

Comments received on  
Public Discussion Draft

# TREATY RESIDENCE OF PENSION FUNDS

1 April 2016





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Tax Treaties,  
Transfer Pricing and Financial Transactions Division,  
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RE: DISCUSSION DRAFT ON CHANGES TO THE OECD MODEL TAX CONVENTION CONCERNING THE  
TREATY RESIDENCE OF PENSION FUNDS

We refer to the above discussion draft.

The 1818 Society is the organization of World Bank Group alumni. For details please see:  
<http://web.worldbank.org/WBSITE/EXTERNAL/EXTSTAFF/1818SOCIETY/0,,contentMDK:21185831~menuPK:444075~pagePK:64156201~piPK:64156133~theSitePK:444067,00.html>

We are writing to request that the definition of “recognised pension fund” that you propose should specifically include pension funds established by international organisations, such as the World Bank Staff Retirement Plan and that such pension funds should be treated as resident in the state in which they are established or principally administered.

Although these pension funds do not always meet all the local regulatory or tax requirements in the state in which they are established or administered they are frequently run as a practical matter in accordance with those requirements. For example, the World Bank Staff Retirement Plan has undertaken to the IRS to be administered in accordance with United States tax rules relating to qualifying pension plans under the Internal Revenue Code and is administered in this way.

The controls exercised over these pension funds and the legal rules they operate under mean that they are not vehicles for tax avoidance.

This would bring clarity to an area that is obscure in some countries both for the funds themselves, their employees and the employees’ dependants.

Yours faithfully

Nicki Marrian

Chair, 1818 Society, British Chapter

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**April 1, 2016**

### **VIA E-MAIL**

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### **Re: Comments on Discussion Draft on Treaty Residence of Pension Funds**

Dear Ms. de Ruiter:

This letter is submitted on behalf of the members of the Association of Global Custodians ("AGC" or "Association") to provide you with comments in respect of the OECD Discussion Draft: Treaty Residence of Pension Funds, issued on 29 February 2016 (the "Discussion Draft") as part of the follow-up work on Action 6 of the BEPS Action Plan.

As you know AGC members have been keenly following (and in some cases actively participating in) the work of the Organisation for Economic Co-Operation and Development ("OECD") for many years on various key tax developments and welcome the opportunity to provide comments to you on the Discussion Draft.

The Association is an informal group of 11 member banks that provide securities safekeeping and asset serving functions to cross-border institutional investors worldwide including investment funds, pension funds, and insurance companies.

In providing global custody services, AGC members routinely seek appropriate tax treaty withholding tax relief on behalf of custody clients. The members typically collectively process millions of such relief claims each year, affecting substantial amounts of cross-border portfolio investment flows in and out of countries worldwide. A significant portion of the income for which the members process treaty relief claims is income received by institutional investors, including pension funds. As such, the AGC members experience on a daily basis the costs, inefficiencies, and excessive withholding that arises when the procedures for claiming lawful relief are unduly burdensome or complicated for the

investors involved, or when the standards for entitlement to treaty relief are too unclear or complicated to effectively accommodate treaty relief claims, whether at source or by refund.

Our comments are attached in the Annex.

Sincerely yours on behalf of the Association,

A handwritten signature in black ink, reading "Mary C. Bennett". The signature is fluid and cursive, with a long horizontal stroke extending from the end of the name.

Mary C. Bennett  
Baker & McKenzie LLP  
Counsel to the Association

Annex  
Appendix 1  
Appendix 2

## ANNEX

### AGC comments on the 29 February 2016 Discussion Draft on the Treaty Residence of Pension Funds

The Association welcomes the effort to ensure that “recognised pension funds” will be guaranteed treatment as residents of the State where they are established for tax treaty purposes. Our comments are therefore primarily focused on the definition of “recognised pension funds”. We address below the four specific questions (“a” through “d”) posed by the Discussion Draft, after which we provide some additional comments.

a) *As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1j):* Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?

The condition of being a separate person for tax purposes could result in the exclusion of certain contractual trust or similar arrangements that are not treated as separate persons for tax purposes in their home country but are effectively granted special treatment there as pension vehicles. An example of this problem can be found in relation to contractual trust arrangements that are set up by employers under German law to fund pension benefits to employees. Under German tax law, the assets of such funds are treated as belonging to the employer, but the employer can reduce its taxable profits by the incremental pension obligation to the employee, based on an actuarial computation, and the employee is not taxed until there is a distribution. In order to address the fact that such a segregated fund is not a separately identifiable “person” for German tax purposes, the 2006 Protocol to the U.S.-German Tax Treaty included language to clarify that such arrangements would be treated as pension funds that are residents of Germany, thereby making them eligible for the exemption on U.S. dividend withholding tax provided under Article 10(3)(b) of that Treaty, and this position was further clarified by a 2012 Competent Authority Agreement between the United States and Germany.<sup>1</sup>

This example shows that requiring an arrangement to constitute a “separate person” under the taxation laws of the State where the arrangement is established in order to qualify as a “recognised pension fund” may lead to inappropriate results if the intention is to ensure that income derived by pension vehicles will be treated as the income of a “resident” of the State where the vehicle is established (and as potentially eligible for specific treaty exemptions provided to “pension funds” of that State). The approaches used by different States to accord “pension fund” status to vehicles established in those States differ enough that a blanket requirement that an arrangement constitute a “separate person” for tax purposes will likely inappropriately exclude certain pension fund arrangements.

<sup>1</sup> A copy of the 2012 Competent Authority Agreement between the United States and Germany is attached as Appendix 1, and a copy of the following article, which provides further background on this arrangement, is attached as Appendix 2: Portner, “Challenges in Characterizing a German Contractual Arrangement”, *Worldwide Tax Daily* (2013 WTD 111-18). The Portner article notes that a contractual trust arrangement (CTA) may be set up in Germany for the employees of a German branch of a foreign employer, which underlines the significance of effectively treating the CTA as a resident of Germany even though its assets are treated for German tax purposes as belonging to the employer.

Another example relates to pension schemes arranged through insurance companies. These arrangements are quite common in the United Kingdom and are known there as unit-linked pension funds, i.e. a separate, identifiable, pool of assets that represent the pension business of an insurance company. The fund is registered with HMRC and treated as a pension fund for tax purposes. It is not however a separate entity and it is therefore questionable if it can be said to be a separate tax person. Where treaty partners wish to characterize such funds as pension funds eligible for treaty benefits, they typically do so by defining eligible funds in a way that eliminates any requirement that they be treated as a separate person for tax purposes<sup>2</sup> or by including a specific reference to such funds in their definition.<sup>3</sup>

**Suggestion:** The Association therefore suggests that the OECD eliminate the requirement that an entity or arrangement be a “separate person” for tax purposes in the State where it is established. Treaties that have omitted such a requirement in their description of pension funds that will qualify as “residents” have avoided the kinds of problems which the special U.S.-German Protocol and Competent Authority Agreement were needed to solve.<sup>4</sup>

**Suggestion:** If for any reason delegates decide not to eliminate this requirement from the definition of “recognised pension fund” as a general matter, the Association recommends that the OECD Model specifically accommodate a bilateral agreement designating pension entities or arrangements that do not constitute separate persons for tax purposes as “recognised pension funds”.<sup>5</sup>

b) *As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):* Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact

<sup>2</sup> See, e.g., the U.K.-Switzerland Tax Treaty, which defines “pension scheme” to mean “any plan, scheme, fund, trust or other arrangement established in a Contracting State which is: (a) generally exempt from income taxation in that State; and (b) operated principally to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such arrangements”.

<sup>3</sup> See, e.g., the U.K. treaties with Belgium, Canada, the Netherlands, and Spain, which refer to “pension schemes (other than a social security scheme) registered under Part 4 of the Finance Act 2004, including pension funds or pension schemes arranged through insurance companies and unit trusts where the unit holders are exclusively pension schemes”.

<sup>4</sup> See, e.g., Article IV(1)(b) of the U.S.-Canada Tax Treaty, which provides that: “The term ‘resident’ of a Contracting State is understood to include... a trust, organization or other arrangement that is operated exclusively to administer or provide pension, retirement or employee benefits ... that was constituted in that State and that is, by reason of its nature as such, generally exempt from income taxation in that State.” See also Article 4(3)(a) and 3(1)(o) of the U.S.-U.K. Tax Treaty, which provide, respectively, that “The term ‘resident of a Contracting State’ includes ... a pension scheme” and “the term ‘pension scheme’ means any plan, scheme, fund, trust or other arrangement established in a Contracting State which is: (i) generally exempt from income taxation in that State; and (ii) operated principally to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such arrangements.”

<sup>5</sup> See, e.g., Article 10(4)(c) of the Canada-United Kingdom Tax Treaty for an example of a provision that allows the competent authorities to agree to treat additional pension plans as “recognised pension plans”.



that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?

We are somewhat concerned that the use of the word “exclusively” in proposed Article 3(1)(j)(i) may be too restrictive, notwithstanding the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”. We note that the proposed Commentary indicates that the term “retirement benefits” is “broad enough to cover one or more payments made at or after retirement to a self-employed person even if these payments are not made in the form of regular pension payments”, and that examples of “similar benefits” would include “payments made as a result of the death or invalidity of an individual”. We also note, however, that the OECD’s publication *“Private Pensions: OECD Classification and Glossary”* indicates that many plans “cover many other risks in addition to old-age pensions including, survivor’s, disability, sickness, maternity, adoption, and unemployment benefits”.<sup>6</sup>

**Suggestion:** The Association therefore suggests replacing “exclusively” with “principally” in order to avoid the possibility that minor purposes other than “retirement or similar benefits” would disqualify a fund from classification as a “recognised pension fund”.

c) *As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):* Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?

See our comments under item (b), above.

d) *As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j):* Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

For reasons similar to those outlined under item (b), above, the Association is somewhat concerned that the use of the term “exclusively” could be overly restrictive in this context. One example of this concern relates to so-called “81-100 group trusts”<sup>7</sup> which are generally used as a vehicle to pool the assets of U.S. qualified retirement plans but which may also include a minor amount of assets from Puerto Rican retirement plans.<sup>8</sup> Because large U.S. employers may have Puerto Rican subsidiaries and may have to maintain a separate Puerto Rican retirement plan for the benefit of the employees of those subsidiaries, sponsors of

<sup>6</sup> Available at <http://www.oecd.org/finance/private-pensions/privatepensionsoecdclassificationandglossary.htm>.

<sup>7</sup> The name “81-100 group trust” comes from the fact that the original ruling from the U.S. Internal Revenue Service which set forth the requirements for such arrangements was Revenue Ruling 81-100.

<sup>8</sup> See Revenue Ruling 2014-24, which confirms the ability of 81-100 group trusts to include assets from Puerto Rican retirement plans.

group trusts like to be able to allow such employers to include in the 81-100 group trust not only the assets of the U.S. qualified retirement plans established for the U.S. employees but also the assets of the (typically much smaller) Puerto Rican retirement plan established for the employees of the Puerto Rican subsidiary. Since a Puerto Rican plan presumably would not qualify under proposed Article 3(1)(j)(i) (i.e., on the grounds that it is not established in the United States), an 81-100 group trust that included a Puerto Rican plan would appear not to be constituted and operated “exclusively” to invest funds for the benefits of entities or arrangements referred to in Article 3(1)(j)(i).

**Suggestion:** The Association therefore recommends that the term “exclusively” in proposed Article 3(1)(j)(ii) be replaced with “principally”.<sup>9</sup> The Association further notes, however, that any terminology used in this definitional provision may need to be coordinated with the requirements, if any, imposed by a Limitation on Benefits or other anti-abuse provision in the relevant treaty. This is because the latter provisions may, for example, accommodate a certain level of participation by third country funds in the types of group arrangements or entities described in proposed Article 3(1)(j)(ii), and that policy should not be undercut by the definitional language used in Article 3(1)(j)(ii).

#### Additional comments

If States introduce the proposed definition of “recognised pension fund” into their treaties, the Association suggests that the OECD recommend that it would be a matter of good practice for treaty partners to enter into a mutual agreement or memorandum of understanding to confirm the treatment of specific categories of pension vehicles in their States under the new definition, in order to eliminate any uncertainty as to whether those vehicles satisfy the new definition.

While the Association appreciates that the Discussion Draft has as its objective to provide certainty to pension funds that they can satisfy the residence requirement of treaties, we note that paragraph 8.6 of the existing Commentary on Article 4 of the OECD Model states that “most States” already agree that pension funds can qualify as “residents”. It therefore appears that the Discussion Draft’s “solution” may be needed only in a minority of States. Depending on how some of the issues described in our comments above are resolved, we note that the introduction of new language regarding “recognised pension funds” could create new limits on the extent to which pension funds would be treated as residents of the States where they are established, including by those States that already treat pension funds as residents of their treaty partner States. The Association therefore suggests that the OECD make the proposed new definition a part of the Model to be used only by those States that

<sup>9</sup> We note that comparable less restrictive language can be found in a number of treaties. See, e.g., Article 3(1)(l) of the 2015 United Kingdom-Croatia Tax Treaty (which defines “pension scheme” to mean “any scheme or other arrangement established in a Contracting State which: (i) is generally exempt from income taxation in that State; and (ii) operates principally to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such arrangements”); paragraph 2 of the 2009 Protocol to the Switzerland-United Kingdom Tax Treaty (which defines “pension scheme” in a similar way); Article 3(1)(k) of the 2006 U.S.-Belgium Tax Treaty (which defines “pension fund” to mean “any person established in a Contracting State that is: i) operated principally: A) to administer or provide pension or retirement benefits; or B) to earn income for the benefit of one or more arrangements described in A)” and which meets certain other requirements).

would not otherwise recognize pension funds established in their treaty partner States as residents of the latter States, so that treaties between States that already share the majority view would not have to introduce the new definition.

As you know, the Association filed comments with the OECD in respect of BEPS Action 6 on January 9, 2015 and June 16, 2015 in which we addressed the problems facing pension funds seeking treaty benefits to which they are duly entitled. As indicated in those letters, while resolution of the treaty residence of pension funds would be a positive step, there remain very serious issues concerning the practical aspects of pension funds' satisfaction of the procedural requirements often imposed on them by treaty country tax administrations, particularly under the increasingly prevalent anti-abuse provisions being introduced into treaties, including various Limitation on Benefits tests and other provisions. We wish to stress the importance of addressing those practical issues as a matter of priority if there is to be any hope of avoiding a continuing deterioration of the climate for providing treaty benefits to pension funds. The Association is in the process of reviewing the Discussion Draft on Treaty Entitlement of Non-CIV Funds released on March 24, 2016, and we will provide separate comments on that Discussion Draft to the extent we feel they are needed to address these concerns.

Finally, in its previous comments, including its letter of July 26, 2013 in relation to the OECD's initiative with respect to the Common Reporting Standard, the Association stressed the importance of making near-term progress on the implementation of the OECD's TRACE (Treaty Relief and Compliance Enhancement) Project. We wish to emphasize the importance of that goal once again, as elimination of legal barriers to pension funds' access to treaty benefits (e.g., the "residence" requirement) will be meaningless if no progress is made on eliminating the ever-increasing procedural impediments, and implementation of the TRACE recommendations would be the best possible near-term step that could be taken toward that goal.

# **APPENDIX 1**

## Announcement 2012-21

DATED MAY 7, 2012

**Countries:** United States; Germany

**Official Citations:** Announcement 2012-21

**Tax Analysts Citations:** Doc 2012-9508

**Related Treaty Texts:**

U.S.-Germany: 1989 Income and Capital Tax Convention (Doc [93-31206](#))

U.S.-Germany: 2006 Protocol to the 1989 Convention (Doc [2006-10666](#))

U.S.-Germany: 2012 Competent Authority Agreement (Doc [2012-7762](#))

### SUMMARY BY TAX ANALYSTS

#### IRS ANNOUNCES AVAILABILITY OF 2012 GERMANY-U.S. COMPETENT AUTHORITY AGREEMENT

The IRS has announced (Announcement 2012-21, 2012-19 IRB 898) that the U.S. and German competent authorities on March 19 reached a mutual agreement on the eligibility of certain pension arrangements for tax exemption under the Germany-U.S. income tax treaty.

Published by Tax AnalystsTM

#### U.S.-Germany Agreement on Pensions

The following is a copy of the Competent Authority Agreement ("the Agreement") entered into on March 19, 2012, by the Competent Authorities of the United States and Germany, regarding the eligibility of certain pension arrangements for benefits under Article 10(3)(b) of the Convention Between the United States of America and Germany for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital and to Certain Other Taxes, together with a related Protocol signed on August 29, 1989, and amended by the Protocol signed on June 1, 2006.

The text of the Agreement is as follows:

#### COMPETENT AUTHORITY AGREEMENT

The Competent Authorities of the Federal Republic of Germany and the United States of America hereby enter into the following agreement (the "Agreement") regarding the eligibility of certain pension arrangements for benefits under paragraph 3(b) of Article 10 (Dividends) of the Convention Between the United States of America and Germany for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital and to Certain Other Taxes, together with a related Protocol signed on August 29, 1989, and amended by the Protocol signed on June 1, 2006 (the "Treaty"). The Agreement is entered into under paragraph 3 of Article 25 (Mutual Agreement Procedure) of the Treaty.

It is understood that for purposes of the Agreement, the term "Article" refers to an Article of the Treaty.

Article 10(3)(b) provides that dividends shall not be taxed in the Contracting State of which the company paying the dividends is a resident if the beneficial owner of the dividends is a pension

fund that is a resident of the other Contracting State, provided that such dividends are not derived from the carrying on of a business, directly or indirectly, by such pension fund.

Article 10(11) provides that for purposes of Article 10, the term "pension fund" means any person that: (a) is established under the laws of a Contracting State; (b) is established and maintained in that Contracting State primarily to administer or provide pensions or other similar remuneration, including social security payments, disability pensions and widow's pensions or to earn income for the benefit of one or more of such persons; and (c) is either, in the case of the United States, exempt from tax in the United States with respect to the activities described in subparagraph (b) or, in the case of Germany, a plan the contributions to which are eligible for preferential treatment under the Income Tax Act.

Paragraph 8(b) of the Protocol to the Treaty, as amended by the Protocol signed on June 1, 2006, provides that in the case of Germany, it is understood that Article 10(3)(b) applies to the person treated as the owner of the assets of the pension fund under section 39 of the Fiscal Code, provided the dividends may only be used for providing retirement benefits through such fund.

In order to provide certainty for taxpayers, the competent authorities of Germany and the United States clarify the treatment of a contractual trust arrangement (CTA) established by an employer to hold assets set aside to fund the employer's simple employer sponsored pension plan (SESP). Provided that the SESP meets all of the requirements set out in section 6a of the German Income Tax Act and that the assets of the CTA are treated as owned by the employer under section 39 of the German Fiscal Code, then dividends derived by the CTA are eligible for benefits under Article 10(3)(b), if all other requirements of the Treaty are satisfied. In such a case, the employer that establishes the CTA shall make the claim for benefits under Article 10(3)(b).

The competent authorities of Germany and the United States also clarify that the term "pension fund" within the meaning of Article 10(11) includes the following entities and that dividends derived by such entities are eligible for benefits under Article 10(3)(b), as if the entity is the beneficial owner of the dividends, if all other requirements of the Treaty are satisfied:

1. A special German investment fund to which the provisions of the German Investment Act (Investmentgesetz) apply, provided such fund is established exclusively to hold the assets of one or more of the following:
  - a. A pension fund within the meaning of Article 10(11) that is established in Germany, or
  - b. A CTA established by an employer to hold assets set aside to fund the employer's SESP provided the assets of the CTA are treated as owned by the employer under section 39 of the Fiscal Code.
2. A group trust described in IRS Revenue Ruling 81-100, as modified by IRS Revenue Rulings 2004-67 and 2011-1, provided that all of its participants are pension funds within the meaning of Article 10(11) that are established in the United States.
3. A common trust fund (within the meaning of Internal Revenue Code section 584) provided that all of its participants are pension funds within the meaning of Article 10(11) that are established in the United States.

In the case of an entity described in paragraph 1), the investment management company (Kapitalanlagegesellschaft) shall make the claim for benefits under Article 10(3)(b) on behalf of the investment fund. In the case of entities described in paragraphs 2) or 3), the trustee of the group trust or common trust fund, as the case may be, shall make the claim for benefits under Article 10(3)(b) on behalf of the group trust or common trust fund.

Agreed to by the undersigned competent authorities:

Michael Danilack U.S. Competent Authority

[Name] German Competent Authority

# **APPENDIX 2**



# Challenges in Characterizing a German Contractual Trust Arrangement

BY ROSEMARIE PORTNER ON JUN. 10, 2013

**Countries:** Germany

**WTD Citations:** 2013 WTD 111-18

**Tax Analysts Citation:** Doc 2013-12639

**SUMMARY BY TAX ANALYSTS** Rosemarie Portner explains how a German contractual trust arrangement works.

Rosemarie Portner is a lawyer/tax adviser with Deloitte & Touche in Düsseldorf.

\* \* \* \* \*

A contractual trust arrangement (CTA) constitutes one of several diverse German pension funding vehicles. Surprisingly, the term "contractual trust arrangement" is used for German tax purposes; it is not, what might be assumed, the translation of a German term. But don't get misled -- German law still does not acknowledge the concept of a trust.

## What Is a CTA Used For?

A CTA is used within the framework of German occupational pension plans in which the employer company makes a direct pension promise to its employees (*Direktzusage*). According to that type of German pension scheme, which is one of the five types of German pension schemes, the pension grant is internally funded by the employer -- the pension liabilities are recognized on the employer company's balance sheet through a provision for pension liabilities that must be proportionally built up (section 6a of the German Income Tax Act (Einkommensteuergesetz)). Thus, a company's pension assets and business assets are integrated and not segregated. The direct (unfunded) company promise is widely used in Germany, especially for high-level executives, because it leads to deferred taxation until pension disbursements are made at generally unlimited amounts.

