Public Discussion Draft

TREATY ENTITLEMENT OF NON-CIV FUNDS

24 March 2016

OECD
BETTER POLICIES FOR BETTER LIVES

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BEPS CONSULTATION DOCUMENT ON THE TREATY ENTITLEMENT OF NON-CIV FUNDS

Paragraph 14 of the final version of the report on Action 6 *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances* indicates that the OECD will continue to examine issues related to the treaty entitlement of non-CIV funds to ensure that the new treaty provisions included in the Report on Action 6 address adequately the treaty entitlement of these funds.

This consultation document has been produced as part of the follow-up work on this issue. It includes a number of specific questions (which appear in boxes) related to concerns, identified in comments received on previous discussion drafts related to the Report on Action 6, as to how the new provisions included in the Report on Action 6 could affect the treaty entitlement of non-CIV funds as well as to possible ways of addressing these concerns that were suggested in these comments or subsequently. Commentators are invited to respond to these specific questions in order to facilitate the Working Party's analysis of these concerns and suggestions. Commentators may also offer additional suggestions as indicated in the box appearing at the end of this document.

The Committee invites interested parties to send their responses to the questions included in this consultation document. Since a number of questions are likely to be relevant only for commentators who supported specific approaches, it is expected that most commentators will only address some of the questions. The consultation document and the responses received will be discussed by Working Party 1 at its May 2016 meeting.

Responses should be sent by **22 April 2016** at the latest by email to taxtreaties@oecd.org in Word format (in order to facilitate their distribution to government officials). They should be addressed to the Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA.

Please note that all responses to this consultation document will be made publicly available. Responses submitted in the name of a collective "grouping" or "coalition", or by any person submitting responses on behalf of another person or group of persons, should identify all enterprises or individuals who are members of that collective group, or the person(s) on whose behalf the commentator(s) are acting.

The proposals included in this consultation document were previously put forward by commentators and do not, therefore, represent proposals by the CFA or its subsidiary bodies. They are merely included in this document in order to obtain further information that will be used for the purpose of analysing these proposals.

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TREATY ENTITLEMENT OF NON-CIV FUNDS

Introduction

1. Paragraphs 9 to 14 of the final version of the report on Action 6 *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances* (the "Report on Action 6") indicates that follow-up work will be carried on with respect to the policy considerations relevant to the treaty entitlement of investment vehicles that do not qualify as "collective investment vehicles" within the meaning of the 2010 OECD Report *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles*.

2. The Report on Action 6 indicates that the follow-up work will address three different topics. First, changes will be made to the final version of the Commentary on the LOB rule included in the Report on Action 6 in order to confirm the conclusions of the 2008 OECD report *Tax Treaty Issues Related to REITs*, which deals with the treaty entitlement of Real Estate Investment Trusts (REITs). The wording of the changes that will be made for that purpose was included in paragraph 11 of the Report on Action 6.

3. Second, changes to the OECD Model Tax Convention, to be finalised in the first part of 2016, will ensure that a pension fund should be considered to be a resident of the State in which it is constituted, regardless of whether that pension fund benefits from a limited or complete exemption from taxation in that State (see paragraph 12 of the Report on Action 6). Proposed changes to the OECD Model Tax Convention that were drafted for that purpose were released for comments on 29 February 2016[1] and are expected to be finalised at the May meeting of Working Party 1 in the light of the comments that will be received on the discussion draft.

4. Third, the OECD will continue to examine issues related to the treaty entitlement of non-CIV funds to ensure that the new treaty provisions included in the Report on Action 6 address adequately the treaty entitlement of non-CIV funds. As noted in paragraph 14 of the Report on Action 6:

> … there is a need to continue to examine issues related to the treaty entitlement of non-CIV funds to ensure that the new treaty provisions that are being considered adequately address the treaty entitlement of non-CIV funds. The continued examination of these issues would also address two general concerns that governments have about granting treaty benefits with respect to non-CIV funds: that non-CIV funds may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits and that investors may defer recognition of income on which treaty benefits have been granted.

