William Morris
Chair, BIAC Tax Committee
13/15, Chaussée de la Muette, 75016 Paris

Achim Pross
Head, International Co-operation and Tax Administration Division
Organisation for Economic Cooperation and Development
2 rue André-Pascal
75775, Paris, Cedex 16

September 8, 2016

Ref: DISCUSSION DRAFT: BEPS ACTION 4 – "APPROACHES TO ADDRESS BEPS INVOLVING INTEREST IN THE BANKING AND INSURANCE SECTORS"

Dear Achim,

Thank you for the opportunity to comment on the Discussion Draft: BEPS Action 4 – *Approaches to Address BEPS Involving the Banking and Insurance Sectors* ("the Discussion Draft"). BIAC was pleased that the Action 4 Final Report published in October 2015 acknowledged it would be inappropriate to apply its main recommendations to the banking and insurance sectors and that further analysis was required.

While we welcome the reinforcement in the Discussion Draft of the uniqueness of financial services businesses and recognition of the fact that debt is not a significant BEPS risk for this sector, we are disappointed that the Discussion Draft did not develop a best practice recommendation. The BEPS Project has always sought to introduce consistency between different tax systems, and an overlapping system of different optional rules, as set out in the Discussion Draft, will frustrate that aim. It will also create additional uncertainty and complexity for business and tax authorities alike, with no particular impact on reducing actual BEPS activity.

The attached BIAC paper suggests a best practice rule. In summary, prudential regulatory constraints on the banking and insurance sectors already restrict the use of debt in these businesses. For banking and insurance groups ***predominantly*** engaged in the active conduct of banking and insurance businesses that are ***globally regulated*** (referred to in the attached paper as Regulated Finance Groups or "RFGs"), prudential regulation is substantial and increasing. BIAC's view is that the primary option in the Discussion Draft of disaggregating solo-regulated entities from all other entities in RFGs and applying the fixed ratio limit to the other entities is misguided. It would create the potential for tension with regulatory considerations even though the Discussion Draft itself found little BEPS risk. As a consequence, BIAC advises, as a best practice recommendation, that RFGs be exempted from Action 4.

The attached BIAC paper explains there are existing tax rules in different jurisdictions that adopt the notion of financial services groups. The attached paper also mentions different countries' approaches to prudential regulation of financial services groups and thus builds on the Discussion Draft's Annex 2 description of capital regulation in the banking and insurance sectors. The BIAC comments that follow make the point that to be considered "globally regulated" a financial services group would either be subject to global "umbrella" regulation by the regulator of the home country of its ultimate shareholder, or would have the substantial majority of its gross income earned from entities subject to prudential regulation within the financial services group.

The attached BIAC comments also observe that the EU Anti-Tax Avoidance Directive elevates Action 4 to a minimum standard and therefore EU Member States are legally obliged to implement interest limitation rules. The move towards a legally binding (albeit not fully harmonised) approach at EU level is to be contrasted with the Discussion Draft where there is a movement away from a best practice approach to a series of flexible options for the banking and insurance sectors to be considered by countries. BIAC is hopeful this will be changed in the final the Discussion Draft recommendations. BIAC believes it sets a better international standard for global guidance for the OECD to adopt a best practice rule for RFGs.

For completeness, the attached BIAC comments will also address the attribution of free capital to permanent establishments of banks and insurance companies, and the issue of interest expense funding non-taxable income, both of which are raised in the Discussion Draft.

We would welcome the opportunity to discuss our comments with you or assist in any other way that you would consider helpful.