The purpose of a CTA is to allow the employer company to net the pension obligation with the pension assets for commercial balance sheet purposes. Taxwise, a netting is not permitted. Thus, the CTA can be viewed as an off-balance-sheet vehicle for pension liabilities. Also, the employee will be protected against the employer company's insolvency in addition to protection they receive from the pension security association (*Pensionssicherungsverein*, or PSV). The PSV is an independent entity established by the Confederation of German Employers' Associations, the Confederation of German Industry, and the Association of Life Insurance Companies. All employers who guarantee pension disbursements are required to become contributing members of the PSV.

## The Importance of CTAs

First, when the trustee to a CTA invests the contributions received from the employer company as the trustor to a CTA in shares in foreign corporations or debt instruments (for example, bonds) and thus generates foreign-source dividends or interest that is subject to withholding tax abroad, it must be determined whether the CTA trustee or the employer company as the trustor is regarded as the beneficial owner and thus entitled to claim the treaty benefits. The issue gets even more challenging when the employer company as the trustor resides in another country than the trustee. A CTA, for example, may be established for the benefit of employees working in a German

branch of a foreign employer corporation in connection with a company pension granted to these employees. In that case, different tax treaties may apply that may provide for different withholding tax rates for dividends or interest applicable in the country of source, or provide for specific rules that apply to pension funds.

Second, internationally mobile employees who are assigned to a host country often continue their participation in a German occupational company pension scheme during their assignment abroad. The benefit from a company pension may be includable in taxable gross employment income according to the host country tax law and, generally, be taxable there according to a tax treaty. Or, taxation of the benefit from an occupational company pension may be deferred according to the host country's tax law until pension disbursements are made, at a time when the assigned employee may have returned to the home country. When Germany is the home country and the employee was granted an unfunded company pension promise (*Direktzusage*) from its German employer, the fringe benefit is deferred for German tax purposes until pension disbursements are made and taxed at that point as income from dependent personal services. This applies regardless of whether the employer company has set up a CTA. However, according to the national tax law and tax rules in the host country, a CTA may trigger immediate taxation of the benefit from the pension grant in the hands of the employee. Thus, double taxation may occur if the pension disbursements are fully taxed as income from dependent personal services in Germany after the employee's return.

### **How Does a CTA Work?**

A CTA is created through a fiduciary contract (*Treuhandvertrag*) between the employer company as trustor (*Treugeber*) and a legal entity established by the employer company (for example, a registered association, a limited liability company, or a foundation) as the trustee (*Treuhänder*). The provisions of the German Civil Code (*Bürgerliches Gesetzbuch*) governing labor contracts (sections 662 et seq.) constitute the legal basis. Thus the CTA is not a legal entity as such but constitutes a contractual arrangement between two contracting parties, the employer company as the trustor and the legal entity established by the employer company as the trustee.

The trustor transfers assets to the trustee who acquires legal title in the assets. The term "fiduciary" is not defined in German law. According to German jurisprudence the trustee must strictly comply with the trustor's instructions and is not attributed any discretion at all. The employer company gives instructions regarding the investment of the pension assets and issues investment guidelines with which the trustee must comply. The trustor bears the economic risk of a decrease of the assets' value and benefits from an increase of the assets' values. A fiduciary is acknowledged for German tax purposes if the trustee does not constitute more than an empty shell (German Federal Supreme Fiscal Court (*Bundesfinanzhof*) judgment of November 24, 2009, docket no. I R 12/09).

The trustee holds the assets in an account or deposit at a financial institution that is marked as a fiduciary account/deposit. It must be clearly recognizable that the trustee acts exclusively on behalf of the trustor. The CTA assets -- consisting of assets transferred by the employer company, proceeds generated from investment of the assets, and any capital gains -- must be segregated from the trustee's assets (*Sondervermögen*).

The trustor must be entitled to claim for the return of the assets transferred, which is permitted according to a CTA if the remaining plan assets cover the total liability resulting from the pension promise, or when costs are reimbursed by the employer company.

### **Administrative Fiduciary**

An "administrative fiduciary" (*Verwaltungstreuhand*) is assumed when the trustor concludes a contract that mandates the trustee to manage and administer assets which the employer company

transfers to the trustee. Such an administrative fiduciary is established by the employer company for ease of administration of a company pension or outsourcing of the asset management. The main purpose of a CTA is, however, to create plan assets that according to accounting rules and standards (for example, international accounting standards, international financial reporting standards, German generally accepted accounting principles) can be offset against the employer's pension obligation. A CTA permits for accounting purposes a netting of the pension obligation with the plan assets. Further, the plan assets are no longer accessible to the employer or the employer's creditors but are set aside exclusively to serve the pension obligations. The type of occupational pension scheme as a direct company promise, however, remains unchanged.

According to the German Fiscal Code (Abgabenordnung) (section 39, paragraph 2, no. 1, second sentence), the assets a trustee holds in its own name but on behalf of the trustor are for tax purposes allocated to the trustor. Accordingly, the trustor is taxed with the proceeds generated through investment of the assets transferred to the trustee (section 20(5), second sentence of the German ITA).

Thus, German income tax law recognizes the pension assets segregated through transfer of title to the trustee as the company's (trustor's) assets. The trustor is regarded as the economic owner of the assets that are legally transferred to the trustee and generally entitled to claim for the tax relief according to a tax treaty if the deposit is marked as a fiduciary deposit. Accounting standards treat the assets held by the trustee as pension plan assets.

### **Double-Sided Fiduciary**

The administrative fiduciary may be expanded by an additional "protective fiduciary" (*Sicherungstreuhand*) that protects the employee's accrued rights and claims for pension disbursements against the employer company's insolvency. The administrative fiduciary together with the protective fiduciary is known as a "double-sided fiduciary" (*Doppelseitige Treuhand*). The fiduciary contract constitutes regarding the protective fiduciary a contract for the benefit of a third party (section 328 of the German Civil Code) with the employee being the third party. The protective fiduciary thus entitles the employee to claim pension disbursements to be made from the segregated pension assets. The employee's claim cannot be revoked without the employee's consent. That claim is directed against the trustee under the suspensive condition of the employer company's insolvency. When the suspensive condition is not met, the employee's right to claim pension disbursements is solely directed against the employer company as the trustor. The employer makes the pension disbursements but is reimbursed by the trustee. In practice, the flow of the pension disbursement may be shortened in a way that the trustee directly pays pension disbursements to the employee on behalf of the employer.

According to German general principles that govern the taxation of income, the employee's taxation is deferred until pension disbursements are made because the employee acquires a mere company promise as opposed to a direct claim for pension disbursements against a third party (for example, a life insurance company or pension fund) that the employee could enforce independently from the employer. The employee's taxation is deferred even though the employee is protected against the employer company's insolvency by the PSV. Nor does the claim under the suspensive condition of the employer's insolvency trigger a taxable event for the employee, neither when the CTA is set up nor when the employer's insolvency occurs (section 3, no. 65, lit. (c) of the German ITA). The employee's taxation remains deferred until pension disbursements are made and at that time the employee is taxed with employment income for German tax purposes.

### **Anglo-American Pension Trust and CTAs**

German civil law does not acknowledge the concept of a trust as it is known in Anglo-American countries and that involves three parties -- the settlor, the trustee, and the beneficiary. However, the German fiduciary as a contractual arrangement between the trustor (*Treugeber*) and the trustee

(*Treuhänder*) has a long-standing tradition. The use of the term "contractual trust arrangement" for a fiduciary contract is confusing in an international context in connection with Anglo-American trusts, especially when the CTA is referred to as an entity that might or might not be entitled to claim for treaty benefits applicable to dividends and interest, for example. The question should be whether the trustee or the trustor would be entitled to claim for treaty benefits.

The double-sided CTA consisting of an administrative and a protective fiduciary, however, comes close to an Anglo-American trust, yet there are differences:

- The fiduciary (*Treuhand*) is established on the basis of the fiduciary contract that permits the trustee (*Treuhänder*) to act in its own name but in the trustor's (*Treugeber*) interest; the trustee, being not more than an empty shell, must strictly comply with the trustor's instructions and cannot exercise any discretion regarding the investment of the assets or the determination of the beneficiaries or their survivors.
- In a CTA, the trustee (*Treuhänder*) is established as a legal entity by the employer company as the trustor to which assets are outsourced; the pension assets serve exclusively the purpose of meeting the employer company's pension obligation and are not accessible for the employer company's creditors.
- The pension obligation, however, remains primarily with the employer company.
- The CTA primarily serves the employer company to segregate plan assets, thus permitting a netting with the employer's pension obligation resulting from a pension promise in order to offset the pension liability with the plan assets.
- The proceeds from the invested separated fiduciary assets (pension assets) are -- for German tax purposes -- allocated to the employer company as the trustor who is deemed to be the economic owner of the pension assets.
- The employee acquires a right as a third party benefiting from the fiduciary contract under the suspensive condition of the employer company's insolvency; in the case of the employer company's insolvency, the claim for pension disbursements is directed against the trustee who satisfies the claims out of the pension assets.

The pension trust may be more comparable with one of the four German pension schemes when a separate legal entity is obligated to make pension disbursements to the employee rather than the unfunded company pension, in which the employer company primarily remains obligated to provide pension disbursements. This does not necessarily mean, however, that contributions to a pension trust would trigger immediate taxation at the level of the employee, as is the case when the employee acquires a direct and separately enforceable claim against a life insurance company, a pension fund, or as a pension pool (*Pensionskasse*). The particular facts and circumstances had to be evaluated, especially taking into account the scale of discretion allocated to the trustee of a pension fund in order to determine whether the employee acquires a direct, irrevocable claim for pension disbursements that the employee could enforce independently and without the employer company's cooperation.

Whether a German unfunded company pension promise for which a CTA is established leads to a deferred taxation or triggers immediate taxation at the level of the employee in the host country must be determined based on the host country's tax law; the above elaborations may be helpful to better understand how a CTA works.

### **Treaty Benefits for a CTA**

For German tax purposes, the employer company being the trustor to a CTA is entitled to claim relief from tax withheld on dividends and interest the trustee receives from investments in foreign equity or debt instruments. However, the employer company does not meet the criteria of a pension fund. The trustee meets the criteria of a pension fund but is not the beneficial owner of the investment income. The claim for application of tax treaty benefits becomes especially

challenging when pension funds enjoy more generous treaty benefits than the employer company as the trustor would enjoy.

This is true when the trustee to a CTA receives dividends from a U.S. corporation. Under article 10(3)(b) of the Germany-U.S. tax treaty of 1989, as amended by the 2006 protocol, dividends are not taxed by the country of source if the beneficial owner of the dividends is a pension fund residing in the other contracting state unless the dividends are derived from a business directly or indirectly carried on by the pension fund. The term "pension fund" is defined in article 10(11) as any person organized under the laws of the United States or Germany that is established and maintained to primarily administer or provide pension or other similar remuneration. Also, in the case of the U.S., the pension fund must be exempt from tax in the U.S.; and in the case of Germany, it must be a pension scheme the contributions to which are eligible for preferential treatment under the German ITA. Preferential treatment under the German ITA is granted to three of the five German pension schemes when the contributions trigger immediate taxation for the employee, but a tax exemption is granted at a limited amount if further conditions are met. The unfunded company pension promise, however, is not granted preferential treatment. The tax deferral results from application of the general tax principle governing the taxation of income.

Paragraph 8b) of the protocol regarding article 10(3) (dividends) of the Germany-U.S. tax treaty states:

subparagraph b) of paragraph 3 of Article 10 applies to the person treated as the owner of the assets of the pension fund under section 39 of the Fiscal Code, provided the dividends may only be used for providing retirement benefits through such fund.

The U.S. and the German competent authorities reached a consultation agreement (article 25(3) of the Germany-U.S. tax treaty) dated March 19, 2012, to clarify that the term "pension fund" includes a CTA. The competent authority agreement clearly states, however, that the employer company as the trustor can claim the benefits of article 10(3)(b). From there it follows that the employer company as trustor is entitled to claim an exemption from withholding tax on dividends according to article 10(3)(b) of the Germany-U.S. tax treaty. I believe that the trustee must meet the specific preconditions set out in article 28(2)(e) of the Germany-U.S. tax treaty (limitation on benefits). Accordingly, an exemption from withholding tax requires that either more than half of the beneficiaries of a CTA are individuals who are residing in Germany or that the trustor is entitled to claim the tax treaty benefits of the Germany-U.S. tax treaty.

## **The UK Insurance Industry**

The UK insurance industry is the third largest in the world and the largest in Europe. It is a vital part of the UK economy, managing investments amounting to 26% of the UK's total net worth and contributing £11.8 billion in taxes to the Government. Employing over 315,000 people in the UK alone, the insurance industry is also one of this country's major exporters, with 28% of its net premium income coming from overseas business.

Insurance helps individuals and businesses protect themselves against the everyday risks they face, enabling people to protect themselves, their families, their homes and assets, provide for a financially secure future and manage the risks faced in their businesses. Insurance underpins a healthy and prosperous society, enabling businesses and individuals to thrive, safe in the knowledge that problems can be handled and risks carefully managed.

## **The ABI**

The Association of British Insurers (ABI) is the voice of the UK insurance, representing the general insurance, protection, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 250 [members](#), accounting for some 90% of premiums in the UK.

The ABI's role is to:

- Be the voice of the UK insurance industry, leading debate and speaking up for insurers.
- Represent the UK insurance industry to government, regulators and policy makers in the UK, EU and internationally, driving effective public policy and regulation.
- Advocate high standards of customer service within the industry and provide useful information to the public about insurance.
- Promote the benefits of insurance to the government, regulators, policy makers and the public.

## **Introduction**

1. The ABI welcomes the opportunity to comment on the discussion draft<sup>1</sup> on the proposed changes to the OECD Model Convention concerning the treaty residence of pension funds.
2. This consultation is of interest to insurers because many tax treaties provide for a limited or complete exemption from withholding taxation for pension schemes. The amendment to the definition should help enable pension schemes to obtain treaty benefits across a wider range of investment arrangements as long as those structures are only accessible to pension schemes. However, we do not believe the current definition of "recognised pension fund" covers all pension schemes that should benefit from treaty benefits.
3. In the UK there is an increasing trend for pension schemes to be arranged through UK life insurance companies. This is particularly so following the pension auto enrolment initiative of

<sup>1</sup> Discussion draft on treaty Residence of Pension Funds released 29 February 2016.

the UK Government, which has seen 6 million people automatically enrolled in the last 3 years. So, valuable pension schemes being offered to customers through UK life insurance companies are therefore increasingly becoming the norm.

4. Pension schemes arranged through UK life insurance companies will fall outside the definition of “recognised pension fund” which it is proposed be added to paragraph 1 of Article 3. As these pensions schemes are regulated and are constituted and operated to administer or provide retirement benefits, we believe they should be within the definition. If they are not within the definition then they will suffer inappropriate taxation which will impact on returns to consumers. This will also perpetuate current differences in economic outcomes between legal structures with the same commercial goal.
5. Many UK life insurance companies that are incorporated and resident in the UK operate a long term business fund which is divided into a number of different fund sections which cover all the different types of business they write including protection life assurance, life insurance investment products and pension schemes. In addition there are a small number of so-called composite insurers who write both life and general insurance. We believe that the requirement that the entity is operated “exclusively” for the benefit of pension schemes would create issues for most UK insurance companies (see paragraph 8).
6. The vast majority of the pension scheme funds within the long term business fund of insurers are maintained solely for the benefit of United Kingdom pension schemes which are registered under Part 4 of the UK Finance Act 2004 (i.e. they are regulated) and are constituted and operated to administer or provide retirement benefits. These funds are solely accessible to pension schemes and operate in much the same way as standalone pension funds so we believe the definition of “recognised pension fund” should encompass such funds. However, they are not within the definition as drafted because the pension scheme funds are not treated as a separate person under UK Taxation laws. We believe they should be within the definition and make some suggestions in paragraphs 10 and 11 on how this could be achieved.
7. If the definition of “recognised pension fund” does not include pension schemes arranged through UK life insurance companies then these schemes will suffer inappropriate taxation which will impact on returns to consumers.
8. There are some UK Life insurance companies that have a separate company that only administers the pension schemes it operates. However, the UK life insurance company may also operate and administer pension schemes which are registered overseas (this is likely to be a small part of the UK life insurance companies business). Although, such a company would be an entity that is treated as a separate person under the taxation laws of the UK, as not all of its pension schemes would be regulated by the UK, it would not be within the definition because of the “exclusively” requirement. Furthermore, shareholders would expect to get a return from an insurance company operating a pension scheme, which would again mean an “exclusively” test would not be met.

9. We therefore believe “almost exclusively”, as suggested in the first bullet in paragraph 12 of the final report on Action 6<sup>2</sup>, which is set out on page 2 on the discussion draft, would be more appropriate than “exclusively” and would overcome the issues identified in paragraph 8.

10. In view of the above we suggest paragraph 1 of Article 3 be amended to

the term “recognised pension fund” of a State means an entity or arrangement established in that State that is treated as a separate person under the taxation laws of that State and:

- i) that is constituted and operated *exclusively or almost exclusively* to administer or provide retirement or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities; or
- ii) that is constituted and operated *exclusively or almost exclusively* to invest funds for the benefit of entities or arrangements referred to in subdivision (i); or
- iii) *that is a fund or one of a number of funds, operated through an entity, that although the fund is not treated as a separate person under the taxation laws of that State it (i.e. the fund) is constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities and the entity through which it operates is treated as a separate person under the taxation laws of that State.*

11. An alternative approach would be to amend paragraph 1 of Article 3(i) to enable funds, within an entity, that are constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities to be within the definition of a “recognised pension fund”

12. We believe the Commentary should also specify that “entity” in (iii) above would include an insurance company or identifiable sub-divisions of an insurance company.

Association of British Insurers  
31 March 2016

<sup>2</sup> Action 6 of the BEPS Action Plan (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances)



File Name: 2016/06

1 April 2016

Tax Treaties  
Transfer Pricing and Financial Transactions Division  
OECD/CTPA  
Paris, France

Email: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

Dear Sir/Madam

**Re: OECD Public Discussion Draft – “Treaty Residence of Pension Funds”**

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the above OECD Discussion Draft (“DD”).

#### **About ASFA**

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90 per cent of the 14 million Australians with superannuation.

ASFA notes that the primary term for “pension funds” in Australia is “superannuation fund” and these terms are used interchangeably throughout this submission.

ASFA also notes that all comments on the DD will be made publicly available by the OECD, and agrees to ASFA being publicly identified in this way.

ASFA has also provided a copy of this submission to representatives of the Treasury of the Commonwealth of Australia to inform Treasury’s representations and ongoing discussions in respect of the proposed changes to Articles 3 and 4 of the OECD Model Tax Convention (“the Convention”) and to the Commentary on these Articles (“the Commentary”).

#### **General comments**

ASFA welcomes the OECD’s moves to enable pension funds to access the benefit of tax treaties by treating them as a resident of the State in which they are constituted under the Convention.

Australian superannuation or pension funds are some of the largest Australian investors in foreign jurisdictions. The present total funds under management (“FUM”) of Australian superannuation funds is approximately AUD \$2 trillion, and is anticipated to rise to more than AUD \$9 trillion by 2030. A significant share of the existing FUM is invested outside Australia, and this share is anticipated to increase as the total size of the Australian superannuation sector increases.

Accordingly, greater clarity in the residency status of Australian superannuation funds would assist in removing or reducing taxation barriers caused by double taxation of income or capital gains derived by such funds, and thus would assist the entire Australian superannuation industry in its primary objective to advance the retirement outcomes for Australians.

The DD was framed in the context of potential changes to Articles 3 and 4 of the Convention and Commentary, to ensure that a pension fund is considered to be a resident of the State in which it is constituted for the purposes of tax treaties.

ASFA notes that, for many large Australian superannuation funds, this is a significant practical issue for Australia’s present tax treaties. Australian superannuation funds have encountered practical issues in some jurisdictions in being treated as residents of Australia for the purposes of the treaty, and these impose costs in making detailed representations or collating substantial documentation in respect of funds’ underlying members in those jurisdictions. Accordingly, by providing certainty in respect of the funds’ residency status, the proposed changes have the potential to increase economic efficiency.

The DD notes that the proposed changes to Articles 3 and 4 of the Convention, and related Commentary, in respect of the definition of “recognised pension fund” will likely include the following elements:

- the definition will refer to entities or arrangements established in a State and constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals
- the entities or arrangements to which the definition will apply will need to be treated as separate persons under the taxation laws of that State
- in order to cover only funds that the tax law recognises as pension funds, these entities will need to be regulated as pension funds by the State in which they are established
- the definition will also need to cover entities and arrangements that are constituted and operated exclusively or almost exclusively to invest funds for the benefit of entities or arrangements that will themselves qualify as “recognised pension funds”
- the definition will need to be accompanied by detailed Commentary that will explain some of these requirements, in particular the requirement that a pension fund “be regulated as a pension fund”.

ASFA understands that, pursuant to the broader Action Plan on Base Erosion and Profit Shifting (BEPS), Australia may sign up to a “multilateral agreement” to streamline the implementation of the measures developed to address BEPS, in particular by modifying bilateral tax treaties. If so, this may result in changes to the Convention and Commentary being taken into account in determining residency for Australian pension funds in relation to the treaties with all of the other countries that sign up to this agreement. In this way, the proposed changes may have broader application, and not be limited only to Australia’s new or renegotiated treaties.

### **Specific Responses to the Matters Raised in the DD**

In respect of the specific matters raised in the DD, ASFA sets out its comments below.

- a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j):**  
*Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?*

ASFA considers that this phrase deals adequately with all Australian superannuation funds.

- b) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):**  
*Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?*

In relation to this question, ASFA notes that the purpose for which an Australian superannuation fund may be maintained is expressly set out in section 62 of the primary Australian legislation governing superannuation funds, being the *Superannuation Industry (Supervision) Act 1993 (Commonwealth of Australia)*. This section is commonly known within Australia as the “sole purpose test”.

Section 62 requires that a superannuation fund must be maintained solely for one or more of the purposes set out in subsection 62(1)(a) (“the core purposes”), or for one or more of the core purposes together with one or more of the purposes set out in subsection 62(1)(b) (“the ancillary purposes”).