5. This consultation document has been produced as part of the follow-up work on this issue. It includes a number of specific questions (which appear in boxes) related to concerns, identified in comments received on previous discussion drafts related to the Report on Action 6, as to how the new provisions included in the Report on Action 6 could affect the treaty entitlement of non-CIV funds as well as to possible ways of addressing these concerns that were suggested in these comments or subsequently.

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1. See Discussion draft on the treaty residence of pension funds.

Commentators are invited to respond to these specific questions in order to facilitate the Working Party's analysis of these concerns and suggestions. Commentators may also offer additional suggestions as indicated in the box appearing at the end of this document. Since a number of questions are likely to be relevant only for commentators who supported specific approaches, it is expected that most commentators will only address some of the questions. The consultation document and the responses received will be discussed by Working Party 1 at its May 2016 meeting.

1. Concerns related to the LOB provision

6. Most of the concerns concerning the treaty entitlement of non-CIV funds that were identified in comments received on previous discussion drafts were related to the effect that the limitation-on-benefits rule included in paragraph 25 of the Report on Action 6 (and especially the detailed version of the rule) would have with respect to non-CIV funds that have a geographically diversified base. The following deal with various suggestions that were made in order to address that issue.

Suggestion that treaty benefits be granted to regulated and/or widely-held non-CIV funds

7. A number of commentators suggested that an exception to the LOB rule should be provided for funds that would be subject to certain types of regulatory frameworks. For instance, these proposals included suggestions for an LOB exception for:

- "regulated widely held funds";
- "non-CIV funds whose characteristics are similar to those of UCITS";
- funds that meet "a test based on a 'genuine diversity of ownership' (GDO) principle [and] … holding companies controlled by a collective investment scheme which meets the GDO principle";
- "Alternative Investment Funds (AIF) in the European Union";
- "Investment companies whose shares are admitted to trading on a regulated market in the EU [and therefore] comply with the Transparency Directive, the Prospectus Directive, the Alternative Investment Fund Managers Directive and the Consolidated Admissions and Reporting Directive";
- "funds that are intended for use as private investment funds, such as the 'qualifying investor alternative investment funds' ('QIAIFs') in Ireland, the 'specialized investment funds' in Luxembourg, Resident Fund Scheme in Singapore, and their equivalents in other countries".

8. Other commentators suggested that the mere fact that a fund would be "widely held" would offer sufficient protection against treaty abuse. Some of these commentators added that an additional safeguard could take the form of a rule that would deny treaty benefits if, for example, 10% or more of the fund was owned by a single non-equivalent beneficiary (and connected persons).

SUGGESTION THAT TREATY BENEFITS BE GRANTED TO REGULATED AND/OR WIDELY-HELD NON-CIV FUNDS

1. What would be the threshold for determining that a fund is "widely held" for the purpose of such a proposal?

2. What types of regulatory frameworks would be acceptable in order to conclude that a fund is "regulated" for the purposes of such a proposal? For instance, would these include the types of regulatory requirements described in paragraph 16 of the 2010 CIV report (i.e. "regulatory requirements relating to concentration of investments, restricting a CIV's ability to acquire a controlling interest in a company, prohibiting or restricting certain types of investments, and limiting the use of leverage by the CIV") as

well as disclosure requirements relating to distribution of interests (e.g. “know your customer” rules)?

3. Since the proposed exception would apply regardless of who invests in the funds, it would seem relatively easy for a fund to be used primarily to invest in a country on behalf of a large number of investors who would not otherwise be entitled to the same or better treaty benefits with respect to income derived from that country. How would this treaty-shopping concern be addressed?

4. Is it correct that investors in a non-CIV are typically taxable only when they receive a distribution? Would there be mandatory distribution requirements for a fund to be eligible for the proposed exception and if yes, would intermediate entities be required to distribute earnings up the chain of ownership on a mandatory basis? If not, how would concerns about deferral of tax be addressed?

