corporate borrower is able to raise debt financing on a cost-effective basis (although in the great majority of cases this is a simplification rather than an absolute tax-saving, and typically regimes of this kind have anti-avoidance rules to prevent them being used abusively).

As this proposal is drafted, SPVs falling to be taxed within the above special rules would be caught. Other debt funds that are taxed under rules (or practice) which provide for a preferential effective rate of tax would also be caught.

Our view is that these onerous provisions are not necessary, and that, as drafted, they are disproportionate. Where it is appropriate to deny relief to entities falling within a specific tax regime, we think that this can be achieved through the application of the PPT.

If, however, the decision is made to proceed with this proposal, then we would strongly recommend that consideration is given to extending the exception included at sub-para (vii) of the proposed "special tax regime" definition so that it extends to securitisation companies (and other debt funds). We see no reason why investment vehicles for real estate and securities portfolios should benefit from a specific exclusion to the proposed rules, but that debt funds should not. Indeed those debt funds that issue debt securities are in principle incapable of facilitating base erosion (i.e. because most jurisdictions will tax an investor holding debt securities in a very similar manner to that if the investor had held the fund's underlying debt assets directly).

In addition, we would ask that relevant guidance (with examples) is added to the Commentary.

Please do not hesitate to contact us if you require further information in relation to any of the above.

Yours sincerely

[Signature]

**Clare Dawson**
Chief Executive

cc HM Treasury
Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division  
OECD/CTPA  

17 June 2015  

By email: taxtreaties@oecd.org  

BEPS Action 6: Prevent Treaty Abuse  

Dear Ms de Ruiter:  

We are writing to you further to our letter of 18 December 2014 in relation to our concerns that the previous proposals in relation to Action 6 could deny Treaty benefits to debt funds (used herein to refer to debt funds, CLOs, securitisations and other special purpose entities established to advance or acquire loans to individual or corporate borrowers).  

The proposals in the BEPS Action 6: Prevent Treaty Abuse discussion draft released on 22 May 2015 still do not consider the positions of debt funds that would not qualify as "collective investment vehicles" (CIVs) and this may severely adversely impact this important source of funding for businesses.  

As explained in our earlier letter, US debt funds lend to borrowers in Europe and across the world, either directly or via special purpose vehicle subsidiaries established in other jurisdictions. Although US borrowers are unlikely to be affected by the Action 6 proposals because of the existing features of the US tax system, the range of approaches suggested in the revised proposals document will in our view have a very material adverse effect on US funds and investors, and on many borrowers outside the US. The concerns that we raised in our 18 December 2014 letter remain relevant to the proposals in the 22 May 2015 revised discussion draft.  

With respect to the revised draft, we have seen a copy of the letter submitted today by the Loan Market Association (LMA) (“LMA Letter”) and we share the LMA's concern that these proposals may deny Treaty benefits to debt fund SPVs with potentially very serious adverse consequences for the loan market and the wider economy.  

We respectfully urge the Working Party to recognize the important commercial role that debt funds play in providing funding to businesses around the world and revise the proposals so as to not deny these entities access to Treaty benefits. As discussed in full in the LMA Letter, the main points of concern are:
1. With respect to both the proposed simplified or full form LOB Rule, if implemented as proposed, debt funds will be denied access to Treaty benefits because these entities will be unable to identify their ultimate noteholders. Like the LMA, we would welcome appropriate exemptions for debt funds to be included in the LOB and simplified LOB.

2. Under the proposed simplified LOB rule, without specific clearance debt funds would not be eligible for Treaty relief because debt funds are (a) unlikely to satisfy the “qualifying persons” test for the reason identified above and (b) will also be unable to meet the "active business" test. As identified in the LMA Letter, reliance on discretionary relief in the form of specific clearance is likely to be unsatisfactory to investors and thus is not a meaningful option for debt funds. We echo the LMA’s requests of the Working Party to address this problem in the Commentary with the specific proposals set forth in the LMA Letter.

3. We are heartened to see that the Working Party acknowledges that it should continue to look at solutions to issues relating to the Treaty entitlement of non-CIV funds and, to that end, will be discussing the possibility of adding a specific provision on non-CIV funds in the LOB Rule, or adding examples on non-CIV funds to the Commentary to the principal purpose test (PPT) Rules (among other options). Like the LMA, we strongly encourage the Working Party to move forward with both alternatives. Finally, we hope that the Working Party recognizes that the objective of debt funds to provide debt funding to borrowers on a tax-neutral basis does not run afoul of the concerns noted in paragraph 24 of the 22 May 2015 draft.

4. For the reasons stated in the LMA letter, we do not think the benefits of the new Special Tax Regime proposal outweigh the costs associated with its implementation and, furthermore, the stated objectives of the proposal can be accomplished through other aspects of the Action 6 proposals. However, if the Working Party chooses to pursue the adoption of the proposal, we concur with the LMA’s recommendation that consideration be given to extending the exception included at sub-para (vii) of the proposed "special tax regime" definition so that it extends to securitisation companies (and other debt funds).

5. In relation to the proposed PPT, we would generally be confident that CLOs and other debt funds should be regarded as having a wholly commercial principal purpose. However, the subjective nature of the test creates some concern that tax officials may apply the PPT (or consider applying it) to vanilla CLO and debt fund structures. It would therefore be very helpful if the examples included in the final guidance could include typical CLO and debt fund structures, and we would be happy to work with you in that regard.
Please do not hesitate to contact us if you would like further information on any of the above.

Sincerely,

R. Bram Smith
Executive Director

Cc: Robert Stack, Deputy Assistant Secretary for International Tax Affairs, United States Department of the Treasury (robert.stack@do.treas.gov)
17 June 2015

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Dear Ms de Ruiter

RE: OECD Discussion Draft: BEPS Action 6, Preventing Treaty Abuse

Thank you for the opportunity to respond once again in relation to this issue. M&G\(^1\) welcome the attention that has been given to the funds industry in relation to Action 6 and set out our further comments for your consideration.

1. **Collective Investment Vehicles (CIVs)**

We agree with the inclusion of subparagraph 2(f) in the Simplified LOB and support the conclusions of the 2010 CIV Report. Whilst we fully support TRACE as a mechanism to claim treaty benefits, we believe that the recognition of certain CIV funds types as ‘qualified persons’ is an important first step in addressing the practical challenges that arise when CIVs attempt to claim benefits. Accordingly, M&G welcome any proposals which will reduce the uncertainty and improve consistency of treatment for funds. We believe that the work on Action 6 provides a good opportunity to do this.

2. **Non-CIVs**

We recognise that work on this will continue but would like to take this opportunity to comment on the two concerns that governments have about granting treaty benefits to non-CIVs.

(i) **Non-CIVS may be used to provide treaty benefits to investors that are not themselves entitled.**

The use of fund vehicles which are designed solely to claim treaty benefits can indeed be considered an abuse of treaties. However, we note the following:

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\(^1\) M&G is the UK and European fund management business of the international financial services group Prudential plc. It has over £270 billion of funds under management, making it one of the largest UK fund managers. M&G manage a range of different fund types in the three major fund jurisdictions in Europe, which include UK Open Ended Investment Companies, UK partnerships, Irish Variable Capital Investment Companies, Irish Common Contractual Funds, Luxembourg SICAVs and FCPs.
Such abuse is far less likely where the fund is professionally managed and is widely held, or has ‘genuine diversity of ownership’ – a UK concept which is designed to prevent small groups of investors from taking advantage of the tax treatment available to investors.

This is primarily attributed to the fact that the investor does not have control over the investment decisions of the fund. A professional investment manager with the relevant market expertise is typically responsible for making the investments.

An important consideration is the investment strategy of the fund – it may be necessary to distinguish between a fund which makes and holds a diversified portfolio of investments with a long term view compared to one which buys/sells assets over short periods of time or over income events.

Accordingly, we suggest that the current distinction between CIVs and non-CIVs is unnecessary, and the focus should be on clarifying the types of funds that should qualify for treaty access (e.g. widely held, professionally managed, long term investments) and those which should not. This may be through revisiting how non-CIVs are defined.

Only in circumstances where certain requirements are not met for the fund entity to qualify for treaties in its own right should it be appropriate to look to apply the equivalent beneficiaries tests as we can anticipate significant administrative burdens to prove the status of investors. For example, the practical application of looking through to equivalent beneficiaries would be particularly burdensome where a fund makes private loans to a trading company. The company would be required to determine the application of treaties and apply the correct withholding tax rates, both of which are activities which a borrower would not typically expect to do. The consequence of such requirements would be detrimental to the private finance and securitisation industry which has been critical to the wider economy.

We re-iterate the fact that funds which are caught by the current ‘non-CIV’ definition provide an important alternative investment opportunity for many institutional investors (e.g. pension schemes, insurance companies), and provides an option for diversification. Without such funds, the institutional investors would not benefit from the economies of scale and would find it difficult to access certain investment markets due to the expertise and specialist knowledge that is required.

(ii) Investors may defer recognition of income on which treaty benefits have been granted

A deferral of income is a point already considered in para 6.25 of the Commentary on Article 1 so should not be of primary concern. Furthermore, many European countries already have tax reporting requirements in place which serves to ensure investors are taxed appropriately.

Thank you again for the opportunity to provide comment in relation to this important issue. If you would like to discuss any of our comments please do not hesitate to contact me at Malcolm.richardson@mandg.co.uk or on 0207 548 2316.

Yours sincerely

Malcolm Richardson
Head of Tax, M&G Investments
June 17, 2015

Via email: taxtreaties@OECD.org

Marlies de Ruiter
Head, Tax Treaties
Transfer Pricing and Financial Transactions Division
OECD/CTPA
2, rue André Pascal
75775 Paris Cedex 16
France

Re: Managed Funds Association Comments on OECD BEPS Project

Dear Ms. de Ruiter:

Managed Funds Association (“MFA”)\(^1\) appreciates the opportunity to submit for your consideration comments regarding the tax treaty proposals on collective investment vehicles (“CIVs”) that have been published by the Organisation for Economic Co-Operation and Development (“OECD”) as part of its Base Erosion and Profit Shifting (“BEPS”) project. MFA supports the goals underlying the OECD’s project of preventing tax abuse in connection with granting tax treaty benefits. We also believe that it is important for the BEPS project to establish a treaty benefit framework that avoids imposing double taxation on investors who would be entitled to treaty benefits when making a direct investment, but who choose to invest through a pooled investment vehicle, such as a private investment fund, in order to have some of their capital managed by third-party managers. To the extent investors, including pension plans, endowments, and charitable foundations, would be subjected to an additional layer of tax simply because they choose to invest through a pooled vehicle, they likely would no longer choose to invest through that type of asset management structure, thereby losing the benefits of such investments and to the detriment of capital markets in which investment funds participate.

Private investment funds are sold through non-public offerings to sophisticated investors and are able to invest in a broad range of assets pursuant to different investment

\(^1\) The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.
strategies. Private investment fund, like other pooled investment vehicles such as UCITS or mutual funds, are formed for commercial purposes to facilitate investment by underlying investors such as pension plans and charitable foundations. The commercial rationale of CIVs, as identified by the OECD,\(^2\) applies equally to private investment funds (e.g., risk diversification and economies of scale).

Our overarching goal is to achieve a neutral result for investors that pool their capital in private investment funds and not increase their incidence of taxation – or at least try to minimize tax disadvantages to them from investing in such funds (as compared to their tax treatment if they had made the investment directly themselves). As there is no single pooling vehicle in any jurisdiction that would preserve such neutrality for all of our international investors, what private investment funds seek to achieve with tax treaties is to mitigate double taxation – the raison d’être for tax treaties.

Private investment funds utilize a variety of investment strategies and invest in diverse assets, such as listed securities, distressed debt, emerging markets securities, transport and infrastructure assets, real estate, commodities, and derivatives. Private investment funds can take the form of private equity funds, hedge funds, distressed credit funds, real estate funds and special situations funds. As noted above, investors in private investment funds are sophisticated, not retail investors, and are predominantly institutional investors from around the world, such as public and private pension funds, sovereign wealth funds, corporations with investable capital (such as insurance companies), foundations, endowments, as well as high net worth investors.

Private investment funds and their managers are subject to a variety of regulations. For example, private fund managers operating in the EU are subject to regulation under the Alternative Investment Fund Managers Directive (“AIFMD”) and in the U.S., fund managers are subject to registration and regulation at the state level (for smaller managers) and at the Securities and Exchange Commission for larger managers as well as at the Commodity Futures Trading Commission. Private investment funds and their managers also are subject to a wide range of securities and commodity futures laws and regulations, which govern their market conduct.

In addition to the benefits private investment funds provide to investors, these funds also serve a valuable role in capital markets, including by acting as an alternative source of capital to business, especially where there is limited risk appetite from traditional sources of capital. There are currently more than 11,000 hedge funds globally with more than $3 trillion in assets under management. These funds invest globally and are increasingly providing capital and liquidity in areas where traditional sources of capital have declined. The European Commission has recognized the valuable role that alternative investment funds play in its recent green paper, *Building a Capital Markets Union*. In that paper, the Commission notes that the asset management industry plays a “pivotal role” in channelling investors’ money into the economy. The Commission goes on to note that the UCITS and the AIFMD\(^3\) frameworks have played a key role in providing the asset management industry

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\(^3\) Directive 2011/61/EU.
with a regulatory environment that allows them to effectively provide this intermediating role.

Given the global nature of the private investment fund industry, we believe all OECD member jurisdictions have an interest in ensuring that the limitation-on-benefits action item includes as CIVs private investment funds that do not present the risks of tax abuse underlying the OECD project. To the extent private investment funds are not able to rely on tax treaty benefits for certain treaty countries, institutional investors in those jurisdictions would be adversely affected in their ability to obtain the risk management, portfolio diversification, and investment expertise provided by private funds. Private investment funds also would be less likely to invest in such jurisdictions, adversely affecting capital markets and the businesses that seek financing from such markets and the economies in those countries. To avoid these unintended, adverse consequences, while developing a framework that addresses policy makers’ concerns about tax abuse, we encourage the OECD to adopt the suggestions discussed below.

We emphasize at the outset that our proposals build on the considerable work done by the OECD to pave the path for recognizing CIVs as tax treaty residents. Our proposals regarding treaty residence for CIVs are mostly based on proposals already made by the OECD in the following publications.

- BEPS Action 6 discussion draft published on 22 May 2015 ("2015 Discussion Draft")
- BEPS Action 6 discussion draft published on 21 November 2014 ("2014 Discussion Draft")
- Commentary to Article 1 of the OECD Model Tax Treaty ("Article 1 Commentary"),
- Treaty Relief and Compliance Enhancement ("TRACE") project.

Within the context of the OECD’s global objective of preventing the abuse of tax treaties, the OECD has recognized for several years the special case of CIVs with international investors, when they seek to obtain tax treaty benefits. We wholeheartedly agree with the OECD, when it stated about CIVs:

The goal is to achieve neutrality between a direct investment and an investment through a CIV in the international context, just as the goal of most domestic provisions addressing the treatment of CIVs is to achieve such neutrality in the wholly domestic context.4

The words of the OECD capture the crux of the issue for private investment funds, which have many investors that would in their own right qualify for tax treaty benefits, if the

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4 Paragraph 6.18 of the Article 1 Commentary.
cross-border investments made by the investment fund were made directly by its investors. The OECD has already proposed tax treaty language to implement additional residence requirements for CIVs. As private investment fund managers, we appreciate the OECD’s work to date but have several concerns. First and foremost, the OECD generally refers to CIVs as being “widely-held”, but many private investment funds may not meet that requirement. So our references to “CIVs” in this letter are to those that are not widely-held. We accept that the test of being widely-held is indeed a relevant consideration for the tax treaty treatment of an investment fund, and its relevance can be preserved by imposing additional requirements on CIVs that do not meet that requirement. We see no compelling international tax policy rationale for excluding non-widely-held CIVs categorically from qualifying for tax treaty benefits.

In short, we believe that any regulated investment fund should be regarded as a CIV but that tax treaty access is based on certain qualifications of the CIV. First, any "widely-held" CIV, such as a US mutual fund or a European UCITS fund, should qualify as a treaty resident and as a per se “qualified person” under any limitation-on-benefits article. Secondly, if a fund is not regarded as "widely-held", then it would still be a CIV but would need to meet the ownership and equivalent beneficiaries tests of a limitation-on-benefits provision, outlined below, to be entitled to full or proportionate treaty access.

In summary, the core elements of the approach that we hope the OECD will adopt include the following.

a) Amend the OECD’s current description of a CIV in its model tax treaty commentary to include those fund entities that are intended for use as private investment funds, such as the “qualifying investor alternative investment funds” (“QIAIFs”) in Ireland, the “specialized investment funds” in Luxembourg, Resident Fund Scheme in Singapore, and their equivalents in other countries. This would mean that a CIV would not be required to be “widely-held” (however defined) to be considered a treaty resident.

b) We believe that the appropriate requirement for an investment fund to be regarded as a CIV should be that the fund or the fund’s investment manager is subject to regulation in the country in which it was established6 – for example, all EU funds within the scope of the AIFMD. We believe that limiting the definition of CIV to these regulated funds significantly reduces the risk of providing tax treaty benefits to entities structured to avoid taxes. Regulated funds and their managers are subject to significant compliance and regulatory costs and provide significant transparency to their government regulators with respect to their investment activities and, as such, are highly unlikely to be established or operated as tax avoidance vehicles.

Including regulated funds within the scope of the definition of a CIV also would allow the OECD to use relevant definitions from the securities and financial services regulations of a treaty country, rather than having to create a stand-alone definition for purposes of tax treaties, which could cause confusion and uncertainty for market participants and policy-makers.

5 Paragraphs 6.17, 6.21, 6.26 and 6.32 of the Article 1 Commentary, and TRACE.
6 In this letter, we refer to investment funds subject to regulation or whose investment manager or investment adviser is subject to regulation with respect to the management of the investment fund as “regulated funds.”
To the extent the OECD does not agree with the above recommendation, at a minimum, we believe the OECD should include funds that are regulated in its country of establishment within the definition of a CIV. As a precedent, the tax treaty between Ireland and the United States does not include references to “widely-held” or “diversified”; it simply refers to “Collective Investment Undertakings”, which includes QIAIFs that are not widely-held.

c) In the definition of a CIV within a treaty, adopt the approach proposed by the OECD in paragraph 6.21 of the Article 1 Commentary, paragraph 36 of the "Commentary on the LOB Rule" in the 2014 Discussion Draft and 2014 Report on Action 6, and in TRACE.

   i. This definition would simply enumerate a list of specific entities that would be treated as CIVs in accordance with the relevant regulations of the country of residence. Certification of “CIV” status could be confirmed by reviewing regulatory filings with a country’s fund regulatory body or tax authority as well as through discussions with such authorities;7

   ii. The list could be amended from time-to-time by agreement of the competent authorities, as needed;

   iii. The definition would confirm that a CIV is treated as the beneficial owner of any income it receives.

d) To address any particular concerns about CIVs that are not “widely-held” (however defined), we further propose that CIVs that are not “widely-held” meet the additional limitation-on-benefits (“LOB”) requirements set out below.

   i. We support the “simplified LOB” included in the recent 2015 Discussion Draft that grants treaty benefits to treaty residents that are more than 75% owned, directly or indirectly, by “equivalent beneficiaries.”

   ii. For CIVs in particular, we would propose modifying the “simplified LOB” to grant proportional benefits of up to 75% based on the percentage ownership of the resident by equivalent beneficiaries.8 If equivalent beneficiaries own more than 75% of a CIV, then the CIV would be entitled to 100% of the treaty benefits (in accordance with the general equivalent beneficiaries proposal, above).

   iii. Documenting the tax residence and equivalent beneficiary status of a CIV’s investors, would be done on an annual basis and through investor self-certifications.9

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7 This equivalent beneficiaries ownership test is also found in paragraph 36 of the "Commentary on the LOB Rule" in the 2014 Discussion Draft and 2014 Report on Action 6, which is based on 6.21ff of the Article 1 Commentary.

8 See paragraph 6.27 of the Article 1 Commentary and the TRACE Implementation Package for the Adoption of the Authorised Intermediary System (the "TRACE Report").

iv. Investor-specific information would be shared only with either the tax authority of the source country or the CIV’s country of residence (which in turn could provide such information to the source country and investors’ residence countries under exchange of information agreements).

e) Implement the comprehensive “Authorized Intermediary System” (“AIS”), as found in the TRACE Report, for streamlining the collection of withholding taxes and claiming of treaty benefits by financial institutions (including CIVs) in respect of its customers or investors. As an organization that represents many U.S. managers of private investment funds, we note and welcome in TRACE’s AIS proposals a convergence with the US “Qualified Intermediary” system and the FATCA/IGA regimes. We believe such convergence will result in very tangible efficiencies for industry participants and enhance the administration and collection of tax for tax authorities.

f) If a CIV qualifies as a treaty resident by virtue of the foregoing tests, then any “principal purpose test” (“PPT Rule”) should not apply – or at least there should be a rebuttable presumption that the CIV has complied with the PPT Rule.

i. Tax considerations are inherently a principal reason (but not the sole reason) for choosing to form a CIV in a particular treaty country. As the OECD has acknowledged, neutrality is a goal of investing internationally through a CIV – as distinct from the more complex considerations of a multinational enterprise in deciding where to locate its people and assets around the world. Without an exception or special presumption for CIVs, it may be difficult for a CIV to comply with a PPT Rule.

ii. Similarly, there should be no additional "substance" requirements imposed on the CIV, such as a need for control, management, employees or other activity to be located in the relevant treaty state. “Substance” for a CIV is the fact that the regulated fund or its manager (1) is subject to regulation in that treaty state (which regulations impose certain local requirements, such as mandatory use of a locally regulated administrator) and (2) meets the LOB requirements.

The rationale for the "Equivalent Beneficiary" LOB approach is explained very well in paragraph 23 of the OECD's own Article 1 Commentary:

The effect of allowing benefits to the CIV to the extent that it is owned by equivalent beneficiaries as defined in subdivision (b)(ii) is to ensure that investors who would have been entitled to benefits with respect to income derived from the source State had they received the income directly are not put in a worse position by investing through a CIV located in a third country. The approach thus serves the goals of neutrality as between direct investments and investments through a CIV. It also decreases the risk of double taxation as between the source State and the State of residence of the investor, to the extent that there is a tax treaty between them. It is beneficial for investors, particularly those from small countries, who will consequently enjoy a greater choice of investment vehicles. It also increases economies of scale, which are a primary economic benefit of investing through CIVs. Finally, adopting this approach substantially simplifies
compliance procedures. In many cases, nearly all of a CIV’s investors will be equivalent beneficiaries given the extent of bilateral treaty coverage and the fact that rates in those treaties are nearly always 10-15 percent on portfolio dividends.

