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By email: taxtreaties@oecd.org

Date: **17 June 2015**

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.

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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

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