5. States that support the inclusion of LOB rules in their treaties are unlikely to agree to a broad exception from the LOB rule that would apply to any widely-held fund, even if it is regulated, especially since that exception would seem more generous than the exception already provided for publicly-listed companies. What features could be incorporated into a specific non-CIV exception in order to make it more acceptable to these States?

6. One argument that was put forward in relation to suggestions for a specific LOB exception for non-CIV funds was that it would avoid or reduce the cascading tax when investment is made through a chain of intermediaries. In practice, what is the intermediate entity-level tax, if any, that is typically payable with respect to income received from a State of source? Are there special purpose vehicles that are commonly used by funds to invest indirectly? How are intermediate entities typically funded, debt or equity? If debt, is it unrelated party financing?

Non-CIV funds set up as transparent entities

9. Paragraph 14 of the Report on Action 6 notes that the new treaty provision on transparent entities that was included in Part 2 of the Report on Action 2 *Neutralising the Effects of Hybrid Mismatch Arrangements* will ensure that where income derived through entities that one of the two Contracting States treats as fiscally transparent is taxed in the hands of the investors in these entities in the State of residence of these investors, treaty benefits with respect to that income will generally be available at the level of these investors under the treaty between the State of source and the State of residence of the investor. That provision reads as follows:

> *For the purposes of this Convention, income derived by or through an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State shall be considered to be income of a resident of a Contracting State but only to the extent that the income is treated, for purposes of taxation by that State, as the income of a resident of that State.*

10. That provision will ensure, for example, that treaty benefits are available to an investor in a non-CIV fund as long as the non-CIV is treated as transparent by the State of residence of that investor so that the investor is taxed directly on its share of the income derived through that non-CIV.[2] It will therefore ensure that treaty benefits are granted in these circumstances whilst addressing the two tax policy concerns identified in paragraph 14 of the Report on Action 6, *i.e.* that non-CIV funds may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits and that investors may defer recognition of income on which treaty benefits have been granted.

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2. Unless the income is derived through a non-CIV that is resident of the State of source.

11. Whilst it is recognised that there are a number of non-tax reasons why a non-CIV would not be structured as a transparent entity, it seems that the new transparent entity provision will offer a partial solution to some of the cases where treaty benefits might otherwise be denied with respect to income derived through a non-CIV.

12. The comments received included the suggestion that a non-CIV should be able to elect to be treated as fiscally transparent for treaty purposes. Such an election, however, would be a matter of domestic law and could hardly be provided in tax treaties as it would require domestic tax law provisions that would attribute the income of a non-CIV to the investors of the non-CIV rather than to the non-CIV itself.

13. Another suggestion was that a non-CIV should be allowed to claim treaty benefits on behalf of its ultimate investors who would themselves be entitled to treaty benefits under the transparent entity provision. Such an administrative measure would probably not require a change to tax treaties and could be considered by each State not only for non-CIV funds that are transparent entities but also for other types of transparent entities.

14. A key practical difficulty in the application of the transparent entity provision to non-CIV funds is that it requires that the State of source be provided with all the relevant information concerning the investors in the non-CIV. The same practical difficulty would arise with respect to any approach under which the treaty entitlement of a non-CIV would be related to the treaty entitlement of all, or a high percentage of, the investors in that non-CIV. A number of commentators indicated that at least some types of non-CIV funds may be unable to identify the tax residence of their investors despite the evolving requirements of anti-money laundering legislation and tax reporting regimes. Examples that were provided were that of a securitisation company which "may not be in a position to identify who its bondholders are", a fund of funds and "where a financial institution invests in a collective investment scheme on behalf of its own clients or for the purposes of structured investments which it sells to its own clients". One commentator suggested that even solutions based on the principles of the TRACE project would not offer a practical solution for private equity funds.