The core purposes include:

- the provision of benefits for each fund member on or after the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged
- the provision of benefits for each fund member on or after the member's attaining age 65

- the provision of benefits to the legal personal representative and/or the dependants of a fund member on or after the death of the member, provided that the death of the member occurred before he or she retired or attained age 65.

The ancillary purposes include:

- the provision of benefits for each member on or after termination of employment (which includes resignation, redundancy, etc.) from an employer who had at any time contributed to the fund in relation to the member
- the provision of benefits for each member on or after the member's temporary or permanent cessation of work on account of physical or mental ill-health
- the provision of benefits in respect of a deceased member, to the member's legal personal representative and/or to dependants of the member, where the member dies after retirement or after reaching age 65 (commonly referred to as "reversionary benefits")
- the provision of such benefits as the primary Australian prudential regulator of superannuation funds (the Australian Prudential Regulation Authority or APRA) approves in writing.

ASFA notes that paragraph 10.5 of the proposed Commentary on Article 3 in the DD cites payments made as a result of the death or invalidity of a person as an example of other "similar benefits".

In an Australian context, this example would appear to result in "retirement or similar benefits" including all of the above core and ancillary purposes.

However, ASFA submits that for clarification, the Commentary should expressly state that "retirement or similar benefits" includes:

1. Payments made by funds on or after the ordinary retirement date, notwithstanding that the person may continue in employment beyond that date. In Australia, a member has limited access to his or her entitlements after age 55 (or later "preservation age"), and unfettered access at age 65 (historically Australia's ordinary retirement date), notwithstanding that he or she may still be working at those dates.
2. Payments made by funds as a result of the temporary invalidity of a person - that is, that the reference in the Commentary to "invalidity" extends not just to permanent incapacity but also to temporary incapacity. In Australia, temporary incapacity benefits are able to be paid in the form of income payments replacing part or all of the salary or wages that would otherwise have been received by members.
3. Payments made by funds following the certification that a member is suffering from a terminal medical condition that is anticipated to result in death within 2 years. In Australia, a member has access to his or her entitlements following such a certification, notwithstanding that the member's illness may not yet have reached the point of invalidity.

4. Payments made by funds in rare circumstances following the termination of a member's particular employment. In Australia, most superannuation entitlements are subject to strict rules, such that access is not available until age 55 at the earliest. However, due to rules applying to some benefits that accrued prior to 1999, a portion of member's entitlements (known as "non-preserved benefits") may still be accessible upon termination of a member's particular employment prior to age 55.
5. Payments made by funds to temporary residents only, upon cessation of residence. In Australia, it is mandatory that the accrual of benefits in Australian pension funds for temporary residents of Australia be paid out to the members or to the Australian Government within 6 months of the cessation of residence by such members.
6. Payments made by funds in rare or special circumstances. In Australia, benefits may be paid outside the usual access restrictions to persons who satisfy the definition for being in "severe financial hardship", or who satisfy the conditions for APRA to allow payment on "compassionate grounds". Recipients of benefits prior to age 55 on the grounds of "severe financial hardship" are limited to payments of no more than AUD \$10,000 in a 12 month period. APRA specifically determines the extent of benefits on "compassionate grounds" on a case by case basis, taking into account the reasons for the member's need for such access.
7. Payments made by funds below a de minimus amount. In Australia, benefits below AUD \$200 may be paid outside the usual access restrictions to persons upon the termination of a member's particular employment.

Subject to the Commentary expressly dealing with each of the above circumstances, ASFA considers that the word "exclusively" is not too restrictive given the normal operations of Australian superannuation funds.

c) ***As regards the phrase "similar benefits" included in subdivision l) of the definition of "recognised pension fund" in proposed Art. 3(1) j):***

*Are there examples of "benefits" that are typically granted by pension funds that would not be covered by the phrase "similar benefits"? If yes, please describe these benefits.*

ASFA refers you to its comments in its response to question b) above.

As noted, Australia's superannuation legislation specifically restricts the purposes for which an Australian pension fund may be established and maintained. These restrictions set clear boundaries in respect of the circumstances in which an Australian pension fund can pay benefits to its members.

However, beyond these types of monetary benefits paid by funds, Australian superannuation funds may also provide other benefits to members.

These may include:

- incidental advantages that may accrue to members arising from an Australian pension fund's investments (for example, investment in a well-researched and commercially sound project that might incidentally create employment opportunities for the fund's members); or
- fund-sponsored member awareness, education and financial advice programs, targeted at fund specific issues such as benefit features (including insurance options, investment options).

In Australia, the extent of these other benefits is significantly curtailed. For example, whilst a fund may offer a financial planning service aimed only at a member's interest in the fund, APRA has stated that the provision by a fund of financial planning services aimed at broader non-superannuation savings and investment opportunities, products or services, such as investment or tax advice and health insurance would contravene the "sole purpose test". APRA notes that, in an Australian context:

- it would be inappropriate for the cost of such services to be borne by a fund, as the subject for such advice is not within the core or ancillary purposes for which a fund must be established and maintained; and
- funds wishing to make such broad services available to members would need to consider other means for funding the services.

ASFA submits that the Commentary should expressly note that the provision of incidental advantages arising from investments of the kind noted above, and financial planning services aimed only at a member's interest in the fund, would not result in a pension fund not being regarded as "constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals".

**d) As regards the phrase "that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements" included in subdivision ii) of the definition of "recognised pension fund" in proposed Art. 3(1) j):**

*Is the word "exclusively" too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?*

ASFA notes the comments in paragraph 10.8 of the proposed Commentary on Article 3 in the DD that pension funds often invest together with other pension funds pooling their assets in certain arrangements or entities and may, for various commercial, legal or regulatory reasons, invest via wholly owned entities or arrangements that are residents of the same State. ASFA concurs with these comments, and supports the following sentence in the same paragraph in the DD that, since such arrangements and entities act only as intermediaries for the investment of funds used to provide retirement benefits to individuals, it is appropriate to treat them like the pension funds that invest through them.

In Australia, the primary entities presently used to pool the assets of superannuation funds are:

1. Life insurance companies, which as corporations established and maintained in Australia would already be treated as Australian residents for treaty purposes.
2. Pooled superannuation trusts (“PSTs”), which are taxed in Australia in the same manner as Australian superannuation funds. The beneficial owners of the units in a PST are restricted by Australian law to Australian superannuation funds and/or life insurance companies in respect of policy holders who are themselves Australian superannuation funds.
3. Unit trusts (“UTs”), which are flow through entities in Australia, such that any Australian tax is paid by the beneficial owners of the units in the UT. The beneficial owners of the units in a UT are not restricted to Australian superannuation funds, and thus may also include individuals, corporations, and non-Australian pension funds.

As noted, it is not necessary that life insurance companies in Australia be covered by proposed Article 3(1) j), as the residency of corporations is already addressed in the Model Convention.

ASFA considers that the word “exclusively” is not too restrictive in an Australian context given the normal operations of an Australian PST or UT. In Australia, these entities are by their very nature restricted to activities relating to the investment of funds, and any other operations would be wholly incidental and subordinate to these investment functions.

However, ASFA submits that the Commentary should clarify two aspects.

*1. Passive versus active investment*

ASFA notes that the nature of the investments for some pension funds may involve the pension fund taking an active role, rather than just being the passive recipient of investment income. For example, a fund (or the wholly owned or pooled investment vehicle) may undertake property development rather than just the holding of property for rent.

In this light, ASFA submits that the Commentary should note that the references to investment are not restricted to passive investment only.

*2. Entities not exclusively owned by pension funds from the particular State*

As noted above, it is possible for an Australian UT to have unit holders that are not exclusively Australian pension funds.

For some UTs, there will be no such possibility, for example:

- a UT that is established and maintained exclusively:
  - as the wholly owned investment vehicle for a single Australian superannuation fund, or

- for the pooling of investments of Australian superannuation funds only; or
- a “closed fund” UT that is established with its only unit holders being Australian superannuation funds, and which has no capacity for new unit holders to be admitted or for the transfer of units to other persons

For these UTs, ASFA considers that the word “exclusively” is not too restrictive in an Australian context, and that the Australian Taxation authority (the Australian Taxation Office (“ATO”)) should readily be able to provide a Certificate of Residency or similar support to such entities to provide to jurisdictions with which Australia has treaties based on such words.

ASFA submits that the Commentary should note that, for entities not exclusively owned by pension funds from the particular State, reference would need to be had to the existing guidance in the 2010 OECD Report *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles* (CIVs), and to the outcomes of the separate consultation and Public Discussion Draft of 24 March 2016 in respect of the Treaty Entitlement of Non-CIV Funds.

In an Australian context, ASFA notes that it is likely that for any UT that is not exclusively owned by Australian pension funds to be treated as an Australian resident, it would have to prove that its existing unit holders do not include non-Australian residents, and provide such other evidence as the ATO may require in order to obtain a Certificate of Residency.

\*\*\*\*\*

Should you have any questions on any of the matters raised in this submission please contact Julia Stannard via email [jstannard@superannuation.asn.au](mailto:jstannard@superannuation.asn.au).

Yours sincerely



Glen McCrea  
Chief Policy Officer



For the attn. of  
Tax Treaties, Transfer Pricing and Financial  
Transactions Division OECD / CTPA

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Luxembourg, 1<sup>st</sup> April 2016

Dear Sirs,

**Response to OECD Discussion Draft on Changes to the OECD Model Tax Convention  
concerning the Treaty Residence of Pension Funds - 29 February 2016**

The Association of the Luxembourg Fund Industry (ALFI) is the representative body of the Luxembourg investment fund community<sup>1</sup>. The Luxembourg Fund Industry is the largest fund domicile in Europe and a worldwide leader in cross-border distribution of funds. Luxembourg-domiciled investment structures are distributed on a global basis in more than 70 countries with a particular focus on Europe, Asia, Latin America and the Middle East.

ALFI is grateful for this opportunity to express its views and suggestions on this OECD Public Discussion Draft on the proposed changes to the OECD Model Tax Convention concerning the treaty residence of Pension Funds. ALFI welcomes the recognition of the importance of ensuring treaty entitlement for pension funds and is willing to participate to the follow-up work as contemplated by the Final report on OECD BEPS Action 6 released on 5 October 2015.

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<sup>1</sup> Created in 1988, the Association today represents over 1300 Luxembourg domiciled investment funds, asset management companies and a wide range of service providers such as custodian banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax experts, auditors and accountants, specialist IT providers and communication companies.

## **Response to the questions raised in the Discussion Draft**

**Question a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?**

Currently, while most Luxembourg pension funds are treated as a separate person under Luxembourg tax law (according to article 159 Income Tax Law), this may not be the case for certain pillar 1 pension funds, which may have the legal form of a public establishment. Therefore, in order to make sure that they can also benefit from the same access to double tax treaties as other pension funds, the definition should be extended to include pension funds that are part of the State itself, which may have different treatment in a double tax treaty than the State itself, like, for example, the “Caisse Nationale d’Assurance Pension” or the “Fonds de Compensation commun au régime général de pension”.

In addition, in order to cover the case of sub-funds or compartments of funds, which are not treated as a separate person for tax purposes but which may also be established to invest funds for the benefit of entities or arrangements referred to in subdivision i), Paragraph ii) should be completed as follows: **“, including an arrangement within an entity or arrangement which is itself treated as a separate person under the taxation laws of that State.”**

**Question b) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?**

In order to ensure that all types of pension funds fall within this definition, we would suggest to amend the current text as follows and in line with Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision:

**“that is constituted and operated exclusively to administer or provide retirement or similar benefits to individuals, where “retirement benefits” may be defined as “benefits paid by reference to reaching, or the expectation of reaching, retirement or, where they are supplementary to those benefits and provided on an ancillary basis, in the form of payments on death, disability, or cessation of employment or in the form of support payments or services in case of sickness, indigence or death. In order to facilitate financial security in retirement, these benefits usually take the form of payments for life. They may, however, also be payments made for a temporary period or as a lump sum”**

Finally, in section 10.3 of the commentary, we would suggest to specify that all types of pensions are covered, *i.e.* all three pillars.

**Question c) As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?

Since section 10.5 of the commentary reads “Examples of other “similar benefits” would include payments made as a result of the death or invalidity of an individual.”, we understand that there is no strict definition of “similar benefits” and that there is some flexibility left in order to make sure that the scope is broad enough so as to enable all types of pension funds to fall within that definition. Thus, we do not recommend any change.

**Question d) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

In order to make sure that this provision is in line with EU law, the scope should not be limited to intermediaries of the same State as the pension fund but instead should be extended to any equivalent intermediary which is acting on behalf of one or more pension funds established either in another EU member State and/or in a country which has concluded a double tax treaty with the source State.

Also, we would suggest to clarify in the commentary that an intermediary which would be set up by a state pension fund in order to invest excess cash would also be covered. This is justified since the aim of this investment would be to maximize the pension return.

Finally, to cover the case of sub-funds or compartments, which we already addressed under question a), we would recommend to amend commentary 10.8 as follows: “10.8 Subparagraph (ii) of the definition covers entities that pension funds covered by subparagraph (i) use to invest indirectly, **as well as specific arrangements within a legal person (frequently known as sub-funds or compartments).**”

We are grateful in advance for your attention to the comments expressed in this letter and we welcome the opportunity to discuss these with you.

Should you need any additional information, ALFI would be pleased to assist you.

Kind regards,

ALFI

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Paris, France

1. April 2016

## Comment Letter from ATP, Denmark - Public Discussion Draft Treaty Residence of Pensions Funds

As being an interested party Arbejdsmarkedets Tillægspension (ATP) hereby wish to respond to your invitation to comment on the discussion draft on changes to the OECD Model Tax Convention concerning the Treaty Residence of Pensions Funds dated 29 February 2016

ATP is established in Denmark as a public pension fund for the purpose of paying supplementary pensions to wage earners in Denmark on top of the state pension. ATP is regulated by a specific Danish act – the ATP Act – comparable to the regulation of private pension funds and companies in Denmark.

ATP had at year-end 2015 approximately DKK 705 billion assets (USD 104.6 billion) under management and is one of the largest pension funds in Europe with close to 5 million members. Further information on ATP can be found at our website: [atp.dk](http://atp.dk)

**Comments:**

The phrase ***“similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j)*** and the phrase ***“that is constituted and operated exclusively to administer or provide retirement or similar benefits”***:

Besides paying out ordinary pension benefits the ATP Act includes an obligation for ATP to pay certain survivor benefits. If a member dies before retirement age, his or her spouse or common-law partner and children under the age of 21 will generally receive lump-sum survivor benefits.

We expect the phrase *“similar benefits”* to be interpreted broadly and that the wording in paragraph 10.5: *“Examples of other “similar benefits” would include payments made as a result of the death or invalidity of an individual.”* includes the

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above mentioned survivor benefits.

In addition to the ordinary ATP pension scheme ATP manages for the time being the Supplementary Labour Market Pension Scheme for Disability Pensioners (SUPP) as part of the ATP Act. SUPP is a voluntary scheme, giving disability pensioners an attractive opportunity to save for lifelong pension. For every disability pensioner contributing to SUPP the Danish government contributes twice the amount of the disability pensioner. More than 4 out of 10 disability pensioners pay SUPP contributions. SUPP contributions are managed together with ATP contributions, and its members accrue current guaranteed lifelong pension in the same way as ATP members. Over the years ATP has administered other savings and pensions schemes, which are now closed, but the Danish government may in the future ask ATP to administer new savings and pensions schemes.

The OECD has asked if the word “*exclusively*” would be too restrictive given the normal operations of a pension fund. To be certain that the word “*exclusively*” is not interpreted in an too narrow way and thereby will exclude persons or entities with other or multiple pension and savings activities from the definition of a recognized pension fund, we can suggest to rephrase the wording to: “*exclusively or almost exclusively*” in the necessary places in the articles or in the commentaries of the OECD Model Tax Convention.

Finally ATP is aware of a comment letter from an informal coalition of global pension funds including Pension Denmark, which comments in certain areas will align with our comments. In that matter ATP can support a suggestion from the coalition of adding the word “pension” to paragraph 1, subsection j) letter (i) of Article 3 of the Model Tax Convention in order to make this definition widely applicable, considering that not all OECD Member States may interpret the terms “pension” and “retirement” in the same way.

Arbejdsmarkedets Tillægspension

Mia Line Byrk  
Head of Tax, Tax

# The BEPS Monitoring Group

## **Comments on the Public Discussion Draft on CHANGES TO THE OECD MODEL CONVENTION CONCERNING THE TREATY RESIDENCE OF PENSION FUNDS**

These comments have been prepared by the [BEPS Monitoring Group](#) (BMG). The BMG is a network of experts on various aspects of international tax, set up by a number of civil society organizations which research and campaign for tax justice including the Global Alliance for Tax Justice, Red de Justicia Fiscal de America Latina y el Caribe, Tax Justice Network, Christian Aid, Action Aid, Oxfam, and Tax Research UK. These comments have not been approved in advance by these organizations, which do not necessarily accept every detail or specific point made here, but they support the work of the BMG and endorse its general perspectives. It has been drafted by Sol Picciotto, with contributions and comments from Jeffery Kadet, Tommaso Faccio and Francis Weyzig.

We begin with some general comments on the broader implications of the treatment proposed, and the way in which the proposals on Action 6 are being formulated, and may be implemented. These are also relevant to the consultation on non-CIV funds. In our view it is important for there to be proper consultation and public debate on these policy issues, and we regret that these discussion drafts have focused on technical details, without even any explanation of the more general issues. The BEPS project has received strong support from political leaders due to the widespread public concerns about the evident defects of the international tax system. While repairing those defects inevitably involves some abstruse technical issues, it is essential that proposals should be formulated in a way which explains how they contribute to the broader goals identified by the G20 world leaders.

### **SUMMARY**

Under these proposals a pension fund would be treated as resident in the state where it is formed, provided that it fulfils specified conditions, especially that it is regulated there. This would mean that such funds would normally be eligible for tax treaty benefits, in particular exemption from withholding taxes on interest and dividend payments, even if the funds are exempt from tax on this income in their state of residence, and even if their investors are resident in other states. This therefore leaves the right to tax payments made by the fund to the countries of residence of the investors. They would have the responsibility to ensure that they do not authorize the sale of interests in such a fund to their residents unless the country where it is formed satisfies the global common reporting standard and agreements for automatic exchange of tax information.

These proposals focus rather on ensuring that a fund is not used to avoid source country taxes. We make two suggestions for strengthening the conditions to ensure that eligibility for treaty benefits is not abused.

These proposals, as well as others, entail changes to the OECD model tax convention and its commentaries, and are intended to be implemented through the proposed multilateral convention being negotiated under the BEPS process. All states may join this negotiation and

the proposed convention, including developing countries which would normally use the UN model convention as their starting point for treaty negotiation. We call for the issuing of a policy paper for public discussion to explain how the proposed multilateral convention is intended to be structured, and exploring its implications for the future of the OECD and UN models, and their relationship.

## GENERAL COMMENTS

### 1. Implications of the Residence Rules on Investment Funds

This consultation concerns relatively minor technical details of clarifications consequential on the proposals under BEPS Action 6 on Preventing the Granting of Treaty Benefits in Inappropriate Circumstances. The Action 6 measures entail inclusion in tax treaties of provisions to prevent treaty shopping or other abuse of tax treaties. In particular they will allow a source state to deny exemptions from withholding taxes on payments to entities formed in the partner state principally to take advantage of the treaty. Such entities often take the form of some kind of investment vehicle. This raises the question of whether treaty benefits might be denied to widely-held collective investment vehicles (CIVs), such as pension funds or other collective investment funds. This issue was considered a few years ago by the OECD, which issued a report in 2010 on *Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles*.

The questions raised are whether and under what conditions a CIV can be assured of treaty benefits (i) for itself, and (ii) for its investors. The generally accepted principle is that investment income should be taxed either at the level of the CIV itself, or when payments are made to beneficiaries. Hence, where CIVs are themselves exempt from tax on investment income, they would be required to apply withholding taxes on their payments to their investors or beneficiaries, at least to those who are not resident in the same state as the CIV. This can pose significant problems, as investments are often made through banks or other intermediaries and nominee accounts, and may be very fluid. However, CIVs which are regulated in their country of residence can be subject to know-your-customer requirements to ensure that they apply withholding taxes unless they know that the recipient is a resident.

The question of eligibility of CIVs and of their investors for tax treaty benefits has become even more complex as a result of their internationalization. When a CIV such as a pension fund was formed and resident in the same country as its beneficiaries, eligibility could be relatively easy to determine. Since they may now be formed and resident in any country, and have beneficiaries also in many countries, this has become a highly complex matter. Also, countries now compete to offer themselves as financial centres, including by negotiating an extensive network of tax treaties. Some are small countries which traditionally operated as tax havens and many of which aim to be offshore financial centres, such as Jersey and Mauritius. The facilities offered by such a financial centre are likely to include formation of investment vehicles, even if the actual investment management function may take place elsewhere.

Many of these countries have now been persuaded to ensure that they comply with the highest global standards of regulation not only for financial services, but also for combating tax evasion and avoidance and the often related activities of laundering the proceeds of crime and corruption. These include in particular the requirements to collect and automatically exchange tax-related information established by the US Foreign Account Tax Compliance Act (FATCA), and the Common Reporting Standard (CRS) developed by the OECD for the G20. In these circumstances, it is understandable that some countries may be willing to sign normal tax treaties with such countries, even if some of them may have low or zero taxes on



income. However, this makes it especially important that the model tax treaty which will be used as the basis for negotiating such treaties should include truly effective anti-abuse provisions.

The approach now proposed is to accept that CIVs can be treated as resident in the country where they are formed, provided that they are regulated there. This would mean that such vehicles would be eligible for treaty benefits, in particular exemption from withholding taxes on interest and dividend payments, even if they are exempt from tax on this income in their state of residence. This therefore leaves to the countries of residence of the investors in the CIV the right to tax payments made by the fund to those investors. They would have the responsibility to ensure that they do not authorize the sale of interests in CIV to their residents unless they have in place adequate arrangements to ensure appropriate taxation. In our view this should include acceptance of automatic exchange of information with the country where the CIV is formed in compliance with the OECD global standard and the CRS.