Furthermore, a proportional benefits approach is especially needed by CIVs, because, unlike multinational enterprises that structure entities within their group and choose the jurisdiction(s) of those entities, the manager of a global fund does not choose the jurisdiction of its investors. It would thus be arbitrary, in the case of CIVs, and inconsistent with the goal of neutrality to impose a minimum equivalent beneficiary ownership threshold.

g) In considering the treatment of intermediate entities, we believe it is important to understand the basic structure for private investment funds. A common structure for private investment funds is the “master-feeder” structure (see attached diagram), in which investors invest in feeder funds, which in turn invest in one or more master funds. In a master-feeder structure, many private investment funds use Cayman Islands companies as intermediate entities - one reason for which is to facilitate investment by U.S. tax-exempt institutional investors, which may be limited in their ability to invest in the U.S.-domiciled feeder fund because of the application of U.S. debt-financed income rules for U.S. tax-exempt entities. The use of Cayman Islands-based funds allows managers to set up a corporate entity that is itself not subject to tax in its country of residence.

i. We generally advocate looking through such intermediate entities to beneficial owners in applying the equivalent beneficiaries ownership test.

ii. We believe that the explanation given in paragraph 44 of the 2015 Discussion Draft for the requirement that each intermediate owner be a resident of either Contracting State (i.e., that it is necessary to prevent the interposition of a company in a tax haven to which income derived from the State of source could be paid through a base eroding payment) is not relevant in the context of a CIV. A CIV is typically tax-exempt and would not therefore make base eroding payments. Accordingly, we consider that the intermediate owner requirement should not apply to CIVs.

iii. A special purpose vehicle owned by one or more CIVs formed in the same country as the vehicle should aggregate all of the investors in the intermediate CIVs to determine the proportional benefits of the special purpose vehicle.

h) With respect to the issue of income deferral, we recognize that, in paragraph 24 of the 2015 Discussion Draft, a concern was raised about "non-CIV" funds being used by investors to defer recognition of income on which treaty benefits have been granted. While we understand policy maker concerns about deferral, we believe deferral is a separate issue from the ability of a CIV to obtain treaty benefits. It also is important to note that many countries already have CFC rules and similar legislation dealing with income deferral. To the extent such domestic legislation is absent or deficient, we believe that amending domestic legislation is the best approach to dealing with issues of income deferral. In any event, we would note that work is already being undertaken under BEPS Action 3 with a view to strengthening CFC rules and accordingly addressing regimes that permit income deferral.
Lastly, we note that if a treaty includes CIVs as residents, then the tax regime applicable to CIVs should not be treated as a “special tax regime” (paragraph 53 of 2015 Discussion Draft). This is already envisaged in sub-paragraph (vii) of Proposal 1 but in our view the exemption should apply to any CIV and should not specify any additional criterion such as 'widely held', 'diversified portfolio' etc.

If you have any questions regarding any of the information provided above, or if we can provide further information with respect to the application of the limitation on treaty benefits to private investment funds, please do not hesitate to contact Benjamin Allensworth or me at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice-President and Managing Director, General Counsel
Schedule

Basic "Master-feeder" Structure

U.S. Tax – Exempt Investors

Foreign Investors

Offshore Feeder, Ltd. (Cayman Islands)

Master Fund, LP (Cayman Islands)

U.S. Taxable Investors

Onshore Feeder, LP (Delaware)

SPV

SPV

SPV
Dear Ms de Ruiter

Revised discussion draft on Action 6 (Preventing Treaty Abuse)

We welcome the opportunity to comment on the revised discussion draft issued under BEPS Action 6 issued on 22 May 2015 (the “Revised Discussion Draft”).

Matheson is an Irish law firm and our primary focus is on serving the Irish legal and tax needs of Irish and international companies and financial institutions doing business in Ireland. Our clients include over half of the Fortune 100 companies. We also advise seven of the top ten global technology companies and over half of the world’s 50 largest banks. We are headquartered in Dublin and also have offices in London, New York and Palo Alto. More than 650 people work across our four offices, including 75 partners and tax principals and over 400 legal and tax professionals.

In this letter, the “Report” refers to the report issued under BEPS Action 6 in September 2014 report. The “2010 Report” refers to the OECD Report “The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles”. “LOB” refers to the limitation of benefits clause proposed in the Report. “PPT” refers to the principal purposes test proposed in the Report. “CIV” refers to collective investment vehicles 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.

Comments in this letter are made solely on our own behalf.

1. The simplified LOB

• CIVs should be included as a separate category of qualified person in paragraph 2 of the simplified LOB. Failure to do so will undermine the conclusions reached under the 2010 Report and the agreed position reached in respect of CIVs under Action 6.
- Non-CIV funds (including securitisation companies) should be included as a separate category of qualified person in paragraph 2 of the simplified LOB. This would reflect the acceptance that non-CIV funds play an important role in the broader economy. A simplified LOB must be accompanied by a PPT, this should be sufficient to address any concerns about non-CIV funds and securitisation companies being used for treaty abuse.

2 Non-CIV funds

- As a general rule, non-CIV funds should be entitled to claim treaty benefits. We welcome the recognition of the economic importance of non-CIV funds and the acceptance that non-CIV funds should be entitled to avail of treaty benefit where appropriate. In our opinion, the basic principle should be that non-CIV funds should always be eligible to claim treaty benefit, save in clear cases involving treaty abuse.

- The LOB is a wholly inappropriate test for securitisation companies. Securitisation is a fundamental part of the capital markets. Financial regulators are currently seeking to improve and develop the securitisation market. We remain very concerned that insufficient recognition has been given to the economic importance of the securitisation market in Action 6. Securitisation companies should be wholly distinguished from other non-CIV funds such as private equity or REITs. In particular, securitisation companies issue debt securities into clearing systems and accordingly will not be in a position to verify who owns those securities. As a result, securitisation companies cannot confirm if the derivative benefits test or the local ownership provision is satisfied. Accordingly, special provision for such entities must be made in the LOB rule (and Action 6 as a whole) to ensure that the global securitisation market is not undermined by rules designed to address other concerns.

- The derivative benefits provision must be amended. As currently drafted the derivative benefits provision is likely to be of limited assistance to non-CIV funds because of the ‘seven or fewer’ test. The requirement that the interests in the entity seeking treaty relief are held by seven or fewer investors will not be satisfied by the vast majority of non-CIV funds. This arbitrary limitation, which seems to have no policy basis, must be removed.

3 Issues related to the LOB rule

3.1 The derivative benefits provision

- The derivative benefits provision is unnecessarily restrictive. As noted in our previous submissions on the various Action 6 papers, the limitation in the draft derivative benefits provision to entities that are owned by seven or fewer investors is arbitrary and should be removed. There is no policy rationale that justifies limiting the provision in this way. It should not matter if an entity is owned by five or 100 investors if all of those investors are equivalent beneficiaries. We again strongly urge that this limitation is removed.
Special tax regimes provision

- **Stakeholders should be provided a fair opportunity to comment on this new provision.** It is surprising to see two entirely new concepts introduced to the Action 6 proposals at this late stage (the ‘special tax regimes’ provision and the ‘future changes’ provision). No guidance or draft commentary has been provided with the draft provisions. Stakeholders have been requested to keep comments on the Revised Discussion Draft short. However, stakeholders must be given an adequate opportunity to review the draft provisions along with detailed commentary on how it is intended they will operate before considered comments and suggestions can be provided. It will damage the credibility of the consultation process if the new draft provisions are included in the report due to be issued in September. We strongly urge that no final decision on the inclusion of either provision should made until 2016 after full consultation on the proposals.

- **The new provisions go much further than their stated aim.** Both new provisions are designed to deal with concerns some countries had in respect of the derivative benefits provision. It is not clear what those objections are. In any event, the new provisions appear to deny treaty benefit to a much broader range of taxpayers than only those who rely on the derivative benefits provision.

- **If adopted, the ‘special tax regimes’ provision should be limited to payments between related parties.** We note that the ‘special tax regime’ provision is very similar to the provision that has been proposed for inclusion in the US Model Tax Treaty. However, the draft US provision only applies to payments between related parties. That reflects a more practical approach as it does not require the payer to obtain detailed information about the recipient’s tax status (which in a third party context, it is unlikely to get). At the very least, any provision proposed for inclusion in the OECD Model Convention should be limited in the same way.

- **Many of the concepts included in the ‘special tax regimes’ provision are unclear and subjective.** Here are some examples:

  - it is not clear how the ‘effective rate of taxation” should be calculated. Is it a comparison of the cash tax paid by a company in a particular year against accounting profits recognised in that year?;
  - it is not at all clear when an effective rate of taxation would be considered preferential or, what it would be compared to in determining whether it is preferential;
  - arguably, there is nothing to prevent taxpayers that take standard tax deductions for payments made on an arm’s length basis from being treated as benefitting from a special tax regime;
  - arguably, there is nothing to prevent taxpayers that rely on standard tax reliefs (for example tax depreciation, tax losses) in the usual way from being treated as benefitting from a special tax regime (eg, if the tax depreciation differs from accounting depreciation which would often be the case);
treaty relief would only be denied if the taxpayer is subject to a special tax regime “with respect to” interest, royalties or other income. It is not at all clear when a regime would be considered to apply “with respect to” any particular item of income;

it is not clear when a tax regime would be considered to “disproportionately benefit interest, royalties or other income or any combination thereof”;

it is not clear when a "substantial activity requirement" would be considered to be satisfied;

it is unclear what, if anything, contracting states would be permitted to carve out of the special tax regimes provision under paragraph (viii) if only regimes that do not result in a low effective rate of taxation may be carved out.

Definitions would be required for each of the new concepts introduced along with detailed commentary. Indeed, it is difficult to understand or comment on the draft provision in the absence of draft commentary.

The subjective nature of the ‘special tax regimes’ provision will weigh heavily against taxpayers. The absence of a clear definition of ‘special tax regime’ and the subjective nature of the terminology used throughout the provision will permit tax authorities to deny treaty benefits to taxpayers at will. It is unclear how a taxpayer can successfully appeal against a decision made under an inherently subjective and unclear provision. Inclusion of such a provision in double tax treaties will significantly shift the balance of rights away from taxpayers and in favour of tax authorities. The process of claiming treaty relief will be entirely devoid of certainty for taxpayers seeking to rely on double tax treaties that include such a provision. This lack of clarity will undermine the rule of law. As an aside, we note that these comments equally apply to the PPT.

Countries should be permitted to determine for themselves what, if any, of their tax rules or administrative practices amount to ‘special tax regimes’. We note that the US technical explanation accompanying the similar draft US provision states that no US legislation, regulations or administrative practices that apply with respect to interest, royalty and other income would satisfy the definition of ‘special tax regime’. Is it intended that other countries that include a ‘special tax regime’ provision in their treaties should similarly be permitted to determine whether or not any of their domestic provisions or administrative practices amount to ‘special tax regimes’?

The provision will have broad-ranging unintended consequences. It could be used to deny treaty relief to taxpayers that claim deductions for expenses incurred in the usual course of business, including deductions for tax depreciation in respect of investment in fixed assets and expenditure on research and development. It could be used to deny treaty relief to taxpayers who utilise tax losses to shelter taxable profit. Any of these outcomes will negatively affect real business. Is this provision intended to have negative consequences for treasury company activities? Is it intended to have negative consequences for leasing activities?
Non-CIV funds and securitisation companies should be specifically carved out from the ‘special tax regimes’ provision. The absence of a carve-out would undermine their treatment under the LOB.

A time limit should be included in paragraph 3 of the ‘future changes’ provision. Countries who deny treaty benefits under the ‘future changes’ provision should be required to conclude amendments to the treaty to restore the balance of benefits provided within a specified timeframe.

4 Issues related to the PPT

4.1 The anti-conduit rule

The anti-conduit rule should not be applied to CIVs or non-CIV funds. Any attempt to apply an anti-conduit rule to CIVs or non-CIV funds would undermine the conclusions reached under the 2010 Report and the positions agreed to date in respect of CIVs and non-CIV funds under Action 6. The commentary on the anti-conduit rule should be amended to include an explicit statement that it is not designed to apply to CIVs or non-CIV funds.

4.2 Examples for commentary on PPT

Additional examples of the application of the PPT to CIV and non-CIV funds should be included in the commentary. We have provided examples in Schedule 1.

5 Application of the new tie-breaker rule

The conclusions reached on the tie-breaker rule underestimate the difficulties inherent in the approach for taxpayers. Amending the default tie-breaker rule so that residence is determined by mutual agreement ignores how mutual agreement procedures (“MAP”) usually operate in practice. Comprehensive comments were provided by stakeholders under BEPS Action 14 on the inadequacies in practice of MAP. It is unwise to amend the default tie-breaker rule to one based on MAP until it is demonstrated that MAP operates effectively and efficiently. If MAP is retained as the default tie-breaker, time limits for reaching agreement must be included. The statement included in the revised draft commentary (that competent authorities should “deal with it expeditiously and should communicate their response to the taxpayer as soon as possible”) is not sufficient.

Should you wish to discuss any of the comments raised, please let us know.

Yours faithfully

Sent by email

MATHESON
Schedule 1

1 Securitisation company

RCo, a securitisation company resident in State R, was established by a bank which sold to RCo a portfolio of loans and other receivables owed by debtors located in a number of jurisdictions. RCo is fully debt-funded. RCo has issued a single one dollar share which is held on trust and has no economic value. RCo’s debt finance was raised through a note issuance. The notes are widely held by investors and are held in a clearing system and are listed on a recognised stock exchange. To comply with regulatory requirements, the bank also retained debt securities issued by RCo. RCo currently holds 60% of its portfolio in receivables of SMEs resident in State S, in respect of which it receives regular interest payments. Under the tax convention between State R and State S, the withholding tax rate on interest is reduced from 30% to 10%.

In establishing RCo, the bank took into account a large number of issues, including a robust securitisation framework, securitisation legislation, skilled and experienced personnel and support services in State R and the existence of tax benefits provided under State R’s extensive tax convention network. It is likely that a majority of investors in RCo would be financial institutions and pension funds located in OECD member states. Investors’ decisions to invest in RCo are not driven by any particular investment made by RCo and RCo’s investment strategy is not driven by the tax position of the investors. RCo is taxed in State R on income earned and is entitled to a full deduction for interest payments made to investors.

In making its decision to sell receivables owed by companies resident in State S, the bank and RCo considered the existence of a benefit under the State R / State S tax convention with respect to interest, but this alone would not be sufficient to trigger the application of paragraph 7. The intent of tax treaties is to provide benefits to encourage cross-border investment and, therefore, to determine whether or not paragraph 7 applies to an investment, it is necessary to consider the context in which the investment was made. In this example, unless RCo’s investment is part of an arrangement or relates to another transaction undertaken for a principal purpose of obtaining the benefit of the Convention, it would not be reasonable to deny the benefit of the State R / State S tax convention to RCo.

2 CIV

RCo, a collective investment vehicle resident in State R, manages a diversified portfolio of assets. The interests in RCo are widely-held. RCo currently holds 60% of its portfolio in shares of companies resident in State S, in respect of which it receives annual dividends. Under the tax convention between State R and State S, the withholding tax rate on dividends is reduced from 30% to 10%.

RCo’s investment decisions take into account the existence of tax benefits provided under State R’s extensive tax convention network. A majority of investors in RCo are residents of OECD member states or countries with which State S has a tax convention. Investors’ decisions to invest in RCo are not driven by any particular investment made by RCo and RCo’s investment strategy is not driven by the tax position of the investors. RCo is subject to investor protection regulation in State R and is not taxed in State R on income or gains.
In making its decision to invest in shares of companies resident in State S, RCo considered the existence of a benefit under the State R / State S tax convention with respect to dividends, but this alone would not be sufficient to trigger the application of paragraph 7. The intent of tax treaties is to provide benefits to encourage cross-border investment and, therefore, to determine whether or not paragraph 7 applies to an investment, it is necessary to consider the context in which the investment was made. In this example, unless RCo’s investment is part of an arrangement or relates to another transaction undertaken for a principal purpose of obtaining the benefit of the Convention, it would not be reasonable to deny the benefit of the State R / State S tax convention to RCo.
17 June 2015

SENT VIA E-MAIL TO TAXTREATIES@OECD.ORG

Marlies de Ruiter
Head-Tax Treaties, Transfer Pricing and Financial Transactions Division
Centre for Tax Policy and Administration
Organisation for Economic Cooperation and Development
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France

Re: Comments on the OECD Revised Discussion Draft on BEPS Action 6

Dear Ms. De Ruiter:

The National Association of Real Estate Investment Trusts (NAREIT) appreciates the opportunity to provide comments on the OECD’s 22 May 2015 Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse (Revised Discussion Draft). These comments build on our 9 January 2015 comments on the OECD’s 21 November 2014 Discussion Draft on Follow Up Work on BEPS Action 6 Preventing Treaty Abuse (Original Discussion Draft). Like our earlier submission, this submission focuses on the treaty entitlement issues with respect to U.S. REITs.

EXECUTIVE SUMMARY

The Revised Discussion Draft contains a proposal for language to be included in the Commentary to the OECD Model Tax Convention under the proposed LOB provision that would explicitly reference the OECD’s prior work on the treaty qualification and resident status of REITs. This proposed language is a valuable addition to the Commentary and we urge the OECD to include it in its final recommendations under Action 6. The proposal also includes language that would make clear that any specific provision for treaty qualification of CIVs would not be relevant to entities that would be qualified persons under other tests of the LOB provision. This is an important clarification for U.S. REITs and we urge that the OECD include the proposed language in its final recommendations with the addition of a specific reference to REITs as a category of entity that would fall within such language.

1 NAREIT is the worldwide representative voice for real estate investment trusts (REITs) and publicly traded real estate companies with an interest in U.S. real estate and capital markets. NAREIT’s members are REITs and other businesses throughout the world that own, operate, and finance income-producing real estate, as well as those firms and individuals who advise, study, and service those businesses.
The Revised Discussion Draft also contains a proposal for a new provision addressing special tax regimes which excludes specified regimes for investment in real estate. Should the OECD decide to include the special tax regime proposal in its final recommendations under Action 6, we request that it be made clear that the U.S. REIT regime (and tax regimes in the more than 30 countries that have adopted similar REIT regimes) would fall within the specified exclusion.

DISCUSSION

The Revised Discussion Draft addresses the various issues that had been identified in the Original Discussion Draft with respect to the changes to the OECD Model Tax Convention and related Commentary that were proposed in the 16 September 2014 Report on Action 6. These issues include the application of the proposed limitation on benefits (LOB) provision, and treaty entitlement more generally, in the case of collective investment vehicles (CIVs) and other types of investment vehicles.

Commentary Language Related to REITs

The Original Discussion Draft had included introductory language that equated REITs to CIVs in some circumstances and that suggested parallels between REITs and non-CIV investment funds. As discussed in detail in our January submission, while U.S. REITs share some characteristics in common with CIVs, they do not fall within the CIV definition set forth in the OECD’s 2010 CIV report because they do not meet the asset ownership or regulatory regime requirements contained in that definition. Moreover, also as discussed in detail in our January submission, U.S. REITs are not “investment funds,” but rather are active businesses that are characterized as operating companies for a variety of regulatory, capital markets and related purposes in the United States.

We appreciate that the Revised Discussion Draft addresses REITs in a separate paragraph, consistent with their unique characteristics.

Paragraph 20 of the Revised Discussion Draft indicates that the OECD Working Party responsible for the work on Action 6 noted the concern of the REIT industry that the OECD had not in such work confirmed the conclusions of the OECD’s 2008 Report Tax Treaty Issues Related to REITs (REIT Report). We believe that it is critically important to incorporate into the proposed changes to the OECD Model Tax Convention an explicit reference to the prior work done by the OECD on the residence status and treaty qualification of REITs as memorialized in the REIT Report. Therefore, we welcome the proposal, set forth in the Revised Discussion Draft, to add to the proposed Commentary on the proposed LOB provision a footnote that contains both a general reference to the REIT Report and the paragraphs in the existing Commentary on Article 10 that deal with the treaty entitlement of REITs and a specific citation to the particular paragraphs of the REIT Report that address the application of the treaty resident definition to REITs. The Revised Discussion Draft indicates that this proposal will be further discussed by the Working Party at its June meeting. We urge the OECD to include this proposed footnote in the final agreement with respect to the LOB provision and related Commentary.
Paragraph 20 of the Revised Discussion Draft also includes a proposal to add language to the proposed Commentary on the proposed LOB provision that would make clear that, while specific rules regarding the application of the LOB provision may be needed for CIVs, no such special rules would be needed with respect to “an entity that would otherwise constitute a ‘qualified person’ under other parts” of the proposed LOB provision. This reiteration of the availability and application of the “regular” LOB provisions is very important for U.S. REITs which are qualified persons under the LOB provisions in existing U.S. bilateral tax treaties and will be qualified persons under the proposed LOB provision being advanced under BEPS Action 6. As noted above with respect to the proposed footnote, the Revised Discussion Draft indicates that this proposed language is to be further discussed by the Working Party at its June meeting. We urge the OECD to include this language in the final agreement with respect to the LOB provision and related Commentary. In addition, we urge the OECD to add to this language an explicit reference to REITs as an illustration of a category of “entity that would otherwise constitute a ‘qualified person’ under other parts” of the proposed LOB provision. This could be accomplished with for example a parenthetical reference to REITs in the language proposed to be included in the Commentary or a footnote to such language.

Special Tax Regimes

The Revised Discussion Draft includes a new proposal, not included in the Original Discussion Draft, for an addition to the OECD Model Tax Convention to address special tax regimes. Under the proposal, treaty benefits under the provisions related to interest, royalties, and other income would be denied in the case of persons that are subject to a special tax regime with respect to the particular category of income. For this purpose, a special tax regime with respect to an item of income or profit would mean a legislative or regulatory provision or administrative practice that “provides a preferential effective rate of taxation to such income or profit, including through reductions in the tax rate or the tax base.” Several exclusions from special tax regime status are provided, including an exclusion for a provision or practice “that facilitates investment in widely-held entities that hold real property (immovable property), a diversified portfolio of securities, or any combination thereof, and that are subject to investor-protection regulation in the Contracting State in which the investment entity is established”.