NON-CIV FUNDS SET UP AS TRANSPARENT ENTITIES

7. Where an entity with a wide investor base is treated as fiscally transparent under the domestic law of a State that entered into tax treaties, the application of the relevant tax treaties raises a number of practical difficulties. Are there ways in which these difficulties could be addressed? Are there other practical problems that would prevent the application of the new transparent entity provision in order to ensure that investors who are residents of a State are entitled to the benefits of the treaties concluded by that State?

Suggestion that certain non-CIV funds be granted treaty benefits where a large proportion of the investors in the funds would be entitled to the same or better benefits if they had received the income directly

15. A suggestion that was included in the comments received was that the LOB should include a derivative benefits rule applicable to certain non-CIV funds under which such an entity would be entitled to treaty benefits under a tax treaty if it met certain conditions and had a sufficiently high level of investors (e.g. 80%) who would be entitled to the same or better treaty benefits. The rationale given for that suggestion was "[t]he investors in Alternative Funds are primarily institutional investors, and are often entitled to benefits that are at least as good as the benefits that might be claimed by the Alternative Fund. The fact that Alternative Funds pool capital from investors and make investments in different jurisdictions

should not cause such investors to forfeit the treaty benefits to which they would be entitled if they invested directly".

16. That approach, unlike the transparent entity provision, would grant treaty benefits to the fund itself based on the treaty entitlement of a high level of investors even though the income of the fund would not be attributed to these investors for tax purposes. For that reason, it could raise the concerns about treaty-shopping and deferral that were described in paragraph 14 of the Report on Action 6.

17. It was suggested that these concerns could be addressed by restricting the application of the approach to funds that would meet certain criteria, such as the fund being an institutional investor or being wholly owned by institutional investors, being subject to customer due diligence requirements under anti-money laundering legislation in addition to being subject to automatic information reporting requirements, having a bona fide investment objective and being marketed to a diverse investor base. It was also suggested that specific anti-abuse rules could be provided to minimize the creation of abusive investment vehicles.

18. Under the suggested approach, a fund that would meet these conditions would satisfy the LOB through the addition of a derivative benefits provision (which would include a 50% base erosion test) that would provide that the fund would be entitled to treaty benefits under a tax treaty if it met these conditions and had a sufficiently high level of investors (e.g. 80%) who would meet the following two requirements: a) if they had received the income directly, they would have been entitled to the same or better treaty benefits to which the fund is entitled and b) they are tax-exempt entities described in paragraph 2(b) and (d) of the LOB provision rule (generally government entities including sovereign wealth funds, pension funds, and charitable organisations) or they include their proportionate share of the fund's income on a current basis (for instance, under an anti-deferral regime).

SUGGESTION THAT THE LOB INCLUDE A DERIVATIVE BENEFIT RULE APPLICABLE TO CERTAIN NON-CIV FUNDS

Questions related to certain aspects of the proposal

8. The rationale that was given for the above proposal refers to the fact that "investors in Alternative Funds are primarily institutional investors, and are often entitled to benefits that are at least as good as the benefits that might be claimed by the Alternative Fund". What is the meaning of "institutional investors" in that context? In particular, does it include taxable entities or other non-CIVs? Absent a clear definition of "institutional investors", how can it be concluded that institutional investors "are often entitled to benefits that are at least as good as the benefits that might be claimed by the Alternative Fund"? Also, is it suggested that "institutional investors" are less likely to engage in treaty-shopping and, if yes, why?

9. Unlike CIVs, which are defined in paragraph 6.8 of the 2010 Report on CIVs, the term "non-CIV" has no established definition. What would be the main types of investment vehicles to which the proposal could apply?

10. Paragraph 17 above refers to the possible inclusion of "specific anti-abuse rules". What would these rules be?

11. What would constitute a "bona fide investment objective" for the purpose of paragraph 17 above?

12. How would it be determined that a fund is "marketed to a diverse investor base" for the purpose of paragraph 17 above?

Questions related to the identification of the investors in a non-CIV

13. Is the ownership of interests in non-CIV funds fairly stable or does it change frequently like the interests in a typical collective investment fund that is widely distributed?