From the viewpoint of the source country, the concern is to ensure that a CIV is not used to avoid taxes it applies to the beneficial owners of assets in that country. The Action 6 proposals provide for both a general anti-abuse provision in the form of a Principal Purpose Test (PPT), and a more specific and very detailed Limitation of Benefits (LoB) article, which may also be combined. The PPT provides a broad power to deny treaty benefits in cases identified as abusive, while the LoB article attempts to define in detail those recipients which should be deemed eligible. Thus, for countries adopting the LoB it is essential to define accurately the criteria for eligibility for treaty benefits of entities, such as investment funds (i.e. their legal nature, ownership and activities). However, even for countries which apply a PPT, the definition of which entities are considered to be residents, and hence in principle eligible for benefits, is important, to guide the application of the test.

## **2. Implementation of the Proposals**

This DD includes proposed revisions to the OECD model convention and its Commentary. The intention is that they will be included in the proposed Multilateral Convention under Action 15, together with the other Action 6 proposals and other BEPS outputs involving treaty changes. The BEPS project will now be implemented through the Inclusive Framework agreed by G20 leaders, which will apply to all states.<sup>1</sup> Participating states will be expected to implement the BEPS Project Minimum Standards. These include the Action 6 proposals.

Indeed, the inclusion of effective anti-abuse rules is a high priority for all countries, and they should be an essential element of the proposed Multilateral Convention. However, this will involve some difficult technical and perhaps policy issues, especially for non-OECD countries. Developing countries will normally expect to prefer the UN to the OECD model as a basis for negotiation, even if their treaties eventually include elements from both. The Action 6 proposals, including those in this DD, entail not only the inclusion of an anti-abuse provision, but revisions to other articles, as well as changes to the Commentaries. This DD in particular entails changes to articles 3 and 4, and to their commentaries. These are presented in this DD as changes to the OECD model, but with the understanding that they will be included in the proposed multilateral convention.

However, no mention is made of how it is proposed to deal with these changes in the multilateral convention. In particular, we do not know whether all states which wish to accede to one of the versions of anti-abuse provisions would also be required to accept these changes to articles 3 and 4. Indeed, nothing has been released publically about the format of

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<sup>1</sup> Proposed in the OECD Secretary-General's Report to the G20 Finance Ministers meeting in Shanghai, February 2016, which was accepted in their Communiqué.

the proposed multilateral convention, especially whether it will be ‘à la carte’ and allow states to decide which of its provisions to accept, or a package deal, or a combination. We have alluded to this issue in several of our previous submissions, and this has still not been clarified formally.

The proposals also raise wider questions about the future relationship between the OECD and UN model conventions. States which accept the invitation to join the Inclusive Framework will be participating in BEPS-related work which results in changes to the OECD model and its commentaries. In the case of measures which are regarded as minimum standards, such as these Action 6 proposals, they will be treated as committed to implement them. They may nevertheless wish to formulate reservations, for example to some of the proposed wording in the Commentaries. Would they be allowed, or indeed expected, to express such a reservation for inclusion in the OECD model?

The opening up of the Inclusive Framework therefore raises even more fundamental questions about the relationship between the OECD and UN models, and indeed the role of the UN Committee. That Committee will now also be represented in the Inclusive Framework, as well as being one of the organisations forming the Platform for Collaboration on Tax.

We urge that a policy paper should be issued for public discussion to explain how the proposed Multilateral Convention is intended to be structured, and exploring its implications for the future of the OECD and UN models, and their relationship.

#### SPECIFIC COMMENTS

### **3. Commentary on Articles 3 and 4 regarding the term “recognised pension fund”**

Proposed paragraph 10.5 of the commentary on Article 3 provides examples of “similar benefits” and paragraph 10.7 provides examples of entities and arrangements that would satisfy the definition of a “recognized pension fund”. To discourage treaty abuse, it would be useful to also provide relevant examples of payments or investments that do *not* qualify as “similar benefits” and of entities or arrangements that do *not* meet the definition of a “recognized pension fund”. Such examples may include benefits or entities that resemble a recognized pension fund set up for one individual, as investment structures with one individual beneficiary might be abused to obtain unintended treaty benefits, especially in case of an individual who is tax resident in more than one country.

Newly proposed paragraph 10.8 provides an example of why special status is needed for entities “constituted and operated exclusively to invest funds for the benefit of entities or arrangements referred to in subdivision i)”. This example makes good sense and we support this approach. We are concerned, though, that the broad language of newly proposed paragraph j)(ii) would appear to include a wider range of persons than is intended by this example. The broad language seems to extend for example to a normal “for profit” organization that provides services to a pension arrangement. No special status should be provided for such persons.

## Discussion draft on changes to the OECD Model Tax Convention concerning the treaty residence of pension funds

1 April 2016

### Introduction

The BBA welcomes the opportunity to make this written submission in response to the OECD discussion draft on “Changes to the OECD Model Tax Convention Concerning the Treaty Residence of Pension Funds” which was published on 29 February 2016.

The BBA is the leading trade association for the UK banking sector with 200 member banks headquartered in 50 countries, with operations in 180 jurisdictions worldwide. Eighty per cent of global systemically important banks are members of the BBA.

The International Custody Liaison Group at the BBA constitutes the largest custodian banks in Europe, who have a focus on securing the correct withholding tax on cross-border investments for investors, who include a substantial number of pension funds.

### Response

The discussion draft published on February 29, 2016 includes proposed changes to Articles 3 and 4 of the OECD Model Tax Convention and to the Commentary on these Articles. We have considered the proposed changes, and have the following comments to add:

***a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?***

We understand that these rules are intended to distinguish recognised pension funds that are entitled to treaty benefits from fiscally transparent entities that are not themselves persons and are not therefore entitled to treaty benefits in their own name. However, there are a number of cases where we believe the intention is for there to be access to treaty benefits which would not be permitted under this definition.

### Unit-linked pension funds

In the UK, a common structure is that defined contribution pension schemes are created as contractual arrangements with insurance companies. In this arrangement, the insurance company will recognise a segregated pool of assets on their balance sheet (known as a unit-linked pension fund) which are subject to a different tax regime to the normal assets of the insurance company, analogous to the taxation of UK pensions funds.

The unit linked pension fund is a Registered Pension Scheme for the purpose of applying UK tax rules, but it cannot be said to be a separate person. Typically, the insurance company will engage in other activities, and therefore a legal person based approach will deny treaty benefits to the pension fund.

### **Contractual trust arrangements**

Although the discussion draft specifically acknowledges contractual arrangements and pooling vehicles, in a similar manner to the above, the condition of being a separate legal person for tax purposes could result in certain contractual trust arrangements that are regarded as fiscally tax transparent entities in their home country from being excluded as they are not treated as separate persons.

UK Pension Fund Pooling Scheme (PFSP) and UK Common Investment Funds are established as unauthorised unit trust scheme, such that so the legal owner is not the fund itself but the trustee, and the beneficial owners of the funds' assets are the underlying investors. Again, the requirement to be treated as a separate person could restrict the availability of treaty benefits.

### **Suggested approach**

We would suggest that the language used might be amended to state a recognised pension fund "that is treated as a separate person **or as part of the business of a separate person** under the taxation laws of that State". We believe this would address the unit-linked pension fund issue and is also supported by the UK Investment Association.

In addition, we believe that the IRS' Explanatory Memorandum to the Competent Authority Agreement between the US and Germany, signed in 2012 provides a useful model for language which recognises the treatment of pensions created under contractual relationships.

***b) As regards the phrase "that is constituted and operated exclusively to administer or provide retirement or similar benefits" included in subdivision i) of the definition of "recognised pension fund" in proposed Art. 3(1) j): Is the word "exclusively" too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to "retirement benefits" but also to "similar benefits"?***

And

***c) As regards the phrase "similar benefits" included in subdivision i) of the definition of "recognised pension fund" in proposed Art. 3(1) j): Are there examples of "benefits" that are typically granted by pension funds that would not be covered by the phrase "similar benefits"? If yes, please describe these benefits?***

We feel "exclusively" could possibly be seen as too restrictive and use of "principally" would achieve the desired result without unintended consequences. Apart from this we have no particular concerns on the language given the inclusion of the phrase "similar benefits". We agree that it would be useful to include further examples of the term "similar benefits" within the commentary, which might include payments (periodic or lump sums) paid to an employee or his/her beneficiary/beneficiaries on retirement, on death, on having reached a particular age, on the on-set of serious ill-health or incapacity or other similar circumstances.

However, we would defer to national pension associations in defining this term.

***d) As regards the phrase "that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements" included in subdivision ii) of the definition of "recognised pension fund" in proposed Art. 3(1) j): Is the word "exclusively" too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?***

As noted in (a) above, it is common for life insurance companies to be involved in administering pension business and the availability of treaty benefits may come down to the way in which the life company arranges its businesses/subfunds. However, it is likely that in some circumstances a life company would not meet the definition as the "arrangement" would not be operated "exclusively to invest funds for the benefits of entities or arrangements" that are constituted and operated exclusively to administer or provide retirement or similar benefits to individuals.

This would limit UK Life Companies that have separate businesses from claiming the correct tax rate on behalf of their pension business, we would suggest that subparagraph j)(ii) could be amended as follows:

"(ii) that is constituted and operated **principally** to invest funds for the benefit of entities or arrangements referred to in subdivision i)."

### **Other issues/further comments**

We believe it would be desirable that any changes to the current rules for pensions to secure withholding tax relief should be accompanied by appropriate administrative guidance to facilitate the making of treaty relief claims.

At present, substantial time and effort is invested in ensuring that pension funds can receive income on cross-border investments at the correct rate of withholding tax. One of the principal blockers to securing that are the administrative provisions in host countries which make it difficult for pension funds to provide the correct documentation to local tax authorities.

If the changes above introduce uncertainty or further complication to the documentation requirements and administrative process, the practical result maybe that pensions are disadvantaged even where that is not the intent of the proposals.

Alternatively, we would encourage consideration of agreements governments have already concluded under the CRS and the FATCA IGAs, which give a great deal of thought to for example under the IGAs and in the OECDs commentary on the CRS clear definitions of 'what is a pension fund' have been set out with the primary aim to exclude such arrangements from themselves for having to comply with the due diligence and information reporting obligations imposed under the IGA and CRS respectively.

An obvious alignment would benefit plan operators, custodians and the source and residence country tax authorities when claims for a refund under an applicable treaty are made. With the ability to refer to agreed understandings of these type of entity it would presumably remove, or at least reduce, the need for the provision, by the pension fund, numerous ad-hoc documentation that we routinely see being requested by source country tax authorities.



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5 April 2016

Dear Sirs

**OECD Discuss Draft: Treaty residence of pension funds**

We refer to the Discussion Draft the OECD published on 29 February 2016 suggesting possible changes to Articles 3 and 4 of the OECD Model Tax Convention, and to the Commentary on these Articles, intended to ensure that a pension fund is considered to be a resident of the State in which it is constituted for the purposes of tax treaties. We understand that these changes are follow up work from the main BEPS project, reflecting the work on Action 6 of the BEPS Action Plan.

We support the objective of focussing treaty benefits by reference to the place of establishment of the fund and consider that the draft provision is helpful. However, the suggested definition of “recognised pension fund” appears to be too narrow. There are also wider implications that would need to be considered if the proposed changes were to be implemented.

**(1) Article 3 – new “recognised pension fund” definition**

The suggested definition of “*recognised pension fund*” appears to be too narrow. In particular, the following terms could be problematic.

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**“Established in that State”**

The term “**established in that State**” is not defined and could sometimes be unclear.

In particular, we are concerned that it may not necessarily apply to the pension plans of international organisations. We draw your attention to the debate this term caused in the *Macklin v HMRC* [2015] UKUT 0039 (TCC). In that case, the UK’s Upper Tribunal (Tax and Chancery Chamber) held that World Bank’s staff retirement plan (SRP) was ‘established’ in the USA for the purposes of the USA/UK Double Tax Treaty. In that case, the plan was run in accordance with US tax law on pensions but could not meet all the requirements to qualify as a US plan because of its special status.

The changes being proposed do not appear to assist in dealing with the points raised in *Macklin* at all. We suggest that it might be better to remove this requirement or at least include a definition of what “*established*” means?

Our concern is that if the changes are introduced as proposed, where the new definition appears in treaties pension schemes and their pensioners (such as the World Bank SRP in *Macklin*) may be the unintended victims of the change. Although such pension plans themselves may enjoy exemption in some cases under international law, any benefit to recipients of pension benefits may be dependent on tax treaties. Since treaties now deal with a variety of situations involving pensions such as cross-border contributions, the issue is of increasing importance.

**“Separate person”**

A country will not necessarily treat a pension scheme as a “*separate person*”, even where that country’s laws require that the scheme’s assets can only be used for the members’ benefits. Again, might it be better to remove this requirement?

**“Exclusively...provide retirement or similar benefits”**

Even a locally approved/regulated pension scheme may well not “**exclusively...provide retirement or similar benefits**” – for example, US qualified 401(k) plans provide loans and other “early withdrawal” benefits. Might it be better to use the words “**principally...provide retirement or similar benefits**”?

**(2) Article 4 – amended definition of “resident”****Caveat at the end of Article 4(1)**

Should it be made clear that the caveat at the end of Article 4(1) “*This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein*” will not apply to a recognised pension fund?

Otherwise, there might be circumstances where a *recognised pension fund* could be regarded as being liable to tax, but only in respect of locally sourced income or capital – and so would not be regarded as a “*resident*” by virtue of such caveat.

**Meaning of term “liable to tax”**

The words “**as well as a recognised pension fund**” seem to imply that a *recognised pension fund* would normally not be regarded as being “*liable*” to tax. However, this is contrary to the general view up to this point as is reflected in the existing OECD

Model Commentary, at para 8.6. And so, if a double tax treaty (DTT) itself is to suggest that a person who is not actually subject to tax is therefore not “*liable*” to tax, this could have significant implications for many individuals (e.g. individuals who have recently moved to a country and who, under that country’s laws, are exempted from taxation for a transitional period). The residency status of charities etc. might also be questioned.

We do not think this is a good idea. Indeed, we suggest the OECD should consider dealing with this point by making a generic change to Article 4 (without needing to refer to *recognised pension funds* at all) – for example, providing that a person who is liable to tax by reason of domicile, residence etc. or would be so liable but for any statutory exemption shall be treated as resident?

### **(3) Other comments**

If the proposed changes are made to Articles 3 and 4, they will “flow through” to many other DTT provisions, for example the dividends Article.

However, where any DTT is amended to reflect the revised model treaty, the precise implications and necessary consequential amendments will need to be carefully considered.

#### ***Pensions Article***

The proposed changes will not necessarily impact the DTT pensions Article. The pensions Article:

- a) may not refer to “pension schemes” at all; or
- b) may rely on an existing definition of “pension scheme” (either in the pensions Article or elsewhere in the DTT).

Is it the intention that the pensions Article should, for example, replace any existing definition of “pension scheme” with the new *recognised pension fund* definition? If so, the potential implications will need to be examined carefully.

We would ask that the Committee considers supplementing/amending the proposed changes to ensure that these unintended consequences would not arise.

Yours faithfully

Glyn Fullelove  
Chair of International Taxes

### **The Chartered Institute of Taxation**

The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it –



taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 17,500 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

To: Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CPTA



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## Public Discussion Draft - Treaty Residence of Pension Funds

### 1. Introduction

The Danish Insurance Association (DIA)<sup>1</sup> welcomes the opportunity to comment on OECD's Public Discussion Draft "Treaty Residence of Pension Funds".

The DIA fully supports the decision to insert a definition of "recognised pension fund" in the OECD Model Tax Convention.

We are, however, concerned that the proposed definition and supporting remarks might fail to also include all pension providers on the Danish market; namely the life insurance companies that are one of the main providers of occupational pension schemes in Denmark and therefore rightfully also should be covered by the definition.

In addition, we would like to ensure that all the typical elements of a typical Danish pension scheme will be included under "benefits" and "similar benefits".

Below, we have briefly outlined the company form of the DIA members that provide and offer pension schemes and products in Denmark along with a description of the typical pension products.

Next, we have commented on questions a) to d). The comments are inserted in the "Introduction" to the draft which follows below.

### 2. Pension providers

DIA member companies that provide and offer pension schemes and products include multi-employer pension funds and life insurance companies.

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<sup>1</sup> The Danish Insurance Association (DIA) is the trade association of Danish insurance companies and industry-wide pension funds. The majority of life insurance companies and industry-wide pension funds operating in the Danish market are members of the DIA. Most non-life insurance companies are members, as well. Link to DIA: <http://www.forsikringogpension.dk/english/Sider/forside.aspx>

01.04.2016

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Vores ref. TSC  
Sagsnr. GES-2015-00225  
DokID 369402

Brancheorganisation  
for forsikringsselskaber  
og pensionskasser

Multi-employer pension funds typically offers defined contribution pension schemes for employees of specific common educational background that are organised under the same collective agreement on the labour market.<sup>2</sup> These schemes fall under pillar II.

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Some life insurance companies only offer multi-employer pension schemes similar to the multi-employer pension funds while other life insurance companies offer different types of pension schemes, hereunder defined contribution pension products and pension schemes for employees of specific common educational background, but also single-employer pension schemes i.e. schemes that cover all employees with a single employer. These schemes also fall under pillar II. Some life insurance companies also offer individual pension products i.e. pension schemes that are not necessarily linked to an employment. These schemes fall under Pillar III.

Pillar II occupational pension schemes are almost always mandatory for the employees in Denmark and form a part of the total compensation package.

Individual Pillar III pension schemes are not that widespread in Denmark due to the fact that more than 90% of the active work force in Denmark has an occupational pension.

To put the above into perspective, multi-employer pension funds administer app. 20 % of the total pension assets related to Pillar I & II, while life insurance companies administer app. 60 % of the total pension assets related to Pillar I & II. Most of the remaining app. 20 % is placed in banks.

During the later years, we have seen an ongoing tendency to an increased regulation of the pension sector – e.g. Solvency II. The increased regulation has called for consolidation of the pension institutions in order to keep administrative costs to a minimum. This has among other things lead some life insurance companies to take over multi-employer pension funds.

### 3. Regulation

Danish multi-employer pension funds and life insurance companies are subject to the same set of regulation:

Multi-employer pension funds are thus regulated as life insurance, since Denmark has decided to have these providers included in the scope for of the European Life Insurance Directive.

The Danish common regulation for multi-employer pension funds and life insurance companies is implemented in the Danish Financial Business Act, which also implements Solvency II.

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<sup>2</sup> Danish multi-employer pension funds are also commonly referred to as "labour-market pension funds" – thus referring to the collective, labour market-agreements, on which they are based.

#### 4. The typical occupational pension scheme in Denmark

A pension scheme whether it is provided by a life insurance company or a multi-employer pension fund will typically contain the following elements:

- Old age pension – with a mix between:
  - Lifelong annuities
  - Term annuities
  - Lump sums
- Disability pension
- Pension for spouse and children in case of the scheme members' death
- Critical illness
- Health care insurance – though not as prevalent as the other elements

#### 5. Questions raised by WP 1 on Tax Conventions and Related Questions:

- a) As regards the phrase "that is treated as a separate person under the taxation laws of that State" included in the definition of "recognised pension fund" in proposed Art. 3(1) j):** Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?

##### **Answer to a):**

Yes - the phrase deals adequately with life insurance companies and multi-employer pension funds established in Denmark

- b) As regards the phrase "that is constituted and operated exclusively to administer or provide retirement or similar benefits" included in subdivision i) of the definition of "recognised pension fund" in proposed Art. 3(1) j):** Is the word "exclusively" too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to "retirement benefits" but also to "similar benefits"?

##### **Answer to b):**

In our view, the wording "exclusively" poses a small risk that the typical occupational pension scheme provided by life insurance companies as well as multi-employer pension funds in Denmark may contain elements which are not covered by the definition – in which case, the corresponding operations of the provider will not be encompassed by the proposed definition. The elements in question are discussed in section c)

Regarding other (possible) operations performed by Danish life insurance companies as well as multi-employer pension funds, the scope of such operations are regulated in the Danish Financial Business Act, thereby restricting them to be tightly connected to the provision of pension products. But in this case too,

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the wording "exclusively" may pose a small risk of such operations falling outside the definition.

Forsikring & Pension

In both cases, the wording "almost exclusively" would soften the definition sufficiently to remove this risk, albeit the risk is considered small.

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We propose this to be reflected in the third sentence of the commentary, section 10.5 to Article 3, as follows:

"It is important, however, that the entity or arrangement be constituted and used solely or almost solely for the purpose of administering or providing retirement or similar benefits to individuals".

- c) As regards the phrase "similar benefits" included in subdivision i) of the definition of "recognised pension fund" in proposed Art. 3(1) j):** Are there examples of "benefits" that are typically granted by pension funds that would not be covered by the phrase "similar benefits"? If yes, please describe these benefits?

**Answer to c):**

As mentioned in section b), the typical occupational scheme provided by life insurance companies as well as multi-employer pension funds in Denmark may contain elements not covered by the definition with full certainty.

Insurance covering sickness like "critical illness" and / or "health care insurance" are prevalently integrated elements in the typical occupational pension scheme in Denmark. Sickness is thus a classic biometric risk covered.

We propose the following wording of the last sentence of the commentary section 10.5 on Article 3, so that sickness is included in "similar benefits":

"Examples of other "similar benefits" would include payments made as a result of the death, sickness or invalidity of an individual, i.e. from biometric risk coverage."

- d) As regards the phrase "that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements" included in subdivision ii) of the definition of "recognised pension fund" in proposed Art. 3(1) j):** Is the word "exclusively" too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

**Answer to d):**

It is our opinion, that the proposed definition will cover the majority of Danish life insurance companies and multi-employer pension funds or some subgroup of these with the common purpose of providing pension benefits – on the assump-

Side 4

tion, of course, that life insurance companies as well as multi-employer pension funds falls under the proposed definition j) of paragraph 1 of Article 3.