The special tax regime proposal was tabled by the U.S. delegate to the Working Party and it mirrors a draft modification to the U.S. Model Tax Convention that has been released by the U.S. Department of the Treasury for consideration and comment. The draft U.S. Model provision is accompanied by a description in the form of draft Technical Explanation language that provides that the exclusion specified above applies to U.S. REITs, noting that they are designed to facilitate collective investment and are subject to investor-protection regulation. In this regard, as discussed in detail in our January submission, U.S. REITs are not generally within the scope of the Investment Company Act of 1940, which regulates the organization and disclosure of financial information of entities that engage primarily in investing, reinvesting, and trading in securities and whose own securities are offered to the investing public. However, U.S. REITs that are registered with the U.S. Securities and Exchange Commission, which is the case for REITs that are publicly traded on a stock exchange or whose interests are sold through broker-
dealers, are subject to provisions in the Securities Exchange Acts of 1933 and 1934 that contain rigorous disclosure obligations. The draft U.S. Technical Explanation language reflects the determination that these obligations are sufficient for U.S. REITs that are widely held to meet the requirements for the specified exclusion from the definition of special tax regime.

The Revised Discussion Draft indicates that the Working Party has concluded that it will need to reach decision on this proposal with respect to special tax regimes at its June meeting, taking into account the comments that are received. Should the Working Party decide to include the special tax regime provision in its recommendations, we request that the Commentary language accompanying such provision include an explicit statement that the U.S. REIT regime qualifies for the exclusion from special tax regime status for legislation that facilitates investment in widely-held entities that hold real property. We note that more than 30 other countries have adopted REIT rules and that the exclusion from special tax regime status should apply to them as well.

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NAREIT appreciates the OECD’s focus on the treaty qualification of REITs in the Revised Discussion Draft, which builds on the important work that was done by the OECD in connection with the 2008 REIT Report. NAREIT welcomes the opportunity to provide these further comments, which are intended to clarify the treatment of U.S. REITs under new proposals contained in the Revised Discussion Draft.

We would be happy to discuss the matters addressed in this letter or to respond to questions or to provide additional information. I can be reached at (202) 739-9408 or tedwards@nareit.com and Dara Bernstein, NAREIT’s Senior Tax Counsel, can be reached at (202) 739-9446 or dbernstein@nareit.com.

Respectfully submitted,

[Signature]

Tony M. Edwards
Executive Vice President and General Counsel

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NATIONAL ASSOCIATION OF REAL ESTATE INVESTMENT TRUSTS®

289
June 17, 2015

Attn. Marlies de Ruiter
Head of Tax Treaties, Transfer Pricing and Financial Transactions Divisions
Organisation for Economic Cooperation and Development
Centre for Tax Policy and Administration

Re: Comments with Respect to May 2015 Revised Discussion Draft
"BEPS Action 6: Prevent Treaty Abuse"

Dear Ms. de Ruiter:

The National Association of Publicly Traded Partnerships ("NAPTP")\(^1\) is pleased to provide written comments with respect to the Revised Discussion Draft referenced above with respect to the entitlement of treaty benefits of Collective Investment Vehicles ("CIVs") and similar vehicles.

NAPTP is a trade association representing U.S. publicly traded limited partnerships, more commonly known as master limited partnerships ("MLPs"). NAPTP currently has 157 full and associate members and represents over 100 MLPs. NAPTP appreciates the opportunity to comment on this matter. Background on MLPs is provided in our letter dated January 8, 2015, and attached hereto. Very generally, MLPs have the following features: (1) they are taxed as partnerships for U.S. Federal income tax purposes, which in practice results in MLPs distributing some or all of their available cash flows each year to their investors; (2) their interests are widely-held and traded on U.S. regulated public exchanges; and (3) the business activities that may be conducted by MLPs are limited by U.S. Federal income tax law to certain activities that were historically conducted in partnership form, primarily in the natural resources sector. Natural resource MLPs currently constitute about 80 percent of MLPs by number, and about 85 percent of the MLP market capital.

NAPTP reiterates its prior comments that the treatment afforded CIVs to ensure appropriate entitlement to tax treaty benefits should be extended to MLPs because they are widely-held and subject to investor-protection regulation in the country in which they are established. This letter provides recommended language related to the presentation of the proposed Limitation on Benefits ("LOB") rules in the OECD Model Tax Convention and Commentaries as well as in the definition of Special Tax Regime.

\(^1\) The members of NAPTP are listed on Attachment 1.
May 2015 Revised Discussion Draft Treatment of CIVs and Similar Vehicles

The May 2015 Revised Discussion Draft addresses the entitlement to treaty benefits of CIVs and similar vehicles in two contexts – the application of LOB rules, and the entitlement to treaty benefits of income taxed under a special tax regime. In the context of LOB rules, the Revised Discussion Draft concludes that subparagraph 2(f) of the LOB rule in the Report on the work on Action 6, which itself references relevant paragraphs of the Commentary to Article 1, adequately addresses the treatment of CIVs, and that a footnote should be provided that references the treatment of Real Estate Investment Trusts (REITs). For these purposes, CIVs are defined as 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.

In the context of special tax regimes, the Revised Discussion Draft includes proposed language that would deny tax treaty benefits to income taxed under a special tax regime unless, among other things, such regime “facilitates investment in widely-held entities that hold real property (immovable property), a diversified portfolio of securities, or any combination thereof, and that are subject to investor-protection regulation in the Contracting State in which the investment entity is established.” The Revised Discussion Draft explains that the treatment of non-CIV funds and the proposals related to special tax regimes would be discussed in meetings in late June and possibly thereafter.

Recommendation: Neutral Treatment Regardless of Underlying Investments

The treatment of CIVs in the Revised Discussion Draft is based on two rationales. First, an investor pooling its capital with other investors in a widely-held vehicle should not be in a worse position than it would have been had it invested directly in the underlying income producing property held by the vehicle. Second, procedural or administrative accommodations should be afforded to CIVs because of the practical difficulties of determining the tax treaty eligibility of each of its owners on a daily basis. It is noteworthy that neither rationale depends on the type of income producing property held by vehicle. Notwithstanding this, the relevant language referenced or provided in the Revised Discussion Draft is limited to vehicles that invest in a diversified portfolio of securities or real property.

NAPTP recommends that the relevant language referenced or provided in the Revised Discussion Draft be modified to provide equal treatment to all vehicles that are widely-held entities and subject to investor-protection regulation in the Contracting State in which the entity is established. Accordingly, NAPTP recommends the following revisions be made to the Commentary to Article 1 of the OECD Model Tax Convention (the “Commentary”).

First, the language in the Commentary providing considerations and alternatives related to the treaty eligibility of CIVs (notably paragraphs 6.8 – 6.34 of the Commentary on Article 1) should be expanded to include all vehicles that raise similar issues regardless of the nature of the income producing property they hold by adding the following language to paragraph 6.8 of the Commentary:
The issues discussed in paragraphs 6.8 – 6.34 are also relevant to vehicles that are widely-held and are subject to investor-protection regulation in the country in which they are established, regardless of the income producing property held by such vehicles. Accordingly, countries may consider extending the treatment provided to CIVs to all vehicles that are widely-held and are subject to investor-protection regulation in the country in which they are established.

Second, the definition of a “special tax regime” to be included in Article 3 of the Commentary should not include widely-held entities that are subject to investor-protection regulation in the country in which they are established. Accordingly, proposed subparagraph vii) of the definition of special tax regime, which provides an exception for certain vehicles, would be revised as follows:

vii) facilitates investment in widely-held entities that hold real property (immovable property), a diversified portfolio of securities, or any combination thereof, and that are subject to investor-protection regulation in the Contracting State in which the investment entity is established

* * * * * *

We appreciate your willingness to consider this submission as you continue your work on Action 6. Please let us know if you have any questions.

Sincerely yours on behalf of NAPTP,

/s/ Linda E. Carlisle

/s/ Rocco V. Femia

Miller & Chevalier Chartered Counsel to NAPTP
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January 8, 2015

Attn. Marlies de Ruiter  
Head of Tax Treaties, Transfer Pricing and Financial Transactions Divisions  
Organisation for Economic Cooperation and Development  
Centre for Tax Policy and Administration  

Re: Comments with Respect to November 2014 Public Discussion Draft  
"Follow Up Work on BEPS Action 6: Preventing Treaty Abuse"

Dear Ms. de Ruiter:

The National Association of Publicly Traded Partnerships ("NAPTP")\(^2\) is pleased to provide written comments with respect to the Public Discussion Draft referenced above with respect to the entitlement of treaty benefits of Collective Investment Vehicles ("CIVs") and similar vehicles.

NAPTP is a trade association representing U.S. publicly traded limited partnerships, more commonly known as master limited partnerships ("MLPs"). NAPTP currently has 157 full and associate members and represents over 100 MLPs. NAPTP appreciates the opportunity to comment on this matter. In general, NAPTP believes that the treatment afforded CIVs to ensure appropriate entitlement to tax treaty benefits should be extended to MLPs because they are widely-held and subject to investor-protection regulation in the country in which they are established, and the income earned by such MLPs is subject to tax in the country in which they are established at the investor level on a current basis.

MLPs – In General

MLPs have been in existence in the United States since 1981, and they were first created to allow businesses to raise capital from individual investors who could not afford the more sizeable investments often demanded by non-traded partnerships. The majority of the investors providing this capital are individual U.S. investors. MLPs are traded on U.S. stock exchanges, are widely held, and are subject to investor protection regulation in the United States.

MLPs typically are organized as limited partnerships or limited liability companies under the laws of one of the states of the United States. Their distinguishing features, which are discussed in more detail below, are: (1) they are taxed as partnerships for U.S. Federal income tax purposes; (2) their interests are widely-held and traded on U.S. regulated public exchanges;

\(^2\) The members of NAPTP are listed on Attachment 1.
and (3) the business activities that may be conducted by MLPs are limited by Federal income tax law to certain activities that were historically conducted in partnership form.

The taxation of MLPs under U.S. Federal income tax law differs from the standard corporate taxation of U.S. publicly traded companies. MLPs are taxed under the rules applicable to partnerships. As a general matter, partnerships are treated as fiscally transparent or "pass-through" entities for tax purposes. Thus, no tax is paid at the partnership level. A partnership's income is considered earned by all the partners; it is allocated among all the partners in proportion to their interests in the partnership, and each partner pays tax on his or her share of the partnership income. Because partners are subject to tax on the income of the MLP regardless of whether the income is distributed, in practice MLPs distribute some or all of their available cash flows each year.

Historically, all widely-traded U.S. partnerships were taxed in this fashion with all income "passing through" the entity to the individual investors, who then were subject to tax on their share of the income generated by the MLP. However, changes in law in 1987 limited pass through tax treatment to publicly traded partnerships engaging in only certain types of activities that historically had been conducted by non-traded partnerships, primarily in the natural resources sector. As a result, natural resource MLPs currently constitute about 80 percent of MLPs by number, and about 85 percent of the MLP market capital. At the end of December 2014, the total market capital of MLPs was about $581 billion, of which about $489 billion was in the natural resource sector.

The MLP structure provides small individual investors with opportunities to invest in capital-intensive businesses with a lower (but generally steady) rate of return through readily tradable partnership interests. This investor base, however, gives rise to the same investor tracing concerns described for CIVs in paragraphs 18 – 21 of the OECD publication, "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles", adopted by the OECD Committee on Fiscal Affairs on April 23, 2010.

MLPs – Cross-Border Investment and Activity

While there is no restriction on the type or nationality of investors in MLPs, as noted above investors in MLPs organized in the United States and traded on U.S. exchanges are primarily U.S. individuals as well as the U.S. corporations that formed the MLP. There are several practical reasons for this. Non-U.S. investors typically do not invest in MLPs because such investments expose them to unfavorable substantive and administrative U.S. Federal and state income tax consequences. In particular, the activities of a U.S. MLP are attributed to foreign investors, subjecting them to substantive U.S. Federal and state tax and reporting requirements comparable to those imposed on foreign persons that directly conduct trades or businesses in the United States. Distributions are subject to withholding tax to the extent they are attributable to income effectively connected to a U.S. trade or business, and investors

3 In addition to natural resource activities, U.S. MLPs may be used for traditional investment activities.
generally are required to file tax returns with the U.S. Internal Revenue Service. Investments by foreign persons in U.S. widely-held companies taxed as corporations do not carry such negative consequences.

In addition, wealthy U.S. investors have access to opportunities to invest in capital-intensive businesses in the natural resources sector through direct investments such as non-traded partnerships, the income from which is subject to a single level of U.S. tax. MLPs were designed to offer small U.S. investors similar investment opportunities, and therefore are attractive to such investors.

There are no restrictions on the location of U.S. MLP business investments or activities. Accordingly, MLPs may engage directly or indirectly in business activities outside the United States. This may be the case, for example, when integrated natural resource facilities, such as pipeline systems, cross borders. Accordingly, U.S. MLPs may earn and be subject to tax on income from business activities in other jurisdictions. To the extent that U.S. MLPs structure these activities in local entities, such entities are subject to local country income tax and withholding taxes are imposed on dividend distributions or payments of interest from such entities.

Application of Tax Treaties to MLPs

The issues raised with respect to the application of tax treaties to CIVs, which have been explored by the OECD and are reflected in paragraphs 6.8 – 6.34 of the Commentary to Article 1 of the OECD Model Convention (the "Commentary"), are also raised in the context of U.S. MLPs. Section 6.8 of the Commentary defines CIVs as 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. Paragraph 6.21(b) of the Commentary, however, permits treaty negotiators to specify the categories of investment funds, arrangements, or entities to which a CIV provision would apply. As is the case with CIVs described in paragraph 6.8 of the Commentary, all U.S. MLPs are widely-held and are subject to investor-protection regulation. In contrast to CIVs, however, U.S. MLPs allow small investors to pool their capital to invest in business assets in certain limited sectors, predominately natural resources, rather than in equity or debt securities issued by such businesses or other entities.

This one difference between U.S. MLPs and CIVs should not cause tax treaties to treat U.S. MLPs and CIVs, as defined in paragraph 6.8 of the Commentary, differently for two reasons. First, the treatment of CIVs in the Commentary is based on a desire to ensure that an investor pooling capital with other investors in a widely-held vehicle be in no worse a position than it would have been had it invested directly in the underlying income producing property held by the vehicle. See, e.g., paragraphs 6.8 and 6.23 (noting favorably the tax policy goal of neutrality as between direct investments and investments through a widely-held vehicle). This tax policy goal is equally applicable to U.S. MLPs. Second, the procedural or administrative accommodations afforded to CIVs because of the practical difficulties of determining the tax treaty eligibility of each of its owners on a daily basis are equally justified in the case of U.S. MLPs given the fact that U.S. MLP interests are widely held and traded on regulated exchanges.
Investors in U.S. MLPs should also be able to claim, directly or indirectly, appropriate tax treaty benefits on non-U.S. source income earned by such MLPs under standards that are clear, practicable, and take into account the widely-held nature of MLPs. Accordingly, the treatment provided CIVs to ensure appropriate entitlement to tax treaty benefits should be extended to MLPs that are widely-held and subject to investor-protection regulation in the country in which they are established, provided that the income earned by such MLP is subject to tax at the investor level on a current basis.

There are two classes of issues related to the application of tax treaties to CIVs and U.S. MLPs. The first is the substantive entitlement to treaty benefits by such vehicles, either in their own right or on behalf of their investors. The Commentary provides for several alternatives in this regard, including the provision of treaty benefits to a vehicle organized in a country based on the extent to which the vehicle is owned by same-country treaty-eligible investors or based on the extent to which the vehicle is owned by treaty-eligible investors in the same country or third countries. See paragraphs 6.21 and 6.26. The Commentary also includes an alternative by which a vehicle that is publicly traded in its country of organization would be entitled to treaty benefits without regard to the residence of its investors. See paragraph 6.32. This alternative is justified on the basis that a publicly-traded vehicle cannot be used effectively for treaty shopping. Each of these proposals has a strong policy basis as each has the effect of putting the investor in the vehicle in no worse a position than it would have been in had it invested directly in the underlying income producing property held by the vehicle rather than pooled its capital with other investors. See, e.g., paragraphs 6.8 and 6.23 (noting favorably the tax policy goal of neutrality as between direct investments and investments through a widely-held vehicle).

NAPTP endorses these approaches and recommends they be extended to U.S. MLPs.

The second class of issues relates to procedural or administrative standards for actually determining, claiming, and providing treaty benefits. The OECD has undertaken several projects in recent years aimed generally at simplifying and harmonizing countries’ treaty relief withholding procedures, including the Treaty Relief and Compliance Enhancement ("TRACE") system, and at providing practical rules in the context of CIVs that are widely held. In cases where the entitlement to treaty benefits depends on the extent to which investors would have been entitled to treaty benefits on direct investments, paragraphs 6.29 – 31 of the Commentary acknowledge that it would be impractical for widely-held vehicles to collect investor ownership information on a daily basis. It therefore concludes that countries should be willing to accept practical and reliable approaches that do not require daily tracing.

The Commentary provides two examples of "practical and reliable" approaches. First, countries could presume that all investors are resident in the country of organization of the vehicle where there are circumstances that discourage investment by third country residents, as is the case with U.S. MLPs. Paragraph 6.30. Second, countries could require the vehicle to disclose the extent to which investors are treaty-eligible on an annual basis, or if conditions suggest that turnover in ownership is high, on a quarterly basis. Paragraph 6.31. Again, NAPTP supports simplifying and harmonizing countries' treaty relief provisions and recommends that they be extended to U.S. MLPs. Moreover, with respect to U.S. MLPs, NAPTP recommends that countries presume that all investors are U.S. persons because of the practical obstacles and
disadvantages that discourage non-U.S. investment. As noted above, interests in U.S. MLPs are generally not marketed to non-U.S. investors and are not attractive to non-U.S. investors because the ownership of such interests would subject non-U.S. investors to U.S. Federal and state tax and reporting requirements comparable to those imposed on foreign persons that directly conduct trades or businesses in the United States, including the application of U.S. withholding tax on distributions at generally the highest U.S. income tax rates.

Like other commentators, NAPTP is concerned that the OECD’s March 2014 Discussion Draft on “Preventing the Granting of Treaty Benefits in Inappropriate Circumstances” did not appropriately reflect paragraphs 6.8 – 6.34 of the Commentary which deal with potential treaty abuse issues in the context of CIVs. NAPTP believes that the alternatives provided in paragraphs 6.21, 6.26, and 6.32 of the Commentary, which are outlined above, adequately address potential treaty abuse issues, and that no further limitation on benefits provisions or the imposition of a principle-purpose test is needed with respect to CIVs or U.S. MLPs. These alternatives permit treaty benefits to the extent the investors in such vehicles would be entitled to such benefits, achieving the goal of neutrality as between direct investments and investments through widely-held vehicles. Further, these alternatives allow due flexibility to countries in determining the extent to which investors would be so entitled to treaty benefits (e.g., on a presumptive basis under appropriate circumstances, as in the case of U.S. MLPs). Accordingly, widely-held CIVs and U.S. MLPs that meet the requirements set out in the Commentary should be entitled to treaty benefits.

In summary, the OECD should ensure that the treatment afforded to CIVs also is afforded to similar vehicles that raise similar policy considerations. U.S. MLPs are similar to widely-held CIVs that have been the subject of the OECD’s work because they are widely-held and subject to investor-protection regulation in the country in which they are established. As noted above, the only distinction between CIVs (as defined in paragraph 6.8 of the Commentary) and U.S. MLPs is that CIVs invest indirectly in operating businesses by holding a diversified portfolio of securities, whereas U.S. MLPs invest directly in operating businesses such as pipelines or other natural resource businesses. In cases where U.S. MLPs receive income from sources outside

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their country of organization, however, the tax treaty issues faced by MLPs and their investors are identical to those faced by CIVs.

* * * * * *

We appreciate your willingness to consider this submission as you continue your work on developing a final version of the Discussion Draft. Please let us know if you have any questions.

Sincerely yours on behalf of NAPTP,

/s/ Linda E. Carlisle

/s/ Rocco V. Femia

Miller & Chevalier Chartered
Counsel to NAPTP
MEMBERS OF THE NATIONAL ASSOCIATION OF PUBLICLY TRADED PARTNERSHIPS
Publicly Traded Partnership Members

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June 17, 2015

By email

Ms. Marlies de Ruiter
Head of the Tax Treaty, Transfer Pricing and Financial Transactions Division
Centre for Tax Policy and Administration
OECD/CTPA
taxtreaties@oecd.org

Re: Comments on Revised Public Discussion Draft, “BEPS Action 6: Prevent Treaty Abuse

Dear Ms. de Ruiter:

The National Foreign Trade Council (NFTC), organized in 1914, is an association of some 250 U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial and service activities, and our members have for many years been significant investors in many countries, including all of the OECD member countries and the G20 countries.

NFTC seeks to foster an environment in which companies can be dynamic and effective competitors in the international business arena. To achieve this goal, businesses must be able to participate fully in business activities throughout the world, through the export of goods, services, technology, and entertainment, and through direct investment in facilities abroad. As global trade grows, it is vital that companies be free from double taxation that can serve as a barrier to full participation in the international marketplace. Tax treaties provide the certainty and stability in the investment environment that is necessary to allow business to participate in the global marketplace. That is why NFTC has long supported the expansion and strengthening of the U.S. tax treaty network.

I am writing in response to the Revised Public Discussion Draft released May 22, 2015 in connection with the BEPS Action Plan, entitled “BEPS Action 6: Prevent Treaty Abuse” (the “revised Discussion Draft”). According to the OECD, most of the proposals included in the revised Discussion Draft are in response to public comments on the previous Discussion Draft (November 21, 2014) but it also contains new proposals not included in the previous Draft.

The NFTC generally supports the adoption of anti-treaty shopping provisions in treaties. In treaties, governments often reduce source country taxation on nonresidents. In order to be willing to do so, governments negotiate for reductions in foreign taxation on their own residents. As double and excessive taxation are reduced between the two states, trade between them is
enhanced. If the residents of a non-treaty state are able to access an income tax treaty between two other states, the residents of that third country will have no reason to urge their government to make the concessions required to enter into an income tax treaty with either of the two aforementioned states; and that third country’s government would gain nothing, and only lose revenue, by entering into such treaties. Thus, well-crafted anti-treaty shopping measures further the development of tax treaty networks.

However, if these measures are overly restrictive they can undermine the tax treaty network by shutting off legitimate businesses from access to treaties. Consequently, NFTC generally supports the adoption of anti-treaty shopping measures, but it also strongly believes that efforts in this regard must not distract from the primary purpose of income tax treaties, which is to prevent double taxation and provide taxpayers with a stable cross-border investment environment which one government alone cannot provide. As discussed more fully below, NFTC believes that the treaty shopping proposals in the Discussion Draft could result in the subjective application or denial of treaty benefits.

