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July 19, 2011

Jeffrey Owens
Director, CTPA
OECD
2, rue André Pascal
75775 Paris
France

Re: Discussion Draft – Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention (the "Discussion Draft")

Dear Mr. Owens:

On behalf of the Securities Industry and Financial Markets Association (SIFMA)[1], we are writing in response to your request for comments on the Discussion Draft the OECD released on April 29, 2011.

Our members would welcome greater clarity and consistency in respect of the treatment of financial instruments that they hold for their own account and for the account of their customers. We applaud the OECD's effort to clarify the concept of beneficial ownership. We would, however, like to stress the importance of providing clear guidance to OECD member states so that measures that are intended to clarify the meaning of this important concept do not inadvertently have the effect of creating rather than reducing uncertainty. A definition of beneficial ownership that does not fully take account of the realities of financial transactions and markets, where financial institutions and investors must manage their risk in the ordinary course of their businesses, would give rise to significant market disruption.

The complexity of the concept of beneficial ownership, particularly in the context of interest and dividends, cannot be underestimated. Even putting aside the difficulties associated with efforts to develop a common definition for use by countries with different tax systems, tax authorities around the world have struggled to define the concept, and many have shied away from making rules based on beneficial ownership because of the definitional difficulty. The United States, for example, recently enacted rules intended to address concerns regarding the use of equity derivative transactions

[1] The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

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1101 New York Avenue, 8th Floor | Washington, DC 20005-4269 | P: 202.962.7300 | F: 202.962.7305

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involving U.S. equities. The rules quite deliberately do not seek to characterize swap counterparties receiving payments measured by reference to dividends on U.S. equities as the owners of the underlying shares, and instead impose withholding tax on dividend-equivalent payments on equity swaps without addressing this issue.

The Discussion Draft proposes to add to the Commentary's explanation of the term "beneficial owner" as used in Articles 10, 11 and 12 of the OECD Model Tax Convention (the "Model Convention") that "[t]he recipient of a [dividend, interest or royalty payment] is the 'beneficial owner' of that [payment] where he has the full right to use and enjoy the [payment] unconstrained by a contractual or legal obligation to pass the payment received to another person."

We are concerned about the breadth of this proposed formulation. We assume that it was intended principally to deal with custody, depositary and similar nominee arrangements. Read literally, however, it conceivably could call into question a taxpayer's entitlement to treaty benefits in the context of a broad range of everyday economic relationships where, we believe, there has never been a meaningful question concerning beneficial ownership. For example,

- A holding company that has announced its intention to distribute its earnings to public shareholders on a current basis conceivably could be said to have a legal or contractual obligation to remit interest and dividends received from its subsidiaries to its shareholders, but we believe that no tax authority would take the view that such an obligation affects the company's status as the beneficial owner of interests in its subsidiaries.

- A unit investment trust that is required by law to distribute its earnings in the year of receipt similarly is not considered to have transferred beneficial ownership of its portfolio to unitholders.

- A company that has significant arm's length indebtedness may be required by loan covenants to apply all of its free cash flow to make interest and principal payments on its outstanding debt. We believe that this fact pattern does not call into question the company's ownership of its assets, or cause its creditors to be deemed to own them.

We do not believe that any of these examples falls within the intended scope of the Commentary, or that the Commentary was intended to change the generally-accepted meaning of beneficial ownership , but the examples appear to fall within the literal scope of the proposed language.

As applied to complex financial transactions, the language regarding an "obligation to pass the payment received to another person" could call into question the entitlement to treaty benefits in a broad range of widely used financial arrangements, potentially causing a great deal of confusion in the market. For instance, it would be nearly impossible for custodians to determine whether a securities account holder is entitled to treaty benefits under the proposed formulation, and tax authorities in different jurisdictions could take divergent views given the openendedness of the proposed language. In global or American depositary receipt programs, depositaries are responsible for determining whether receipt holders are beneficial owners of dividends, and they would likewise have difficulty making such determinations.

We also believe that the proposed guidance was not intended to change the criteria applied to determine beneficial ownership in the context of hedging arrangements (where the holder of an interest in a financial instrument enters into a transaction to hedge interest rate or foreign exchange exposure or to reduce its risk of loss on equity, credit or commodity positions, and as a result may have an obligation to make payments measured by reference to the return on the hedged position) or conventional derivative transactions (in which a dealer or market maker agrees to make payments determined by reference to the return on a specified reference asset, but is not obligated to hold the reference asset, does not pledge the asset as collateral, and does not pass through voting or other contractual rights associated with ownership of the reference asset). A wide variety of financial products involve payments determined by reference to the return on an underlying security but are not thought to transfer beneficial ownership of the security to the recipient of those payments.

In a conventional credit default swap, for example, the protection buyer—the party that will receive a very substantial net payment upon the occurrence of a credit event—is not obligated to own an interest in the underlying reference obligation or to deliver that obligation upon the termination of the swap, and the protection seller—the party that will be required to make a very substantial net payment upon the occurrence of a credit event—has no right to participate in bondholders' meetings or to play any role in a restructuring of the issuer of the reference obligation. The guidance should be revised to indicate clearly that, in the absence of other unfavorable facts, a conventional credit default swap does not constitute a transfer of beneficial ownership of the reference obligation.

We believe that clear examples in the Commentary to confirm that the conventional financing, hedging and derivative arrangements of the kind described above do not affect a treaty resident's claim to beneficial ownership for purposes of the Model Convention would go a long way toward providing certainty for participants in the financial markets. If considered desirable, the Commentary could provide guidance on relevant factors to be considered, and the weight to be given to each factor, in the analysis of beneficial ownership. Consideration should be given to a recipient's economic entitlements (such as risk of loss, opportunity for gain and

residual value) and legal entitlements (such as notice provisions, voting rights, veto rights, creditor and default rights, workout participation rights and rights to physical settlement) to use and enjoy a dividend or interest payment under local law.

We would welcome the opportunity to assist the OECD in developing and refining a considered definition of beneficial ownership that addresses the OECD's policy objectives while minimizing the risk of unintended consequences. Given SIFMA's membership, we have first-hand exposure to relevant facts and particular familiarity with the issues they implicate, including the complications and concerns that an ambiguous definition would cause in the global marketplace, and we would be pleased to work with you on an ongoing basis. If you have any questions, please contact Benjamin Lopata, Chairman, Committee on Federal Taxation, Securities Industry and Financial Markets Association (lopata_benjamin@jpmorgan.com; 212-552-1040).

Sincerely,

N. Ellen McCarthy
Managing Director,
Government Affairs
and Tax Counsel
Securities Industry and Financial
Markets Association