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Some forms of ownership, for example common ownership by recognized pension funds from different countries, seem not to be covered by the definition.

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Also, investment entities with separate departments for pension funds and for other investors are not covered by the definition. This might pose problems for some investments by Danish life insurance companies and multi-employer pension funds.

We find it sufficient just to address these two problems, leaving it to WP 1 to judge whether it may be appropriate and possible to revise the definition in this respect.

**Some further comments:**

In Denmark, as in some other countries, life insurance companies are regulated the same way as pension funds and indeed provide the same pension schemes and products as the pension funds, cf. above.

Thus, it is very important to clarify explicitly that they in this role receive the same treatment and are also covered by the definition of "recognized pension fund" in the OECD Model Tax convention - to ensure a level playing field. If life insurance companies are not covered by the definition an essential part of the Danish workforce may be taxed more heavily than in other countries organized in a different way.

We thus suggest amending the commentary, section 10.4, to article 3, as follows:

"10.4 The first part of the definition refers to "an entity or arrangement established in that State". There is considerable diversity in the legal and organisational characteristics of pension funds around the world and it is therefore necessary to adopt a broad formulation. For example, in some countries it is very widespread that both occupational and individual personal pensions are provided by life insurance companies as well as by single- and multi-employer pension funds." [...]

Furthermore, we suggest that the considerable administrative burden of obtaining certainty of whether or not a pension fund is covered by the different states' interpretation of the new definition "recognised pension fund" would be alleviated by having the term "recognised pension fund" automatically comprise pension funds which are subject to national regulation for pension funds and national supervision as such.

Sincerely,  
Torsten Schiøler  
Senior Consultant, Msc. Econ.  
Taxation, DIA

Side 5

Tax Treaties, Transfer Pricing and Financial Transactions Division,  
Centre for Tax Policy and Administration  
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By e-mail: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

24 March 2016

Our Ref: WJID/LS

Dear Sir/Madam

## **Treaty Residence of Pension Funds: Public Discussion Draft**

Thank you for the opportunity to comment on the Treaty Residence of Pension Funds: Public Discussion Draft published on 29 February 2016 (the 'Discussion Draft'). Our comments are made from the perspective of the UK.

We have set out our responses to the questions raised in the Discussion Draft in the appendix to this letter. In general, we consider that the draft changes to the OECD Model Tax Convention and associated Commentary will operate as intended to ensure that a pension fund is considered to be a resident of the State in which it is constituted for the purposes of tax treaties. There may be a question as to the treatment of UK life insurance companies under the OECD Model Tax Convention as a result of activities undertaken alongside the pensions business and we have included further comments below.

If you would like to discuss this point further please do not hesitate to contact me ([bdodwell@deloitte.co.uk](mailto:bdodwell@deloitte.co.uk)).

Yours faithfully



**WJI Dodwell**  
**Deloitte LLP**

## Appendix 1 – Responses to questions raised in the Discussion Draft

- a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?**

Pension funds established in the UK are treated as a separate person for tax purposes.

There are examples of pension arrangements that may not be legally separate.

Employees of regional authorities are generally eligible to join defined benefit pension schemes. The assets and liabilities of these local government pension schemes (LGPS) typically form part of the local authority’s balance sheet and may not be held as a separate trust arrangement. Where this is the case, the LGPS is treated separately for tax purposes. An LGPS should therefore qualify as a recognised pension fund under the proposed wording. It would be helpful to have confirmation of this point in the Commentary.

A UK life insurance company is typically a UK incorporated company which writes both pension business and life assurance business (such as protection or permanent health business). Pension business is defined in Section 57 Finance Act 2012 as “the effecting or carrying out of contracts entered into for the purposes of a registered pension scheme [or the re-insurance of such business]”.

As a company incorporated in the UK, a UK life insurance company is a separate legal person. A UK life insurance company will be subject to the life insurance tax regime in the UK, however there are separate tax rules for each category of business undertaken by the UK life insurance company. The pension business is one of these categories and it is not clear whether that business is a separate person for tax purposes. See our further comments below in respect to question d.

- b) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?**

No- the word exclusively should not be too restrictive for the UK.

- c) As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j): Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?**

No- In addition to retirement benefits, the most common additional benefits in the UK are death in service or similar benefits which are specifically referred to in the Commentary as a ‘similar benefit’.

- d) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?**

Common intermediaries in the UK include Common Investment Funds (‘CIFs’) and UK life insurance companies which write pension business.

CIFs typically operate exclusively to invest funds for the benefit of entities or arrangements such that they should qualify under the definition of ‘recognised pension fund’. In some countries a CIF may be viewed as tax transparent such that it would be necessary to consider the treaty status of the investing pension funds rather than the CIF itself.



When considering a UK life insurance company, the word 'exclusively' may be too restrictive as many UK life insurance companies carry on business other than the management of pension fund assets, including issuing life insurance, health policies, etc. In some cases, non-UK pension funds may invest in these vehicles.

A UK life insurance company is typically a UK incorporated and tax resident company such that it should be eligible for treaty relief in its own right. A number of UK treaties include clauses within the articles and/or protocols to the treaty which seek to treat a UK life insurance company as a pension fund with respect to its pension investments, irrespective of the fact it might not meet the definition of a pension fund otherwise. As a consequence, the UK life insurance company may be entitled to a lower dividend withholding tax rate. The protocol to the UK-US treaty includes a clause to this effect (See <http://www.hmrc.gov.uk/manuals/dtmanual/dt19939zd.htm>)



## EMPLOYEES PROVIDENT FUND

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31 March 2016

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## **The Malaysia Employees Provident Fund's comments to the proposed changes to the OECD Model Tax Convention concerning the treaty residence of pension funds.**

### Introduction

The Malaysia Employees Provident Fund ("the EPF") welcomes the opportunity to comment on the definition of "recognized pension fund" which the OECD proposes to insert into the OECD Model Tax Convention. In addition, the EPF welcomes the OECD's moves to enable pension funds to access the benefit of tax treaties by treating them as a resident of the state in which they are constituted under the OECD Model Tax Convention.

The EPF is a defined contribution fund which is established and regulated by the laws of Malaysia<sup>1</sup>. The EPF's sole purpose is to provide retirement benefits for employees in Malaysia. According to rankings compiled by Towers Watson, the global authority on pension fund rankings, EPF is the seventh largest state pension fund in the world with US\$184 billion worth of assets under management, and the 13th biggest pension fund generally.<sup>2</sup> The EPF is a global investor: the book value of its offshore investments as at the end of 2014 being RM145.29 billion (approximately USD 41.48 billion)<sup>3</sup>.

As will be explained below, the EPF's model differs from typical pension funds as members are able to withdraw a portion of their savings prior to reaching Malaysia's statutory retirement age (55 years) to finance certain specified purposes. This model is aimed at improving members' financial position and earning capacity to enable them to adequately prepare for retirement.

### Executive summary

Given the EPF's model and its global investment footprint, we have engaged in the OECD consultation process to ensure that any concept of "recognised pension fund" included in the OECD Model Convention is drafted in sufficiently broad terms to encompass EPF's operating model.

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<sup>1</sup> [Employees Provident Fund Act 1991 \(Act 452\)](#) ("the EPF Act")

<sup>2</sup> Towers Watson: P&I / TW 300 analysis year ended 2014: September 2015.

<sup>3</sup> EPF Annual Report 2014, page 48

[http://www.kwsp.gov.my/portal/documents/10180/5382689/4.OUR\\_BUSINESS\\_REVIEW\\_BY\\_DIVISIONS.pdf](http://www.kwsp.gov.my/portal/documents/10180/5382689/4.OUR_BUSINESS_REVIEW_BY_DIVISIONS.pdf)

The current proposed definition of “recognised pension fund” in proposed Article 3(1)(j), which requires that the fund “is constituted and operated *exclusively* to administer or provide retirement or similar benefits”, may not encompass EPF if “retirement benefits” are construed narrowly to only include the payment of pensions to members, as appears to be contemplated in paragraph 10.5 of the proposed amendments to the OECD’s Model Commentary.

Therefore, our submission is focused on ensuring that the OECD’s conception of “recognized pension fund” is sufficiently broad to encompass funds which achieve their aim of helping members prepare financially for retirement by means other than simply providing for pensions upon a member attaining retirement age.

As such, the focus of our submission is on the second question in the OECD’s consultation paper: whether the concept of a pension fund provided in proposed Article 3(1)(j) of the OECD Model Tax Convention, being a fund “that is constituted and operated exclusively to administer or provide retirement or similar benefits”, adequately covers EPF. In particular, we suggest the following amendments to the proposed definition of “recognised pension fund” to be inserted as Article 3(1)(j) and the accompanying model commentary:

- 1 The definition of “recognised pension fund” be amended by removing the reference to “exclusively to administer retirement or similar benefits” and be replaced with a reference to “primarily to administer retirement or similar benefits”.
- 2 Alternatively, paragraph 10.5 of the proposed OECD Model Commentary should be amended to make it clear that retirement benefits should be construed widely to not only constitute the provision of a pension upon retirement. In this way, the EFP recommends that the Commentary should also encompass other measures designed to enable members to improve their asset position and earning capacity during the period to their retirement, as is permitted under the EPF Act.

## Background to EPF

As is explained in further detail below, EPF is a defined contribution fund under which each member is allocated two accounts. Contributions are credited into these accounting in according to the following percentages:

1. Account I - 70% of monthly contribution
2. Account II- 30% of monthly contribution

Account I cannot be withdrawn unless the member either:

- Reaches the Malaysian statutory retirement age of fifty five;
- Becomes incapacitated;
- Permanently leaves the country; or
- Dies.

Account II was established in 2007 as part of the Malaysian government’s push to ensure its citizens have sufficient savings to support their retirement. Account II is aimed at assisting members to prepare for retirement and “enhancing the value of life after retirement.”<sup>4</sup> Subject to

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<sup>4</sup> Document prepared by EPF for members entitled “Are your retirement savings sufficient”? Page 8. This document can be accessed at [http://www.kwsp.gov.my/portal/documents/10180/4459038/BOOK\\_-\\_EPF\\_Saving\\_and\\_Your\\_Retirement\\_\\_CS5\\_.pdf](http://www.kwsp.gov.my/portal/documents/10180/4459038/BOOK_-_EPF_Saving_and_Your_Retirement__CS5_.pdf)

the prior approval from EPF, withdrawals from Account II are allowed on application to EPF only for specific purposes/reasons aimed at enhancing a member's future earning potential to ensure they are adequately prepared for retirement (these purposes are explained in more detail below).

The EPF does provide retirement incomes directly to its members under Account I and is subject to specific regulation by the Malaysian government as a provider of retirement benefits. However, the ability for members to withdraw from their Account II entitlement prior to retirement for certain specified purposes may cause the EPF to not satisfy the requirement in proposed Article 3(1)(j) (based upon proposed paragraphs 10.5 to 10.7 to be inserted into the OECD Model Convention Commentary) if the concept of "retirement or similar benefits" are construed to only encompass the payment of pensions. Therefore, the EPF requests that the OECD clarify this position in the OECD Model Convention and Commentary to ensure a pension fund which is established and governed by the laws of a state such as EPF is covered by the concept of a "recognised pension fund".

OECD consultation question (b)

***As regards the phrase "is constituted and operated exclusively to administer or provide retirement or similar benefits" in the definition of "recognised pension fund":*** Is the word "exclusively" too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to "retirement benefits" but also to "similar benefits"?

EPF comments

We are of the opinion that the word "exclusively" is too restrictive and may not adequately accommodate funds which are established and regulated under appropriate laws of the state in which they were established, with the explicit intention of enabling members to prepare for retirement, but which achieve this purpose in a manner different to typical pension funds.

Therefore, we recommend that the word "exclusively" be replaced with "primarily", in order to ensure that if the term "retirement or similar benefits" is construed as only including the payment of pensions to members at retirement, the EPF's additional method of helping its members prepare for retirement via pre-retirement withdrawals from Account II do not prevent the EPF from obtaining the benefit of the proposed amendments to the OECD Model Tax Convention.

This is consistent with EPF's clearly defined role as a fund which provides for its members' retirement, and would ensure that the EPF is not excluded from accessing the OECD Model Tax Convention due to a technicality in the definition of "recognised pension fund".

In addition, this suggestion is consistent with consultation currently taking place in the United States regarding the definition of a 'qualified foreign pension fund' in the *Protecting Americans from Tax Hikes Act* ("the PATH Act"). Similar to the proposed definition of "recognised pension fund" in the OECD Model Convention, the original definition of 'qualified foreign pension fund' in the PATH Act was felt to be too narrowly drawn and potentially prevented a number of foreign pension funds from accessing the benefits of the PATH Act due to the specific features of the foreign pension funds. As such, one of the technical corrections proposed in consultation on the PATH Act is to insert a "primarily"- based test into the definition of 'qualified foreign pension fund', such that the definition covers an entity which was established "primarily" to provide retirement or pension benefits". Given the experience in the US context of the difficulties that arise from a narrowly-drawn definition of "pension fund", we propose that the OECD adopt a



similar “primarily”-based concept of “recognised pension fund” to ensure the specific features of the EPF and other significant pension funds does not prevent them from accessing the benefits of the OECD Model Convention.

### The EPF Act – explanation of the nature of the EPF

The preamble to the EPF Act makes it clear that the EPF is established for the purpose of providing retirement income for their members and states that it is:

*An Act to provide for the law relating to a scheme of savings for employees' retirement and the management of the savings for retirement purposes and for matters incidental thereto<sup>5</sup>.*

Pursuant to the EPF Act, all persons who meet the definition of an “employee” and “employer” under the EPF Act are required to pay monthly contributions of a statutorily prescribed percentage of monthly wages to EPF. Under this model, monthly mandatory contributions are collected from employees until retirement. These contributions, together with declared dividends on these contributions, can be withdrawn upon members reaching the Malaysian statutory mandatory retirement age of 55 years.

Based on the above, the EPF falls within the standard conception of a pension fund, as its aims and methods are consistent with a fund established to assist members save for their retirement. Furthermore, its enabling legislation (the EPF Act), makes it clear that it is established and regulated for the sole purpose of assisting members to prepare for retirement.

### Account II entitlements

However, unlike typical pension funds, members are able to make withdrawals from Account II for the purposes outlined below before reaching the Malaysian statutory retirement age. As mentioned in the Background section, the reason for allowing members to make these withdrawals is to enable them to prepare for their retirement and enhance their future asset position / earning potential to ensure they are financially prepared for retirement. This aim is reflected in EPF's 2013 annual report in which it was stated:

*Our ultimate objective is to ensure members have sufficient savings to see them through their retirement. At the same time, we believe that certain pre-retirement investments, such as health, education and housing, add quality to our members' golden years. Hence, EPF is structured into two accounts, one of which can be used for various life-enhancing purposes, while the other can only be withdrawn when a member reaches age 55<sup>6</sup>.*

In addition to providing typical retirement benefits such as a pension or lump sum upon reaching retirement age, the EPF also allows members to make withdrawals from Account II (i.e. the 30% contributions from contributors) strictly for the following purposes:

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<sup>5</sup> Employees Provident Fund Act 1991 < <http://www.kwsp.gov.my/portal/en/web/kwsp/about-epf/epf-act/epf-act-reports#intro> >

<sup>6</sup> EPF Annual Report 2013, page 113 (“Operational Performance”).

- To aid contributors in preparing for retirement. Withdrawal for this purpose is allowable for contributors who attain the age of 50 years old, and before reaching the mandatory retirement age of 55 years old.
- As down payment for purchase of first house.
- To reduce or redeem housing loan.
- To finance education for self and/or children.
- To finance medical expenses for critical illnesses or purchase medical equipment for self and/or allowable family members.
- To finance contributors expenses whilst performing the Hajj.

The integrity of the EPF's mission is enhanced by a pre-approval process for withdrawing amounts from Account II, and strict penalties (including potential imprisonment) for withdrawals from Account II for purposes other than those listed above.

The EPF also allows contributors to invest not more than 20% of their Account I balance with appointed fund management institutions approved by the Malaysia's Ministry of Finance. These funds should never be released to the contributors before the mandatory retirement age of 55 years old. Should the contributors decide to terminate the fund management services, the funds (together with interests earned) must be returned to the EPF.

Withdrawal from Account I balance is allowable strictly upon contributors attaining the mandatory retirement age of 55 years old.

The EPF's status as a pension fund

The EPF's model has been specifically adopted by the Government of Malaysia to enable members to prepare for retirement in the context of a rapidly developing economy with an ageing population. Furthermore, as mentioned in the Background section, EPF is considered by respected observers of the pension fund industry to be one of the largest pension funds in the world. Towers Watson, which is reputed as the global authority on pension classification and ranking, ranked EPF as the 7th largest sovereign pension fund in the world in the *Pensions & Investments/Towers Watson 300 Analysis* for the year ended 30 June 2014<sup>7</sup>. We note that the *Pensions & Investments/Towers Watson 300* only covers entities which meet an accepted industry definition, being funds "established by national authorities for the meeting of pension liabilities".

In addition, we note that Mercer has published a study entitled "Pension Design and Marketing – the Annuity Malaysia Experience"<sup>8</sup> in which it discusses schemes that were established by EPF to allow members to diversify their investments and thus increase their pool of retirement savings by utilising some of their EPF savings to acquire specific annuity schemes. The premise of the Mercer study is that EPF is a typical pension fund which is dealing with a common social and economic phenomenon in developing countries, namely, increasing life expectancy and how traditional pension schemes can continue to provide benefits after retirement given the contributions to the fund would likely be insufficient to cover the anticipated life expectancy.

In this report, Mercer briefly considered the ability to withdraw from Account II and noted these "early withdrawal schemes were basically 'life cycle benefits'". To this end, it is clear Mercer did not consider the ability to withdraw amounts from Account II to compromise the overall characterisation of EPF as a pension fund. As will be discussed in this ruling request, it is important to ensure that one does not place undue focus on the ability to draw upon Account II,

<sup>7</sup> For further information, please see Towers Watson: P&I / TW 300 analysis: Year End 2014.

<sup>8</sup> For further information, please see: <http://www.oecd.org/finance/financial-markets/2638128.pdf>

when one considers the overall nature of EPF as clearly being a pension fund which is recognised as such by leading industry observers.

Concerns with the existing definition of “recognised pension fund”

Notwithstanding the above, whilst the EPF is clearly established and regulated under laws of Malaysia exclusively for the purpose of providing or administering retirement benefits (and thus satisfies the majority of the requirements set out in paragraph 10.5 of the OECD’s proposed commentary on the definition of “recognised pension fund”), the ability of EPF’s members to make withdrawals from Account II could prevent EPF from satisfying the definition of “recognised pension fund” if the OECD defines the concept of “retirement or similar benefits” narrowly to only include the payment of pensions or disability / death benefits.

Paragraph 10.5 of the draft commentary which is proposed in the Discussion Draft states that a pension paid upon retirement from active employment would be the typical example of a “retirement benefit”. The draft commentary then goes on to say that examples of other “similar benefits” would include payments made as a result of the death or invalidity of the individual.

As mentioned above, whilst EPF is clearly constituted solely to manage retirement benefits for its members, it achieves this objective through methods other than simply providing for pensions and death / disability benefits to its members after retirement. As such, if the provision of pensions once a member reaches retirement age, or the provision of death and disability benefits upon a member dying is the sole criterion for “retirement benefits or similar benefits”, then EPF would not be taken to be “exclusively” providing “retirement or similar benefits”.

Therefore, we suggest that the use of the word “exclusively” in proposed Article 3(1)(j) is too restrictive. As a result, we suggest that the OECD replace “exclusively” with “primarily”, as this would ensure that the EPF would not fall foul of these provisions, due to the particular way in which it provides retirement benefits.

Alternatively, we would recommend the OECD Model Commentary adopts a broader conception of “retirement or similar benefits” which covers all benefits provided during a member’s working life that are directed at improving the member’s financial position after retirement. Whilst we are happy to work with the OECD in drafting this wording, we would expect the additional commentary would make reference to the role of the entity under local social security and pensions laws, rather than specifically referencing the benefits to be paid to members under the scheme, to determine whether an entity is a “recognised pension fund”. To this end, we would suggest an explanation of the concept of “recognised pension fund” in the OECD Model Commentary to the following effect:

*“An entity must be established under the laws of a Contracting State relating to the provision of retirement benefits as an entity whose sole object is to help members prepare for retirement”.*

In our view, this would adequately encompass entities such as the EPF which have been established and regulated under specific pensions / social security laws whose objects are clearly geared towards assisting their members prepare financially for their retirement, and would cover entities regardless of how they achieve this object.

**As regards the phrase “similar benefits” included in the definition of “recognised pension fund”:** Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?

#### EPF comments

As mentioned above, the EPF provides a clear example of benefits granted by pension funds that would arguably not be covered by the phrase “similar benefits”. That is, EPF enables members to save for their retirements by using a portion of their savings to acquire a residence, pay for either their own education or the education of their immediate family, or other similar purposes aimed at increasing members’ earning potential / net wealth.

The intention of EPF’s model is to reduce the financial burden on the Government of Malaysia from a rapidly aging population and enable contributors to enhance their earning potential to support their income in retirement.

In addition to its sole purpose of providing a pension upon retirement from active employment, the EPF also provide other related services which entail allowable withdrawals from contributors’ Account 2 strictly for the following general purposes:

- To aid contributors is preparing for retirement. Withdrawal for this purpose is allowable for contributors who attain the age of 50 years old, and before reaching the mandatory retirement age of 55 years old.
- As down payment for purchase of first house.
- To reduce or redeem housing loan.
- To finance education for self and/or children.
- To finance medical expenses for critical illnesses or purchase medical equipment for self and/or allowable family members.
- To finance contributors expenses whilst performing the Hajj.

The EPF also allows contributors to invest not more than 20% of Account 1 balance with appointed fund management institutions approved by the Malaysia’s Ministry of Finance. This funds should never be released to the contributors before the mandatory retirement age of 55 years old. Should the contributors decide to terminate the fund management services, the funds (together with interests earned) must be returned to the EPF.

