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Ref: DISCUSSION DRAFT: BEPS ACTION 6 – "NON-CIV EXAMPLES"

Dear Mr. VanderWolk,

Thank you for the opportunity to comment on the *Discussion Draft: BEPS Action 6 – Non-CIV Examples* ("the Discussion Draft") issued on 6 January 2017. We acknowledge and thank the OECD for the time and effort put into this draft and the opportunity to provide comments.

BIAC welcomes the work undertaken by the OECD to provide clarity around the treaty entitlement of non-CIV funds. We believe that the Discussion Draft represents a valuable start in helping us to understand the OECD's position on tax treaty entitlement of non-CIV funds.
Additionally, BIAC commends and supports the OECD's observation that the TRACE project could serve as a critical tool in providing tax certainty for non-CIV funds with respect to their ability to obtain treaty relief, and to this end we encourage the OECD and participating States to enhance the operation and availability of TRACE. We would welcome the opportunity to provide additional assistance to help the OECD meet this objective.

The examples included in the Discussion Draft are a helpful starting point, and we believe that some modifications and additional examples would provide a greater degree of certainty to many common investment structures that are relevant to non-CIV investment funds, which is essential to encourage continued cross-border investment and growth. While we understand the breadth of examples received and carefully considered by the OECD, we believe that the three examples included are not sufficient in quantity or diversity to provide the necessary guidance for taxpayers and tax authorities to cover many common commercial investment structures that are relevant to non-CIV investment funds. The examples included to support the application of the BEPS Action 6 Recommendations should be sufficiently detailed to provide guidance under the common facts and circumstances of a wide range of non-CIV funds in order for such examples to be applied effectively and consistently.

Again, we thank you for the opportunity to comment on this discussion draft, and look forward to working with you further on this project.

Sincerely,

Will Morris, Chair
BIAC Tax Committee

General Comments

1. BIAC believes that the examples included in the Discussion Draft frame a standard of business activity in the State in which the non-CIV fund seeks to access treaty benefits that is unrealistic in comparison to the structure of almost all non-CIV funds. In particular, Example 1 (*Regional investment platform)* describes a non-CIV fund that not only employs an experienced local management team to review, approve and monitor investments, but also to carry on treasury functions, maintain the books and records, and ensure regulatory compliance. While we support the requirement for there to be sufficient business substance in a State for which treaty benefits are sought, the standard for such activities should be within the parameters of what is realistic in practice and crucially is consistent with what is required for other taxpayers that are not non-CIV funds. The treasury, accounting, and regulatory functions are often performed from a location separate from the non-CIV fund and this geographical separation occurs for legitimate commercial reasons including, but not limited to, administrative simplicity and centralised management. Many other types of taxpayers also perform their treasury, accounting, regulatory and other "back-office" functions from locations that are separate from their core revenue generating activities. Therefore, we urge the OECD to caution against creating an implicit safe harbour from a set of facts and circumstances that do not accurately reflect the structure of the vast majority of non-CIV funds.
2. The examples included in the Discussion Draft imply a threshold whereby no single investor in a non-CIV fund may obtain treaty benefits that are better than the benefits to which it would have been entitled if they had made the same investment directly. While there are mechanisms to confirm whether investors would be entitled to the same treaty benefits had they invested directly, it is likely there will be instances where a small minority of the underlying investors in a non-CIV fund would not be entitled to equivalent benefits. The denial of treaty benefits to a non-CIV fund in such a case would seem to potentially run counter to the overall objective of encouraging continued cross-border investment growth, and also be at odds with the application of the PPT to other taxpayers (which may, for example, have a minority of shareholders residing in non-treaty partner States). Moreover, where the non-CIV fund itself or an entity set up by the non-CIV fund is established in a certain jurisdiction for legitimate business reasons that are not principally motivated by obtaining treaty relief, it is not clear why application of the principal purpose test would then require that no investor at all can obtain treaty benefits that are better than the benefits it would have been entitled to if it invested directly.
3. We were hopeful there would be examples that provide guidance for taxpayers and tax authorities as to those facts and circumstances that may *prevent* a non-CIV fund from accessing treaty benefits in a particular State. In other words, in what circumstances would a non-CIV have demonstrated a principal purpose to avail itself of the benefits of a tax treaty. We would encourage such an example to be drafted in a manner that provides a valuable contrast from the examples currently included in the Discussion Draft. In addition to understanding the commercial activities and particular motivations necessary to access treaty benefits, it is of critical importance that non-CIV funds also understand the level of commercial activity and/or particular motivations that may result in a denial of treaty benefits.
4. We encourage the inclusion of additional examples as a means to provide greater clarity surrounding what constitutes a non-CIV fund. The examples included in the Discussion Draft are limited to private market and real estate investments with no accommodation for non-