**Anti-treaty Shopping Provisions**

The revised Discussion Draft includes a Simplified Limitation on Benefits (LOB) provision. This rule relaxes a number of the common LOB tests: 1) it simplifies the public trading test by eliminating primary trading/management control tests, 2) eliminates base erosion components of ownership-based tests, 3) it reduces ownership threshold and simplifies the derivatives benefit test. The Simplified LOB lacks a rule to qualify pensions, charities, and collective investment vehicles for treaty inclusion. The Simplified LOB is intended to be coupled with a Principal Purpose Test (PPT), and is not intended to be a standalone provision. Passing the Simplified LOB does not mean that the PPT could not also apply.

The NFTC is concerned that by combining the Simplified LOB with the PPT, that it will be hard to determine if a company qualifies for treaty benefits. Business needs clarity and certainty in determining if treaty benefits will apply before they make an investment in a treaty partner country. The PPT is subjective and the revised Discussion Draft does not specify how the “Principal Purpose” will be determined by governments. Determining whether treaty benefits will apply to an investment should be done expeditiously or it could have a negative effect on global commerce.

**Specific Anti-Abuse Rules**

**Intermediate Owners**

The November Discussion Draft included a requirement in the subsidiary of public company test, the ownership-base erosion test, and the derivatives benefit test, that each intermediate owner be a resident of either of the contracting states. The revised Discussion Draft observes that the purpose of the intermediate resident requirement is to prevent the interposition of a company in a tax haven to which base-erosing payments could be made. The policy rationale behind the restriction on intermediate owners is not clear and would result in ineligibility for treaty benefits for companies where no treaty shopping is present. The potential for base-erosing payments to a tax haven company has nothing to do with whether the recipient is an intermediate owner; the recipient could readily be an entity that is not in the chain of ownership. The only relevance of
an intermediate owner is that dividends can be paid to the intermediate owner and those dividends would rarely, if ever, be deductible in the tested company making the payment. Any treaty-benefited income has been fully included in the income of the tested entity without deduction for dividend payments funded by that income. Any payments made by the intermediate owner do not erode the tax base of the tested company.

**Special Tax Regimes**

The revised Discussion Draft includes proposals designed to address some of the objections to the addition of a derivative benefits provision in the LOB rule. One provision is designed to deal with “special tax regimes” and the other would make a tax treaty responsive to future changes in a country’s domestic tax laws.

New provisions would be added to articles 11 (Interest), 12 (Royalties), and 21 (Other Income) providing that payments of such income are not eligible for tax treaty benefits if beneficially owned by a person subject to a special tax regime. A “special tax regime” would be defined as any legislation, regulation, or administrative practice that provides a preferential effective rate of taxation to such income or profit including through reductions in the tax rate or the tax base. With regard to financing income, the term “special tax regime” includes notional interest deductions that are allowed without regard to liabilities for such interest. Several exceptions apply. The exceptions are meant to narrow the special tax regime rule, but the NFTC is concerned that rule is still overly broad and subject to misinterpretation. A large number of provisions could be considered to be special tax regimes that could result in the denial of treaty benefits. The NFTC is concerned that the broad scope of this provision will lead to considerable uncertainty and controversy. This is a new rule, and because of the BEPS short-time frame, is not available for a public consultation. We recommend that this provision be included with the OECD work on Harmful Tax Practices, and be further reviewed. The primary purpose of income tax treaties is to prevent double taxation and to provide taxpayers with a stable cross-border investment environment. This provision does not accomplish that goal and should be removed from the treaty work moving forward.

**Partial Treaty Termination Because of Subsequent Changes in Tax Laws**

The revised Discussion Draft proposes a new rule which provides that if, at any time after the treaty signing, either contracting states provides an exemption from taxation to resident companies for substantially all foreign source income, the provisions of treaty articles 10 (Dividends), 11 (Interest), 12 (Royalties) and 21 (Other Income) may cease to have effect with regard to those articles. The NFTC is concerned that this provision will raise constitutional issues in many jurisdictions, and is an extraordinary measure to add to the Model Convention. It also adds uncertainty for taxpayers as to what treaty benefits apply if a treaty is partially terminated. If a treaty partner makes significant changes to their tax system, it would be better for the treaty partner to renegotiate the treaty based on those changes, rather than have a partial treaty termination. If the treaty no longer applies to particular income, then the treaty should be rewritten to the satisfaction of both contracting parties.

**New Restrictions on the Trade or Business Test**

Under the revised Discussion Draft, a new proposal, specifically identified as a proposal
presented by the U.S. Delegate, relates to the active trade or business test. Under the proposal, the active trade or business test would not allow a resident to attribute the local activities of a connected person if the resident claiming treaty benefits is 1) subject to a special tax regime, or 2) is not engaged in the same or a similar line of business. A holding company, for example, would not be able to qualify for treaty benefits under the active trade or business test. We understand that the trade or business test is included in the LOB article to recognize that a taxpayer engaged in the active conduct of a trade or business in its resident jurisdiction has sufficient nexus to the jurisdiction to establish the absence of a treaty shopping motive with respect to income connected to that trade or business. This provision appears to be designed to prevent a holding company or a financing entity from resorting to the “active trade or business” test in order to satisfy the LOB rule. Denying treaty benefits for dividends from a related business activity in the source state if received by a holding company, but allowing treaty benefits if the company conducting the trade or business received the dividends does not make sense from a policy perspective.

Discretionary Relief

The revised Discussion Draft states that more guidance should be provided about the factors that a competent authority should take into account when considering a discretionary relief request. The revised Discussion Draft also notes that the competent authority that receives a discretionary relief request should process that request expeditiously. Discretionary partial relief may be available where a benefit would be denied to the immediate recipient of the income and a treaty benefit would have been available had the ultimate owner invested directly. Although the NFTC welcomes additional guidance on when and how discretionary relief will be granted, we are concerned that the revised Discussion Draft adds further restrictions on when discretionary relief may be granted. Adding “clear non-tax business reasons”, and a “substantial relationship” to the residence state makes it more subjective to determine when discretionary relief can be granted. How clear does the non-tax business reason need to be? Who determines that clarity? What constitutes a “substantial relationship?” The discretionary benefit test is intended as a safety net for companies that are not treaty shopping, and vests broad discretion to the Competent Authorities to look at each case individually. Adding additional restrictions on when they can review a case seems unnecessary and we recommend that the restrictions be eliminated.

Residency Tie-breaker Rule

The revised Discussion Draft addresses the residency tie-breaker rule by proposing to revise the Commentary under Article 4 of the OECD Model Income Tax convention to clarify that a determination that a person is not a resident of a contracting state under the tie-breaker rule will only apply to disallow benefits to that person and will not affect other provisions where that person’s residence remains relevant to other persons. The revised Discussion Draft simply proposed adding to the Commentary that requests to the Competent Authority regarding residency should be dealt with “expeditiously.” The revised Discussion Draft modifies the November 2014 to change the Competent Authority standard from “required” to “encouraged” and from a fixed time frame for action, to “expeditiously.” The NFTC recommends that the Competent Authority be required to act within a very specific timeframe, such as within 6 months of a specific request.
Conclusion

As stated earlier, the NFTC generally supports the adoption of anti-treaty shopping measures, but it also strongly believes that efforts in this regard must not distract from the primary purpose of income tax treaties, which is to prevent double taxation and provide taxpayers with a stable cross-border investment environment which one government alone cannot provide. Unilateral discretions to deny tax treaty benefits based on subjective criteria should cause concern, not only to taxpayers, but also to tax authorities, as taxing rights may be unexpectedly usurped. The value of tax treaties is significantly reduced if their application becomes less certain.

Sincerely,

Catherine G. Schultz
Vice President for Tax Policy
cschultz@nftc.org
202-887-0278 ext. 2023
Appendix to NFTC Comments on BEPS Action 6: Prevent Treaty Abuse

NFTC Board Member Companies:

McKenna Long & Aldridge LLP
ABB Incorporated
AbbVie Inc.
Applied Materials
British American Tobacco Company
Baxter International, Incorporated
Caterpillar Incorporated
Chevron Corporation
CIGNA International Health Benefits
Cisco Systems, Inc.
Coca Cola Company (The)
ConocoPhillips, Inc.
Deloitte & Touche
DHL North America
eBay Inc.
E.I. du Pont de Nemours & Company
Ernst & Young LLP
ExxonMobil Corporation
FCA US LLC
Fluor Corporation
Ford Motor Company
General Electric Company
Google Inc.
Halliburton Company
Hanesbrands Inc.

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Johnson & Johnson
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Mars Incorporated
Mayer Brown
McCormick & Company, Inc.
Microsoft Corporation
National Foreign Trade Council
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Oracle Corporation
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Prudential Insurance Company
Ridgewood Group International, Limited
Siemens Corporation
Sullivan & Worcester LLP
TE Connectivity
Toyota Motor Sales, USA, Incorporated
Tyco International
United Parcel Service, Inc.
United Technologies Corporation
Visa Inc.
Wal-Mart Stores, Incorporated
NN

Ms. Marlies de Ruiter
Tax Treaties, Transfer Pricing and Financial Transactions Division
OECD / CTPA
2, rue André Pascal
75775 Paris Cedex 16
France

Re Revised discussion draft on BEPS Action 6 ("Preventing the Granting of Treaty Benefits in Inappropriate Circumstances")

Dear Ms. de Ruiter,

NN Group appreciates the opportunity to provide comments with respect to the revised discussion draft on BEPS Action 6. With this letter NN Group seeks to reiterate its concerns with respect to treaty entitlement of widely-held CIVs and non-CIVs under the proposed LOB rules (standard and simplified).

NN Group
NN Group is a Dutch publicly-listed company that is the holding company of various insurance and investment management companies around the world. NN Group’s investment management business offers a wide variety of actively managed investment products and advisory services to institutional and retail customers. NN Group currently manages CIVs and non-CIVs domiciled in Benelux, Poland, Japan and the Cayman Islands. NN Group’s investment management business currently manages EUR 203 billion.

Comments
- We respectfully disagree with the statement in item 14 of the revised discussion draft according to which there is "no need for additional changes to the Report on Action 6 in order to address" issues relating to treaty entitlement of CIVs. Numerous concerns were raised in previous comment letters and we observe that a significant number of them have not been addressed at all in the revised discussion draft.
- One of the main concerns is what seems to be a purely arbitrary differentiation between publicly-traded CIVs, which always qualify as qualified persons, and non-publicly-traded (widely-held) CIVs which have to meet additional conditions in order to be qualified persons. Publicly-traded CIVs and their non-publicly-traded counterparts are very similar in that they both serve the same purpose, i.e. they both enable investors to delegate the management of their savings to professional managers in order to achieve various investment objectives in an efficient and cost-effective manner. Both types of CIVs are variants of the same investment product. They are both close substitutes and compete for the same market. The main difference lies in the way investors access these investment products. Investors in publicly-traded CIVs generally invest in shares or units of such CIVs via the secondary market (i.e. stock exchanges) whereas investments in non-publicly-traded CIVs are mainly done through the primary market. This difference in itself is not relevant to justify diverging tax treatments. Item 6.32 of the Commentary on article 1 correctly points out that a “publicly-traded CIV cannot be used effectively for treaty shopping because the shareholder or unitholders cannot individually exercise control over it”. We
expressly invite your attention to the fact that the same is true for any widely-held CIV, be it publicly-traded or not. This in turn leads us to the conclusion that the “publicly-traded” criterion should be substituted by the “widely-held” criterion when it comes to treaty entitlement of CIVs. An alternative approach, which would achieve the same objective, would be to explicitly list widely-held CIVs in paragraph 2 of the proposed LOB rule as one of the categories of qualified persons.

- We also note that due to critical differences in operating models it is practically impossible to transform a non-publicly-traded widely-held CIV into a publicly-traded CIV in order to avoid the unintended tax consequences of the LOB rule. Therefore the only plausible solution is to adapt the LOB rule so that it ensures a fair and equal treatment for all types of widely-held CIVs. Failure to do so is likely to distort the market by arbitrarily privileging one investment product over another, thereby reducing competition and ultimately harming the investors.
- Finally we note that the rationale outlined above also applies to widely-held non-CIVs.

**Conclusion**

NN Group appreciates the opportunity to offer its views on the revised discussion draft on BEPS Action 6. Please do not hesitate to contact Tjeerd Valk (tjeerd.valk@nn-group.com), Frederik Evelein (frederik.evelein@nn-group.com) or Nenad Ilic (nenad.ilic@nnip.com), should you have any additional questions.

Respectfully submitted,

NN Group,

Nenad Ilic
Senior Tax Specialist
Dear Mrs. De Ruiter,

The NOB (the Dutch Association of Tax Advisers) welcomes the opportunity to provide brief comments on the Revised Discussion Draft (“RDD”) on the Prevention of Treaty Abuse, issued on 22 May 2015.

1. The NOB welcomes the recognition in paragraph 35 of the RDD that EU law issues may lead to changes to the model provisions and the Commentary to deal with those issues. That paragraph goes on to say that alternatives dealing with EU law issues should not be restricted to EU/EEA States to avoid giving “preferential treatment to EU/EEA residents” The NOB observes that the EU/EEA States are obliged by the EU treaty to exercise their taxing powers in accordance with that treaty. There are few groups of countries, if any, to which the same or similar treaty obligations apply. In light of that, treating the EU as one bloc to deal with EU law issues, should not, in our opinion, be viewed as ‘preferential treatment’ of its residents.

2. The NOB notes that the Simplified LOB presented in the RDD still discriminates a company on the basis of the ownership of its shares. We refer to our comments on the September and November 2014 Drafts.

3. While a proposed simplification of the LOB rules is welcome, other important issues (such as the application of treaty benefits to headquarters holding companies provided they have substance in terms of people functions) continue to be unresolved. The distinction made in the RDD between headquarters holding companies and trading companies for the access to treaty protection, is not fair if that headquarters company has substance in that it carries on active functions through its own qualified
employees. Furthermore, the attribution of the activities of operating companies to a holding company in the same State is missing in the Simplified LOB. The NOB thinks that this omission should be rectified in the next draft.

4. The NOB understands that under an LOB – which contains a set of fairly objective criteria - it is up to the taxpayer claiming a treaty benefit to demonstrate that he, she or it qualifies for that benefit. The NOB does not, however, understand why the burden of proof should also be on the taxpayer under the proposed Principal Purposes Test (“PPT”), because this test does not include any objective, verifiable criterion to distinguish treaty shopping from the legitimate use of tax treaties. The NOB is very concerned that the vagueness and subjectivity of this PPT will lead to massive legal uncertainty and an unmanageable number of disputes between taxpayers and tax administrations and between the tax administrations of the countries involved. The various technical examples provided on the operation of the PPT rule foreshadow the difficulty taxpayers will have in proving the requisite facts to prevent denial of treaty benefits. As a result, it will be virtually impossible for many subsidiary companies of multinational groups to determine whether reduced withholding rates apply under a particular treaty. This is entirely counter to the original primary objective of tax treaties: to provide legal certainty that no double taxation will arise from a proposed cross-border business transaction.

5. The NOB therefore proposes that, as a minimum, the PPT-article should contain a rebuttable presumption of non-abuse if the treaty with the jurisdiction of the ultimate parent provides for a rate of withholding tax that is not higher than the rate provided in the treaty with the jurisdiction of the direct recipient of the income.

6. The NOB also proposes to further reduce legal uncertainty by adding to the text of the PPT-article a provision saying that the taxpayer shall be eligible for the treaty benefits if he plausibly demonstrates (a) that, absent any taxation under the domestic tax laws of the State in which the income arises, the taxpayer would have entered into essentially the same arrangement or transaction as the arrangement or transaction the taxpayer actually entered into (except for the language concerning taxation) or (b) that the beneficial owner of that item of income would have been entitled to essentially the same treaty benefits as the taxpayer absent this treaty article, had that beneficial owner received that item of income direct.

7. The NOB would further suggest that if two tax authorities have differing views about whether or not the obtaining of treaty benefits was one of the principal purposes of a transaction or arrangement, there should be rebuttable presumption that the obtaining of treaty benefits was not one of the principal purposes.

8. The NOB would like to propose that to reduce double taxation, it would not be more than fair to provide partial relief from withholding tax on dividends, interest and royalty’s if the treaty with the jurisdiction of the ultimate beneficiary of the income contains a higher rate of withholding tax than the treaty with the jurisdiction of the direct recipient. In that case the withholding tax rate of the former treaty should apply.
That would make the anti-abuse rule proportionate. This comment valid for the PPT as well as for the LOB.

9. The NOB notes that the changes proposed in points 4 through 8 are necessary to ensure that the PPT does not conflict with EU law. For this we refer to the decisions of the European Court of Justice EU in SIAT (C-318/10, para. 58) and ITELCAR (C-282/12, para. 44) which spell out the requirements which an anti-abuse rule must meet to be ‘proportionate’.

10. The NOB welcomes the addition to the Commentary of the example of a ‘regional company’. In this context the NOB would like to reiterate that the Commentary to the PPT-article should be further expanded to include situations that are also not primarily tax-driven, such as companies that serve to reduce the cost of external borrowing of the group or joint venture companies.

11. We reiterate that Action 6 should be limited to combatting treaty shopping and should refrain from denying treaty benefits, for example on the grounds that the recipient of the income benefits from a preferential regime in his home country. Expanding the scope of Action 6 beyond treaty abuse would, in our view, be an inappropiate use of tax treaties and would further complicate their normal application.

12. Like all commentators on the previous drafts on Action 6, we are of the opinion that the tie-breaker rule should not be changed. The selection of the ‘place of effective management’ as the decisive criterion to break the tie, fits in with the nexus approach of the BEPS-project. Letting competent authorities deal with this, would add to unnecessary legal uncertainty and delays.

Yours sincerely,
the Dutch Association of Tax Advisers

Marnix van Rij
Sieste Faber
Bartjan Zoctmulder
SUBMITTED ELECTRONICALLY

June 17, 2015

Marlies de Ruiter
Head, Tax Treaties,
Transfer Pricing and Financial
Transactions Division, OECD/CTPA

Re: Comments on the New Discussion Draft on BEPS Action 6: Preventing Treaty Abuse

Dear Madam:

The Private Equity Growth Capital Council (the “PEGCC”) is pleased to submit these comments on the Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse released by the OECD on 22 May 2015 (the “Revised Draft”). The PEGCC, based in Washington, DC, is an advocacy, communications and research organization established to develop, analyze and distribute information about the private equity and growth capital (together, “private equity”) industry and its contributions to the U.S. and global economy. For further information about the PEGCC and its members, please see our website at www.pegcc.org.

In September 2014, the OECD released its report in respect of the OECD/G20’s BEPS Project Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances (the “2014 Report”). The 2014 Report made a number of recommendations aimed at curtailing treaty abuse, including introducing in treaties (i) limitations-on-benefits provisions that would limit the availability of treaty benefits to certain “qualified persons” within the relevant jurisdiction (the “LOB rule”), and (ii) a more general anti-abuse rule based on the principal purpose of transactions or arrangements (the “PPT rule”). Following the release of the 2014 Report, the OECD released the Public Discussion Draft Follow-up Work on BEPS Action 6: Preventing Treaty Abuse, 21 November 2014 (the “Discussion Draft”), which invited comments on particular issues, including (i) the issues that the proposed LOB rule created for collective investment vehicles (“CIVs”) and non-CIV funds, including private equity funds, and (ii) how the PPT rule would operate in relation to the non-tax motivated use of special purpose vehicles by investment funds. The PEGCC submitted comments on the Discussion Draft in January 2015.

The Revised Draft includes a simplified alternative LOB rule intended to be used in combination with the PPT rule. The simplified LOB rule broadens the derivative benefits provision so that an entity in which more than 75% of the direct or indirect investors are equivalent beneficiaries may be entitled to treaty benefits. The Revised Draft also treats certain CIVs as “qualified persons” eligible for treaty benefits under the LOB rule. It offers additional examples involving holding companies intended to clarify the scope of the PPT Rule. None of these examples, however, relates to non-CIV funds.
While the Revised Draft acknowledges the economic importance of non-CIV funds and discusses their entitlement to treaty benefits, it declined to make the changes recommended by the PEGCC regarding the application of the LOB rule to non-CIV funds and the PPT rule. In the Revised Draft, the OECD working group identified two issues of concern to governments in relation to granting benefits to non-CIV funds: (i) that such funds may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits and (ii) that such funds may allow investors to defer recognition of income on which treaty benefits have been granted.

The PEGCC believes that its comments in relation to the Discussion Draft remain applicable to the Revised Draft. In particular, as described in more detail below, the PEGCC believes that the LOB rule as it stands in the Revised Draft would still substantially and inappropriately limit the ability of private equity funds and their affiliated entities to claim treaty benefits. As a result, the PEGCC continues to support treating private equity funds and their affiliated investment entities as “qualified persons” under the LOB rule.

The PEGCC continues to believe that a properly tailored PPT rule is a better method of addressing potential treaty-shopping concerns with respect to private equity funds than an LOB rule. As it stands in the Revised Draft, however, the PPT rule looks to whether one of the principal purposes of an arrangement or transaction is to obtain treaty benefits, which is overly broad and likely to be applied inconsistently across jurisdictions. The PEGCC recommends that the PPT rule be drafted to apply in cases where it is determined that “the principal purpose” of an arrangement or transaction is to obtain the benefits of a tax treaty.

In addition, the PEGCC believes that the two key concerns raised by the OECD working group in the Revised Draft (i.e., that non-CIV funds may be used by investors for the purpose of treaty shopping and that granting treaty benefits to non-CIV funds would result in the deferral of income for investors) are substantially mitigated in the context of private equity funds, for the reasons discussed below.

Private equity funds are not vehicles for treaty shopping

Private equity funds do not present the treaty-shopping concerns that the 2014 Report seeks to curtail. Private equity funds are closed-end investment vehicles formed for the purpose of pooling capital of a broad base of investors and investing that capital in portfolio companies. As outlined in our prior comments, private equity funds share many of the characteristics of other CIVs as described in the OECD’s 2010 report on The Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles. Notably, similar to CIVs, private equity funds generally have a broad investor base, invest in a broad range of jurisdictions and industries and are subject to substantial regulation.