Therefore, as mentioned above, we recommend that the OECD Model Commentary be expanded to make it clear that “life cycle” benefits granted to members during their employment, which are strictly regulated and solely aimed at improving members’ asset position and earning capacity so as to improve their financial position at retirement, should be included in the concept of “similar benefits”.



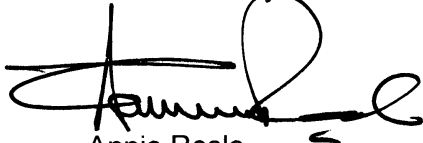
OECD question (d)

**As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” in the definition of “recognised pension fund”:** Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

EPF comments

Depending on the recognition of the EPF as a pension fund pursuant to questions (b) and (c) above, we are of the opinion that the word “exclusively” should not be a concern as all investments made (and therefore, returns generated) by the EPF whether through another funds, subsidiaries or special purpose vehicles will solely be for its purpose of providing retirement benefit to its contributors and other related services highlighted in response to question (c) above.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Annie Rosle', with a large loop at the end.

Annie Rosle  
Senior Manager  
Employees Provident Fund

Dear Sir/Madam,

Please find hereafter a few comments from the French Banking Federation (FBF) regarding the discussion draft on treaty residence of pension funds.

If the objective of the proposed changes are to allow pension funds not liable to tax to be considered as residents for the purposes of the model tax convention, it would be preferable to modify the way the paragraph is articulated :

In order to avoid diverging interpretations, including by local tax administrations, we believe it would be best to separate point 1 into 2 distinct paragraphs :

*Replace paragraph 1 of Article 4 of the OECD Model Tax Convention by the following:*

1. For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.  
The term “resident of a Contracting State” also includes that State and any political subdivision or local authority thereof *as well as a recognised pension fund of that State*.

Regarding the expression “that is treated as a separate person under the taxation laws of that State” (modification of article 3 paragraph 1), this may be interpreted by certain tax administrations as a condition imposing an effective taxation of the entity.

Regarding the expression “recognized pension funds”, it will be very difficult for paying agents / custodians to see whether such a condition is met. Further clarification rules / guidance will be needed in addition to the provisions of the OECD Model Treaty.

Finally, in paragraph 8.7. of the commentary, we believe the reference to « pension funds » should be kept. Pension funds may be residents :

- Either by virtue of the general clause « liable to tax » (and it is sufficient to be exempted by way of conditions of tax law in the state of residence in order to be considered as « resident »)
- Or by virtue of the specific provision « recognised pension fund ».

To delete the first option would worsen the situation for « non-recognised pension funds ».

Please do not hesitate to contact us.

Best regards,

**Blandine Leporcq**  
Directrice de Département  
Fiscalité  
Affaires Bancaires et Financières, Europe et International



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Dear Sir/Madam,

On behalf of the Federation of the Dutch Pension Funds we would like to share our point of view and to propose amendments with regard to the OECD Model Tax Convention, and in response to the public discussion draft on the Treaty Residence of Pension Funds, of 29 February 2016.

### **Background**

On behalf of approximately 250 pension funds, the Federation of the Dutch Pension Funds promotes the pension interests of 5.8 million participants, 2.7 million pensioners and 8.6 million early leavers. About 85% of the total number of Dutch employees is participant of a pension fund which is associated with the Federation of the Dutch Pension Funds. The Dutch pension funds together manage approximately 1200 billion euro of assets.

### **Our point of view**

We appreciate that the OECD committee on Fiscal Affairs provides us this opportunity to give our point of view regarding the Treaty Residence of Pension funds. Before we answer the submitted questions in the Public Discussion Draft, we want to explicitly express our support for the OECD's objective to provide a definition of 'pension funds'. This ensures that the main types of pension funds are covered by one definition, regardless of whether or not a pension fund is subject or liable to tax in its own state. Our answers to the submitted questions are stated below:

### **Our specific answers to the questions in the discussion draft**

- a.) The phrase 'that is treated as a separate person under the taxation laws of that State' does not pose a problem for the pension funds established in The Netherlands.

- b.) In the phrase ‘that is constituted and operated exclusively to administer or provide retirement or similar benefits’ the use of the word ‘exclusively’ is too restrictive for the Dutch situation. We would suggest the phrase ‘*(almost) exclusively*’ instead of the phrase ‘*exclusively*’.
- c.) In the Dutch context, pension funds carry out the pension arrangement made by employers and trade unions. Within these arrangements, a broad variety of possible benefits may be provided, but should contain at least old age-pension, survivors’ pension, and disability pension.
- d.) In the phrase ‘that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements’ the use of the word ‘exclusively’ is too restrictive for the Dutch situation. We would suggest the phrase ‘*(almost) exclusively*’ instead of the phrase ‘*exclusively*’ in article 3, paragraph 1, subparagraph j) under (ii) of the Model Tax Convention, as to ensure that an intermediary would also be allowed to invest funds of pension funds that are a resident in other contracting states. In our opinion, this would not be allowed if the use of the word ‘exclusively’ is not extended to ‘(almost) exclusively’.

The Federation also subscribes to the response of an informal coalition of global pension funds, of which the Dutch pension service providers APG and PGGM are co-signatories.

Please do not hesitate to contact us if you have any questions or we can be of further assistance.

Sincerely,



Gerard Riemen  
Managing Director  
Federation of the Dutch Pension Funds

A	Tax treaties, Transfer Pricing and Financial transactions Division OECD/CTPA	Date	1 April 2016
De	Laurent Leclercq, FIDAL Séverine Lauratet, FIDAL	Réf.	OECD_Residence of Pension Funds
Copie à	Charlotte Delsol, FIDAL Cédric Philibert, FIDAL		

## **Discussion Draft on Changes to OECD Model Tax Convention Concerning the Treaty Residence of Pension Funds**

*1 April 2016*

We thank the OECD for inviting stakeholders to share their views on the decisive issue of pension funds' treaty residence. Hereafter you will find our analysis of the proposed changes to Articles 3 and 4 of the OECD Model Tax Convention. We take this opportunity to make a few comments on certain practical aspects of the definition provided for in Article 3 and on the conditions attached to the LOB rule as such.

### **I. Insertion of 'recognised pension funds' in Article 4 - Residence**

We welcome the OECD's work to 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"*.

This statement asserts the clear separation of the notion of pension funds' residence from their exemption from taxation.

The insertion of 'recognised pension funds' in paragraph 1 of Article 4 of the OECD Model Tax Convention well ensures that pension funds are treated as residents in the State where they are constituted even though they are exempt from taxation.

**When France acts as the source country** and considering the French administrative Supreme Court's recent case law as regards foreign pension funds' residence, this clarification would be highly welcomed. In a recent case (*Santander Pensiones SA EGFP*, 9 November 2015 n° 371132), the French administrative Supreme Court held that pension funds that are exempt from taxation in their State of residence are not *liable to tax* under bilateral tax conventions and are therefore not deemed to be resident of that State unless otherwise stated in the relevant tax treaty.

Assuming that France incorporates the proposed changes to Article 4 of the OECD Model Tax Convention in its bilateral tax conventions, the issue of the treaty residence of pension funds would thus be clarified and we hope that it will put an end to misleading contagious effects.

**When France acts as the residence country**, the proposed amendments may raise some difficulties of interpretation since France does not have “pension funds” as such. Indeed, undertakings established in France qualified as non-profit organizations (i) whose corporate purpose are to pay retirement pensions (ii) whose management are disinterested and (iii) whose non-profit activities are “significantly predominant” are called “*caisses de retraites*”. They are similar to pension funds to a large extent but not identical. As from 2010, the French “*caisses de retraites*” are subject to a 15% CIT rate on dividends they receive (either from French companies or from foreign ones) and then are normally entitled to request the benefit of the treaty provisions on said income.

By contrast they are exempt from corporate income on the interest they receive. The intended amendments would lead to extend the benefit of the tax treaty provisions and especially to the reduced rates of withholding taxes (0% in the model treaty) on inbound interest. It should also have positive effects as far as capital gains are concerned since the according to the model treaty, the entitlement to tax capital gains on shareholdings other than substantial shareholdings is limited to the State of residence and “*caisses de retraites*” are tax exempt upon capital gains.

In view of the foregoing, we would suggest to refer to the notion of “recognised pension funds or similar entities” in order to cover also specific bodies like French “*caisses de retraites*”.

## II. Definition of ‘recognised pension funds’ in Article 3

### 1. Comments on the proposed definition

**Question a)** does not call for specific comments on our part for paragraph i) because the French “*caisses de retraites*” are considered as separate person. However for paragraph ii), funds of pension funds or pooling of pension funds may be French FCPs (“*fonds commun de placement*”), whose activities consist of managing collective securities portfolios on behalf of their investors. French FCPs have no legal personality and are outside the scope of corporate income tax. The French tax administration has affirmed this fact in these terms: “*even though their fiscal, legislative and regulatory status does not provide any specific guidance on this point, it is nonetheless self-evident that FCPs are not subject to corporate income tax*”<sup>1</sup>. Strictly speaking, French FCPs are not tax transparent either. In such a context, the term “*treated as a separate person under the taxation of laws of the State*” would lead to discussions from a French perspective.

**On question b)**, we favour a definition that leaves some space for profitable activities. French “*caisses de retraites*”, i.e. non-profit organisations that provide retirement benefits, are deemed to be non-profit organisations if they mainly serve a non-profit purpose. Therefore it would be preferable to leave the expression “exclusively or almost exclusively” in the proposed changes to Article 3 of the OECD Model Tax Convention.

**Question c)** does not call for specific comments on our part.

**On question d)** concerning funds of pension funds, Article 10 2-d iii) provides that those entities can benefit from the articles of the convention “provided that substantially all the income of that person is derived from investments made for the benefits of these persons”. The proposed definition of ‘recognised pension funds’ should not contradict the LOB rule as such. The term substantially would have to be clearly defined to avoid interpretation and discussions for qualification.

<sup>1</sup> Adm. D. 4 K-1712 nos. 2, 5 and 6, 1 November 1995

## 2. Analysis of France's current position re pension funds : an EU law perspective

The French tax authorities' position as regards pension funds in the context of EU law highlights one aspect that could prove to be problematic for recognised pension funds from the source country perspective.

Indeed, the French administrative Supreme Court held in 2009 that, under EU law, a pension fund located in an EU/EEA State that receives dividends from a company located in France cannot be treated worse than a "*caisse de retraites*" which is based in France (*Stichting Unilever Pensioenfond*s, 13 February 2009 n°298108).

In order not to discriminate foreign pension funds located in the EU/EEA, France – as a State of source – should not apply withholding taxes on dividends paid by French companies to EU/EEA-based pension funds similar to a "*caisse de retraites*" up to 2009 or should limit the withholding tax to 15% as from 2010.

However, in order to benefit from the same regime, foreign pension funds located in the EU/EEA must demonstrate to French tax authorities that they have similar characteristics to those of domestic "*caisse de retraites*". Given the diversity of foreign pension funds, it is difficult and burdensome in practice to bring evidence of such similarity.

Confronted with the obligation to grant pension funds located in the other Contracting State the benefits of the bilateral tax convention, the French tax authorities may not recognise foreign pension funds under bilateral tax conventions.

Hopefully, the qualification as a "*recognised pension fund*" is dependent upon the Contracting State in which the pension fund is constituted and not upon the source country. Even if these circumstances, the implementation of the LOB rule for pension funds may raise practical issues.

## 3. Practical implementation of the LOB rule for pension funds

We are concerned about the level of complexity attached to Article X 2-d ii).

The conditions applicable to Article X 2-d ii) in order to benefit from the convention seem to be very difficult to apply in practice.

To apply the convention where the beneficial interests in a pension fund are owned by individuals which are resident in a third State, the tax authorities of the State from which the benefits of the Convention are claimed would have to be informed that those individuals are "entitled to the benefits of a comprehensive convention for the avoidance of double taxation" between their State of residence and the State from which the benefits of the convention are claimed.

Moreover, in order to apply Articles 10 and 11 of the bilateral tax convention, the tax authorities would also have to verify that the pension fund would be entitled, if it were located in that third State, to a tax rate at least as low as the tax rate applicable between the State where it is constituted and the State from which the benefits of the convention are claimed.

Pension funds will indirectly suffer from such requirements. They will have to prove that the individuals that own beneficial interests in them are entitled to the benefits of a convention for the avoidance of double taxation between their State of residence and the State from which the benefits of the convention are claimed. If in practice the majority of pension funds are set up to the benefit of individuals who for most of them are residents in the same country as the one where the fund is established, more and more pension funds are set up to the benefit of group of companies in order to harmonize the benefits paid to the people moving from one entity to the other. Would it not be

preferable to mention that the source State is entitled to refuse the application of the treaty benefits to a recognised pension fund in case of abusive situations?

In the case of dividends and interest payments, they will also have to prove that, were they located in that third State, the tax rate applicable to such payments made to them by a company located in the State from which the benefits of the convention are claimed would be at least as low as the tax rates applicable between the State where they are constituted and the State from which the benefits of the convention are claimed.

In addition, changes happen between the individual owning beneficial interest in the recognised pension fund at the time of the payment income for which the benefit of the tax treaty is required and the time when the pensions will be allocated.

We remain at your entire disposal.

Best regards





**DELIVERED BY ELECTRONIC MAIL**

taxtreaties@oecd.org  
Tax Treaties, Transfer Pricing and Financial Transactions Division  
Centre for Tax Policy and Administration  
Organisation for Economic Co-operation and Development  
Paris, France

April 1, 2016

Dear sir/madam,

With this letter, the parties signed below are responding to the OECD's invitation to provide comments with respect to the discussion draft on changes to the OECD Model Tax Convention (the "**Model Tax Convention**") concerning the treaty residence of pension funds (the "**discussion draft**"), released on February 29, 2016.

This letter is prepared by an informal coalition of global pension funds, which has decided to collaborate on preparing this joint submission to provide constructive input on the OECD's work to secure treaty access for the long-term benefit of pension funds and their beneficiaries. With combined assets under management of approximately 1.5 trillion USD, this group is representative of a larger global constituency of pension funds that manages the retirement security of citizens from countries around the world and also provides investment capital to drive economic growth in a number of developed and emerging economies.

We have previously responded to invitations from the OECD to provide comments in relation to items that are of considerable relevance to pension funds and their pension beneficiaries.<sup>1</sup> As such, we welcome and value that the OECD has again reached out to interested parties to continue the constructive dialogue on the tax treatment of pension funds worldwide. We consider this additional work to ensure that a pension fund should be considered a resident of the State in which it is constituted for tax treaty purposes to be of great importance and have therefore decided to provide you with our joint comments and observations below.

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<sup>1</sup> Reference is made to the previous submission dated June 17, 2015 in relation to the Revised Discussion Draft on BEPS Action 6 released May 22, 2015, and the three separate submissions all dated January 9, 2015 submitted by the Canadian parties to this letter, by the Dutch parties and by the Australasian Parties (in this letter referred to as the "Canadian Submission", the "Dutch Submission" and the "Australasian Submission" respectively, and collectively, as our "Submissions").

## 1. Comments requested by the OECD

The OECD has invited comments in particular to several phrases included in the definition of a recognised pension fund. Below we will respond to the OECD's invitation in the same order as in the discussion draft.

### 1.1. As regards the phrase "that is treated as a separate person under the taxation laws of that State"

As recognized by the OECD in the draft Commentary on Articles 3 and 4 of the Model Tax Convention, there is considerable diversity in the legal and organizational characteristics of pension funds around the world. It is important that the pension fund definition which is scheduled for adoption by the planned revision to the Model Tax Convention appropriately captures the diverse range of such organizations. We agree that the reference to an "*entity or arrangement established in that State that is treated as a separate person*" should be interpreted in a broad manner, although we are concerned that the addition of the term "separate" may introduce a new concept that may be difficult for some entities to demonstrate in a way that would satisfy all OECD Member States.

To avoid certain types of pension fund organisations being put at risk of not qualifying for the definition of a recognised pension fund, we suggest that the proposed wording of paragraph 1 of Article 3 is aligned for consistency with the wording currently used in Article 3 and Article 4 of the Model Tax Convention, which does not require a person to be a "separate" person. Also Article 3, paragraph 1, subparagraph k) of the 2016 US Model Tax Convention refers to a pension fund as "*any person established in a Contracting State (...)*".

We are confident that even with the omission of the word "*separate*" the phrase should sufficiently address situations in which income of a pension fund may be treated as income of another person for tax purposes, considering that the definition requires that entity or arrangement to be considered a person "*under the taxation laws of that State*". Furthermore, the conditions set out under subsections (i) and (ii) of paragraph 1, subparagraph j) of Article 3 make sure that only entities or arrangements exclusively (or almost exclusively) providing retirement benefits should be in scope of the definition of a recognized pension fund. As such, it would not be possible for persons which partially carry out some pension activities to be considered a recognized pension fund.

Paragraph 10.4 of the draft Commentary refers to trust-like vehicles and arrangements which may not be considered an entity under the applicable legislative framework, albeit that such a vehicle may be considered a separate person for tax purposes in its own right or by virtue of the qualification for tax purposes of its body of trustees. We are concerned that this sole example may not sufficiently illustrate the breadth of arrangements that exist under the legal frameworks of the numerous OECD Member States and that in practice, referencing only a single example may mean that the definition is applied in a narrow manner. Therefore, we recommend amending the Commentary to include additional examples, such as superannuation funds, government sponsored pension schemes designed for its citizens, UK trusts and other dedicated trusts/funds as follows (with addition in **bold underline**, deletion in ~~strikethrough~~):

*10.4 (...) The reference to an "arrangement" is intended **amongst other things** to cover cases where pension benefits are provided through vehicles such as a trust **or any other arrangement** which, under the relevant ~~trust~~ law, would not constitute an entity **(such as a superannuation fund or certain government funds constituted to provide retirement benefits)**: the definition will apply as long as ~~the trust or the body of trustees is treated~~, for tax purposes, **that trust (or its body of trustees) or (an entity within an) arrangement is treated** as a separate entity recognised as a separate person. It is required, however, that the entity **or (entity within an) arrangement** be treated as a separate person under the taxation laws of the State in which it is constituted: if that is not the case, it is not necessary to deal with the issue of the residence of the pension fund itself as the income of that fund is treated as the income of another person for tax purposes.*

In addition, within some pension arrangements a separation takes place between entities or arrangements that provide or effect the pension benefits and entities or arrangements that hold the funds invested on behalf of the pension beneficiaries. A further clarification in the Commentary would be welcomed in this

respect to ensure that such pension arrangement is considered a recognized pension fund as defined in Article 3, paragraph 1, subparagraph j) under (i) of the Model Tax Convention. A similar set-up may for example be used by certain government funds constituted to administer or provide retirement benefits for beneficiaries of that State or local subdivision thereof, where the actual provision of those benefits to individuals may be effected indirectly by another part of the government. We recommend that it is clarified that the mechanics of the manner in which retirement benefits are paid out to the beneficiaries or the separation between holding the funds invested on behalf of the pension beneficiaries and paying out the benefits should not hinder the qualification of such fund as a recognized pension fund of the State in which it is constituted.

### **1.2. As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits”**

The OECD has invited comments on whether the word “exclusively” would be too restrictive given the normal operations of a pension fund. Pension funds often have other activities which are complementary or related to the main activity of administering or providing retirement benefits or similar benefits and may also perform activities which are outside the strict scope of providing these types of benefits. Such activities often serve a social and public purpose, but not all OECD Member States may capture these activities under the phrases “providing retirement benefits” or “similar benefits”.

By requiring a pension fund to operate exclusively to administer or provide retirement or similar benefits, pension funds that also perform activities of which it is unclear whether these activities may be considered equivalent or similar to that purpose would be excluded from the definition of a recognised pension fund. We therefore suggest that this phrase is amended in accordance with Paragraph 12 of the final version of the Report on Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances), as follows: “*that is constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits*”. By rephrasing this sentence in this manner, a recognised pension fund would still be required to operate with the purpose of administering or providing retirement benefits or similar benefits, but would allow for some leeway for relatively small activities that are subordinated to the main purpose of providing retirement benefits (we will address such activities below under section 1.3.).

The wording “exclusively or almost exclusively” would also tie in with the definition of a pension fund included in Article 3, paragraph 1, subparagraph k) of the 2016 US Model Tax Convention, whereby a pension fund is considered “*any person established in a Contracting State that is (...) operated exclusively or almost exclusively a) to administer or provide pension or retirement benefits or similar benefits (...)*”.

Furthermore, there are examples of OECD Member States with a large pension sector where the specific pension fund provisions included in the respective legislative framework also allow for some leeway in view of activities that can be performed by pension funds. For example, the Dutch exemption from corporate income tax applicable to pension funds can only be applied if a pension funds meets several tests, one of which being a “purpose test”. Under this purpose test, the objective of a pension fund should be to operate exclusively or almost exclusively to provide benefits for the care of (former) employees in case of disability or old age, based on a pension scheme.<sup>2</sup>

### **1.3. As regards the phrase “similar benefits”**

The draft Commentary in relation to the purpose of a recognized pension fund to administer or provide retirement or similar benefits to individuals, as included in paragraph 10.5, properly reflects the primary objective of pension funds worldwide. First of all, we appreciate that the OECD aims to make the definition of a recognized pension fund and the Commentary thereto broadly applicable, so that the main forms of pension funds that currently exist are covered. In this respect, the acknowledgement in paragraph 10.5 that a pension fund can include a self-employed individual is a helpful reference since many government sponsored pension funds will not only support individuals that were employed by a third-party but also

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<sup>2</sup> Unofficial translation of an excerpt from Article 5, paragraph 1, subsection b. of the Dutch Corporate Income Tax Act 1969.

individuals that are self-employed. Such plans support a wide citizenry of a country, where the entitlement to benefits is based on the locally defined concept of pensionable earnings. Also, both government sponsored and single employer pension funds may provide pension benefits for directors and officers of a company. None of these factors should disqualify a pension fund from being considered a 'recognized pension fund'. Therefore, it would be advisable for the Commentary included in paragraph 10.5 to be expanded to provide a more complete reference to the self-employed (more than that of a single individual), corporate officers who are not employees, non-executive board members and other persons who would not be considered common law employees of an employer.