14. How would the proposal address the concern, expressed by some commentators, that many non-CIV funds would be unable to determine who their ultimate beneficial owners are and, therefore, would not know the treaty residence and tax status of these beneficial owners?

15. What information do those concerned with the management and administration of non-CIV funds currently have concerning persons who ultimately own interests in the fund (for example under anti-money laundering, FATCA or common reporting standard rules)?

16. Is this information currently sufficient for relevant parties to identify the treaty benefits that an owner would have been entitled to if it had received the income directly? If not, what types of documents and procedures could be used by a non-CIV to demonstrate to tax authorities and/or payors that the residence and treaty entitlement of its ultimate beneficial owners are such that the non-CIV qualifies for treaty benefits under that suggested derivative benefits rule? What barriers would exist to the communication of these documents or the implementation of these procedures? In particular, does intermediate ownership present obstacles to obtaining information about ultimate beneficial ownership and, if yes, how might these obstacles be addressed?

Questions related to the prevention of treaty-shopping

17. Since beneficial interests in non-CIV funds are frequently held through a chain of intermediaries, including multiple subsidiary entities (which is not the case of typical CIVs), how would the proposal overcome the difficulties derived from such complex investment structures with multiple layers and ensure that a fund is not used to provide treaty benefits to investors that are not themselves entitled to treaty benefits?

18. The proposal would grant treaty benefits if a certain high percentage of a non-CIV is beneficially owned by investors entitled to similar or better benefits. Even a percentage as high as 80% would leave substantial room for treaty-shopping as a 20% participation in a very large fund could represent a significant investment. How could this concern be addressed?

19. One of the proposed requirements for the application of the suggested derivative benefits rule would be a 50% base erosion test. Since one of the main concerns expressed by governments relates to the possible use of non-CIV funds for treaty-shopping purposes, wouldn't the 50% threshold proposed for the base erosion test be too generous?

Questions related to the prevention of deferral

20. According to the proposal, acceptable ultimate beneficial owners would include persons who would "include their proportionate share of the fund's income on a current basis". How would a State of source be able to determine when this requirement is met? Also, what would be considered an acceptable anti-deferral regime? In particular, would a regime under which a taxpayer is taxed on a deemed amount of income or deemed return on investment be considered as an anti-deferral regime even if the amount that is taxed is significantly lower than the actual return? Would the United States PFIC regime be an example of an acceptable anti-deferral regime?

21. As regards the application of the proposal in the case of indirect ownership, who will be tested in

relation to the condition that an ultimate owner is either tax exempt or taxed on a current basis?

Questions related to the new derivative benefits provision of the United States Model

22. The proposal above was presented as a possible additional derivative benefits rule that would apply specifically to non-CIV funds but that would not replace the more general derivative benefits provision that appeared in the detailed version of the LOB rule included in the Report on Action 6. The Working Party is now looking at possible changes to that derivative benefits provision in the light of the new derivative benefits provision included in the United States Model Treaty released on 12 February 2016 (see ***https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-US%20Model-206.pdf***, paragraph 4 of Article 22 "Limitation on Benefits"). Based on previous comments, it is acknowledged that many non-CIV funds could not satisfy the "seven or fewer" condition of that derivative benefits provision. What other aspects of the new derivative benefits provision included in the United States Model Treaty would be problematic for non-CIV funds?

Suggestion that the LOB should not deny benefits to a non-CIV resident of a State with which the non-CIV has a sufficiently substantial connection

19. Another suggestion that was included in the comments received was to amend the provisions of paragraph 3 of the LOB rule, under which treaty benefits are granted with respect to income that is derived in connection with the active conduct of a business, in order to provide that the activities of certain non-CIV funds would be considered to constitute the active conduct of a business. Funds would qualify for such treatment if they had a "sufficiently substantial connection" with their State of residence. It was suggested that such a "sufficiently substantial connection" could be based on criteria such as the residence of members of the board of the fund or its manager/administrator, whether the board members resident in the jurisdiction have the relevant expertise to direct the business of the fund, whether the fund (or its manager/administrator) has qualified personnel in the jurisdiction that can fulfil and administer the transactions undertaken by the fund, whether decisions of the board are taken in the jurisdiction, or whether the bookkeeping of the fund is performed in the jurisdiction. Another criterion that was proposed in different comments referred to a non-CIV that would maintain an "active investment management business enterprise" involved in the management of its activities in its State of residence.