Sincerely,

Will Morris

Will Morris, Chair BIAC Tax Committee

BIAC THE VOICE OF BUSINESS AT THE OECD

ACTION 4 Public Discussion Draft "Approaches to Address BEPS Involving Interest in the Banking and Insurance Sectors"

Background and Introduction

1. BIAC welcomes the opportunity to comment on the OECD's discussion draft on BEPS Action 4 on Approaches to Address BEPS Involving Interest in the Banking and Insurance Sectors ("the Discussion Draft"), released on July 28, 2016. BIAC observes that the Discussion Draft is required because of the conclusions reached in Chapter 10 of the OECD's October 2015 Final Report on Action 4 ("Chapter 10").
2. The OECD/G20 consensus in the Action 4 Final Report at paragraph 183 was that "a number of particular features of groups in the banking and insurance sectors need to be taken into account" and, further at paragraph 190, that more work was to be done "to identify best practice rules to deal with potential base erosion and profit shifting risks posed by banks and insurance companies, taking into account the particular features of these sectors."
3. BIAC's own comments of February 6, 2015 (in response to the Discussion Draft on Action 4 released on December 18, 2014) applauded the development of best practice rules stating at the very beginning of its comment letter that "BIAC supports the development of tax rules based on 'best practices' as a general matter."
4. BIAC also cautioned that while it "agrees that efforts to develop best practices … should minimise distortions in investment and competition, minimise administrative/compliance costs to tax authorities and taxpayers, avoid double taxation, promote economic stability and provide certainty of outcomes, in addition to addressing BEPS concerns. Tax rules that create significant collateral economic damage should not be considered as 'best practice' rules."
5. BIAC continues to hold these views and it is against this background that the following comments are submitted.

Preliminary Points and Overview

6. BIAC commends the Discussion Draft for acknowledging that interest expense for the banking and insurance sectors "is broadly comparable with … cost of sales for entities in non-financial sectors" (page 5). BIAC also appreciates the Discussion Draft's recognition of the significant role of prudential regulation and regulatory capital requirements imposed on these sectors (page 5 and Annex 2).
7. BIAC is however disappointed that the Discussion Draft has deviated from developing best practice rules as directed in Chapter 10. Instead, as stated in the OECD's press release of July 28, 2016, the Discussion Draft takes an approach where "flexibility is provided for a country to take into account the particular features of its tax law and policy… [where] stakeholders [are provided] with substantive options ... ." Paragraph 27 of the Discussion

13/15 Chaussée de la Muette, 75016 Paris, France
Tel. +33 (0)1 42 30 09 60 | Fax +33 (0)1 42 88 78 38
email: biac@biac.org | www.biac.org

Draft states, in contradiction with Chapter 10 just seven months earlier, "there is no need at this time to develop a single common approach … ."

8. BIAC is concerned that adoption by different countries of flexible, and thus different, options that derived from the fixed ratio and group ratio rules will create confusion, complexity and uncertainties for tax administrators and MNEs in the banking and insurance sectors. Such flexibility will also result in double taxation and critically risks providing fiscal incentives that could contradict regulatory oversight and control.

9. One of the options described in the Discussion Draft is to disaggregate banking and insurance groups into solo regulated entities and other entities for purposes of the fixed ratio rule (paragraphs 48 to 53) with knock on effects for the group ratio rule (paragraphs 62 to 67 with examples in Annex 3). This disaggregation option, if adopted mandatorily by countries, would run the risk of conflicting with regulatory and prudential requirements that seek to constrain debt in relation to equity. This is because the fixed ratio and group ratio rules of Action 4 favour consistent leverage among group companies. This could result in some group members having more leverage than regulators may deem prudent.

10. Mandatory disaggregation would also increase tax complexity and thereby increase administrative and compliance costs for tax authorities and taxpayers. Further, disaggregation introduces the possibility that interest on third party debt raised by a holding company could be disallowed as the EBITDA of the holding company may be low or even negative. It is also important to note that disaggregation with an exception for only solo-regulated entities could have unintended consequences with different outcomes as between different participants in the banking sector depending on the geographic and other mix of business and entities.

11. We do not believe that mandatory disaggregation of banking and insurance groups of companies should be included as an option under the Discussion Draft's flexible approach for those banking and insurance groups that are (i) predominantly engaged in the active conduct of banking and insurance businesses in multiple jurisdictions and (ii) are subject to global regulation either because (a) there is a home country prudential regulator of the shareholder of the financial services group of companies or (b) the greater part[*] of gross income is from regulated entities in the financial services group (hereafter referred to as Regulated Financial Groups or "RFGs").