Furthermore, the examples provided by the OECD in paragraph 10.5 of the draft Commentary on what can be considered "similar benefits", such as payments made as a result of the death or disability of an individual, in our view accurately describe activities carried out by pension funds that should be considered in line with providing retirement benefits. Considering that the definition is intended to cover many different forms of pension funds we anticipate that the term "similar benefits" should be interpreted broadly, so that it for example also covers payments for the benefit of surviving members of the family of the deceased (widow and orphan benefits), etc. For example in Germany the corporate income tax exemption for pension funds as provided for under §5 (1) Nr. 3 b of the Körperschaftsteuergesetz relies upon the requirement (amongst others) that the pension fund is according to its business plan and the manner and amount of the benefits considered a social institution. This involves benefits provided on the basis of old age, disability, as well as benefits for the surviving members of the family. Furthermore, as mentioned in the final sentence of section 1.2. above, the Dutch corporate income tax act also includes disability, widow and orphan benefits as similar benefits.

In practice, pension funds may also perform activities outside the strict scope of their main purpose of administering or providing retirement benefits, albeit that such activities are often relatively small in size compared to the main activity of providing retirement benefits. Furthermore, such activities often have a social welfare angle and may be considered of importance to the public and to pension beneficiaries. In view of the foregoing, we value that the OECD has welcomed examples of "benefits" that may be granted by pension funds that some OECD Member States may neither consider "retirement benefits" nor "similar benefits", as it is clearly not intended that pension funds granting such benefits would not be considered a recognized pension fund. There are different approaches by OECD Member States as to whether granting such benefits would be considered "similar" to providing retirement benefits, however granting such benefits would generally not disqualify a pension fund from being considered as such under the applicable legislative framework. This is why many OECD Member States allow for some capacity to provide benefits other than retirement benefits (for example by incorporating an "almost exclusively" requirement in the applicable pension legislation, as mentioned under 1.2. above) and maintain a broad definition of what is considered "similar" to providing retirement benefits. A clear break between activities that would be considered "similar" benefits and activities that would fall under "almost exclusively" cannot easily be made as there is overlap and as there is no consistent approach by OECD Member States in this respect.

Activities that may be considered similar to providing retirement benefits by some OECD Member States are for example providing healthcare packages, activities related to providing affordable housing, worker's compensation program benefits, administrative services in the field of occupational health, allowing for amounts to be withdrawn and lent to cover major expenses of a beneficiary such as unexpected medical costs, etc. These examples are not meant to be limitative or exclusive. Furthermore, some of these activities may be embedded in such a manner within the primary service of providing retirement benefits that pension beneficiaries would consider these additional services indisputably part of their retirement packages.

Of course, as suggested under 1.2. above, the addition of the term "almost exclusively" would also provide for proper scope to capture the majority of the pension funds that currently exist. The addition of "almost exclusively" would also ensure that pension funds should only fall within the scope of the definition of a recognized pension fund if the purpose is to administer or provide retirement or similar benefits, whereby only 'other activities' that are relatively small in size and clearly subordinated to the main activity of providing retirement benefits would be permissible. To ensure a broadly applicable pension definition that closely relates to the general treatment of pension funds in OECD Member States, we therefore suggest incorporating "almost exclusively" in the definition of a recognized pension fund as suggested in 1.2. above

and to expand the Commentary in paragraph 10.5 to include more examples of what may be considered “similar benefits”.

As a final remark in relation to paragraph 10.5 of the draft Commentary, we suggest replacing the term “invalidity” as mentioned in the final sentence of this paragraph by the term “disability”. The term disability may be considered more appropriate to address the consequences of impairments of a physical or mental nature.

#### **1.4. As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements (...)”**

We appreciate that the OECD has also included entities and arrangements that are constituted and operated to invest funds for recognized pension funds within the definition of a recognized pension fund for the purpose of the OECD Model Convention. We concur with paragraph 10.8 of the draft Commentary, whereby it is recognized that pension funds often invest together with other pension funds pooling their assets in certain arrangements or entities, or may for example invest via wholly owned entities or arrangements resident in the same State for commercial, legal or regulatory reasons.

The word “exclusively” within this context may be too restrictive for certain cases in which countries have overseas territories which can be considered separate jurisdictions. If a pension fund resident in such overseas territory invests via an entity or arrangement together with a pension fund in the “main” jurisdiction, treaty benefits may be denied to such investment entity or arrangement. As pension funds resident of such overseas territories are often relatively small compared to pension funds in the main jurisdiction, it may be appropriate to insert “almost exclusively” in Article 3, paragraph 1, subparagraph j) under (ii) of the Model Tax Convention.

## **2. Other comments**

Below we will outline our further comments in relation to the discussion draft.

### **2.1. As regards the Proposed changes to paragraph 1 of Article 4 of the Model Tax Convention**

It has been suggested in the discussion draft to amend paragraph 1 of Article 4 of the Model Tax Convention in order to include recognized pension funds as resident of a Contracting State for purposes of the Convention. Article 4 of the Model Tax Convention describes a resident as ‘*any person who, under the laws of that State, is liable to tax therein (...)*’. Paragraph 8.6 and 8.7 of the OECD Commentary to Article 4 mentions that this requirement may sometimes result in uncertainties for pension funds, since these are often exempt from corporate income tax. We therefore welcome the OECD’s endorsement of the explicit recognition of pension funds as tax treaty residents and greatly appreciate that the draft Commentary to paragraph 8.6 now formalizes current practice by acknowledging that most states already view such entities as residents for purposes of the Model Tax Convention.

Pension funds can also be considered liable to tax irrespective of whether they benefit from an exemption from corporate income tax. To ensure the text of Article 4 of the Model Tax Convention is in line with paragraph 8.6 of the draft Commentary, we suggest slightly rephrasing paragraph 1 of article 4 of the Model Tax Convention (with addition in **bold underline** and deletion in ~~striketrough~~) to avoid any doubt as to whether pension funds are considered liable to tax:

*“For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, **including recognized pension funds of that State** and also includes that State and any political subdivision or local authority thereof ~~as well as a recognised pension fund of that State.~~”*

Furthermore, it would be helpful if the text of the current paragraph 8.6 of the Commentary (which will be renumbered to paragraph 8.7) remains unchanged, so that it continues to mention a pension fund as an example of a person that is considered liable to comprehensive taxation even if a Contracting State does not in fact impose tax.

**2.2. As regards the term “retirement” as included in the definition of recognized pension fund in paragraph 1 of Article 3 of the Model Tax Convention**

The suggested definition of a recognised pension fund as is intended to be included in paragraph 1, subsection j) of Article 3 of the Model Tax Convention refers to an entity or arrangement that is constituted and operated to administer or provide “retirement or similar benefits” to individuals. In order to make this definition broadly applicable to the numerous types of pension funds worldwide and to take account of the particular interpretation that OECD Member States may have in relation to what is understood as a pension fund, we suggest adding the following to paragraph 1, subsection j) letter (i) of Article 3 of the Model Tax Convention (with addition in **bold underline**):

*“that is constituted and operated exclusively **or almost exclusively** to administer or provide **pension**, retirement or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities;”*

By also including the term “pension”, it would be ensured that the definition is widely applicable, considering that not all OECD Member States may interpret the terms “pension” and “retirement” in the same way. By including both terms, the definition of a recognized pension fund would also be consistent with the definition of a pension fund as included in the 2016 US Model Income Tax Convention.

**2.3. As regards the phrase “and that is regulated as such by that State or one of its political subdivisions or local authorities”**

The proposed Article 3, paragraph 1, subparagraph j), subsection (i) sets out a secondary condition which must be met in order to qualify as a ‘recognised pension fund’ by requiring a pension fund to be “regulated as such by that State”. This phrase may not be sufficiently broad when considering government funds constituted to provide pensions, for the reason that such funds are government owned and governments do not tend to regulate themselves. Therefore, we consider that the Commentary should acknowledge that, in respect of government funds, the regulation itself can take any form as long as it is endorsed by that State. For example, a government fund would meet the “regulation test” if it can point to the existence of provisions for accountability and review contained in its constituting legislation.

With this in mind, together with the our comments made in the final paragraph of section 1.1 above regarding the fact that some government funds will not be administering or providing benefits to individuals directly, we recommend further amending Article 3, paragraph 1, subparagraph j), subsection (i) to remove the reference to “as such” so that it reads (deletion in ~~strike through~~):

*“(…) and that is regulated ~~as such~~ by that State or one of its political subdivisions or local authorities”*

We are of course willing to further contribute to matter brought forward by the OECD that are of interest to pension funds worldwide and would gladly provide you with further input.

Sincerely,

Jacquelyn Colville  
Chief Financial Officer  
Alberta Investment Management Corp.

Klaus Stürmer  
Managing Director  
Arbeitsgemeinschaft kommunale und kirchliche  
Altersversorgung Corporation (AKA)

[signed]

[signed]

Evert-Jan Spoelder  
Senior Tax Counsel  
APG Asset Management

Neil Marcovitz  
Vice President, Tax  
British Columbia Investment Management  
Corporation

[signed]

[signed]

Steve Bossé  
Vice President, Taxation  
Caisse de dépôt et placement du Québec

[signed]

John Payne  
Head of Tax  
New Zealand Superannuation Fund

[signed]

Doug Michael  
Chief Financial Officer  
OPTrust

[signed]

Maj-Britt Klemp  
Head of Tax  
PensionDanmark

[signed]

Jean-François Ratté  
Vice President, Taxation  
Public Sector Pension Investment Board

[signed]

Jonathan Gilmore  
Head of Tax  
Universities Superannuation Scheme (USS)

[signed]

Kristina Fanjoy  
Managing Director, Head of Tax  
Canada Pension Plan Investment Board

[signed]

Serena Lefort  
Head of Tax  
OMERS

[signed]

Hersh Joshi  
Vice President, Taxation  
Ontario Teachers' Pension Plan Board

[signed]

Niels Krook  
Head of Tax  
PGGM Investment Management

[signed]

Vince Quagliata  
Head of Tax  
QIC

[signed]

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## TREATY RESIDENCE OF PENSION FUNDS

ICAEW welcomes the opportunity to comment on the Public Discussion Draft [Treaty Residence of Pension Funds](#) published by OECD on 29 February 2016.

This response of 31 March 2016 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.



ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 146,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

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[icaew.com](http://icaew.com)

## OUR COMMENTS

1. We are writing to request that the proposed definition of “recognised pension fund” should be extended to specifically include pension funds established by international organisations, and that such pension funds should be treated as resident in the state in which they are established or principally administered.
2. Although these pension funds do not always meet all the local regulatory or tax requirements in the state in which they are established or administered, they are frequently run as a practical matter in accordance with those requirements. See for example, the UK Upper Tribunal decision last year in [Macklin v HMRC \[2015\] UKUT 39](#) (TCC) which examined the World Bank Staff Retirement Plan that is administered in accordance with United States Internal Revenue Code rules relating to qualifying pension plans.
3. The controls exercised over these pension funds and the legal rules they operate under mean they are established and run to provide retirement benefits and do not facilitate tax avoidance.
4. The treatment of these pension funds is not clear in some countries and to include them specifically in the definition of “recognised pension funds” would be a helpful clarification for both the funds themselves and their employees and the employees’ dependants.

## APPENDIX 1

### ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see via <http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax>).

Via email

[taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

Tax Treaties, Transfer Pricing and

Financial Transactions Division

OECD/CTPA

Dear Secretariat,

On behalf of IFA Grupo Mexicano, A.C. (Mexican branch of the International Fiscal Association), below you will find our comments on the Public Discussion Draft “Treaty Residence of Pension Funds” (the “Discussion Draft”). Comments appear in *italics* following the questions of paragraph 2 of the Discussion Draft.

- a) **As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j):** Does that phrase deal adequately with pension funds established in your State? *No*. If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents? *The following: “that is treated as a separate person or estate under the taxation laws of that State”.*
- b) **As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Is the word “exclusively” too restrictive given the normal operations of a pension fund? *No*. If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”? *N/A*.
- c) **As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? *No, because invalidity and death benefits are included in paragraph 10.5 of*

*the Commentary on Article 3. If yes, please describe these benefits?*  
N/A.

d) **As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? *No.* If yes, please describe the operations that might not be covered? *N/A.*

e) **Additional comment:** *We suggest to amend the phrases in Article 3(1) j) subdivisions i) and ii): “that is constituted and operated exclusively to administer or provide retirement or similar benefits” and “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” with “that is—constituted **established** and operated exclusively to administer or provide retirement or similar benefits” and “that is—constituted **established** and operated exclusively to invest funds for the benefit of entities or arrangements”, respectively, to align them with the chapeau of Article 3(1) j), which provides that a “recognised pension fund” may take the form of an entity (or a legal person), which is incorporated or established with legal personality, or an arrangement, which is established or organized without legal personality.*

\* \* \*

The participation of IFA Grupo Mexicano, A.C. is made on its own behalf exclusively as an IFA branch and in no case in the name, or on behalf, of Central IFA or IFA as a whole.

We hope you find these comments interesting and useful. We remain yours for any questions or comments you may have.

Sincerely,

IFA Grupo Mexicano, A.C.

Tax Treaties  
Transfer Pricing and Financial Transactions  
Division  
OECD/CTPA

By e-mail: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

31 March 2016

Dear Sirs,

### **Public Discussion Draft: Treaty Residence of Pension Funds**

ILAG is a trade body representing members from the Life Assurance and Wealth Management Industries.

ILAG members share and develop their practical experiences and expertise, applying this practitioner knowledge to the development of their businesses, both individually and collectively, for the benefit of members and their customers.

A list of ILAG members is at the end of this submission.

#### **General comments**

Our members have considered the discussion draft and decided not to respond to each of the questions it contains. Our response is limited to those matters that may impact on UK life insurance companies.

UK life insurance companies own (legally and beneficially), as well as administer, significant volumes of investment assets on behalf of registered pension schemes. Those assets are often ring-fenced from the companies' other business; for example, where the assets are held in individual unit linked funds.

The assets generate investment income (including dividends) and capital gains, which accrue to the benefit of the pension scheme members. As such, the pension business of a UK life insurance company is an arrangement constituted and operated exclusively, or almost exclusively, to invest funds for the benefit of registered pension schemes. The life company itself is treated as a separate person under UK taxation laws because it is a company; its pension business is not a separate person. Therefore, the definition proposed in Article 3(1)(j) is not clear as to whether pension business of UK life insurance would be included.

This point is not directly an issue in relation to treaty residence, as the life insurance company will be tax resident in the UK and, therefore, be entitled to benefit under the UK's network of double tax treaties. However, the pension business of UK life insurance companies is often currently able to obtain rates of withholding tax applicable to pension schemes under double tax treaties, as it is treated in the same way as pension funds. (It is right that there should be parity between them.) This ensures that pension schemes

investing through UK life insurance companies are not disadvantaged by suffering higher rates of withholding tax than the rates they would suffer if they invested directly in the same underlying assets.

An example of this is the UK: US Competent Authority Agreement, a copy of which is available here: [https://www.irs.gov/pub/irs-utl/competent\\_authority.pdf](https://www.irs.gov/pub/irs-utl/competent_authority.pdf)

Our members are concerned that the proposed definition of 'recognised pension fund' as written in the Discussion Draft does not appear to cover the pension business of UK insurance companies. Our members perceive a risk to the ability of life insurance pension business to access favourable 'pension' withholding tax rates as, and when, tax treaties are re-negotiated. This would lead to a competitive distortion with an adverse effect on insured pension business.

The new proposed Paragraph 10.4 to the Commentary on Article 3 acknowledges that there is considerable diversity in the legal and organisational characteristics of pension funds around the world. Paragraph 10.4 also explains the requirement in proposed Article 3(1)(j) for the entity or arrangement 'to be treated as a separate person under the taxation laws of the State in which it is constituted'. This is because 'if that is not the case, it is not necessary to deal with the issue of the residence of the pension fund itself as the income of that fund is treated as the income of another person for tax purposes'. In other words, the 'separate person' requirement is intended to carve out tax transparent vehicles from the definition.

It appears to be an unintended consequence of the current drafting to exclude the pension business of life insurance companies. We have suggested an amendment to the proposed wording below.

### Responses to questions raised in the Discussion Draft

**a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j):** Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?

UK life insurance companies are not pension funds. Whilst some companies exclusively write pension business, the majority typically write both pension business and life assurance business (such as protection or permanent health business). Pension business is separately defined in UK tax legislation (Section 57 Finance Act 2012) as 'the effecting or carrying out of contracts entered into for the purposes of a registered pension scheme [or the reinsurance of such business]'.

The pension business of a life insurance company would not constitute a 'separate person' for the purposes of the proposed definition in Article 3(1)(j). Our members suggest that the wording is amended to read **'that is a separate person or as a separate part of the business of such a separate person under the taxation laws of that State'**. The Commentary could then explicitly clarify that the pension business of a life insurance company falls within this definition but a tax transparent vehicle does not.

**d) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Is the word

“exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

For the pension business of UK life insurance companies, the word ‘exclusively’ may be too restrictive. In particular, the relevant funds may include some monies invested on behalf of non-UK resident pension schemes. Our members prefer the wording ‘exclusively or almost exclusively’ as in Paragraph 12 of the Report on BEPS Action 6.

We would welcome the opportunity to discuss this representation further.

Yours faithfully,

**Nathan Powell**

**Chair, Tax Practitioner Group,  
Investment & Life Assurance Group**



# ILAG Membership 2016

## Full legal members (30)

Aberdeen Asset Management Life and Pensions Limited

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Canada Life Limited

Forester Life

Hannover Re UK Life Branch

London & Colonial Assurance

MetLife

Old Mutual Wealth

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Phoenix Group

Reliance Mutual

Sanlam Life & Pensions

Suffolk Life

Swiss Re Europe SA (UK Branch)

Wesleyan Assurance Society

(17)

Barnett Waddingham

Defaqto

EY

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Hymans Robertson

Mazars

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PwC

Steve Dixon Associates llp

AIG Life

AXA Wealth

Fil Life Insurance Limited

General Reinsurance (London Branch)

HSBC Bank Plc

LV=

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OneFamily

Partnership Assurance

Police Mutual

RGA

SCOR Global UK Limited

Sun Life Assurance Company of Canada

Vitality

Zurich Assurance Limited

Capita plc

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HCL Insurance BPO Services Limited

Huntswood

Milliman

Pinsent Masons

RPC Consulting

Willis Towers Watson Plc

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NMG Consulting

State Street Investor Services

## Small Mutuals (3)

British Friendly

Forester Friendly

Shepherds Friendly

Ecclesiastical Insurance Group

McCurrach Financial Services

Squire Patton Boggs

**Associate (individual members) (33)**

Sam Achord	Rebecca Jonson
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Kali Bagary	David Macdonald
Alun Beynon	Peter Mannion
Rayon Brown	Neil McCarthy
Ian Buchanan	Phil Moore
Kathy Byrne	Graham Newitt
Zoe Campbell	Veronica Oak
Moiria Casey	Martin Palmer
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Richard Farr	Eric Purdy
John Gillman	Shaun Sandiford
Ron Godfrey	Geoff Shanks
Stephen Gore	Dennis Smith
Philip Govan	David Wells
David Gulland	Brian Wood
Colin Gunney	

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Graham Bateman	Ian King
Marcus Chamberlayne	Peter Lagerberg
Jonathan Cumpstey	Gary McCarthy
Ken Davies	Steve Norman
Anthony Devere -Summers	Gareth Richards
Poppy Hitchings	Karen Walls
Lee Hyam	Steve Williams
Amanda Hurst	Liz Wytchard
Dan Jenkinson	

## COMMENTS ON PROPOSED CHANGES TO THE OECD MODEL TAX CONVENTION CONCERNING THE TAX RESIDENCE OF PENSION FUNDS

To: Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA

Sent via e-mail: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

INVERCO<sup>1</sup> welcomes the opportunity to comment on the OECD Public Discussion Draft on changes to the OECD model tax convention concerning the treaty residence of pension funds.

As a general comment, we agree with the aim of the discussion draft to ensure that a pension fund is considered to be a resident of the state in which it is constituted for the purposes of tax treaties. Moreover, in general terms, the definition of “recognized pension fund” provided in the Discussion Draft matches the general features of pension funds as regulated by the Spanish legislation<sup>2</sup>.

Under Spanish legislation on pension funds, two types of pension funds are foreseen, Occupational Pension Funds and Personal Pension Funds. Apart from the difference on the type of pension plans that Occupational/Personal Pension funds may integrate, their purpose (provision of retirement or similar benefits to plan holders), tax treatment, as well as the applicable legislation to both of them are the same, i.e., the rules on eligible assets, management entities and depositaries do not distinguish between the type of pension funds (occupational/personal pension funds). Therefore, the considerations on the definition of “recognized pension fund” for tax purposes are equally applicable to both of them.

Please find below our answers to the issues raised in the Discussion Draft.

- a) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?

The reference to a “separate person” does not raise concerns. The Spanish corporate tax legislation considers pension funds as taxable entities (although taxed at a 0% rate). Therefore, Spanish pension funds would be covered under said formulation.

- b) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the

<sup>1</sup> INVERCO, is the Spanish Association of Investment and Pension funds. It represents 5.039 CIS with assets amounting to 255.338 million Eur (98,7 % of total assets in Spain), 1.335 Pension Funds with assets amounting to 104. 518 million Eur (99, 8% of total assets in Spain) and 24 UCITS registered for marketing in Spain with assets amounting to de 80.000 million Eur.

<sup>2</sup> Royal Legislative Decree 1/2002, of November 29, on Pension Plans and Pension Funds and Royal Decree 304/2004, of February 20, on Pension Plans and Pension Funds regulation.

normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefit”.

The reference to being exclusively constituted and operated to administer or provide retirement or similar benefits does not raise concerns. Under Spanish legislation pension funds have the sole object to provide retirement or similar benefits to pension plans holders.

- c) As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits.

The definition “similar benefits” should be interpreted broadly so that it covers pension payments that are usually included within the scope of pension funds protection such as payments in case of disability or death.