20. It was also suggested that such an approach could be limited to funds that meet certain conditions, for example, funds that are more than 50% owned by institutional investors.

21. When that approach was discussed in Working Party 1, it was observed that such an approach would not address the two tax policy concerns expressed in paragraph 14 of the Report on Action 6. For instance, by allowing treaty entitlement to a fund resident of a State that is effectively managed in that State but is subject to low-taxation by that State, it would allow treaty-shopping and the deferral of taxation. For these reasons, the Working Party did not consider that it offered a viable alternative to the issues raised by the LOB rule in relation to the treaty entitlement of non-CIV funds.

SUGGESTION THAT A "SUBSTANTIAL CONNECTION" APPROACH BE ADOPTED

23. Are there practicable ways to design a "substantial connection" approach that would not raise the treaty-shopping and tax deferral concerns described in paragraph 21 above?

Suggestion of a "Global Streamed Fund" regime

22. An industry representative has recently suggested to the OECD an approach that could possibly apply to a large number of investment funds. Whilst the proposed approach attempts to deal with concerns that go beyond the narrow issue of the application of the LOB to non-CIV funds, it is presented here as the issues related to the application of the LOB to non-CIV funds are among the key concerns that the approach seeks to address.

23. The key features of the Global Streamed Fund approach are that investment income would be exempt from tax when derived by a qualifying fund (a Global Streamed Fund or "GSF") but the fund would be obliged to distribute its income on a regular basis and tax would be collected upon these distributions (except distributions to other qualified funds) by the State of residence of the fund and remitted to the State of source of the income. The tax so collected would be determined by the treaty entitlement of the ultimate investor under the treaty between the State of residence of that ultimate investor and the State of source of the income. Treatment as a GSF would be elective, not mandatory; that treatment would be intended for closed-end non-CIVs rather than other types of funds (such as CIVs and open-end funds, where distribution of realised capital gains would raise concerns).

24. More specifically, that approach would be implemented through the adoption of uniform domestic laws in each participating State (ideally, every OECD and EU member State). These laws would allow a fund resident of a State to elect, regardless of its legal form, to be treated as a "Global Streamed Fund" (GSF). A standard definition of "fund" would be adopted in order to determine which entities would be eligible for that election. A GSF would be required to distribute 100% of its income and realised gains to its investors on a regular basis.

25. Income derived by a GSF from a participation in another GSF would be exempt in order to avoid cascading tax (and therefore allow "fund-of-fund structures"). Income from cross-border portfolio investments and private equity investments by the GSF would be exempt from any taxation (including withholding tax) in a State of source that is a participating State. Instead of tax being collected by the State of source, a withholding tax would be paid by the GSF to its own State of residence when the GSF would make distributions to its investors that are not GSFs. The tax so collected by the State of residence of the GSF would be remitted to the participating States from which the income was derived. For each distribution by a GSF, a distribution voucher would show the type of income distributed and the tax deducted, which would allow the State of residence to tax the income/gains of its resident investors appropriately.

26. The proposal would accommodate any restrictions on treaty entitlement that participating States would incorporate into their treaties. For example, if a GSF invested in shares of a company resident in a State that included a detailed LOB in its treaties, that LOB would be applied in order to determine which ultimate investors were entitled to which treaty benefits. Items of income not eligible for any treaty benefits would be taxed at the relevant domestic tax rate of the State of source. The domestic law would also determine the documentation (e.g. certificate of tax residence) required from an investor to receive the agreed tax rate on the income derived from a State of source. According to the author of this proposal, this would be "in fact quite similar to any listed company, and is simpler than TRACE". The amount of tax to be collected by the State of residence of the GSF but remitted to the State of source would be calculated on a proportional basis based on the treaty entitlement of each investor in the GSF that is not itself a GSF.