12. RFGs are different from groups of MNEs primarily engaged in non-financial activities that have regulated financial entities embedded within such MNEs. RFGs make extensive use

[*] This implies 50%, but BIAC acknowledges that a different threshold may be appropriate. Additional analysis could be undertaken to identify what the appropriate threshold percentage should be. BIAC would welcome the opportunity to assist in this analysis if this would be helpful to the OECD.

13/15 Chaussée de la Muette, 75016 Paris, France
Tel. +33 (0)1 42 30 09 60 | Fax +33 (0)1 42 88 78 38
email: biac@biac.org | www.biac.org

of debt, both intercompany throughout the group and third party debt, for valid commercial reasons and to be compliant with regulatory obligations.

13. Disaggregating RFGs to impose Action 4's fixed ratio and group ratio rules on parts of the RFGs would interfere with the ordinary course of business of RFGs and would not reflect regulatory constraints within which RFGs operate. Further, disaggregation could have the effect that banks and insurers are put in a worse positon in relation to the group ratio rule than other sectors when it is generally acknowledged that BEPS risk for banks and insurers is low. We believe that best practice, as directed by Chapter 10, would be to not subject RFGs to Action 4's fixed ratio and group ratio rules.

14. If best practice is not adopted in the final recommendations, then additional options should be provided in the final report. One such option countries could adopt would be that RFGs not be subject to the fixed ratio and group ratio rules given the operations of RFGs and the protection from BEPS already afforded by the regulatory environment. Another option would be to broaden the exception for solo-regulated entities so that, in addition to solo regulated entities being excluded from the fixed ratio and group ratio rules (a current option in the Discussion Draft), holding companies, service companies and other entities that are core entities in the RFG must also be excluded.

15. The impact of the EU's Anti-Tax Avoidance Directive, ("ATAD") should also be considered. ATAD includes provisions based on (although not wholly in line with) the BEPS Action 4 interest fixed ratio and group ratio recommendations for EU members. These are thus no longer "best practices" for EU states, rather they are "minimum standards". Accordingly, it should be considered how the flexibility in proposals put forward by the OECD in relation to this ongoing work on Action 4 will interact with the ATAD requirements placed on EU member states.

16. For completeness, our comments below will also address the attribution of free capital to permanent establishments of banks and insurance companies, and the issue of interest expense funding non-taxable income, both of which are raised in the Discussion Draft.

Why Best Practice is Preferred

17. BIAC recognises some might think excluding banking and insurance entities from the Action 4 recommendations would be a "free pass". It is not. The regulatory rules faced by the banking and insurance sectors are unique and substantial. They have been put in place for important systematic reasons and impose meaningful and serious constraints on the banking and insurance sectors. While BIAC agrees with the Discussion Draft at paragraph 20 that "differences exist in how regulators and tax authorities may view the issue of excessive leverage[,]" these differences must be judged in light of (i) the finding at paragraph 26 that excessive leverage in the banking and insurance sectors has not been found, and (ii) the significant international efforts to provide a consistent global framework for prudential regulation.

18. Further, BIAC understands there can be a place for targeted rules, and supports the Discussion Draft statement at paragraph 43 that targeted rules should be considered to address BEPS risks. BIAC observes that the risks listed in paragraph 43 as BEPS risks cover all industries and sectors, and the risk enumerated in that paragraph are not specific to the banking and insurance industries.

19. BIAC also agrees with paragraph 44 of the Discussion Draft that targeted rules applied across all industries "may have an unintended or excessive impact if applied to a bank or insurance company without modification" and also agrees that if targeted rules are applied to banks and insurance companies such targeted rules should take into account the particular characteristics of banks and insurances companies ... ." Critically, any specific targeted measures must be informed by and coordinated with regulatory rules. If an interest-related BEPS risk is found by a taxing authority to exist, then the tax authority should engage with the regulators, when seeking to develop targeted tax rules, to ensure that tax rules and regulatory rules are not in conflict. Tax authorities should be encouraged to be proactive in avoiding conflict with regulatory rules and financial system objectives.