Private equity funds represent an important source of capital in the global economy, including in emerging markets. In order for private equity funds to continue to operate effectively in cross-border situations, it is essential that an investor’s participation in a fund does not result in a lower level of treaty entitlement than would have been accorded to such investor investing directly.
Investors that participate in private equity funds typically include corporate pension plans, public retirement plans, foundations, university endowments, sovereign wealth funds, insurance companies, banks and, to a lesser extent, high net worth individuals and family offices. Such investors often would be entitled to treaty benefits in their own rights if they invested directly in the underlying investments of the fund. If investing in private equity funds were to curtail such investors’ entitlement to treaty benefits, we believe that it would adversely affect the private equity industry’s ability to attract capital from investors and to invest capital effectively on a multi-jurisdictional basis.

_Private equity funds are not vehicles for deferring the recognition of income by their investors_

The concern that granting treaty benefits to private equity funds may allow investors to defer recognition of income on which treaty benefits have been granted is misplaced. Corporate pension plans, public retirement plans, foundations, university endowments and sovereign wealth funds typically make up a large portion of the investors in private equity funds.1 Such investors are typically exempt from tax, and do not benefit from income deferral.

Even for investors who are subject to tax in their jurisdiction of tax residence, private equity funds are not vehicles for deferring the recognition of income on investments. Private equity funds are organized most frequently as fiscally-transparent limited partnerships in order to achieve tax neutrality and the flow-through of the characteristics of the underlying income realized by the fund. Consequently, taxable investors in such a fund generally are subject to tax currently on their proportionate share of the fund’s income, even if no distribution is made by such fund. Since investors are subject to tax on income at the time such income is realized by the fund, these fund structures generally do not provide the opportunity for investors to defer tax.

In addition, private equity funds typically hold investments for periods of between three and seven years prior to exit. The partnership agreements or other governing documents of private equity funds generally do not permit capital to be reinvested except under very limited circumstances, and typically require that amounts received by the fund from the sale of an investment be distributed promptly to the investors in the fund.

Furthermore, the private equity fund model typically penalizes fund sponsors that do not distribute investment proceeds at the earliest opportunity. The performance of a fund and the remuneration of its sponsors are typically measured by reference to the fund’s internal rate of return, which takes into account both the timing and the quantum of investment returns.

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1 According to Preqin, in 2015, corporate pension funds (14%), public pension funds (29%), foundations (6%), endowment plans (7%), sovereign wealth funds (14%) and government agencies (5%) collectively invested 75% of the aggregated capital currently invested in private equity. Source: 2015 Preqin Global Private Equity & Venture Capital Report, Fig 7.2, at p.77.
Accordingly, private equity funds are incentivized for both marketing and remuneration reasons to return investment proceeds to investors promptly.

Finally, a private equity fund is a limited duration investment entity with a typical term of ten years (subject to extension for up to two or three years if needed). This limited duration reduces opportunities for deferral. Following the termination of the fund, any remaining proceeds are distributed to investors.

**The LOB Rule**

While we appreciate that the LOB rule, and in particular the derivative benefits provision, has been broadened in the Revised Draft, we continue to believe that the LOB rule would make it extremely difficult, if not impossible, for most private equity funds and their affiliated investment entities to qualify for treaty benefits when making cross-border investments.

Most private equity funds and their affiliated investment entities would not qualify for treaty benefits under the “qualified person” test because (i) such funds and their investment entities generally are not publicly traded, and (ii) investors in private equity funds typically represent multiple jurisdictions and, in many cases, more than 50% of a private equity fund’s investors would not be representative of any particular jurisdiction or jurisdictions. Most private equity funds and many of their affiliated investment entities would also not qualify for treaty benefits under the “trade or business” test as their activities are limited to making investments and they do not otherwise carry on an active trade or business.

The application of the “derivative benefits” provision of the LOB rule to private equity funds presents administrative and practical difficulties that would frequently prevent the funds (or their affiliated investment entities) from accessing treaty benefits even in cases where the vast majority of their investors qualify.

As with CIVs, private equity funds may have hundreds of investors and these investors often invest through tiered entities, including other funds. Identifying the ultimate beneficial owners of interests in a private equity fund, including interests that are held indirectly through upper-tier entities would require a level of inquiry that is substantially beyond what is required by currently applicable regimes, including the US FATCA rules. This inquiry would require access to information with respect to indirect investors that the private equity fund may not be able to identify and with which it has no legal relationship.

A private equity fund may also make investments in numerous different jurisdictions, each with different treaty rules. The precise jurisdictions in which a fund will invest are often not known at the time investors invest in the fund, especially for funds with multi-jurisdictional investment strategies. It will often be impractical, if not impossible, for a fund to determine which of its direct and indirect beneficial owners are eligible for benefits in respect of a particular item of income under the treaty of each jurisdiction in which the fund invests and to monitor eligibility on an on-going basis. Even if this level of inquiry were feasible as a practical matter, it would be a time consuming and daunting process, particularly for funds with large numbers of investors,
and would impose substantial additional compliance costs upon funds and their investors. See Example 1 in the Appendix.

Moreover, under the derivative benefits provision’s “all or nothing” approach, a private equity fund relying on the derivative benefits provision would be denied treaty benefits entirely if it fails to meet the more than 75% ownership by equivalent beneficiaries test - in other words even if 75% of its investor base consists of investors that are equivalent beneficiaries and are legitimately eligible for treaty benefits. Such investors making an investment in a private equity fund and otherwise eligible for treaty benefits may find themselves in a worse position by pooling capital through the fund to make investments in portfolio companies than they would have been had they invested directly in the underlying portfolio companies. In addition, as private equity funds generally have limited or no control over changes in the tax status or eligibility for treaty benefits of their investors, there could be no assurance that a particular fund would continue to be eligible for treaty benefits, thereby creating substantial uncertainty for private equity fund investors. See Example 2 in the Appendix.

For private equity funds, identifying and monitoring the ultimate beneficial owners of interests on an ongoing basis is administratively complex and commercially impractical. Furthermore, the rule’s “all or nothing” approach has disproportionate consequences for private equity funds, due to the frequency with which investors participate in funds indirectly. Accordingly, we do not believe that the derivative benefits provision of the Revised Draft provides an effective avenue for private equity funds to access treaty benefits in relation to cross-border investment. For this reason, the PEGCC reiterates its recommendation that private equity funds and their affiliated investment entities be treated as “qualified persons” under the LOB rule. Our proposed approach would not require a look through to the treaty status of any investor in the fund and would not subject the fund to a reporting regime regarding the identity of direct or indirect investors in the fund.

The PPT Rule

The PEGCC believes that treaty-shopping concerns are better addressed through a general anti-abuse rule. The current PPT rule applies to arrangements and transactions with respect to which “one of the principal purposes” is obtaining treaty benefits. We believe that the PPT rule, as currently proposed, is overly broad and imprecise and that it invites a subjective analysis in which different countries may reach different conclusions in applying the PPT test to the same set of facts and circumstances. Such a subjective standard creates uncertainty as to how the rule will be applied from jurisdiction to jurisdiction and frustrates the purpose of tax treaties, which is to promote bona fide cross-border investment. To address these concerns, we reiterate our recommendation that the PPT rule be revised to apply in cases where it is determined that “the principal purpose” of an arrangement or transaction is obtaining the benefits of a tax treaty rather than the more subjective standard of “one of the principal purposes”. Formulating the PPT rule based on the principal purpose of a transaction or arrangement will result in a more objective analysis and will minimize the opportunities for varying interpretations of the same set of facts and circumstances across jurisdictions.
We are particularly concerned that the subjective standard of the PPT rule may make it difficult for private equity funds to be certain that their affiliated investment entities will not be disqualified from the benefits of tax treaties. Private equity funds frequently form investment vehicles in order to make, hold, and finance their investment activities. The reasons that such vehicles are formed include (i) to ensure that fund investors have limited liability in respect of the fund’s investments, (ii) to allow co-investment with management or other investors, (iii) to allow borrowing in relation to the making of an investment to be secured against the property being acquired, and (iv) to provide flexibility for future disposition of the investment or in the case the investment becomes insolvent. In selecting a jurisdiction for incorporating such a vehicle, a fund will consider a range of factors, including the local legal and regulatory environment, the cost of establishing and maintaining the vehicle, and the management expertise available in such a jurisdiction. Depending on the vehicle’s purpose, they may also consider any applicable tax treaties. The PEGCC believes such consideration is appropriate, because the availability of treaty benefits for such vehicles will often serve to put investors in a private equity fund in the same position in which they would have been had they invested directly and is consistent with the objectives of tax treaties. Accordingly, we believe that the commentary to the PPT rule should make clear that the rule is not breached simply because, in establishing an affiliated investment entity as a holding vehicle for the fund, the fund considers the availability of tax treaties before selecting a jurisdiction. See Example 3 in the Appendix.

* * * *

We would welcome the opportunity to discuss any of the points raised in this letter with you.

Respectfully submitted,

Steve Judge
President and CEO
Private Equity Growth Capital Council
APPENDIX

Example 1

• Facts: Fund is a limited partnership organized in State F. Fund has numerous investors, many of which are other entities that themselves have numerous beneficial owners. All of the direct and indirect investors in Fund are tax-resident in States A, B, C and D and are eligible for treaty benefits in relation to a direct investment in State P.

• Facts: Fund will invest in Portfolio Company, which is organized and resident in State P. For non-tax business reasons, Fund has established a holding company ("Holdco") in State A, which has a tax treaty with State P. The treaty between State A and State P includes the simplified LOB rule outlined in the Revised Draft. Holdco does not meet the qualifications of paragraph 2 or paragraph 4 of the LOB rule of the treaty between State A and State P, since it is not publicly traded and does not conduct a trade or business. All of the direct and indirect investors in Fund are equivalent beneficiaries for purposes of the LOB rule in the treaty between State A and State P, so that Holdco should be entitled to treaty benefits in respect of income derived from Portfolio Company.
Comments: In order to claim treaty benefits under the derivative benefits provision of paragraph 3 of the LOB rule in respect of an item of income derived from Portfolio Company, Holdco would need to establish that more than 75% of its investors (directly or indirectly) qualify as equivalent beneficiaries. While Fund may make inquiries to its investors, it has no direct contractual relationship with indirect investors that hold their interests in Fund through other entities. As a result, we expect it would be extremely difficult to establish Holdco’s entitlement to treaty benefits under the treaty between State A and State P. If, given the administrative complexity, Fund is not able to timely confirm the status of 25% or more of its investors (directly or indirectly) as equivalent beneficiaries in respect of an item of income derived from Portfolio Company, Holdco will not qualify for treaty benefits for such income even though 100% of its indirect investors would have been eligible for treaty benefits if they had invested directly in Portfolio Company. In that case, all of the investors in Fund, including those that provided confirmation as to their treaty status to Fund, will be tax-disadvantaged in relation to their investment in Portfolio Company because they invested through Fund rather than directly. This would frustrate the principle of tax neutrality, according to which investors should not be in a worse position in relation to tax treaty benefits if they pool capital to make an investment than if they invest directly. For this reason, we believe it is appropriate for Fund and Holdco to be treated as a “qualified person” under the LOB rule.
Example 2

Facts: The facts are the same as Example 1 above, except that in this case 60% of Fund is owned by “Fund of Funds” (a private equity fund that invests in other private equity funds). For purposes of illustration, assume that 50% of Fund of Funds is owned by Investor Alpha, which is eligible for treaty benefits under the treaty between State A and State P. (Such concentrated ownership would be very unusual, since typically private equity funds have large numbers of investors).

Facts: The treaty between State A and State P includes the simplified LOB rule outlined in the Revised Draft. Holdco does not meet the qualifications of paragraph 2 or paragraph 4 of the LOB rule of the treaty between State A and State P, since it is not publicly traded and does not conduct a trade or business. All of the direct and indirect investors in the Fund are equivalent beneficiaries for purposes of the LOB rule in the treaty between State A and State P, so that Holdco should be entitled to treaty benefits in respect of income derived from Portfolio Company. At the time of the investment in Portfolio Company, Fund is able to
establish that Holdco qualifies for benefits under the derivative benefits provision of the treaty between State A and State P.

- **Facts:** At some point in time following the investment, for some non-tax business reason, Investor Alpha transfers its interest in Fund of Funds to Investor Beta. Investor Beta is eligible for benefits under the treaty between State C and State P and is an equivalent beneficiary for purposes of the LOB rule in the treaty between State A and State P.

- **Comments:** Fund has no control over Investor Alpha’s transfer of its interest, since it has no direct contractual relationship with Investor Alpha. Even though the indirect ownership of Fund has changed, Holdco should remain eligible for treaty benefits under the treaty between State A and State P. However, since Holdco has no direct contractual relationship with Investor Alpha or Investor Beta, it may be a difficult or impossible task for Fund to establish that Investor Beta is an equivalent beneficiary in its own right, so as to demonstrate that Holdco continues to meet the more than 75% ownership requirement by equivalent beneficiaries contained in the LOB rule and, consequently, that Holdco continues to qualify for treaty benefits in relation to income derived from Portfolio Company. If Holdco is unable to obtain timely information from Investor Beta and establish that it continues to qualify for benefits under the treaty, the investors in Fund and in Fund of Funds (including Investor Beta) will be tax-disadvantaged in relation to their investment in Portfolio Company because they invested through Fund rather than directly. This creates uncertainty for investors making an investment in Fund that they would not have if they invested directly in Portfolio Company, and is inconsistent with the principle of tax neutrality. For this reason, we believe it is appropriate for Fund and Holdco to be treated as a “qualified person” under the LOB rule.
Example 3

Facts: The facts are the same as in Example 1 above.

Facts: Fund intends to borrow funds to finance the acquisition of Portfolio Company. For non-tax business reasons, Fund is required to establish Holdco to hold its shares in Portfolio Company. Fund has shortlisted three jurisdictions, including State A, for Holdco, each of which are similarly advantageous from a regulatory, financial, legal and management perspective. After considering the fact that State A is the only one of these jurisdictions with which State P has a tax treaty, the decision is made to establish Holdco in State A.

Comment: In such circumstances, where an investment entity is established for reasons not related to tax, but the availability of treaty benefits is one criterion considered in selecting which jurisdiction is used, the PPT rule should not apply to deny treaty benefits to Holdco. In addition, to address a concern that subjective interpretation of the PPT rule would deny treaty benefits to Holdco, we reiterate our recommendation that the PPT rule be revised to apply in cases where it was determined that the principal purpose of a transaction or arrangement was to obtaining the benefits of a tax treaty, which we believe will result in more objective analysis.
To:

Marlies de Ruiter
Head
Tax Treaties
Transfer Pricing and Financial Transactions Division
OECD/CTPA

Petrofac Group Representations

The Revised Discussion Draft on BEPS Action 6 Prevent Treaty Abuse

In response to the paper issued on 22 May 2015 requesting comments from Business and Industry to the proposals on preventing Treaty Abuse, Petrofac Group (Petrofac) would like to make the following comments.

Petrofac Group Background

Petrofac is a FTSE 250 oilfield services company which operates in 29 countries across the globe. Its primary corporate and operational offices are in UAE, India, Malaysia and the UK; project sites are located in a number of countries where we:

- design and build new oil and gas facilities,
- manage and maintain existing facilities,
- enhance the performance of more mature or marginal facilities, and
- develop and train our customers’ staff to work more effectively and safely.

We operate onshore and offshore, and any of our service lines can be delivered on a standalone basis or they can be integrated together, under a range of commercial models. Our workforce numbers almost 20,000 employees around the world.

Petrofac Position Summary

Petrofac understands that the measures set out in the Revised Discussion Draft have been the subject of extensive commentary and consideration but it is concerned both about the number and complexity of the options that are being proposed for the OECD Model Tax Convention under Action 6. As has been noted by many respected commentators and business leaders it is critical in the current challenging economic environment that the conduct of international business is not impeded by an extended period of uncertainty surrounding how the global treaty network will operate.

Changes to Article X

Petrofac welcomes the proposal to include a ‘simplified’ LoB clause in the OECD Model Tax Convention and agrees that the alternative wording addresses many of the criticisms of the full LoB clauses presented in earlier drafts. However it notes that a number of concerns raised by commentators have not been fully addressed:
1. It remains the case that for a MNE which has to rely on Article X Paragraph 4. b) there is the requirement that in order to qualify for treaty benefits the resident of the Contracting State which derives an item of income must be substantial in relation to the business carried on by the related enterprise in the Other Contracting State. It is possible to envisage numerous examples of normal commercial arrangements with no tax avoidance motive that could fail to meet this requirement. This distorts commercial decision making and forces companies to focus on making a judgement not only as to whether one business is currently substantial in relation to the other but that this will continue to be the case over the life cycle of the relationship. This analysis is made even more problematic by the proposal that the other persons have to be engaged in the same or similar line of business. Petrofac does not support the inclusion of this additional condition and we would like to see clear guidance included in the commentary as to how the “substantial” test should be applied by Contracting States to reduce the level of uncertainty faced by companies carrying on normal non contentious commercial activities.

2. Petrofac agrees with previous commentators that the requirement that each intermediate owner be a resident of either Contracting State (Subdivision 2 c)(ii) of the LoB rule Petrofac) is unduly restrictive and disproportionate and could have a material and unnecessary impact on MNE group holding structures and should therefore be removed. Petrofac requests that despite the OECD’s preference not to hold any further consultation the conclusions of the June 2015 meeting be made immediately public and be the subject of a short consultation process.

Regards

Rod Sayers
Group Head of Tax
Petrofac
Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division  
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2 Rue Andre Pascal  
Paris 75775  
France  
17 June 2015

By e mail to: taxtreaties@oecd.org

**PricewaterhouseCoopers Comment Letter on the OECD Revised Discussion Draft on BEPS Action 6: Preventing Treaty Abuse**

Dear Ms. de Ruiter,

We welcome the opportunity to provide comments on behalf of the PwC network of firms on the Revised Discussion Draft on BEPS Action 6 (RDD). Per your request to keep comments as short as possible, we have limited our comments to issues we consider of key importance. We refer to our previous comments letters of 9 April 2014 and 9 January 2015, which commented more extensively on the Action 6 proposals, many of which remain relevant.

The PwC network of firms is one of the largest providers of global professional services. As such, we believe we bring a perspective that reflects our extensive experience in working with the global business and investment communities and bring an understanding of the practical realities that the impact the Action 6 proposals may have on the conduct of international trade and investment. The OECD faces a formidable task in the development of new rules and standards that are responsive to the concerns raised by BEPS in a short time frame. The Working Group is to be commended for their efforts under these circumstances. Our comments are intended to aid in assuring that the end product achieves the basic goals of BEPS in a manner that is workable, balanced and consistent with the underpinnings of international tax treaty policy. Our aim is to help make sure that the end product is consistent with the fundamental purposes of tax treaties to promote bilateral trade and investment and that the rules needed to combat BEPS are formulated in a manner that provides access to tax treaties to their intended beneficiaries by the promulgation of rules that are adequately targeted and balanced to that end.

**A simplified LOB article**

We welcome the introduction in the RDD of the concept of a simplified limitation of benefits (LOB) article. The detailed provisions of the originally proposed Entitlement to Benefits article (ETB) were modelled on the most recent version of the US LOB. A number of those details were controversial and widely criticized, largely because they would deprive taxpayers that are not treaty shopping of access to tax treaties and would impose new and vague concepts. The US LOB on which the ETB was based contains provisions that are oriented to US domestic policy concerns and the US Treasury is in the process of developing a new US Model Income Tax Convention, including revisions to the LOB. It
would be unfortunate if the OECD were to embody these evolving and controversial provisions in a new OECD Model or in a multilateral convention. Some of the more critical aspects are outlined below.

Unfortunately, the RDD ties the use of the simplified LOB to treaties which combine it with a principal purpose test (PPT) test, which means it would only be available to the limited number of treaties where both treaty partners agree to this combined test. The LOB and the PPT are directed to distinct treaty shopping issues – eligibility of treaty residents for treaty benefits in the case of the LOB and combatting abusive use of treaties by eligible treaty residents in the case of the PPT. These independent standards should not be welded together. Some countries will prefer to deal with anti-abuse through a PPT and others may consider a more targeted anti-abuse rule the best avenue. That choice should not dictate whether a simplified LOB is used. We urge that the OECD opt for the simplified version, leaving it to bilateral negotiation to tailor a treaty LOB to the needs of the treaty partners.

**CIVs and Non-CIVs**

We welcome the RDD confirmation that the LOB should apply to CIVs and non-CIVs as set out in the September 2014 Report on Action 6. This recognizes the importance of collective investment vehicles in an efficient operation of the global capital markets. If a LOB does not explicitly set forth how CIVs and non-CIVs are to be accorded treaty benefits - either by opting to include in the treaty one of the six alternatives for specific text spelt out in paragraphs 6.17 and onwards of the Commentary on the Model Article 1, or by following one of these alternatives when settling the wording of an LOB rule in the form in the September 2014 Report – then, many of these forms of collective investment will fail to qualify for treaty benefits and investors in these vehicles will end up paying a tax penalty for investing through the collective vehicle as contrasted with direct investment. Accordingly, there should be a much greater emphasis of the need for treaty partners to follow the recommendations of the 2010 CIV Report in any form of LOB rule, “simplified” or otherwise.

The final report should provide clearer guidance as to where the boundary between CIVs and non-CIVs lies, with broadness of scope being encouraged. For example, the use of an approach as detailed as the UK’s “genuine diversity of ownership” test, as a way of meeting the “widely held” condition, noted at paragraph 13 of the RDD, should be considered further. Similarly, examples of what constitutes “investor-protection regulation” would be useful. For example, confirmation that a fund vehicle whose manager is subject to the full scope of the AIFM Directive within the EU is to be regarded as subject to “investor-protection regulation” would be both useful and reasonable.

Encouragement for implementation of the TRACE project is welcomed. However this should not be seen as allowing Contracting States to be deflected from progress in following the recommendations of the 2010 CIV Report. Agreement on clarifying the tax treaty entitlement of CIVs is essential before TRACE implementation can be effective, and not vice-versa.

The investor base of many investment vehicles is frequently concentrated in large, often tax-exempt organisations and governmental institutions which, if investing directly, would benefit from a further reduced rate of tax (or an exemption often accorded to pension funds and governmental funds). We recommend that CIVs and non-CIVs qualify for treaty benefits if they satisfy a derivatives benefit test similar to that set forth more generally in the simplified LOB. In light of the unique nature of collective investment vehicles, we urge that the required percentage owners of qualified or derivative owners should be the same 50 percent threshold as used in the ownership/base erosion test. This
would ease what would otherwise be a difficult and sometime impractical administrative burden for CIVs and non-CIVs to not only trace the residency of their ultimate investors but also to determine whether they meet the criteria for treaty eligibility. For those for whom the derivative benefits approach is not feasible, we recommend the inclusion of a “look-through” approach as included in the sixth option of the 2010 Report irrespective of whether the CIV is opaque for local tax law purposes, thereby allowing ultimate investors to claim the same treaty benefits that would be available had they invested directly. Tests focused on the eligibility of the investors should allay concerns about treaty shopping. We note that collective investment vehicles will in any event be subject to whatever anti-abuse rule is agreed by the treaty partners although, as noted in our discussion of the PPT, we would urge an example that creates a presumption that the PPT will not apply to collective investment vehicles due to their clear non-tax reasons for existing.

