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Dear Mr Owens

OECD DISCUSSION DRAFT OF THE REPORT ON THE ATTRIBUTION OF PROFITS TO A PERMANENT ESTABLISHMENT - PART IV (INSURANCE) ISSUED JUNE 27, 2005

On behalf of the XL Capital group of companies ("XL"), I am pleased to respond to the request for comments on the OECD Discussion Draft of the Report on the Attribution of Profits to a Permanent Establishment - Part IV (Insurance).

We have had involvement in and have had a significant input into the responses submitted by both the COMITE EUROPEAN DES ASSURANCES ("CEA") and the Business and Industry Advisory Committee to the OECD ("BIAC"). We do not therefore propose duplicating the comments made within their responses here; however, we would like to state that XL fully supports the comments and points of principle contained within their papers.

XL Capital

XL Capital, through its operating subsidiaries, is a leading provider of insurance and reinsurance coverages and financial products and services to industrial, commercial and professional service firms, insurance companies and other enterprises on a worldwide basis. XL has more than 3,300 employees in 90 locations in 30 countries. As of June 30 2005, XL Capital Ltd had consolidated assets of approximately \$53.3 billion and consolidated shareholders' equity of approximately \$8.4 billion.

The methodology in respect of the taxation of permanent establishments ("PEs") is of significant interest to XL.

Future Discussions with Working Party 6 ("WP6")

We believe that to date there has been insufficient discussion between WP6 and the insurance industry. We strongly recommend that if the OECD's timetable for completing Parts I – IV is still to be completed on time, further discussion is necessary as soon as this consultation period has ended. We believe that a meeting with a select few interested parties from the insurance industry would be beneficial, as this should allow a discussion of the real insurance related issues to take place. We would be very interested and happy to participate in this discussion.

Working Hypothesis ("WH")

We are concerned that testing of the authorised OECD approach by application to the insurance industry is not yet complete and we believe that it is incorrect to state that "the testing of the WH is reaching its conclusion and sufficient progress has been made in the development of the WH to mean that the WH has now become the authorised OECD approach" (Preface Paragraph 6) in respect of the insurance industry.

Factual and Functional Analysis of the Insurance Industry

We concur with the view that ultimately a facts and circumstances analysis is the most appropriate approach to reviewing the profit generating activities.

We believe that Part IV should also recognize that underwriting may be a loss-making activity and there should be no assumption that ceding commission will always produce a profit to the ceding entity (Paragraph 19).

The management of a business strategy for a multinational insurance enterprise should also be included in the Factual and Functional Analysis of an insurance business.

Impact of Regulation, particularly Host Country Regulation

As a Global insurance group, we understand that regulation plays a more significant part in insurance operations than noted in Part IV. Insurance PE's are often required by regulators to have surplus contributed or attributed to them.

We believe that the capital requirements currently in place in the insurance industry should be enough to elevate a quasi-thin capitalisation approach from a safe harbour for surplus allocation to an approved OECD approach, irrespective of what the OECD deems is the proper allocation for the purposes of Parts II and III.

Commercial Rationale for Inter-branch Reinsurance

There are many different commercial reasons for inter-branch reinsurance, the principle commercial purpose being the centralization of risk management; this provides for four key benefits: operational efficiencies, improvement to pricing, management on a portfolio basis and helping to manage the risk.

Intra-enterprise reinsurance is a very important tool under the hypothetical distinct and separate enterprise approach to obtain an arm's length result for tax purposes. By recognising intra-enterprise reinsurance dealings, it can be ensured that taxation occurs where the management of the business is actually performed. Intra-enterprise reinsurance reflects the transfer of the functions actually performed from one country to another, and thus ensures that tax revenues will be fairly allocated among the countries in question.

Risks Requiring Surplus

The primary risk requiring surplus under the surplus calculation of the various insurance industry regulators is insurance risk net of insurance risk transferred through reinsurance or an alternative risk transfer method.

Section C

Parts I, II and III focused on the activities of enterprises in branch form and did not attempt to modify the OECD Transfer pricing Guidelines for Multinational National Enterprises. The Authorised OECD approach is based on the application of Article 9 Principles to Article 7 situations. We strongly believe that WP6 should not attempt to modify Article 9 through Part IV. We recommend that the whole of Section C be removed.

With respect to the comments regarding harmful tax competition proper allocation of income under Article 9 or Article 7 will depend upon a functional analysis; the resulting allocation based in part on how a taxpayer legitimately sets up its operations, will be the same irrespective of the tax rates in the effected countries.

KERT Function

We believe that more practical guidance is necessary in order to provide taxpayers with some clarity regarding the weighting of functional activity, given that it is such a critical component of the KERT-based approach.

Compensation of Asset Management Function

The calculation of yield requires more in depth discussion. The fact that some assets may not be income bearing must be reflected in the allocation of the yield.

Attribution of Surplus

In the insurance industry we believe that rating agencies are able to (and indeed do) differentiate between a PE and its HO; as credit ratings are issued based on the mix of business, stratification of risk and available capital.

We believe that the OECD should work towards the acceptance of a single capital allocation approach, either using a single allocation key or multiple allocation keys. This is critical to reducing tax controversy and the risk of double taxation.

The time and expense of seeking unilateral or bilateral Competent Authority relief is not a welcome solution and should not be designed into a consensus set of tax administration guidelines such as these.

As stated above, we believe that the quasi-thin capitalisation approach should not merely be a safe harbour, but an approved OECD approach.

The most practical solution in most circumstances would be to utilize the local regulatory requirements in the country in which the PE is situated. Should no such local regulations exist, then the regulations of the home country should be used. The method of allocating capital to a PE should not result in a total allocation of capital to all PEs greater than the capital of the enterprise.

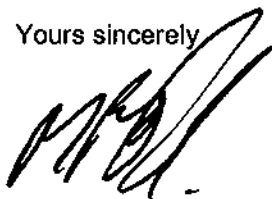
Part E

Until Part IV is finalised, so that it provides unambiguous guidance, we do not believe that Article 7(4) should be eliminated.

Conclusion

As stated above we believe that to date there has been insufficient discussion between WP6 and the insurance industry. We strongly recommend that if the OECD's timetable for completing Parts I – IV is still to be completed on time, some form of further discussion is required as soon as possible.

Yours sincerely



Mervyn Skeet
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