20. The Discussion Draft accepts that the risk of BEPS activities in banks and insurance companies from excessive leverage is low. Paragraph 26 explains: "In connection with the work on Action 4, excessive leverage in a bank or insurance company has not been identified as a key risk at this point in time and so it is anticipated that, in the majority of cases, this risk will be low." BIAC understands this is, in large measure, attributable to regulatory supervision of the banking and insurance sector with the objective of financial stability and soundness, and this is acknowledged at various places in the Discussion Draft, including Annex 2.

21. Even though the Discussion Draft concludes that the risk of BEPS is low, it diverges from its terms of reference found in Chapter 10 to "identify best practice rules." Instead, the Discussion Draft describes a variety of approaches and invites countries to use the information to address the risks of BEPS as specifically determined by each country. Thus, if the Discussion Draft is finalised in its present form, then different countries would be encouraged to adopt different rules that implement Action 4's fixed ratio and group ratio rules in different ways.

22. While different countries have a wide range of reasons for implementing different tax rules, the adoption of tax laws by countries based on different options that derive from the fixed ratio and group ratio rules clearly creates the potential for confusion, complexity and uncertainties for both tax administrators and MNEs in the banking and insurance sectors. Adoption of consistent international tax rules aligned with prudential regulation should be the goal.

23. The OECD / G20 consensus on Action 4 voiced in Chapter 10 was that common approaches and best practices should be adopted in this area. Chapter 10's mandate to identify best practice for the banking and insurance sector was and continues to be prudent in the base case and is even more so given the significant multijurisdictional, cross-border business activities of a major portion of the banking and insurance industries.

24. BIAC therefore suggests that the mandate set forth in Chapter 10 be followed and that it be followed based on the facts that have been found as set forth in the Discussion Draft. Given there is a low risk of BEPS by banking and insurance sectors from excessive leverage, the best practice rule should be that this sector not be subject to the fixed ratio and group ratio rules of BEPS Action 4.

What Are RFGs?

25. As mentioned at the outset of these comments, Chapter 10 (at paragraph 183) stated that "a number of *particular features of groups* in the banking and insurance sectors need to be taken into account." (Emphasis added.) BIAC realises that the best practice suggested above needs to be put within parameters and, building on Chapter 10's paragraph 183, BIAC suggests it be limited to groups that have particular features (i.e., groups of companies meeting certain criteria).

26. The rule to be designed would, in our view, be limited to (i) groups of companies predominantly engaged in the active multijurisdictional conduct of banking and/or insurance businesses and (ii) regulated by a regulator with a global mandate and global scrutiny, or where more than half of the group's gross income is from regulated entities in the group. A definition would thus be needed for this purpose of "group" and understandings would be required of what the active conduct of multijurisdictional banking and/or insurance businesses means, as well as what "predominantly engaged" in such businesses means. Further, definitions of "global regulation by a prudential regulator" and "a group that derives the greater part of its financial services income from entities that are regulated" would be required.

27. These criteria and definitions can be designed with reference to the actual operations and structure of groups that make up the banking and insurance sectors. Much work has already been done in this regard as evidenced throughout the Discussion Draft. Also, as explained below, these criteria and definitions can be adopted (and tweaked) from rules already in place in various jurisdictions for tax and regulatory purposes.