Targeted LOB Proposals

We have commented extensively on many of the detailed aspects of the ETB proposal and refer you to those detailed comments. In the interest of adhering to the request to keep comments brief, we highlight here select key proposals, the resolution of which we view as critically important to the development of a fair and practical approach to LOB, whether found in the text of the LOB or in Commentary.

1. **Discretionary grant of treaty benefits.** It has long been recognized that the objective tests for eligibility for treaty benefits will deny access to the treaty to treaty residents that are not treaty shopping. The discretionary grant provision is a recognition of this reality and is intended to assure those who can establish to the satisfaction of the relevant tax authority that the acquisition, establishment or maintenance of the resident or the conduct of its operations did not have a principal purpose of obtaining the benefits of the treaty. This provision is intended as a safety net for treaty residents. However, the RDD would impose new standards rather than add clarity to the existing standards, including an additional requirement that the claimant have a clear non-tax business reason for establishing residency in the treaty jurisdiction. There are many fact patterns where the ability of a claimant to meet this standard is questionable but the decision to locate in the treaty jurisdiction was not motivated by access to treaty benefits (such as a private equity fund’s acquisition of a publicly traded company). Adding this new hurdle is unnecessary and inappropriate, particularly where the tax authority already has broad discretion in determining whether to grant benefits. Similarly, the RDD could be read to support a determination by a tax authority that a claimant’s considerations for choice of residency included the fact that the jurisdiction had a wide network of tax treaties triggers a principal purpose conclusion, even if the claimant had no interest in the relevant treaty at the time of establishing residency in the country. Further, the discretionary grant process is seriously compromised if there is not a disciplined procedure for assuring prompt resolution of a request for a discretionary grant; simply stating, as suggested in the RDD, that the request should be handled expeditiously is not meaningful. Finally, there should be an opportunity for the tax authority of the country of residence to have a substantive voice in the resolution of a request if a source country is proposing to deny the request.

2. **Intermediate Owners.** The proposal to deny treaty benefits to a subsidiary company where there is an intermediate owner that is not a resident (or, in the case of the derivative benefits test, an equivalent beneficiary) has no defensible policy justification and would severely limit
access to treaty benefits for such subsidiary companies because, either as a result of acquisitions or regional structuring choices, having an intermediate owner in a third jurisdiction is common in the corporate world. A simple example is where a publicly traded company resident in Country A acquires the parent of a corporate group and the parent is in Country B such that the acquired group has a subsidiary in Country A. The RDD offers as a policy reason the fact that base eroding payments can be made by the subsidiary to the intermediate owner. However, base eroding payments can be made by the subsidiary to any member of the corporate group, unrelated to where the recipient is in the chain of ownership. Further, the subsidiary, under most tests, will already have to meet a base erosion test.

3. **Active Business Test.** The active business test treats a company as having adequate nexus to its country of residence if it is engaged in active business in the residence country but limits access to treaty benefits to income connected to that business. In almost all US tax treaties with LOBs, the business activities in the residence country of an affiliate can be attributed to the resident company claiming the treaty benefits. RDD notes that the US delegate has proposed that the attribution rule not apply if the claimant itself is not conducting business in the residence jurisdiction. Under this proposal, an operating company receiving a dividend from an affiliate in the source country could claim treaty benefits as long as the dividend met the requirement that the income be connected with the active business in the residency country (e.g., the payor is in the same business) but that same dividend would not qualify if received by a holding company resident in the treaty jurisdiction. The attribution rule simply is a recognition that, once the business nexus to the jurisdiction is established, the taxpayer should not be deprived of the treaty benefit if the taxpayer chooses a local organization involving multiple entities. The proposal from the US delegate would force companies to distort their operations to have the operating company hold the shares rather than the holding company. For a test that only applies to the business connected income this makes no policy sense and should be rejected.

**New proposals on special tax regimes and partial treaty termination**

For the first time, and at the very end of the BEPS process, the RDD introduces two new proposals that would reflect fundamental changes in treaty policy. A major shortcoming of the BEPS process is the truncated time period allowed to address complex, untested principles. Neither time nor the request for brevity allows us to critique the rules proposed in the RDD for these novel concepts that can have a major impact on entitlement to treaty benefits and the viability of a tax treaty. Determining how these rules would work, the definitional standards to be applied, the appropriateness of the “remedy” and the local constitutionality of the partial termination proposal are among the more obvious issues that should be vetted in a careful, deliberative process. The BEPS process has been an iterative process where new rules are aired, stakeholders respond, revisions are proposed and further input is provided by stakeholders before the end product is produced. We urge that the final report on Action 6 should not attempt to formulate rules that could be faulty and could be embedded in the Model or the multilateral convention, making hastily developed decisions difficult to reverse. Rather, it would be appropriate to set forth general principles for further consideration and development in a deliberative manner.
The Principal Purpose Test

We welcome the inclusion of examples that help provide guidance on the parameters of the principal purpose. Unfortunately, the examples offer limited guidance because they address facts where the outcome is obvious, adding little to the clarity that is so important for the PPT. We urge the Working Group to add further examples based on suggestions made by those who responded previously. We note, in particular, that examples demonstrating that the use of an entity for the purpose of collective investment is a positive factor in determining that such collective investment vehicles ordinarily would not be subject to challenge based on the principal purpose test. Also, in aligning the standards under the discretionary grant procedure in the LOB article with the standards applied to the principal purpose test, we refer to our comments with regard to the standards to be applied for discretionary grants for what we believe are necessary modifications of the standards to achieve an equitable, balanced approach to the discretionary grant (or denial) of treaty benefits.

Finally, we suggest that the last sentence of Paragraph 63.1 be revised to read: “All evidence relevant to the determination of a principal purpose must be provided to the competent authority in order to enable it to determine whether this is the case.” Adding a standard of relevance will protect against information requests that may be motivated by reasons other than the relevant determination.

Other Issues

We welcome the requirement for competent authorities to deal with requests regarding dual residence “expeditiously”. We nonetheless consider that, in the interest of certainty and equity, a timeline be added. Our suggestion is “The competent authorities to which a request for determination of residence is made under paragraph 3 should deal with it within 6 months, unless there are exceptional circumstances preventing this, and should communicate their response to the taxpayer as soon as possible”.

In regard to the design and drafting of the applicable rule to a permanent establishment in third States, we urge the Working Party to reinstate former paragraph f) excepting royalty income from the rule if the royalties are earned with respect to intangible property produced or developed by the enterprise through the permanent establishment. From an EU law perspective, the Cadbury Schweppes case would suggest that taxing rights in regard to an arm’s length profit earned by activities undertaken in the jurisdiction of the permanent establishment should remain with the source country, irrespective of the effective rate of tax.

Yours sincerely

Peter Cussons
Partner
PricewaterhouseCoopers LLP,
London

Steve Nauheim
Managing Director
PricewaterhouseCoopers LLP,
Washington D.C.
cc Stef van Weeghel, Global Tax Policy Leader

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<th>PwC Contact</th>
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<tr>
<td>Steve Nauheim</td>
<td><a href="mailto:Steve.a.nauheim@us.pwc.com">Steve.a.nauheim@us.pwc.com</a></td>
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<tr>
<td>David Ernick</td>
<td><a href="mailto:David.ernick@us.pwc.com">David.ernick@us.pwc.com</a></td>
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Dear Ms. de Ruiter,

I am pleased to have this opportunity to provide comments on OECD’s discussion draft on BEPS Action 6. The comments will be as short as possible, and they aim to discuss additional procedures to specific situations.

In a simple and objective analysis, in spite of the effort to create objective rules, there is an increasing risk of misuse or treaty shopping from paragraph 1 to paragraph 5 of the simplified version of the LOB. More specifically, paragraphs 4(a), (b), (c) and 5 leave some room for misuse of the Double Tax Convention (DTC). Since these provisions have inherently different risks of being circumvented, it is also reasonable that tax authorities have different tools to identify and cooperate when one of these rules is used by a taxpayer. The greater the risk of misuse a specific provision of the LOB, the more transparency and cooperation between the tax authorities becomes necessary.

Items (a), (b) and (c) of paragraph 4 of the LOB simplified version present several open concepts that can lead to subjectivity and abuse, such as “business carried on is […] substantial in relation to”, “on the basis of all the facts and circumstances”. Regardless of all those open concepts, under the current version, (i) the resident is not obliged to inform any tax authority about the use of paragraph 4 of the LOB and (ii) a tax authority is not obliged to share information about the use of paragraph 4 with the other competent authority. The first issue (i) can be unilaterally solved if the domestic law conditions the use of the DTC to a previous request to the tax authorities (it normally occurs to apply a reduced WHT at source). The second issue (ii) can be solved through exchange of information that should be made from source Country to residence Country or vice-versa.

Both questions are connected and the problem may be easily solved through transparency and cooperation between competent authorities. Thus it is necessary to establish that the resident is (i) obliged to inform at least one of the countries (source or residence) about the use of paragraph 4(a), (b) or (c) and (ii) that country is obliged to inform the other country (residence or source, respectively). Thus, the following condition is suggested when paragraph 4(a), (b) or (c) is applied:

“d) In the case of application of paragraph 4(a), (b) or (c), the resident of a Contracting State..."
shall inform that State about the use of that paragraph and the facts and circumstances that justified such use. That state shall exchange such information with the other Contracting State. If the other Contracting State identifies a case of use of that paragraph that has not been informed, it shall inform the first Contracting State.”

As regards paragraph 5, the last sentence establishes that “[t]he competent authority of the Contracting State to which such request has been made by a resident of the other Contracting State shall consult with the competent authority of that other State before rejecting the request.” Thus, under the current terms of the simplified LOB, the request will be presented to the tax authority of the source country that will inform and consult the tax authority of the residence state only if the request is rejected, but not if it is approved.

This approach could benefit from greater transparency and cooperation. Firstly, the approval of the request could negatively affect the residence country that would be unaware of this situation; and secondly, the proposed rule does not mention that the residence country should inform the source country in similar situations. The rule should be changed to require the cooperation in cases of approved requests, and also to require the residence country to inform the source country in such fact patterns. The following alternatives could be considered:

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<td>5. A resident of a Contracting State that is neither a qualified person nor entitled under paragraph 3 or 4 to a benefit that would otherwise be accorded by this Convention with respect to an item of income shall nevertheless be entitled to such benefit if the competent authority of the Contracting State from which the benefit is being claimed, upon request from that resident, determines, in accordance with its domestic law or administrative practice, that the establishment, acquisition or maintenance of the resident and the conduct of its operations are considered as not having as one of its principal purposes the obtaining of such benefit. The competent authority of the Contracting State to which such request has been made by a resident of the other Contracting State shall consult with the competent authority of that other State before deciding whether to approve or reject the request.</td>
<td>5.[idem] xxxxxxxxxxxxxxxxxxxxxxxx […]</td>
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The competent authority of the Contracting State to which such request has been made by a resident of the other Contracting State shall consult with the competent authority of the other State if the request is accepted or consult with the competent authority of the other State before rejecting the request.

If you have any questions or require further information, please do not hesitate to contact me.

Yours sincerely,

Ricardo Augusto Gil Reis Rodrigues

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2 The word “that” was changed by “the” because the request can be presented to the source or to the residence country and the expression “by a resident of the other Contracting State” was deleted.
June 17, 2015

BY E-MAIL: TAXTREATIES@OECD.ORG

Marlies de Ruiter
Head, Tax Treaties
Transfer Pricing and Financial Transactions Division
OECD/CTPA

Dear Madam

Re: BEPS Action 6: Prevent Treaty Abuse

We are grateful for the opportunity to submit comments on the Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse released on 22 May 2015 (the “Revised Draft”), which follows on from the Public Discussion Draft Follow-up Work on BEPS Action 6: Preventing Treaty Abuse, dated 21 November 2014 (the “Discussion Draft”). We submitted comments on certain implications of the proposals described in the Discussion Draft for typical private equity structures in January 2015.

We consider that the concerns and suggestions we raised in respect of the Discussion Draft continue to apply in relation to the Revised Draft. As noted above, our previous representations specifically highlighted the issues that the Action 6 proposals create for common private equity structures. These concerns remain under the current proposals. However, it is also important to carefully weigh the impact that these proposals would have on other categories of non-CIV funds which increasingly constitute a vital source of capital for both SMEs and large businesses. Other non-CIV funds (such as alternative debt finance providers) are typically organised in a very similar manner to the traditional private equity structures that we outlined in our previous comments. Accordingly, these comments focus on the implications of the simplified limitation on benefits rule (the “LOB rule”) for non-CIV funds more generally. We will also note that the concerns that we raised regarding the application of the PPT rule have not been addressed in the Revised Draft.

As a general matter, we consider that the proposals in their current form could have a negative impact on the non-CIV funds sector. There is increasing evidence, recognised in academic literature1, that non-bank, non-market providers of finance (such as non-CIV funds) are a significant source of funds in both developed and developing countries and can help to create higher resilience against systemic risk. However, the OECD’s current proposals for LOB and

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1 See, e.g. Wehinger, Gert, OECD Journal: Financial Market Trends Vol 2013/2, “SMEs and the credit crunch: Current financing difficulties, policy measures and a review of literature”
PPT rules in their current form risk prejudicing the continued development and sustainability of this sector.

In light of this, we strongly welcome the announcement that work regarding the position of non-CIV funds may continue up to and after the expected adoption of the final report on Action 6 in September 2015, and hope that the work undertaken in this additional time will result in an approach to non-CIV funds which is both proportionate to any perceived risk that such vehicles actually pose from a treaty abuse perspective, while acknowledging the importance of a broad-based non-CIV fund industry to both large and small enterprises and a wide spectrum of investors. In particular, the possible solutions proposed in paragraph 24 to the Revised Draft concerning (i) specific provision for non-CIV funds under the LOB rule, and (ii) specific examples in the Commentary to the PPT rule regarding non-CIV funds would be entirely appropriate and welcome developments.

In our view, the risk that non-CIV funds present from a treaty abuse perspective could be adequately met by the use of a clear and properly targeted PPT rule and, in particular, a test that specifically considers whether the principal purpose of the arrangement in question is an abusive purpose.

Please find below specific comments on the form of simplified LOB rule and PPT rule proposed in the Revised Draft.

1. Limitation-on-benefits (“LOB”) rule

   a. Qualified persons and “trade or business” criteria

   As noted in our previous representations, most non-CIV funds and their affiliated investment entities would fail to qualify for treaty benefits as “qualified persons” under the current LOB proposals because (i) the large majority of non-CIV funds are not publicly traded entities, and (ii) it is unlikely that more than “50 per cent of the beneficial interests” in the fund will be held by investors resident in the relevant Contracting State, given that such funds draw investment from a broad and international investor base. Furthermore, the exception for entities carrying on a “trade or business” explicitly excludes entities whose activities constitute “making investments for their own account”. This will exclude many non-CIV funds (including most private equity and alternative debt funds) whose activities are limited to making investments.

   b. “Equivalent beneficiary” test

   As noted in our comments to the Discussion Draft, even where non-CIV funds would theoretically be entitled to the benefit of an equivalent beneficiary provision, any provision that requires non-CIV funds to trace beneficial ownership through to ultimate investors is unlikely to be practicable in many cases. The due diligence exercise involved would extend far beyond any processes required by current law and regulation. However, even if it were possible to identify all beneficial interests, as a practical matter, this would require non-CIV funds, at the time of any fundraising, to diligence: (i) the tax
treaties in place in the possible holding vehicle jurisdictions, (ii) the tax treaties in place in any jurisdictions in which investments may be made, and (iii) the tax treaties in place in the jurisdictions in which any potential investors may be resident for tax purposes. Given that many funds have an international investment mandate (meaning that the list of potential investment jurisdictions could be extensive), this exercise could become prohibitively burdensome.

Many investors in non-CIV funds will indeed be eligible for the benefit of beneficial tax treaties in their jurisdiction of residence. However, the equivalent beneficiary test currently operates as a “cliff-edge” risk for non-CIV funds and their investors if 25 per cent of the beneficial interests are owned by investors resident in jurisdictions that do not have treaties in place with the source jurisdiction providing for at least an equivalent benefit. As a result, there is a significant risk that such investors may actually find themselves worse-off as a result of participating in collective investment, as opposed to investing in assets directly, if other investors in a fund are not able to satisfy these requirements.

In addition, investors from jurisdictions which have tax treaties in place that do not provide for a complete exemption from withholding tax at source on interest and/or dividends, but rather a reduced rate (even 5% – 10%), may find that non-CIV funds are incentivised to reject their capital contribution on the grounds that it may ultimately jeopardise the returns of other investors. As noted above, the effect of this would be exacerbated for non-CIV funds with an international focus, as they may discriminate in favour of investors resident in the few jurisdictions which have treaties providing for a nil rate of source jurisdiction tax in every jurisdiction in which the fund may invest. This could lead to increasingly inefficient allocation of capital from investors in many jurisdictions.

We anticipate that both investors and recipients of capital would be negatively impacted if these proposals were implemented in their current form. We believe that the impact of the LOB rule on non-CIV funds would represent a disproportionate response to any treaty abuse concerns raised by such structures. Accordingly, we welcome the statement that further consideration is being given to making specific provision for non-CIV funds under the LOB rule. We would suggest that a specific category of “qualified person” relating to non-CIV funds should be included in final proposals regarding any LOB rule.

2. **Principal Purpose Test**

The Revised Draft does not address the concern raised in our comments to the Discussion Draft that it is a legal and practical necessity for non-CIV funds to establish investment holding structures. As explained in greater detail in our previous comments, this is largely necessitated by the fact that funds are typically established in partnership form. In deciding where any such holding vehicles should be established, funds will naturally consider a wide range of practical, legal, regulatory and economic factors. However, as part of the general consideration of the legal and regulatory environment in a given jurisdiction, funds will naturally also consider whether the jurisdiction in question has a suitable range of double tax
treaties in place. The fact that a fund has taken such factors into account in this way should not of itself risk failing any PPT rule which may be included. If the view were taken that such consideration might breach a PPT rule, it would create an impact which is wholly disproportionate to the treaty abuse risk posed by non-CIV funds.

Accordingly, and as explained in greater length in our comments to the Discussion Draft, we would welcome clarification that the PPT rule would not be breached in these circumstances. Ideally this clarification would be made through amendment to the PPT rule itself. However, we consider that as a minimum this should be made clear through an explicit example in the Commentary, and strongly welcome the statement that further consideration is being given to including examples specific to non-CIV funds.

We believe that the PPT rule as it is currently drafted is unclear and likely to lead to considerable uncertainty and potential asymmetry in its application by different jurisdictions. In our view any PPT rule that is included should be more tightly drafted to ensure that it only affects behaviour which is truly abusive. Accordingly, we consider that the starting point for any PPT rule should be that it might only apply to the extent that the principal purpose of a given arrangement is an abusive purpose.

3. “Grandfathering”

Non-CIV funds will commonly have a defined lifespan (often 8 – 10 years). Accordingly, there will be a large number of pre-existing funds affected by any proposals that may ultimately be implemented.

These funds will not have conducted detailed due diligence on the treaty benefit entitlement of their ultimate beneficiaries by reference to the jurisdictions in which their investment entities may invest and, accordingly, may already be exposed to the operation of an LOB rule. The LOB rule could restrict such funds’ ability to pursue a variety of further investment opportunities, which might restrict their ability to deploy capital according to their agreed investment parameters.

Furthermore such funds will have pre-existing investments in debt, equity and other instruments that were made on the basis of domestic law and treaties in force as at the date on which such investments were made. If treaty benefits to exempt income and/or capital gains arising in respect of such investments from source jurisdiction taxation (and avoidance of double taxation) were denied under a new LOB or PPT provision, investors in such funds might be adversely affected.

Accordingly, in the event that LOB and PPT rules in their current form (or in similar form) were included in the OECD’s final proposals, we suggest that such provisions be subject to comprehensive grandfathering in order to protect the position of existing funds and the investors that have already committed capital to such entities.

2 A more complete summary of certain issues that is likely to take into account when considering the jurisdiction in which to establish holding or investment entities can be found in our comments to the Discussion Draft.
We hope that there will be further opportunity to engage with the OECD in due course regarding the impact of these proposals on the funds sector more generally, and would welcome any opportunity to discuss the points raised in this letter and our previous comments to the Discussion Draft in further detail.

Yours faithfully

Ropes & Gray International LLP
16 June 2015

Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and Financial Transactions Division  
Centre for Tax Policy and Administration  
Organisation for Economic Co-Operation and Development  
Paris, France

Via Email: taxtreaties@oecd.org

RE: OECD Revised Discussion Draft BEPS Action 6: Prevent Treaty Abuse

Dear Ms. de Ruiter:

On 19 July 2013, the OECD published an Action Plan on Base Erosion and Profit Shifting (hereinafter the Plan) setting forth 15 actions the OECD will undertake to address a series of issues that contribute to the perception that individual countries’ tax bases are being eroded or profits shifted improperly. Pursuant to Action 6 of the Plan “Prevent treaty abuse,” the OECD issued a public discussion draft on 21 November 2014 entitled Follow Up Work on BEPS Action 6: Preventing Treaty Abuse (hereinafter the November Draft). The November Draft followed on the OECD’s first public discussion draft under BEPS Action 6, released on 14 March 2014. A public consultation on the November Draft was held in January 2015. Following on the November Draft and subsequent public consultation, on 22 May 2015, the OECD released a revised discussion draft entitled BEPS Action 6: Prevent Treaty Abuse (hereinafter the Revised Draft). The OECD requested comments on the Revised Draft no later than 17 June 2015. On behalf of Tax Executives Institute, Inc. (TEI), I am pleased to respond to the OECD’s request for comments.

TEI Background

TEI was founded in 1944 to serve the needs of business tax professionals. Today, the organisation has 56 chapters in Europe, North
and South America, and Asia. As the preeminent association of in-house tax professionals worldwide, TEI has a significant interest in promoting tax policy, as well as the fair and efficient administration of the tax laws, at all levels of government. Our nearly 7,000 individual members represent over 3,000 of the largest companies in the world.