27. The categories of investment income to which that approach would be applied (dividends, interest, immovable property income, capital gains etc.) would be agreed on a standard basis by all participating States.

28. Business income of the GSF, including business income derived through a PE located in another country, would not be covered and would therefore not be exempt from tax. There would therefore be a distinction between passive income resulting from investment, which would be exempt, and active business income, which would not be exempt (according to the proposal, the distinction between passive and active income could be based on the number of employees; the proposal suggests a threshold of 20 employees). The exemption from tax of a GSF would be subject to a general anti-abuse rule that would deny the exemption in cases of abuse.

29. The special treatment of GSFs would be confirmed in tax treaties between participating countries (this could be done through the multilateral instrument) by an Article that would apply to funds that would qualify as a GSF. The Article could simply provide that a GSF must apply the appropriate rate in relation to its distributions of the defined income subject to the conditions imposed for treaty entitlement (including LOB and PPT).

30. According to the arguments put forward in support of the proposal, the proposal would address treaty-shopping concerns because only the eligible ultimate owners that are not GSFs would get the treaty benefits to which they are entitled under the treaty between their State of residence and the State of source. The proposal would also address deferral concerns because a GSF would be required to distribute 100% of its income. Another benefit of the proposal would be that it would eliminate the cascading taxation of investment income that results from the taxation of the funds that act as intermediaries between the State of source and the State of residence of the ultimate investors. It would also allow funds to accept investment from investors who are residents of different States and that have different characteristics.

SUGGESTION OF A "GLOBAL STREAMED FUND" REGIME

24. Although the above proposal for a "Global Streamed Fund" regime is very recent and has not yet been examined by Working Party 1, the Working Party wishes to invite commentators to offer their views on its different features. In particular, the Working Party invites comments on:

- Whether the approach would create difficulties for non-CIV funds that do not currently distribute all their income on a current basis?

- Whether the approach would create difficulties for non-CIV funds that cannot, for various reasons, determine who their investors are?

- Whether the suggestion that tax on distributions be collected by the State of residence and remitted to the State of source would create legal and practical difficulties?

- What should be the consequences if, after a payment is made to a GSF, it is subsequently discovered that the fund did not meet the requirements for qualifying as a GSF or did not distribute 100% of its income on a current basis?

2. Concerns related to the PPT rule

31. Some commentators have expressed concerns that the PPT rule included in the Report on Action 6 (see paragraph 26 of the Report) might restrict the treaty entitlement of non-CIV funds in cases where a large proportion of the investors in a non-CIV are residents of States that are different from the State of residence of the fund.

32. Although some of these comments suggested that the PPT rule should not apply to CIVs and other funds which are widely held, this approach was not adopted as it would have been inappropriate to allow a specific group of entities to escape the application of that rule. The PPT rule only applies where it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining treaty benefits was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in these benefits. Where treaty-shopping or other strategies aimed at obtaining treaty benefits are not one of the principal reasons for the geographical diversification of the investor base of a non-CIV, the PPT will therefore not apply merely because non-residents invest in a non-CIV established in one of the Contracting States.

33. As indicated in the discussion draft released in May 2015, a more realistic approach could be to add one or more examples on non-CIV funds to the Commentary on the PPT rule. The Working Party will continue to examine the suggested examples related to non-CIV funds that were already included in the comments received on the November 2014 and May 2015 discussion drafts (e.g. examples dealing with the specific cases of corporate debt funds, securitisation and REITs). It was noted, however, that some commentators offered to provide additional examples.

ADDITIONAL EXAMPLES FOR THE COMMENTARY ON THE PPT RULE

25. Commentators wishing to suggest new examples related to the application of the PPT rule to common types of legitimate arrangements that are commonly entered into by non-CIV funds are invited to do so. These examples should be brief and should focus on common transactions that do not raise concerns related to treaty-shopping or inappropriate granting of treaty benefits.