28. As an example of rules that are instructive, tax rules in the US (in the context of foreign tax credit limitation rules) provide that if a group of companies meets the test of being predominantly engaged the in active conduct of financial services business (and thus a "Financial Services Group"), then every member qualifies. See Section 904(d)(2)(C) of the Internal Revenue Code of 1986 and Treas. Reg. Section 1.904-4(e)(3).[*]

29. Likewise, in the UK, a similar concept is employed in the worldwide debt cap rules of the Taxation (International and Other Provisions) Act 2010 ("TIOPA 2010"). The worldwide debt cap rules don't apply to qualifying financial services groups under section 261(2) of TIOPA 2010 and a group is a qualifying financial services group if, broadly, all or substantially all of the UK trading income, or the worldwide trading income of the worldwide group for the period is derived from lending activities (and activities ancillary thereto), insurance and insurance-related activities, and relevant dealing in financial instruments.

30. BIAC is not suggesting these are the only rules, or necessarily the best rules, but merely that these rules contemplate these issues and are thus informative.

31. On the regulatory side, there are examples of regulators with global "umbrella" regulatory reach. Again, as examples, in the US the Bank Holding Company Act provides for consolidated supervision by the US prudential regulators of US banking groups headed by a Bank Holding Company; in the EU Article 11 of the Capital Requirements Regulation similarly requires consolidated supervision of EU banking groups at the level of the top EU holding company; and in Japan similar requirements are established under Article 52-25 of the Banking Act, and Announcement 20, *Standards on Regulatory Capital for Bank Holding Companies*. Likewise, the Solvency II regime in the EU is informative in this regard for insurers in the EU. Insurers headquartered outside the EU could be considered globally regulated if the great part of their financial services income is generated by regulated companies within the group.

32. These instructive rules, many of which already exist, could be used to design a best practice rule to define RFGs that would be excluded from the fixed ratio and group ratio rules of Action 4. BIAC would be please to assist in this effort.

[*] Section 904(d)(2)(C) provides: "Financial services income shall be treated as general category income in the case of ... a member of a financial services group [and] 'financial services group' means any affiliated group ... which is predominantly engaged in the active conduct of a banking, insurance, financing or similar business. "Predominantly engaged" is defined in Treas. Reg. Section 1.904-4(e)(3) to require that 80 percent of gross income be derived from the active conduct of a financial business.

13/15 Chaussée de la Muette, 75016 Paris, France
Tel. +33 (0)1 42 30 09 60 | Fax +33 (0)1 42 88 78 38
email: biac@biac.org | www.biac.org

33. Given there are rules in various countries to define financial service groups and global umbrella regulation, RFGs need to be distinguished from MNEs that are primarily engaged in other business activities, but have regulated entities embedded within them. While MNEs in other industries use debt to finance their core businesses (or to assist their customers to finance the purchase MNE goods), debt is the core of an RFG business. This is encapsulated in the Discussion Draft statement that interest expense for the banking and insurance sectors "is broadly comparable with … cost of sales for entities in non-financial sectors" (page 5).

Summary of Suggested Best Practice Rule

34. Given the points made above, BIAC suggests a best practice rule which has three prongs. First, RFGs should be exempted from the fixed income and group ratio rules of the Action 4 Final Report. Second, MNEs that are not RFGs, but have regulated entities embedded in them, would be subject to the fixed income and group ratio rules but should be permitted to elect out of the disaggregation rule found in the Discussion Draft.[†] Third, targeted rules should be considered to address identified BEPS risks, but any targeted rules should take account of the characteristics of RFGs and the impact and consequences of regulation to avoid unintended or excessive impact.

Impact of EU's ATAD

35. On July 12, 2016, the Council of the European Union ("EU") adopted the Anti-Tax Avoidance Directive ("ATAD").[‡] The ATAD entered into force, as binding European Union law, on August 8, 2016, and compels EU members to adopt and publish rules necessary to comply with the ATAD (with some derogations) by December 31, 2018 and apply those rules from January 1, 2019. Article 4 of the ATAD provides for an interest limitation rule, reflecting (with some differences) the OECD's Action 4 on the limitation of deduction of interest. EU Member States are, in essence, therefore legally obliged to implement interest limitation rules. Thus, the ATAD has effectively elevated Action 4 from its best practice status in the OECD October 2015 Final Report on Action 4 to a "minimum standard" that must be adopted into law by EU members.