**TEI Comments**

**General Comments**

TEI commends the OECD for its exhaustive work under BEPS Action 6 as most recently reflected in the Revised Discussion Draft and its continued solicitation of stakeholder input on the rules necessary to address the issues set forth in the Revised Draft. Regrettably, the Revised Discussion Draft is a work in progress and it is disappointing that the OECD seemingly cannot reach a consensus on the proper method for addressing what it views as the abusive use of double tax treaties to effect base erosion and profit shifting. Instead, like other recently issued discussion drafts under the BEPS project (e.g., the drafts on CFC rules and mandatory disclosure), the Revised Discussion Draft presents a menu of options that would permit countries to choose one of several approaches to address treaty abuse. Setting forth alternative approaches will result in a variety of treaty anti-abuse rules across the spectrum of double tax treaties. In addition, the lack of a recommended approach will make it more likely that several countries will not adopt any of the treaty anti-abuse alternatives set forth in the Revised Draft. While this result might be preferable from a business standpoint, it undermines one of the primary goals of the BEPS project to adopt uniform rules across jurisdictions.

Moreover, the Revised Discussion Draft again includes a primary purpose test (PPT), the application of which will be uncertain and subjective. While it is clear that the OECD recognises this, it continues to downplay the negative impact the uncertainty created by the PPT and other potential changes will have on cross border investments and tax disputes. In addition, permitting countries to choose whether to use a limitation on benefits (LOB) provision, a PPT, or both, will make it difficult to conclude a multi-lateral instrument under BEPS Action 15.

The Revised Draft also proposes that when the OECD model tax convention is amended the text of the convention will not include any actual treaty language. Instead, the model will contain only bracketed placeholders providing a brief indication of the types of LOB provisions that contracting states could adopt – with the actual, OECD endorsed alternative versions of such provisions being set out in the official commentary to the model convention. If the countries participating in the BEPS project cannot agree on the wording of the model

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1 TEI is a corporation organised in the United States under the Not-For-Profit Corporation Law of the State of New York. TEI is exempt from U.S. Federal Income Tax under section 501(c)(6) of the U.S. Internal Revenue Code of 1986 (as amended).
convention, how can tax authorities and taxpayers possibly agree on the interpretation, application, etc. of the provisions that are ultimately adopted? This will lead to substantial uncertainty and complexity, and require an increase in resources devoted to tax disputes.

The Use of Treaties to Create Taxation

As the OECD is well aware, there are different approaches to international taxation of business activities with most countries adopting a territorial approach, at least for active business income. Thus, in most cases such countries’ tax systems do not need to address holding company structures or intermediary companies because they do not tax the income earned outside the country’s jurisdiction in any event. Moreover, most of these structures are put in place for non-tax business reasons, such as the centralisation of functions, to bundle investment, for cash management, or in preparation for a spinoff (among many others). Similarly, intellectual property (IP) holding companies are generally devised for non-tax business reasons, such as ease of licensing IP rights around the world. While certain structures may be used to avoid secondary withholding taxes, this is again only a problem for certain forms of international tax systems. Yet, the Revised Draft attempts to address these narrow problems as part of the OECD’s model convention.

This approach is present in other areas. For example, the Revised Draft discusses implementing a kind of effective tax rate test to address supply chain planning and the use of principal structures with a permanent establishment or branch in a third jurisdiction. But again this kind of planning is only problematic for certain forms of international taxation and it is unclear why the OECD is including a solution for these issues in its model convention and the accompanying commentary when it will be relevant for very few countries. The Revised Draft also proposes addressing the problem of dual-residency through a tie-breaker mechanism. However, it has never been clear why it is considered abusive for a taxpayer to subject itself to taxation in two separate jurisdictions. If this is truly a problem, then two countries can come to an agreement on how to address it. Overall, cluttering the OECD model convention with minor or insignificant issues is unhelpful and only complicates what should be a uniform approach.

Nevertheless, the recommendations in the Revised Discussion Draft and throughout the OECD publications on BEPS Action 6 seem intent on addressing the perceived abuses of such structures and companies that may be of concern to countries that take a minority approach to international taxation. As a whole, these proposed treaty provisions create taxation where it would not exist in the absence of the treaty, which has not been the traditional purpose of double tax treaties. A treaty has traditionally allocated the right to tax among jurisdictions to ensure income is taxed only once; however the OECD is now proposing to use the treaty as an active or affirmative instrument of taxation, a role traditionally reserved to the treaty partners (i.e., to assert their own taxing rights). Moreover, as noted, the use of a PPT to implement this new treaty approach adds substantial uncertainty to operational business planning whenever it
might include a cross-border tax aspect. TEI therefore recommends that the OECD leave the
decision whether to address these structures generally to the domestic law of a jurisdiction. If
two countries wish to address these issues jointly, then they can of course adopt a (hopefully
objective and well defined) LOB provision in their double tax treaty to address specific issues.

Active Trade or Business Test

With respect to the active trade or business test for qualification for treaty benefits, if
OECD wants to introduce this as a way to qualify for treaty benefits, it should include a
commonly accepted standard for what constitutes an active trade or business. It seems it has
not done so because the 34 OECD countries likely have 34 different definitions of an active
business. This is yet another area where it is more appropriate to rely on the domestic law of an
individual jurisdiction or through the use of an LOB provision, rather than creating a
standalone term in a tax treaty without context or a commonly understood definition.

Transition Period for Implementation

The structures currently used by many multi-national enterprises to conduct their
business operations were put in place over a period of several years, in certain cases as long as a
decade. These structures were implemented, in part, in reliance on the current treaty rules as
generally exemplified by the OECD’s model convention as in existence before the start of the
BEPS project. Thus, most double tax treaties do not include an LOB provision or PPT. If these
provisions are included in the OECD model convention and become the baseline for treaty
negotiations among OECD member states and other countries, they have the potential to
disrupt the business structures currently used by international business by disqualifying
entities within a multi-national group from treaty benefits – sometimes at great and unexpected
tax cost. TEI therefore recommends that the OECD suggest a transition period of at least five
years for countries that incorporate an LOB or PPT into a particular double tax treaty for the
first time to give businesses a sufficient period to adjust their operations to the new rules.

Examples in the Revised Discussion Draft

The Revised Discussion Draft includes additional examples to “clarify” when the PPT
applies. Unfortunately, these examples highlight the significant uncertainty inherent in a rule
that effectively requires a taxpayer to prove that none of its principal purposes was to obtain a
tax benefit – when tax will be a consideration in virtually any transaction. The conclusion in
Example F involves assuming that a business is a “real business . . . using real assets and
assuming real risks.”² It is unclear what is meant by “real” business assets and risks outside;
real in comparison to what?

² Revised Discussion Draft, p.32
Special Tax Regime Definition

The proposed definition of a “special tax regime” is quite broad. The definition could encompass notional interest deductions, companies located in a special tax zone of a jurisdiction or companies that benefit from special tax incentives such as R&D tax credits, manufacturing incentives, etc., unless the regime or tax status at issue meets one of the specific exceptions provided. In addition to the potential exceptions listed in the Revised Draft, TEI recommends that the OECD adopt an exception for circumstances where the effective rate of tax of the “special” regime is above a certain percentage of the “normal” tax rate (such as 60%). That is, it a tax regime should not be subject to a designation as “special” unless the regime has the effect of reducing the effective tax rate below the normal tax rate.

In addition, it is unclear what is meant by the exception to the definition of special regime for “any legislation, regulation or administrative practice . . . that implements the principles of Article 7 (Business Profits) or Article 9 (Associated Enterprises) . . . .” This exception could be interpreted very broadly to exempt most tax regimes or very narrowly to exempt very few. Thus, an additional explanation of what this exception is intended to encompass would be welcome.

Conclusion

TEI appreciates the opportunity to comment on the Revised Discussion Draft regarding concerns over the abuse of double tax treaties. These comments were prepared under the aegis of TEI’s European Direct Tax Committee, whose Chair is Nick Hasenoehrl. If you have any questions about the submission, please contact Mr. Hasenoehrl at +41 786 88 3772, nickhasen@sbcglobal.net, or Benjamin R. Shreck of the Institute’s legal staff, at +1 202 638 5601, bshreck@tei.org.

Sincerely yours,

TAX EXECUTIVES INSTITUTE, INC.

Mark C. Silbiger
International President

3 Id. at 17.
4 Id.
Dear Marlies de Ruiter,

RE: Taxand responds to the revised discussion draft: BEPS Action 6: Prevent Treaty Abuse

Further to the publication on 22 May 2015 of the OECD’s invitation for public comments on the OECD revised discussion draft on Action 6 concerning the prevention of treaty abuse, Taxand is pleased to provide written comments based on the practical experience we have as tax advisors.

The consultation on the prevention of the granting of treaty benefits in inappropriate circumstances is a key initiative of the BEPS Action Plan, which we support. We would like to salute the efforts of the OECD Committee of Fiscal Affairs for its continual and vast work on laying down the cornerstones for the ambitious and comprehensive Action Plan aimed at addressing base erosion and profit shifting in an open format that allows all stakeholders to provide their views.

Taxand can confirm that we have no objections with posting the comments on the OECD website and that comments represent Taxand and are based on our experience working with multinationals worldwide.

We appreciate this opportunity to provide comments to the OECD Committee of Fiscal Affairs and would be pleased to discuss this further and to participate in any further discussion on these matters.

More information about Taxand is provided below. Taxand is wholly committed to supporting the OECD Committee of Fiscal Affairs and we look forward to contributing to further debate.

If you wish to discuss any of the points raised in this letter, please do not hesitate to get in touch with us directly via the contact details below.

Yours faithfully,

Taxand

Taxand’s comments on the previous OECD discussion drafts concerning Action 6 can be accessed here:

- Part II: OECD discussion draft on Action 6 (prevent the granting of treaty benefits in inappropriate circumstances)
- OECD discussion draft on Action 6 (prevent treaty abuse)
ABOUT TAXAND

Taxand provides high quality, integrated tax advice worldwide. Our tax professionals, more than 400 tax partners and over 2,000 tax advisors in nearly 50 countries grasp both the fine points of tax and the broader strategic implications, helping you mitigate risk, manage your tax burden and drive the performance of your business.

We're passionate about tax. We collaborate and share knowledge, capitalising on our expertise to provide you with high quality, tailored advice that helps relieve the pressures associated with making complex tax decisions.

We're also independent—ensuring that you adhere both to best practice and to tax law and that we remain free from time-consuming audit-based conflict checks. This enables us to deliver practical advice, responsively.

Taxand has achieved worldwide market recognition. Taxand ranked in the top tier in Chambers Global Guide 2014 global network rankings and in the International Tax Review's (ITR) World Tax 2015, 41 Taxand locations were commended and a further 26 locations listed in ITR’s World Transfer Pricing Guide 2015. 31 countries were voted top in the ITR Transaction Tax Survey 2014 and 29 in ITR Tax Planning Survey 2013. Taxand has received 69 national awards and 15 regional awards in the ITR European, Americas and Asia Tax Awards since 2009. These include Latin America Tax Disputes Firm of the Year, European TP Firm of the Year, European Indirect Tax Firm of the Year, Asia Transfer Pricing Firm of the Year, and Asia Tax Policy Firm of the Year. Full details of awards can be viewed at www.taxand.com/about-us

www.taxand.com
1. Collective Investment Vehicles

Collective Investment Vehicles ("CIVs") are defined as "funds that are widely-held, hold a diversified portfolio of securities and are subject to investor-protection legislation in the country in which they are established." We understand that, so far, there is no consensus on the distinction between CIVs and non-CIVs. In particular the qualification will clearly depend on certain criteria, eg the concept of widely distributed or diversification. The final report should clearly foresee how these criteria shall be applied, ie according to the law and regulatory system (in that case: of which country?), according to the statutes of the CIVs or on a factual basis. For example, a fund that is owned by a single investor would be deemed to be widely distributed by some states provided that its statutes and the law allow for the distribution to a wider number of investors. In other words, it is not the actual composition of the shareholder base that counts but the principle or the law under which the fund is established.

Subparagraph 2 f) of the LOB rule provides for the inclusion, in the list of "qualified persons", of a provision dealing with CIVs which shall be either drafted, or omitted, based on how CIVs are treated in the Convention and are used and treated in each contracting state. The Commentary on the LOB rule includes a number of alternative provisions that correspond to the various approaches included in the 2010 OECD Report "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles".

While we welcome the fact that there is a general support for the conclusions reached in the 2010 report, we believe that, as stated by many other previous commentators, some specific types of CIVs should per se be considered as qualified persons for the purpose of the LOB clause.

In particular, we are of the view that a widely held open ended CIV is indistinguishable in practice from a company quoted on a recognised stock exchange. Maintaining a distinction in the LOB between CIVs listed on a stock exchange (so called Exchange Traded Funds or ETFs) and other CIVs creates potential distortions which are based on an arbitrary distinction.

We would recommend that the final report on Action 6 should foresee that all CIVs set up as UCITS, as well as all other widely-distributed non-CIVs whose characteristics are similar to those of UCITS, will automatically qualify as resident for the purpose of article 1 of the OECD Model Convention and that they will also be considered as qualified residents for the purpose of the LOB clause.

For this purpose, the wording of Article 1 of the OECD Model Tax Convention would need to be amended in order to include the provision currently proposed in paragraph 6.17 of the commentary on Article 1, which would only have to be slightly amended in order to expressly provide for the treaty entitlement of CIVs established as UCITS and comparable non-CIVs (because such CIVs would then be treated as an individual that is a resident of the Contracting State in which they are established).

Accordingly, subparagraph f) of paragraph 2 of the LOB clause would have to be drafted to ensure that CIVs set up as UCITS and comparable non-CIVs always constitute qualified persons.
In addition, we recommend including a statement that contracting states are encouraged to consider that UCITS and comparable non-CIVs will not be considered as creating opportunities for treaty shopping.

As far as Treaty Relief and Compliance Enhancement (TRACE) is concerned, we believe that the proposed amendment of the OECD Model Tax Convention and the LOB provision should not be implemented without the implementation of the TRACE programme. The current procedures in certain states are complex, onerous and time consuming – not in line with the constraints of CIVs. We believe that the OECD should do what it can to ensure that the TRACE programme is implemented in parallel, in order to avoid individual OECD member states defining their own distinctive rules for the practical application of the LOB clause.

2. Non-CIV Funds

We welcome the fact that some solutions have been developed or are in the process of being developed for REITs and for pension funds.

As far as other types of non-CIV funds are concerned, we welcome the fact that their importance has been recognised and some further work will be needed in order to develop some solutions.

However, as stated above under comment 1, we recommend that the final report on Action 6 should foresee that all widely-distributed non-CIVs whose characteristics are similar to those of UCITS will automatically qualify as resident for the purpose of article 1 of the OECD Model Convention and that they will also be considered as qualified residents for the purpose of the LOB clause.

3. Alternative LOB Provision for EU countries

Based on the revised discussion draft, the general conclusion on EU Law issues is that no changes should be made to the model provisions included in the report in order to address specific EU law issues. Alternatives could however be included in the commentary or changes to the model provisions that would deal with EU law issues whilst addressing other concerns. It was also agreed that, as far as possible, alternatives to be included in the Commentary should not be restricted to EU/EEA States but should address issues more generically.

EU issues, whether they relate to the LOB clause or to any of the proposals made in relation to Action 6 (including the PPT), will have to be EU-compliant and we agree that solutions have to be developed which apply to all countries (ie solutions which are not restricted to EU/EEA states).

We strongly believe that EU issues have to be dealt with in the text of the Model provisions itself and not only in the commentaries. As long as the proposals are not in line with EU law, because they constitute infringements to the fundamental freedoms, as defined in the EU Treaty and as interpreted by the ECJ, it is clear that EU countries will not be in the position to sign a bilateral treaty or a multilateral instrument, as this instrument would contravene EU law.
The ECJ case law has defined the situations in which restrictions to the freedom of establishment and to the free movement of capital may be provided in order to avoid abuses.

Any anti-abuse measures, especially the PTT rule and the LOB clause, should therefore be strictly limited to these situations. Otherwise, we consider that EU and EEA countries which sign the multilateral instrument will put themselves and indeed the whole multilateral instrument at risk.

4. Conditions for the application of the provision on publicly-listed entities

The revised discussion draft suggests adding a new paragraph 71.1 in the commentary on the LOB rule in order to deal with the issue of the alternative conditions in 2 c(i)(A) and B) (the ‘publicly-listed entity’ provision) of the LOB rule being too restrictive for small countries that do not have important stock exchanges and whose companies are therefore listed on foreign stock exchanges.

We consider that the proposal included in the revised discussion draft, which among others refers to the volume of shares traded on the stock exchange in a calendar year, is still too restrictive for small countries that do not have important stock exchanges.

5. Issues related to the derivative benefits provision and new concept of “special tax regime”

The discussion draft suggests including a new concept into the OECD Model Tax Convention: the concept of special tax regimes. According to the proposal, income which falls under one of these regimes would be denied the benefits provided in articles 11 (interest), article 12 (royalties) and article 21 (other income).

According to the revised discussion draft, the aim of this proposal would be to address some of the objections to the addition of a derivative benefits provision in the LOB rule. The derivative provision is, however, not included in the simplified LOB (only in the “standard” draft LOB).

The creation of this new concept of special tax regime means an additional restriction to treaty benefits (additional requirement for a specific investment vehicle to be granted full treaty benefits). To us, this additional restriction to treaty benefits constitutes an additional layer of legal uncertainty for tax payers, which is why we do not support the introduction of such a new definition in the OECD Model Tax Convention.

We are also concerned that the introduction of this new concept at such a late stage does not allow for thoughtful review and comments, also taking into account the fact that the scope of special tax regimes is neither further defined nor explained in the discussion draft. Some of the unclear aspects of the current proposal include:

- What is to be understood as a regime which benefits disproportionately interest, royalties or other income?
- Which regimes could actually be excluded by member states if these have anyway not to result in a low effective tax rate and what can be considered as a low effective taxation?
- What does substantially all of the activity mean?
- What can be considered as an activity which is substantial enough to satisfy the substantial activity requirement? Does it mean that royalties in connection to an IP
regime which is in line with the OECD modified nexus approach will never be regarded as a special tax regime? We understand that this should be the case but we consider that this would need to be expressly mentioned.

Overall, we are of the view that this new concept gives rise to too many different interpretations and would increase once more the level of legal uncertainty for tax payers, a legal uncertainty which is already created by other measures of the proposals made under Action 6, such as the LOB and the PTT.

In addition, we do not see what the benefit would be as we already have the LOB provision / simplified LOB and PPT rules which have the same objective. On the top of that, we consider that such a provision should not be implemented in the multilateral instrument and therefore it should only be put in place on a bilateral basis. As a result, OECD member states should be aware of this specific tax regime and could act accordingly in their bilateral arrangements.

6. Action 15 and multilateral arrangement

The “simplified” LOB rule should be applied by OECD member states that would like to combine the LOB / PPT rule. The question of the incorporation of the simplified LOB provision in the articles of the model has been covered in section 6 and the annex. However, our concern is the articulation of the LOB, the simplified LOB and action 15. The multilateral instrument should be sufficiently precise to cover all the cases that could be applied differently in practice by each individual OECD member state.

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We appreciate this opportunity to provide comments to the OECD Committee of Fiscal Affairs and would be pleased to discuss this further, and to participate in any further discussion on these matters.

More information on how to contact Taxand is provided above. Taxand is wholly committed to supporting the OECD Committee of Fiscal Affairs and we look forward to contributing to further debate.

Yours faithfully,

Taxand

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Via e-mail to taxtreaties@oecd.org

Dear Ms. De Ruiter

TD appreciates the opportunity to submit comments on the OECD’s Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse issued on May 22, 2015.

Before commenting on specific issues raised by this Revised Discussion Draft, we are reiterating our grave concern that the combined BEPS proposals would have a stifling impact on global business and, as a result, have the potential of reducing corporate tax revenues for governments globally. The OECD should not lose sight of the fact that the role of business in the global economy is to produce goods and services and to create jobs – the primary role of business is not to raise revenue for governments. The OECD is on record as saying that governments should rely less and less on corporate tax as a tool to raise revenue, because corporate tax is a highly inefficient tax – corporate tax raises relatively little revenue for governments at an excessively high compliance cost and significantly reduces commercial activity. This is especially a concern because not all businesses are subject to corporate tax, which increasingly is creating an un-level playing field. We encourage the OECD to dedicate more resources to assessing the macro-economic impact of the proposed BEPS measures prior to finalizing these measures.
Regarding the specific issues raised by the Revised Discussion Draft, our comments build on the comments that TD submitted on January 9, 2015 on the OECD’s November 21, 2014 discussion draft on Action 7.

While we believe that the Revised Discussion Draft is an improvement upon the original discussion draft, we continue to be concerned that increasing uncertainty with respect to access to treaty benefits is tantamount to denial of the benefits that treaties are intended to provide. Our most serious concerns in this regard relate to the proposed principal purpose test (PPT) provision. We appreciate the OECD Working Party’s development and inclusion in the Revised Discussion Draft of additional examples illustrating the application of the PPT provision. However, illustrative examples alone cannot allivé the fundamental uncertainty of a standard like “one of the principal purposes.”

We recognize that the OECD has included the PPT provision as part of the minimum standard and does not intend to revisit the merits of this approach. However, as countries consider whether or not to include in their own bilateral treaties a PPT provision such as the OECD is advancing, we believe that they should evaluate the potential harmful macroeconomic impact of the uncertainty that such a test would create and the negative implications for cross-border trade and investment. These harms must be weighed against the expected benefits of such a test as an anti-abuse tool. Moreover, this cost-benefit analysis must also reflect the additional compliance costs for both taxpayers and tax administrations from such a subjective test. It should be noted that these increased costs will further exacerbate the inefficiency of the corporate income tax, which the OECD has already identified as a relatively inefficient tax as compared to other forms of taxation.

With respect to the mechanics of the PPT provision, we appreciate the Working Party’s inclusion in the Commentary of language suggesting that countries may want to establish an administrative process that would ensure that any application of the PPT provision would require pre-approval at a senior level. In addition, we urge the OECD to also incorporate an expeditious advance ruling process that would provide the certainty necessary to reduce impediment to cross-border trade and investment.