3. Concerns related to "anti-conduit rules"

34. A few commentators have expressed concerns that an anti-conduit rule should not be applied to non-CIV funds (and CIVs) and have suggested that the commentary on the anti-conduit rule should be amended to include an explicit statement that it is not designed to apply to CIV or non-CIV funds.

35. The Report on Action 6, however, does not include a specific anti-conduit rule even though it indicates that States that do not include the PPT in their treaties will need to supplement the LOB rule by rules that will address treaty-shopping strategies commonly referred to as "conduit arrangements" that would not be caught by the LOB.

36. As explained in paragraphs 14 and 19 of the Commentary on the PPT rule included in paragraph 26 of the Report, that rule could apply to conduit arrangements (as illustrated by the examples in paragraph 19). To the extent that it is possible that CIVs and non-CIV funds, like other persons, could enter into conduit arrangements one of the principal purposes of which would be to obtain treaty benefits, it would be inappropriate to provide a general exemption from the application of the PPT with respect to such arrangements. If there are significant risks that the PPT rule could apply to some legitimate types of arrangements that are commonly entered into by non-CIV funds because these could be seen as conduit arrangements in the light of the examples already included in paragraph 19, it would, however, be possible to deal with these through the addition of one or more examples.

CONCERNS WITH RESPECT TO CONDUIT ARRANGEMENTS

26. Commentators who share the concern described above in relation to conduit arrangements are invited to provide one or more examples where the PPT rule could apply to legitimate types of arrangements that are commonly entered into by non-CIV funds because these could be seen as conduit

arrangements in the light of the examples already included in paragraph 19 of the Commentary on the PPT rule included in paragraph 26 of the Report. These examples should be brief and should focus on common transactions that do not raise concerns related to treaty-shopping or inappropriate granting of treaty benefits.

4. Concerns related to the "special tax regimes" proposal

37. Some commentators expressed concerns about unintended effects that the proposal for new treaty rules on "special tax regimes", which were included in the May 2015 discussion draft, could have on some non-CIV funds.

38. Paragraph 81 of the Report on Action 6 indicated that the proposal on "special tax regimes" would need to be reviewed once a similar proposal that was released for comments by the United States in May 2015 would have been finalised.

39. The provisions on special tax regimes included in the new United States Model Tax Treaty released in February 2016 include a number of significant differences with respect the provisions that were referred to in the May 2015 discussion draft. For instance, the new provisions that restrict the application of Articles 11 (Interest), 12 (Royalties) and 21 (Other Income) only apply to payments to "connected persons" (it should be noted, however, that the definition of "special tax regime" is also relevant for the application of the LOB rule). Also, the only type of "other income" to which the provisions apply are "guarantee fees". More importantly, the definition of "special tax regimes" has been substantially amended.

CONCERNS RELATED TO THE "SPECIAL TAX REGIMES" PROPOSAL

27. Commentators who shared the concern described above in relation to the proposal for "special tax regime" rules are invited to indicate whether they have similar or different concerns with respect to the new version of the proposal that was included in the new United States Model Tax Treaty released in February 2016 (see question 22 above). If yes, what is the type of "statute, regulation or administrative practice" related to non-CIV funds that could constitute a special tax regime and that would give rise to these concerns?

5. Other suggestions

40. The preceding questions are not intended to restrict the approaches that could be examined as regards the way in which the rules included in the Report on Action 6 could be modified to address issues related to the treaty entitlement of non-CIV funds. It is therefore possible for commentators to suggest other approaches not already mentioned.

OTHER SUGGESTIONS

28. Please describe briefly any approach not already mentioned in this consultation document or in previous comments that could address concerns related to the way in which the new treaty provisions included in the Report on Action 6 may affect the treaty entitlement of non-CIV funds without creating opportunities for treaty-shopping or tax deferral.