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CIV funds that are trading in public securities. It is critical that the examples included in the BEPS Action 6 Guidance do not unintentionally carve out non-CIV funds which would otherwise meet the requisite standards for accessing treaty benefits in any particular State.

5. BIAC notes that the examples included in the Discussion Draft appear to omit consideration of the Global Streamed Fund (GSF) approach, or any similar approach. The omission of such an approach from the examples and further guidance related to non-CIV funds risks a result whereby institutional investors will be diligent in ensuring that investors which might damage potential treaty relief are excluded at all stages of the fund where the imposition of a holding company could result in a worse outcome than direct investment. This will result in making the choice of special-purpose vehicle very difficult.
6. Additionally, the examples included in the Discussion Draft also lack guidance for taxpayers and tax authorities with regard to the application of the PPT to fund-of-fund structures. BIAC welcomes examples to provide clarity on this common structure that faces the difficulty of identifying the tax residence of its investors.
7. We are mindful that tax authorities are concerned that the granting of treaty benefits to non-CIV funds could result in investors deferring recognition of income on which treaty benefits have been granted. However, absent from the examples in the Discussion Draft is guidance for non-CIV funds seeking to establish a vehicle in a State without regard to income deferral. Therefore, it would be beneficial to include an example whereby a non-CIV is established in a particular State for legitimate commercial reasons and without regard for accessing a particular deferral regime.
8. Finally, we have suggested specific edits to the three examples currently included in the discussion draft (*see* Appendix A). While these edits are not intended to fully reflect the comments included in paragraphs 1-7, BIAC believes these changes do represent the minimum necessary to further develop the existing examples and provide the necessary guidance regarding non-CIV funds.

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Appendix A

1. Regional investment platform example

Example [*XX*]: RCo, a company resident of State R, is a wholly-owned subsidiary of Fund, an institutional investor that is a resident of State T and that was established ~~and is subject to regulation~~ in State T. RCo operates exclusively to generate an investment return as the regional investment platform for Fund through the acquisition and management of a diversified portfolio of investments~~private market investments~~ located in countries in a regional grouping that includes State R. The decision to establish the regional investment platform in State R was mainly driven by the availability of directors with knowledge of regional business practices and regulations, the existence of a skilled multilingual workforce, State R's membership of a regional grouping ~~and use of the regional grouping's common currency~~, and the extensive tax convention network of State R, including its tax convention with State S, which provides for low withholding tax rates. RCo employs an experienced local management team to review investment recommendations from Fund and approve and monitor investments~~arry on treasury functions, maintain RCo's books and records, and ensure compliance with regulatory requirements in States where it invests~~. The board of directors of RCo is appointed by Fund and is composed of a majority of State R resident directors with expertise in investment management, as well as members of Fund's global management team. RCo pays tax and files tax returns in State R.

RCo is now contemplating an investment in SCo, a company resident of State S. The investment in SCo would constitute only part of RCo's overall investment portfolio, which includes investments in a number of countries in addition to State S which are also members of the same regional grouping. Under the tax convention between State R and State S, the withholding tax rate on dividends is reduced from 30 per cent to 5 per cent. Under the tax convention between State S and State T, the withholding tax rate on dividends is 10 per cent.