We also appreciate the Working Party’s rejection of the proposal by some delegates to exclude the application of the PPT rule from the reach of any treaty based mutual agreement procedure or arbitration provision.
We continue to be concerned about the operation of the limitation on benefits (LOB) approach, which is an important alternative to the highly subjective PPT provision. In this regard, we welcome the Working Party’s recognition of the need to maintain the range of options for collective investment vehicles (CIVs) that is reflected in the 2010 OECD report on granting treaty benefits to CIVs. We encourage the OECD to make clear that the recommendations of the TRACE project regarding implementation are essential to the proper application of treaty benefits to CIVs. In addition, we appreciate the proposal to incorporate language in the Commentary that would make clear that the special rules for CIVs would not be relevant in those situations where an entity otherwise would be entitled to benefits under other tests in the LOB provision. This is important for CIVs based in Canada that are structured with an entity that is resident for tax purposes. Paragraph 20 of the Revised Discussion Draft indicates that this proposal is to be further discussed at the Working Party’s June meeting and we therefore urge the Working Party to approve the proposal for incorporation in the final report on Action 6.

Finally, we note that the Working Party is continuing to consider two important issues: the potential inclusion of a derivative benefits test in the proposed LOB provision and the potential relaxation of restrictions on non-same-country intermediate entities in the proposed LOB provision. As discussed in our January 9th comment submission, both of these matters are critically important to the operation of an LOB provision in today’s global economy. Therefore, we urge the OECD to continue its work in this area to ensure that the LOB provision included in the final report accommodates multi-country business arrangements.

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We appreciate the opportunity to provide these comments on key issues with respect to the Action 6 Discussion Draft. We would be happy to respond to questions or to provide any further information that would be useful as the OECD continues its work in this important area.

Sincerely,

Peter van Dijk
Senior Vice President, Tax
TD Bank
June 17, 2015

VIA EMAIL
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Re: USCIB Comment Letter on the OECD Revised Discussion Draft on BEPS Action 6: Preventing Treaty Abuse

Dear Ms. de Ruiter,

USCIB\(^1\) is pleased to have this opportunity to provide comments on the OECD’s revised discussion draft (RDD) on BEPS Action 6. USCIB has attempted to keep these comments as short as possible.

**General Comments**

USCIB stands by its comments of April 4, 2014 and January 6, 2015, on the OECD’s discussion draft on BEPS Action 6 and the follow-up work on that discussion draft. The Action 6 2014 Deliverable did not address many of the concerns we raised. In particular, the 2014 Deliverable, the follow-up discussion draft, and the RDD (hereinafter “the guidance”) do not give due regard to the impact on the vast majority of potential beneficiaries of income tax treaties that do not engage in abusive practices and that, due to the broad reach and vagueness of the proposals, would in many cases lose access to tax treaties and, in any event, will be deprived of the certainty and predictability that is a fundamental goal of tax treaties. We want to be very clear that, in our view, the recommendations in the guidance would fundamentally change the role of tax treaties by effectively depriving *bona fide* enterprises and business transactions of the protection accorded by tax treaties from excessive and double taxation, at serious

\(^1\) USCIB promotes open markets, competitiveness and innovation, sustainable development and corporate responsibility, supported by international engagement and prudent regulation. Its members include top U.S.-based global companies and professional services firms from every sector of our economy, with operations in every region of the world. With a unique global network encompassing leading international business organizations, USCIB provides business views to policy makers and regulatory authorities worldwide, and works to facilitate international trade and investment.
cost to the global economy.\textsuperscript{2} We believe a more balanced approach is necessary: one that recognizes the fundamental purpose of treaties while recognizing and addressing legitimate issues of abuse of tax treaties. In our prior letters, we suggested specific changes to help achieve this balance. This letter does not repeat all those recommendations, although we stand by them, and the most important points are reiterated in this letter.

USCIB believes that the difficulty of achieving the proper balance is amplified by the speed at which the OECD is attempting to accomplish these changes. In the context of addressing treaty shopping we find this especially difficult to understand. The US – Netherlands Tax Treaty, which represented a significant shift in government attitudes towards treaty shopping, was signed on December 18, 1992. The need to address treaty shopping concerns has thus been widely understood for more than two decades. During that period the US has been insisting on LOB provisions in all of its treaties. Nevertheless, other countries have not taken steps to address this issue and now the OECD is attempting to develop and implement detailed anti-treaty shopping rules without the time needed to give proper attention to the complex issues and possible repercussions of any changes.\textsuperscript{3} We believe that the failure to take the time to do the necessary work will result in faulty rules which governments and businesses will spend years, if not decades, undoing. This is especially the case in the context of treaty shopping because of the possibility that a faulty rule will be enshrined in the Multilateral Instrument (MLI) under Action 15 and ripple through the treaty networks of many countries rather than having a trial in the bilateral context to see if the rule works appropriately. If a faulty rule has been implemented through the MLI it may be difficult to fix that rule.

The OECD has been basing its Entitlement to Benefits proposal on the most recent version of the US LOB. That version has been subject to considerable criticism and controversy, incorporates elements of US domestic law policy, and continues to be under internal US review as the US develops a new Model Income Tax Convention. Therefore, the detailed provisions of the current US LOB should not be the standard for an internationally accepted model.

\textbf{Specific Comments}

\textbf{Simplified LOB}

USCIB was one of the commentators that suggested the use of a simplified LOB. USCIB is pleased to see the OECD take up this suggestion, but is disappointed with the suggestion in the RDD that the simplified LOB apply in conjunction with the principal purpose test (PPT). The simplified LOB was suggested as a replacement for the complex, US-based rule which is not appropriate for use as a general model. Keeping the complex LOB provision and adding the simplified LOB only for use in conjunction with the PPT is not consistent with our suggestion. We continue to recommend that the complex LOB be deleted from the OECD Model, and the simplified LOB be included in its place.

\textsuperscript{2} The OECD should be attempting to measure the impact of these changes on global trade and investment.

\textsuperscript{3} In particular, the timing on this action item may be wrong. It would be appropriate to look at treaty abuse after other action items are completed. For example, if Action 4 significantly reduces the scope for base eroding interest payments, then the rules proposed in Action 6 may be excessive and their primary impact might be to impose undue restrictions on legitimate cross-border investment.
Further, it is not at all clear that there is any benefit to the inclusion of the simplified LOB since paragraph 5 of the RDD provides that “the non-application of the simplified LOB in a given case should not be interpreted in any way as suggesting that the PPT would not be applicable to that case.” We had previously understood that if an LOB applied in combination with a PPT, it would be intended to reach different forms of so-called “treaty abuse” such that a taxpayer that satisfied an entity level test could not be challenged on the basis that the entity did not qualify for treaty benefits, but rather only that the particular transaction was a conduit arrangement. If this is not the case, and a country can challenge the entity’s status as a qualified resident even though it satisfies the simplified LOB provision, then there is no point to the simplified LOB and it should be deleted entirely. Rather, entity eligibility based on an LOB standard should be treated independently of alternative means of addressing treaty abuse by entities otherwise entitled to treaty benefits – either through a PPT or more targeted anti-abuse rules.

New treaty provisions on “special tax regimes”

USCIB understands the concern that once a treaty is in place, countries find it difficult to deal with changes in the other countries’ law which change the balance of the treaty bargain and may result in the inappropriate granting of treaty benefits. Termination of a treaty is a drastic step and one that countries may be loath to take because of the impact on other taxpayers that are not benefitting from the special regime. Partial termination, although permitted in certain circumstances under the Vienna Convention on the Law of Treaties, is also a difficult step. So providing guidance on circumstances under which it would be considered appropriate to partially withdraw treaty benefits may be a sensible step. We believe, however, that adopting this provision as part of the 2015 Deliverable on Action 6 is premature.

This is a novel proposal that needs appropriate review. It seems clear that the proposal is intended to subject so-called “patent boxes” to additional scrutiny and possible special treatment. On initial reading it is not clear what else may be covered. USCIB would like to point out the following questions we have identified, although given the short timeframe for comment we are certain we have not identified all of the potential issues, and we have no solutions to propose.

The term “special tax regime” is very broadly defined and could call into question a wide variety of commonly adopted tax provisions. For example, would the following types of provisions be considered special tax regimes: research and development credits; amortization deductions, particularly if accelerated; original issue discount deductions – are these notional interest deductions? Is there any requirement that the special regime provide a material benefit? If so, what is material? Will there be any attempt to define the “substantial activity requirement”? Will this be integrated with the decisions made on Action 5 on Harmful Tax Practices?

The suggestion that provisions could be explicitly identified as “special tax regimes”, or not, is a welcome suggestion. However, it is difficult to say how this could be implemented in the context of the MLI. Will a list of good and bad regimes be included? Who will determine what is on the good or bad list? If, for example, a country believes that its patent box legislation is not a special tax regime because it satisfies the substantial activity requirement, would another country be able to reject that conclusion?
and assert that the patent box is, in fact, a special measure in the context of the MLI? If so, how would they do that?

**New general treaty rule intended to make a tax treaty responsive to certain future changes in a country’s domestic tax laws**

As stated above, USCIB understands concerns with changes in law that change the balance of benefits under an already negotiated tax treaty, and an appropriate rule may be necessary to deal with these issues. USCIB believes that inclusion of this rule in the 2015 Deliverable is also premature. Our concern is made clear if the OECD proposal is compared to the recently proposed changes to the US Model. The OECD proposal looks to the adoption of an exemption for substantially all foreign source income (including interest and royalties), while the US proposal looks to the combined aggregate effective rate of tax. These are very different options raising very different issues. The OECD approach is much narrower; presumably reducing the tax rate significantly, but not to zero, would be acceptable under the OECD approach. Would an exemption that was carved back to account for the availability of deductions be considered to exempt substantially all foreign source income?

**Commentary on the discretionary relief provision of the LOB rule**

The ability of taxpayers to have access to an efficient and practical discretionary grant process becomes increasingly important if the objective tests in the proposed LOB article are overly restrictive, with the result that a double tax agreement intended to provide treaty benefits for tax residents of the treaty partners only provides benefits for a limited class of tax residents absent a practical and expeditious process for the discretionary grant of treaty benefits. In the United States, the discretionary grant has been described as the "safety net" in recognition that the objective tests in the LOB article may unintentionally deprive bona fide residents of the treaty country access to the treaty and the protections it affords against double taxation and excessive taxation. Thus, we were disappointed that the discussion of the discretionary relief provision conveys a disturbingly restrictive approach, similar to many aspects of the proposed LOB article more broadly. Importantly, rather than providing greater clarity as to when the standard embodied in the proposed treaty text is met – establishing that the establishment, acquisition or maintenance of the resident, and the conduct of its operations, did not have a principal purpose of obtaining the benefits of the treaty – the proposed commentary focuses on placing burdens on the taxpayer of establishing its residency had a “clear non-tax business reason.” Would a resident company that previously met the publicly traded test and is acquired by a private equity fund be able to meet this clear business reason even if it could establish that there was not a principal purpose of obtaining treaty benefits? Would a company that established residency in the treaty country because the country provided tax incentives for locating manufacturing operations in an economically depressed area meet this standard? Adding additional restrictions to what was originally and appropriately described as a safety net makes the provision more in the nature of an additional limitation on treaty eligibility for treaty residents that are not treaty shopping, a result particularly inappropriate in a rule that already gives the tax authority broad discretion.
Our previously expressed concerns over the restrictive nature of the discussion draft continue to apply, including:

- The statement that the fact that a tested subsidiary company would obtain a treaty rate reduction no greater than could have been obtained by the parent company under its resident country’s treaty with the source country is not sufficient to establish the lack of a treaty shopping motive. The revised discussion draft continues to give insufficient attention to the serious problems of lengthy procedures that can leave a taxpayer deserving of access to the treaty with an extended period of uncertainty and deprivation of treaty benefits during the pendancy of the procedure. Determinations by a tax authority that a transaction violates the principal purpose test should be subject to the treaty’s mutual agreement procedure.

Requirement that each intermediate owner be a resident of either Contracting State

Our prior comments have detailed the reasons why a proscription on access to treaty benefits for a subsidiary company that otherwise meets the relevant LOB criteria based on the fact that the intermediate owner is not a resident of the state of residence of the tested company or, in the case of derivative benefits, an equivalent beneficiary, would extensively limit access to treaty benefits as non-resident/non-equivalent beneficiary intermediate owners are common for legitimate corporate reasons. We submitted in our prior comments that no coherent policy reason has been given for this limitation. The revised discussion draft notes that the tested company could make base eroding payments to the intermediate owner. However, the ability of a tested company to make base eroding payments to an affiliate has nothing to do with where the affiliate is in the group structure. Base eroding payments can be made to a sister company or a subsidiary for example and, in most cases, such payments are already subject to anti-base eroding rules and may be further limited by other proposals. The only relevance of an entity being an intermediate entity in the ownership chain is that dividends can be paid to the intermediate entity, and dividends do not erode the tax base of the tested entity. The proposed requirement would serve no policy goal and would place a severe restriction on the access to treaty benefits.

Proposed new restrictions on application of the “active business” provision

The active business test is based on the sound principle that if a treaty resident is engaged in the active conduct of a trade or business in the country of residence, it has a legitimate nexus to the resident country that establishes that it is not treaty shopping as long as the income for which treaty benefits are claimed is connected to that trade or business and, where the income is received from an affiliate in the source country, the business in the residence country meets a substantiality standard. The test is patterned after the comparable test found in most US income tax treaties. In those treaties, there is typically an attribution rule which allows business activities in the residence country conducted by an affiliate to be treated as conducted by the tested company. This is a recognition that business enterprises may organize their functions in the residence country through multiple entities, including a local holding company and, once it is established that there is a legitimate business presence in the residence country, it is artificial to handcuff the taxpayer to require all business connected income be
received directly by the entity conducting the business. The revised discussion draft notes that the US delegate has proposed that attribution only apply to a tested company if the tested company, itself, is conducting business. Under this proposal a dividend from an affiliate in the source country in the same trade or business would qualify if paid directly to a residence country operating subsidiary of the tested entity but not if the dividend is paid to the tested company in cases where it is a holding company that meets the test through attribution from the operating company. This would place an artificial restriction on taxpayers and is in conflict with decades of US tax treaty policy. It should be stressed that a holding company can obtain treaty benefits under the active business test only for income that is connected to the business; the provision is not an open door for holding companies to broadly obtain treaty benefits. To force the investment in the source country affiliate to be held by the operating entity, rather than the holding company simply impedes the right of the taxpayer to structure its operations in the residence country in a manner most compatible with corporate policy, typically dictated by operational efficiency. Accordingly, the proposal of the US delegate should be rejected as inconsistent with the intent of the test for no justifiable policy reason.

The design and drafting of the rule applicable to permanent establishments located in third States

USCIB does not support the proposal to delete subparagraph f) from the proposed provision relating to income derived by a permanent establishment situated in a third State. Deleting that subparagraph could potentially deny the availability of treaty benefits to royalties earned from the exploitation of an intangible asset generated through the value-creating activities of the PE itself. This would be contrary to the stated goals of the BEPS Project. The suggestion that recipients of such royalties should rely exclusively on subparagraph e), which relates to income derived in connection with or incidental to the active conduct of a business carried on through the PE, is not an adequate response, as that fails to take into account the possibility that some States might not view such royalties as derived in the active conduct of a business unless the PE continued to be engaged in the development of similar intangibles or the royalties were derived from unrelated persons.

USCIB supports the suggestions referenced at paragraph 106 of the RDD (i.e., that the rule denying benefits should not apply to PEs located in a country with which the State of source has a treaty if the effective rate of tax on the PE is not lower than 60 per cent of the rate of tax in that country; that the application of the rule should be subject to some form of discretionary relief similar to that found in paragraph 5 of the LOB rule; and that the rule should not focus on the existence of a low tax rate as such but should focus on situations where shares, loans or intangible rights or property are artificially transferred to a permanent establishment).

Proposed Commentary on the interaction between tax treaties and domestic anti-abuse rules

USCIB supports the statement made at paragraph 108 of the RDD that the conclusions already reflected in the Commentary on Article 1 concerning the interaction between treaties and domestic anti-abuse rules will remain applicable, in particular with respect to treaties that do not incorporate the PPT rule. The RDD indicates that the existing Commentary on Article 1 will nevertheless need to be reviewed (e.g., to prevent overlap with the new proposed Commentary and to take into account any recommendations
for domestic law anti-abuse rules arising from other Action Items, such as Actions 2, 3, 4, and 8-10). USCIB stresses the importance of preserving the conclusions already reflected in the Commentary on Article 1 in undertaking any such amendments, including the conclusions that could limit the application of new domestic law anti-abuse rules in certain cases.

Sincerely,

William J. Sample
Chair, Taxation Committee
United States Council for International Business (USCIB)
Dear Marlies,

The Confederation of Netherlands Industry and Employers VNO-NCW is pleased to provide comments on the Revised Discussion Draft on BEPS Action 6: Prevent Treaty Abuse that was published on 22 May 2015.

General comments

1. We are supportive of a common OECD framework to prevent treaty abuse. In fact, we feel that international consensus and consistent guidance by the OECD, EU and UN is key to improve the international tax system and achieve coherence therein, enhance economic growth, stimulate free trade and cross border investments.

2. The primary function of tax treaties is to benefit international trade and investments by allocating taxing rights and thus prevent double taxation. It is this function of tax treaties that needs to be fostered.

3. The rules determining whether or not access to tax treaty benefits is granted need to be clear, targeted and sustainable. Both taxpayers and governments must be able to rely on objective, predictable and clear-cut rules.

4. To provide the necessary legal certainty to taxpayers regarding the tax treatment of their investments, it is crucial that (1) taxpayers have the possibility to get pre-clearance regarding the access to treaty benefits, (2) the proposals and proposed changes to the Commentary provide ample guidance on the application
of both the proposed LOB and PPT rules, and finally (3) there should be unobstructed access to a mutual agreement procedure (MAP) and mandatory binding arbitration.

5. As the proposals do not yet meet these three conditions, it will be virtually impossible for most arm’s length parties to determine applicability of a certain treaty. Consequently compliance costs of doing business internationally will increase substantially as e.g. (external) tax opinions will be required in many more cases also to provide comfort to the external auditor.

6. Consequently, the unintended result of these proposals could very well be that taxpayers are deterred to engage in cross border trade and investments and as a result will have far-reaching adverse effects on economic growth and job creation.

Specific comments on issues related to the LOB rule

7. We welcome the clarifications that the revised Discussion Draft provides, however, we believe that the proposed alternative LOB rule will still deny treaty benefits to situations where there is no treaty abuse.

8. We welcome the clarification on the discretionary relief provision. However we strongly recommend there should be no unilateral discretion to deny benefits while at the same time there is no requirement to consult – and preferably agree – before either contracting state invokes the LOB or PPT and such a decision is denied access to proper dispute resolution mechanisms. The related changes in the Commentary on paragraph 5 of the LOB rule (i.e. paragraph 65) as proposed in paragraph 32 of the Draft have to be reconsidered.

9. To give the necessary certainty and prevent the unjust denial of treaty benefits resulting in double taxation and thus frustrating cross border trade and investments the LOB rule should focus on the ultimate beneficial owners and eliminate testing intermediary companies.

10. We strongly support a derivative benefit provision in the LOB. The derivate benefit provision would extend the granting of treaty benefits to entities that are controlled by entities that are resident of a third country and that would enjoy the same treaty benefits with the contracting state in question. In such situations, there is no incentive for treaty shopping.

11. We feel that the proposal for a new treaty provision on ‘special tax regimes’ as stated in paragraph 53 is out of place in this Discussion Draft. This issue should instead be considered under Action Point 5: Countering Harmful Tax Practices
More Effectively, Taking into Account Transparency and Substance.

12. We agree with the Working Party that there should be clarification on the active business provision, but note that the Discussion Draft – specifically paragraph 71 – does not provide such.

Specific comments on the issues related to the PPT rule

13. The wording of the proposed PPT rule is very wide and vague. This would allow tax authorities a very broad discretion to challenge the availability of treaty benefits. As a result, there is a risk of misinterpretation or misapplication by tax authorities.

14. The various technical examples aimed at providing more guidance regarding the PPT rule actually prove the difficulty that taxpayers will have in proving the requisite facts to prevent denial of treaty benefits.

15. We welcome the proposal in paragraph 79 that there should be some kind of administrative process that ensures that the PPT rule can only be applied after approval at a senior level. However, there also should be a requirement for contracting states to consult each other – and preferably agree – before invoking the PPT.

16. We welcome the proposal for a discretionary relief provision in paragraph 90 of the Discussion Draft.

17. There should be no unilateral discretion to deny benefits under the PPT rule.

18. We strongly recommend that the application of the PPT is subject to mandatory binding arbitration.

We hope you will take our comments into consideration in further developing this action point. Of course, we are available to elaborate on these comments should this be helpful.

Sincerely Yours,

Jeroen Lammers
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By email: taxtreaties@oecd.org

Berlin, 17 June 2015


Ladies and Gentlemen,  
dear Marlies,

ZIA, the German Property Federation (Zentraler Immobilien Ausschuss e.V.), represents German real estate business in its entirety, including real estate funds, real estate fund managers, and REITs. ZIA speaks on behalf of individual member firms and 25 member associations, thus representing 37,000 branch members.

ZIA welcomes and supports the work of OECD aiming at ameliorating the existing international tax framework towards more predictability and legal certainty while closing tax loopholes and eliminating international mismatches. We encourage OECD to pursue this way to promote a sound taxation climate for the benefit of taxpayers, tax administrations, and the society as a whole.

Referencing the REITs report

With regard to the draft we very much welcome the inclusion of a reference to the 2008 REITs report into a footnote to paragraph 31 of the Commentary on subparagraph 2 f) of the future LoB rule recommendation. Nevertheless, we think that a more holistic approach is needed. Such an approach should find its expression in the wording of a future Model Tax Convention itself, thus ensuring the treaty entitlement of REITs and an appropriate treatment with regard to limitation on benefits clauses and principal purpose tests.
Treaty entitlement of non-CIV funds and treaty shopping concerns

We commend the OECD’s commitment to the economic importance of non-CIV funds and to granting treaty benefits to non-CIV funds where appropriate. Treaty shopping should be tackled by

- defining an adequate percentage of equivalent beneficiaries, be it directly or indirectly, without excluding any wholly owned entities (directly or indirectly held special purpose vehicles) and regardless of the type of management (internally or externally)

or by

- referring to the existence and location of an adequate investment management in the country of residence.

Transparent entities

We appreciate that OECD sees transparent entities as an important and adequate structure for international investments by CIVs and non-CIVs. With regard to the practical consequences of the treaty entitlement of the individual investors we look very much forward to the indispensable relaunch and enhancement of the TRACE project.

We look forward to supporting future progress in this area of tax treaty policy and remain at your disposal.

With kind regards

Roland Franke
Head
Tax and Finance Department