36. BIAC notes that paragraph 7 of Article 4 of ATAD permits (but does not oblige) Member States to exclude "financial undertakings" (which includes regulated banks and insurers)

[†] BIAC suggests that thought be given to situation where an unregulated entity, which is part of an MNE (that is not an RFG), is itself primarily engaged in financial activities as a stand-alone entity. In such cases, disaggregation of the embedded financial entity from the MNE may be the proper outcome. In other words, the status of being regulated or not should not necessarily determine whether disaggregation should apply in the context of MNEs that are not RFGs.

[‡] COUNCIL DIRECTIVE (EU) 2016/1164 of July 12, 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market. http://eur-lex.europa.eu/legalcontent/EN/TXT/PDF/?uri=CELEX:32016L1164&from=EN

from the scope of the interest limitation rules, including where such financial undertakings are part of a consolidated group for financial accounting purposes).[§] The ATAD does not however provide currently for any alternative approach to be applied to financial undertakings. Subject to the point below, Member States must either apply interest limitation rules to financial undertakings or not apply such rules. There are no other alternatives.

37. BIAC also notes that paragraph 6 of Article 11 of ATAD permits EU Member States which have national targeted rules preventing BEPS risks at August 8, 2016, and which are equally effective to the interest limitation rule set out in Article 4 of the ATAD, to apply those rules until the end of the first full fiscal year following the date of publication of the agreement between the OECD members on its official website on a minimum standard with regard to BEPS Action 4, but no later than 1 January 2024. It would appear necessary for such Member States to be able to demonstrate to the European Commission the equivalent effectiveness of such rules.

38. The move towards a mandatory and legally binding (albeit not fully harmonised) approach at EU level may be contrasted to that in the Discussion Draft. In the latter case, there is a movement away from a best practice approach to a series of flexible options for the banking and insurance sectors to be considered by countries. While BIAC is hopeful this will be changed in the final recommendations, BIAC is concerned that the mandatory nature of the ATAD and its exemption of defined financial entities from the interest limitation rules will cause undue confusion and complexity for RFGs and EU tax administrators if the Discussion Draft is adopted in its current form.

39. The EU itself could itself adopt the 3-pronged best practice rule suggested by BIAC above; however, BIAC believes it sets a better international standard for the OECD to adopt the 3-pronged best practice rule for global guidance. The EU could then interpret its exemption from the fixed ratio and group ratio rules for defined "financial undertakings" taking into account the OECD's final recommendations from the Discussion Draft.

Additional Options if Best Practice Not Adopted

40. If best practice is not adopted in the final recommendations emanating from the Discussion Draft and instead the flexible approach is used, then one of the options included in the flexible approach should be that different countries could adopt a rule

[§] Paragraph (9) of the preamble to the ATAD provides the following rationale: "Although it is generally accepted that financial undertakings, i.e. financial institutions and insurance undertakings, should also be subject to limitations to the deductibility of interest, it is equally acknowledged that these two sectors present special features which call for a more customised approach. As the discussions in this field are not yet sufficiently conclusive in the international and Union context, it is not yet possible to provide specific rules in the financial and insurance sectors and Member States should therefore be able to exclude them from the scope of interest limitation rules."

that RFGs are not subject to the fixed ratio and group ratio regime (namely, our suggested best practice above). BIAC strongly prefers that this rule be made the best practice rule, but, if it cannot be, then it needs to be included as a preferred option that could be prudently adopted by countries for the reasons explained above.