In making its decision whether or not to invest in SCo, RCo considers 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, including the reasons for establishing RCo in State R and the investment functions and other activities carried out in State R. In this example, in the absence of other facts or circumstances showing that 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. Securitisation company example

Example [*XX*]: RCo, a securitisation company resident of 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 share which is held on trust and has no economic value. RCo's debt finance was raised through the issuance of notes that are widely-held by third-party investors. ~~The notes are listed on a recognised stock exchange, which allows for their trading on the secondary market, and are held through a clearing system.~~ To comply with regulatory requirements, the bank also retained a small percentage of the ~~listed~~ widely-held debt securities issued by RCo. RCo currently holds 60 per cent of its portfolio in receivables of small and medium sized enterprises resident in State S, in respect of which RCo receives regular interest payments. The bank is a resident of a State T which has a tax treaty with State S that provides benefits equivalent to those provided under the State R-State S tax treaty. Under the tax treaty between State R and State S, the withholding tax rate on interest is reduced from 30 per cent to 10 per cent.

In establishing RCo, the bank took into account a large number of issues, including State R's robust securitisation framework, its securitisation and other relevant legislation, the availability of 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. 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 enterprises 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, in the absence of other facts or circumstances showing that 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.

3. Immovable property non-CIV fund example

Example [*XX*]: Real Estate Fund, a State C partnership treated as fiscally transparent under the domestic tax law of State C, is established to invest in a portfolio of real estate investments in a specific geographic area. Real Estate Fund is managed by a regulated fund manager and is marketed to institutional investors, such as pension schemes and sovereign wealth funds, on the basis of the fund's investment mandate. A range of investors resident in different jurisdictions commit funds to Real Estate Fund. The investment strategy of Real Estate Fund, which is set out in the marketing materials for the fund, is not driven by the tax positions of the investors, but is based on investing in certain real estate assets, maximising their value and realising appreciation through the disposal of the investments. Real Estate Fund's investments are made through a holding company, RCo, established in State R. RCo holds and manages all of Real Estate Fund's immovable property assets and provides debt and/or equity financing to the underlying investments. RCo is established for a number of commercial and legal reasons, such as to protect Real Estate Fund from the liabilities of and potential claims against the fund's immovable property assets, and to facilitate debt financing (including from third-party lenders) and the making, management and disposal of investments. It is also established for the purposes of administering the claims for relief of withholding tax under any applicable tax treaty. This is an important function of RCo as it is administratively simpler for one company to get treaty relief rather than have each institutional investor process its own claim for relief, especially if the treaty relief to which each investor would be entitled as regards a specific item of income is a small amount. After a review of possible locations, Real Estate Fund decided to establish RCo in State R. This decision was mainly driven by the political stability of State R, its regulatory and legal systems, lender and investor familiarity, access to appropriately qualified personnel and the extensive tax convention network of State R, including its treaties with other States within the specific geographic area targeted for investment. ~~RCo, however, does not obtain treaty benefits that are better than the benefits to which its investors would have been entitled if they had made the same investments directly in these States and had obtained treaty benefits under the treaties concluded by their States of residence.~~

In this example, whilst the decision to locate RCo in State R is taken in light of the existence of benefits under the tax conventions between State R and the States within the specific geographic area targeted for investment, it is clear that RCo's immovable property investments are made for commercial purposes consistent with the investment mandate of the fund. ~~Also RCo does not derive any treaty benefits that are better than those to which its investors would be entitled and each State where RCo's immovable property investments are made is allowed to tax the income derived directly from such investments.~~ In the absence of other facts or circumstances showing that RCo's investments are part of an arrangement, or relate 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 tax treaties between RCo and the States in which RCo's immovable property investments are located.

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