41. Another option that could be considered is to broaden the exemption from the fixed and group ratio rules for solo-regulated entities to include (a) holding companies, (b) service companies and (c) core entities in the RFG that are not subject to solo-regulation so that these entities would, like solo-regulated entities, not be subject to the fixed ratio and group ratio rules. To expand on each of these:

A. We do not believe that the Discussion Draft fully addresses the potential impact on holding companies that issue debt-bearing instruments at a "single point of entry" and, in turn, supply regulatory capital to subsidiaries. See paragraphs 55 and 56 and Example 3 and 4. Given the importance of holding companies in providing funds to subsidiaries that are solo-regulated in a RFG, the Discussion Draft's approach of differentiating them from solo-regulated entities would, in BIAC's view, create disproportionate results and could, in certain cases, lead to interest expense becoming non-deductible.

B. Resolution and recovery ("R&R") plans are required of certain banks by regulators with the aim of solvency and orderly resolution in the case of a financial crisis. R&R plans will often separate the service activities into a separate entity. Given this regulatory requirement and given the integral nature of service companies to the functioning of the overall enterprise, service companies should be combined with solo-regulated entities and holding companies under this option.

C. Core entities that are not solo-regulated but are engaged in activities integral to the RFG should likewise be included. Situations exist where entities that are not solo-regulated are, nevertheless, engaged in activities that generate active financing income, the activities of which are integral to the RFG. While BIAC strongly suggest the adoption of the 3-pronged best practice rule, if it is not adopted, then BIAC would be pleased to assist in developing alternatives that address the OECD's concerns.

Attribution of Free Capital to Permanent Establishments ("PEs")

42. BIAC believes that the concerns in paragraphs 22 to 25 of the Discussion Draft can be better addressed by encouraging countries to adopt the Authorised OECD Approach ("AoA") found in the OECD's *2010 Report on the Attribution of Profits to Permanent Establishments* ("2010 Report"). Not all countries have adopted the AoA, and encouraging countries to do so would be preferred as compared to countries creating different methods of attributing "free" capital to permanent establishments to address Action 4 concerns, thereby undermining the carefully considered consensus of the 2010 Report.

Interest Expense Funding Non-taxable Income

43. Paragraphs 35 and 39 of the Discussion Draft state that some countries have expressed concern that solo-regulated entities claim deductions for debt that is in turn used to invest in equity of companies incorporated in low tax jurisdictions that pay dividends that are not subject to tax in the hands of the solo-regulated entities. BIAC commends the Discussion Draft for discussing at some length in paragraphs 36 to 38 that prudential regulation of regulated entities guards against this concern.

44. Despite these regulatory limits, the Discussion Draft suggests at paragraphs 39 and 40 that countries with this concern should consider enacting measures that either (i) disallow interest expense for debt used to fund non-taxable income, (ii) reduce or eliminate participation exemptions or other benefits attributable to such debt or (iii) would tie tax rules to regulatory capital rules so that if regulatory capital rules require that an equity investment be reduced for regulatory capital purposes, then the tax rules would treat the funding amount as equity and not debt, thereby eliminating interest deductions.

45. BIAC observes that tying tax rules to regulatory capital rules in this way would be a substantial exercise. Further, disallowing interest expense or limiting participation-type exemptions in this limited context is a non-proportional response, especially given the points made by the Discussion Draft at paragraphs 36 to 38. Instead BIAC suggests that CFC rules are more appropriate and should be used. BIAC notes that the OECD /G20 consensus on CFCs reflected in the Final Report on Designing Effective Controlled Foreign Corporation Rules (released on October 5, 2015) is apropos to the concern raised. BIAC further notes that Action 3 Final Report is a report of best practices / common approaches, as is the Action 4 Final Report.

CONCLUSION

46. In summary, BIAC suggests a three-pronged best practice rule set forth in paragraph 34 of these comments. This suggestion, if adopted, would adhere to the Action 4 Final Report mandate for best practices in this area and provide a path to minimize potential conflicts between the EU's ATAD and the OECD's Action 4.

47. BIAC thanks the OECD for providing this opportunity to comment and would be happy to assist as the OECD thinks appropriate.

13/15 Chaussée de la Muette, 75016 Paris, France
Tel. +33 (0)1 42 30 09 60 | Fax +33 (0)1 42 88 78 38
email: biac@biac.org | www.biac.org