Moreover, the term “similar benefits” should also include certain withdrawals allowed before retirement, foreseen in national legislations for exceptional circumstances such as long-term unemployment or severe dependence of the pension plan holder or, in general, other anticipated liquidity cases that national legislations might introduce provided that (i) the main purpose of the pension fund as recognized by the relevant national legislation is the provision of retirement benefits and (ii) the anticipated liquidity cases are subject to certain legal requirements (i.e., withdrawals allowed only after a certain period of time has elapsed since contributions were made...).

- d) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

The Spanish legislation foresees a special type of pension funds (master pension funds “*Fondos de Pensiones abiertos*”) which sole object is to pool the investments of other pension funds/plans also regulated under Spanish legislation. Said open-ended pension funds would be covered by the subdivision (ii) of the definition proposed as, for the moment being, it only foresees investments by Spanish pension funds/plans

Notwithstanding the above, it must not be ruled out that other jurisdictions might find the word “exclusively” too restrictive if pooling assets from pension funds resident in other States is foreseen under their legislation. Therefore, in order to adopt a more flexible approach it would be advisable

to include the possibility that the investing pension funds are in a different State than the pension fund that pools the assets.

*Madrid, 1<sup>st</sup> April*

Marlies de Ruiter  
Head, Tax Treaties, Transfer Pricing and  
Financial Transactions Division  
Centre for Tax Policy and Administration  
Organisation for Economic Co-operation and  
Development

By email: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

Date: **1 April 2016**

Dear Ms de Ruiter

**RE: OECD DISCUSSION DRAFT TREATY RESIDENCE OF PENSION FUNDS**

The Investment Association<sup>1</sup> welcomes the opportunity to comment on the OECD's discussion draft on the treaty residence of pension funds. We are glad to be able to provide greater clarity on treaty entitlements of pension schemes in the OECD Model Tax Convention.

In respect of the proposals for changing the OECD Model Convention and Commentary, we have four comments.

**1) Pension scheme arrangements set up as part of an insurance company**

In the UK, the most common form of defined contribution pension scheme is set up as a contractual arrangement with an insurance company. The taxation of insurance companies in the UK is complex, but in relation to pension business, a pool of assets is segregated within the insurance company's balance sheet and subjected to a different tax regime relevant to pensions which ensures that returns on pensions assets are exempt from tax.

The pension business of a UK life insurance company is defined in UK tax legislation (Finance Act 2012 s58) as the effecting or carrying out of contracts entered into for the purposes of a registered pension scheme or the reinsurance of such business. However, pension business is normally just one part of a life insurance company's business. As such, the pension business is not a separate person or treated as a separate person under UK tax law. The life insurance company will, in most cases, be carrying on activities as well as pension business (such as writing protection business).

<sup>1</sup> The Investment Association is the trade body that represents UK investment managers, whose members collectively manage over £5.5 trillion on behalf of clients. The money is in a wide variety of investment vehicles including authorised investment funds, pension funds and stocks & shares ISAs.

The investments of most UK defined contribution pension schemes are therefore not held within a “recognised pension fund” as defined in proposed Art. 3(1) j). A remedy would be to use

“that is treated as a separate person **or as a separate business of a separate person** under the taxation laws of that State”.

## **2) Paragraph 10.4 of the proposed Commentary on Article 3**

We consider it important to refer to trusts in the Commentary, and so welcome the clarification of their treatment in paragraph 10.4.

## **3) Paragraph 10.5 of the proposed Commentary on Article 3**

In the UK most pension funds allow individuals to access retirement benefits from a certain age, typically 55. There is no requirement to retire from employment, and no definition of what it means to “retire”.

We believe this approach (which is common to most countries) could be better reflected in the Commentary with the following amendment:

“... this term is broad enough to cover one or more payments made ~~at~~ **on** or after ~~retirement~~ **reaching a certain age to an employee or** self-employed person even if these payments are not made in the form of regular pension payments.”

## **4) Multinational pension pooling arrangements**

Subparagraph (ii) of the definition includes pension pooling vehicles that are used by different pension funds to pool assets.

Such pooling vehicles are frequently used to pool the assets of pension funds in different jurisdictions. For example, they are commonly used by multinational businesses to rationalise their employee pension arrangements across the various countries in which they operate.

We would strongly support the inclusion of multinational pension pooling vehicles in the definition of recognised pension fund, where all of the pension funds that invest through them are recognised pension funds (provided that the pooling vehicle is treated as a separate person or as a separate business of a separate person under the taxation laws of the state in which it was established).

Thank you for the opportunity to comment on the discussion draft, and I am available at your convenience to discuss anything in this letter at [jorge.morley-smith@theia.org](mailto:jorge.morley-smith@theia.org) or on +44 (0)20 7831 0898.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Jorge Morley-Smith', written in a cursive style.

---

**Jorge Morley-Smith**  
Director





**Irish Tax  
Institute**

*Leaders in Tax*

**FAO:**

**Tax Treaties,  
Transfer Pricing and Financial Transactions Division,  
OECD/CTPA**

## **Irish Tax Institute**

# **Response to OECD Discussion Draft: The Treaty Residence of Pension Funds**

**1 April 2016**

## **About the Irish Tax Institute**

The Irish Tax Institute (“the Institute”) is the leading representative and educational body for Ireland’s AITI Chartered Tax Advisers (CTA) and is the only professional body exclusively dedicated to tax. Our members provide tax expertise to thousands of businesses and individuals in Ireland and internationally. In addition many hold senior roles within professional service firms, global companies, Government, Revenue and state bodies.

The Institute is the leading provider of tax qualifications in Ireland, educating the finest minds in tax and business for over thirty years. Our AITI Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice.

A respected body on tax policy and administration, the Institute engages at the most senior levels across Government, business and state organisations. Representing the views and expertise of its members, it plays an important role in the fiscal and tax administrative discussions and decisions in Ireland and in the EU.

The Institute welcomes the confirmation that a pension fund will be considered to be a resident of the state in which it is constituted and that the OECD Model Tax Convention (“MTC”) will be updated to reflect this.

We set out below comments on the proposed definition of “recognised pension fund” in Article 3(1)(j) of the MTC, specifically addressing questions 2(a) and 2(c) in the discussion draft.

### **Pension Funds recognised as a Separate Person**

There is considerable diversity in the legal structure of pension funds around the world. It is important that the revisions to the MTC are wide enough to ensure that all such pension funds are granted equal entitlement to treaty benefits.

The discussion draft proposes that treaty benefits will only apply to those pension funds that are treated as “separate persons” under the taxation laws of that State. In applying the “separate person” test, the key criterion appears to be that the income in the pension fund is not otherwise attributed to another person for tax purposes.

Not all pension funds are treated as a “separate person” for tax purposes. One such example is an Approved Retirement Fund (ARF), a commonly used investment vehicle in Ireland. An ARF is a Revenue-approved fund in which certain individuals can invest their pension funds on retirement. The income and gains in an ARF accumulate tax-free and an individual is only subject to income tax once drawings are made from the fund (subject to a de-minimis withdrawal being made by the individual each year). For your reference, we have included in the Appendix further details on ARFs as contained in *OECD Reviews of Pensions Systems: Ireland* © 2014. An ARF is just one example of a fund which is not treated as a “separate person”.

To ensure that an ARF, and other such pension funds are captured in the revisions to the MTC, we recommend that the definition of “*recognised pension fund*” in Article 3(1)(j) is reworded as follows;

*“the term “recognised pension fund” of a State means an entity or arrangement established in that State that is treated as a separate person under the taxation laws of that State or is otherwise approved under the laws of that State, or the trustees of which are resident of that State”*

### **Meaning of ‘Similar Benefits’**

The definition of “recognised pension fund” in Article 3(1)(j)(i) of the discussion draft refers to a pension fund which provides “*retirement or similar benefits to individuals*”.

The commentary provided in paragraph 10.5 of the discussion draft recognises that similar benefits would include payments made as a result of the death of an individual and the Institute welcomes this confirmation. However, for avoidance of doubt, we would suggest that the wording in Article 3 explicitly refers to benefits payable on death. Article 3(1)(j)(i) should be amended as follows;

*“that is constituted and operated exclusively to administer or provide retirement or death benefits or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities;*

**Page 34**

In addition, there is a specific financial product available for certain people at the point of retirement. People can invest pension savings upon retirement in an Approved Retirement Fund (ARF). Depending on the level of guaranteed pension income available for life and the size of the pension fund, individuals may only have access to a specific type of ARF, called an Approved Minimum Retirement Fund (AMRF). Since 2011, ARFs and AMRFs are available to members of DC occupational plans.

An ARF is an investment contract in which the money is invested with a “Qualifying Fund Manager” (which includes banks, building societies and insurance companies). The individual can decide how to invest the money which accumulates tax-free. Income tax is payable on any money withdrawn from the fund. To invest in an ARF, the individual must have a guaranteed pension income in payment for life from other sources of at least EUR 18 000 annually. Where the minimum specified income test is not met and the individual does not wish to purchase an annuity, the legislation requires that the first EUR 120 000 of the pension fund (after taking the retirement lump sum), or the entire remaining fund, if this is less than that amount, must be invested in an AMRF. The individual may use the AMRF funds at any time to purchase an annuity. When an individual attains the age of 75 or starts receiving a guaranteed pension income for life from other sources of EUR 18 000 a year, the AMRF automatically becomes an ARF. An AMRF is like an ARF except that the individual cannot withdraw the original capital investment. Only the investment income can be withdrawn in the meantime. As explained below [on Page 38], there are incentives for people to withdraw 5% of their ARF fund each year.

**Page 38**

Any money withdrawn from an ARF is taxed at the individual’s marginal rate. The Budget and Finance Act 2006 introduced an imputed or notional distribution of 3% of the value of the assets of an ARF on 31 December each year, where the notional amount is taxed at the ARF owner’s marginal income tax rate.

The notional distribution measure was introduced to encourage drawdowns from ARFs so that they are used, as intended, to fund a stream of income at retirement. It does not apply to AMRFs. The level of the imputed distribution was increased from 3% to 5% in the Budget and Finance Act 2011, and from 5% to 6% for ARFs with asset values in excess of EUR 2 million in the Budget and Finance Act 2012. The amount of the annual notional distribution is reduced by the amount of actual distributions taken from an ARF and from an associated ARF. In practice, most individuals ensure they withdraw a minimum actual distribution of at least 5% (or 6%) to avoid the notional distribution requirement.

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05 April 2016



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## **Legal & General response to the discussion draft on changes to the OECD Model Tax Convention concerning the treaty residence of pension funds**

### **About us**

As you may know, L&G, established in 1836, is one of the UK's leading financial services groups. At 31<sup>st</sup> December 2015, we had over \$1 trillion in total assets under management. We've over nine million UK customers who rely on us to help them save for the future and to protect their families and their homes. We're one of the UK's biggest providers of workplace pensions with 1.8 million customers. We've also made a commitment to invest c£15bn in infrastructure, with £7bn already invested in, for example, housing, urban regeneration, clean energy and alternative finance.

### **Introduction**

Legal & General welcomes the opportunity to comment on the proposed changes to the OECD model tax convention concerning the treaty residence of pension funds.

Our response is primarily concerned with the implications of the proposed definition on pooled pension funds, and the possibility that policyholders of those pooled pension funds (i.e. UK registered pension schemes and their members) could be disadvantaged by the proposals.

### **Background of UK pension schemes arranged through insurance companies**

Pooled pension funds allow UK registered pension funds to invest in an insurance policy where the surrender value of the insurance policy is directly linked to the value of the assets which are referenced in that insurance policy. All economic risk in the pooled pension fund is borne by the pension fund policyholders, and all investment return accrues to those policyholders, with the insurance company making an annual management charge for investment management and administration services. These arrangements are also referred to as 'unit linked' pension business policies.

Investment via pooled pension funds is common within the UK pension market, as it gives individual pension schemes access to benefits associated with larger scale enterprises, including specialist investment expertise and risk sharing, and cost savings through economies of scale.

Insurance companies may operate purely as a pooled pension funds vehicle or they may also run other types of insurance business alongside their pooled pension fund business. L&G operates two UK life insurance companies, both of which have pooled pension funds alongside other non-pensions business.

## **Pension business and UK insurance companies**

For UK tax purposes, "pension business" is defined in section 57 Finance Act 2012. This states that pension business:

- (a) ... consists of the effecting or carrying out of contracts entered into for the purposes of a registered pension scheme, or*
- (b) it is the re-insurance of business within paragraph (a).*

The term "*registered pension scheme*" relates to pension schemes which are registered under Part 4 of the Finance Act 2004.

As a part of the due diligence undertaken at the time at which a policy is issued to a UK pension scheme by a UK insurance company, checks are made to ensure that the potential policyholder is a pension scheme which has registered with the UK's tax authority, HM Revenue & Customs ("HMRC"). As a part of the policy conditions, the UK registered pension fund is obliged to inform the insurance company if it ceases to be registered as a pension scheme with HMRC.

These requirements ensure that the business written by a UK insurance company which is classified as "pension business" is business that relates in its entirety to UK registered pension schemes and funds.

## **Status under current UK tax treaties**

For the purposes of withholding tax a pooled pension fund of an insurance company should be equivalent to a separate pension fund or scheme in order that the economic owner of the investment return (i.e. the pension scheme or the pension scheme policyholder) is not disadvantaged by investing in a pooled arrangement. Given this, where tax treaties allow for a reduced rate of dividend or interest withholding tax (as compared to another UK person), the UK has sought to include the following wording (or wording that gives similar effect) for clarification<sup>1</sup>:

*In the case of the United Kingdom, the term "pension scheme" means:*

*"Pension schemes (other than social security schemes) registered under Part 4 of the Finance Act 2004, including pension funds or pension schemes arranged through insurance companies and unit trusts where the unit holders are exclusively pension schemes"*

This ensures that insurance companies are able to access the same treaty withholding tax rates as pension schemes with respect to their pension business (but not any other non-pension business) and pass that benefit in full to their pension scheme policyholders. Were the company not able to access these benefits in respect of that pension business, policyholders of the pooled pension fund (i.e. the UK registered pension schemes and its members) to whom all of the investment return of the insurance fund is allocated would be disadvantaged simply by virtue of their participation in the pooled arrangement.

## **Comments on proposed changes**

Having regard to our comments above, our response is concerned with the specific questions a) and d) on which the discussion draft invites comment:

---

<sup>1</sup> *Treaties with US, Japan, Switzerland, Germany, Netherlands, Belgium, Spain and Canada*

- a) Tax law in the UK is applied at a legal entity (i.e. company) level. We are therefore concerned that the criterion *“treated as a separate person under the taxation laws of that State”* will prevent pooled pension funds of UK insurance companies from being able to be classified as recognised pension schemes, as a pooled pension fund is not a separate person for UK tax purposes. A proposed formulation which would ensure that pension funds of this type are captured by the definition is proposed below.
- d) Similarly, UK insurance companies typically undertake other types of insurance business outside of the pooled pension fund, and thus a UK insurance company would rarely meet the *“operated exclusively or almost exclusively...”* criterion. We do, however, note that the pension business is required to be separately identified for both accounting and regulatory purposes and thus can be ring-fenced from other operations of the company, and that there are specific legislative requirements that ensure that the pension business written by a UK insurance company relates in its entirety to UK registered pension schemes and funds.

We believe that that the *“operated exclusively or almost exclusively...”* criterion would be met were one to look at the level of the pooled pension fund of the insurance company. Therefore these issues could be dealt with either by including specific wording equivalent to that in the UK’s current relevant treaties, i.e. *“...including pension funds or pension schemes arranged through insurance companies”* or expanding the proposed definition of a recognised pension scheme to cover arrangements (for example, pooled pension funds) which, although not separate persons for UK tax purposes, are arrangements which are required to be separately identified from the entity which has put those arrangements in place for accounting and regulatory purposes, and which meet the criteria at the second part of the proposed definition. We have set out example wording below:

*The term “recognised pension fund” of a State means:*

- *An entity or arrangement established in that State that is treated as a separate person under the taxation laws of that State; or*
- *An arrangement which is not treated as a separate person under the taxation laws of that State but which is required to be separately identified for both regulatory and accounting purposes*

*and either of the following two conditions are met either in respect of the entity or arrangement:*

- (i) *that it is has been created and operated exclusively to administer or provide retirement or similar benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities; or*
- (ii) *that it is has been created and operated exclusively to invest funds for the benefit of entities or arrangements referred to in subdivision i).*

## Conclusion

Legal & General supports changes to the OECD model tax treaty to clarify the treaty status of pension funds, however we have concerns that the current drafting could lead to unintended negative impacts for the policyholders of pooled pension funds arranged through UK insurance companies (UK pension schemes and their members). We believe the changes we have proposed should extend the availability of any reduced rates of withholding tax applicable to recognised pension funds to such insured arrangements, while continuing to restrict those

benefits to the intended recipients, i.e. genuine retirement savings vehicles, thus helping to preserve equality of treatment across the UK pension market.

We would be happy to further discuss any of the comments made above.

Yours faithfully

Grace Stevens  
Chief Taxation Officer



Organisation for Economic Co-operation and Development,  
Centre for Tax Policy and Administration  
**Attn. Ms Marlies de Ruiter**  
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FRANCE

By email: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

Rotterdam, 1 April 2016  
CS/160274

**Subject:** Comments on the Discussion Draft on Action 6 of the BEPS Action Plan on  
Treaty Residence of Pension Funds

Dear Ms De Ruiter, Dear Marlies,

Thank you very much for the opportunity to provide comments on the Discussion Draft on Action 6 of the BEPS Action Plan (the '**Discussion Draft**') which was released by the OECD for public comments on 29 February 2016. Mazars Global International Taxation and Tax Policy professionals ('**Mazars**') are impressed by all the progress that the OECD has made to date and we are very pleased to provide our input on the Revised Discussion Draft.

Mazars welcomes the results of the work performed by the OECD with respect to issues related to draft changes to Articles 3 and 4 of the OECD Model Tax Convention, and to the Commentary on these Articles, ensuring that a pension fund is considered to be a resident of the State in which it is constituted for the purposes of tax treaties., including the proposals for changes to the definition of recognised pension fund in the OECD Model Tax Convention.

Our specific comments on the Discussion Draft are provided below:

**France:**

France has a specific retirement pension system which does not involve pension funds per se. Statutory pension insurance is managed under the redistribution system (i.e. current workers contribute to finance pensions of current pensioners) by organisms which are not, in principle, tax exempt for investment income – although they generally benefit from a reduced tax rate.

Rotterdam, 1 April 2016  
CS/160274

In addition, there are supplementary pension schemes under the capitalization system, usually managed by insurance establishments. Those insurance entities are liable to French corporate income tax under the standard regime without benefitting from any exemption. As such, they may already benefit from the provisions of Tax Conventions.

This being said, specific organisms similar to pension funds manage supplementary pension schemes for public agents, either under the capitalization or redistribution system. Some of them are totally tax exempt in France.

Since such entities and organisms start investing out of France, difficulties in the application of tax conventions may arise in the absence of a clear entitlement to the benefit of the tax conventions and reliance on the definition of pension funds.

Concerning the definition of pension fund suggested by the Discussion paper we would like to note:

- To our knowledge, French organisms are considered as separate bodies under French taxation laws (notably as “Organismes sans but lucratifs” with dedicated sets of tax rules);
- The French organisms similar to pension funds (i.e. excl. insurance companies) exclusively administer or provide retirement;
- Regarding the condition whereby the entity or arrangement is “regulated as [pension fund] by that State”: it may be controversial for some of the French organisms to demonstrate that they are “regulated as” pension funds. Indeed, even if some may be established by French law under a dedicated regime, others are set up as, for example, standard “associations”, outside a dedicated legal framework, but aiming exclusively at administering pensions to individuals. The criterion of “regulated as pension fund” may therefore be problematic;
- As regards the extension to organisms constituted and operated exclusively to invest funds for the benefit of entities or arrangements of pension funds: in the absence of pension funds in France, retirement contributions collected by pension organisms are to a certain extent invested in entities or arrangements which are not exclusively constituted and operated for the benefit of pension funds, but also for other investment vehicles (e.g. life insurances). Such funds are, in principle, exempt from tax in France.

As such, they may not qualify as tax residents unless specifically provided otherwise. Consequently, there may be a loophole in the entitlement of those entities or arrangements to the Tax Convention’s benefits, either because they would be precluded from the definition of pension fund as not exclusive, or because not covered by another provision of the Tax Conventions referring to CIVs or non-CIVs.

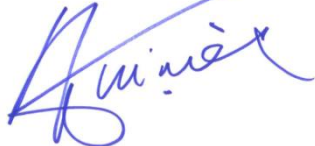
Rotterdam, 1 April 2016  
CS/160274

It is also to be noted that members of the French Government have raised the idea of the creation of private pension funds in France, yet nothing final has been proposed. Therefore, future developments would need to be carefully monitored to combined domestic rules and OECD new provisions relating to pension funds.

On behalf of the global network of Mazars Member Firms, we submit our response to the Discussion Draft on Action 6 of the BEPS Action Plan on Treaty Residence of Pension Funds. For any clarification of this response, please contact the undersigned.

Yours sincerely,

**MAZARS PAARDEKOOPEL HOFFMAN N.V.**



Ton Tuinier  
Chairman Dutch Executive Board



## Position paper on changes to the OECD Model Tax Convention: Treaty Residence of Pension Funds

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With great interest we have welcomed the public discussion draft "Treaty residence of pension funds", dated 29 February 2016. With respect to the public consultation we would like to respond to the invitation of the OECD committee on Fiscal Affairs ("the Committee") to share our comments by means of this position paper. In particular, the committee has requested our response to four specific questions.

MN is a Dutch asset management and pensions administrations company representing various Dutch pension funds with total assets under management of more than Euro 100 billion. We support the objective of the Committee to provide for such a definition of a "pension fund" that the main forms of pension funds are covered by that definition, regardless of whether a pension fund is subject or liable to tax in its own State. In the previous public consultation, "Follow up work on BEPS action 6: preventing treaty abuse 21 November 2014 – 9 January 2015", we explicitly proposed a pension fund definition by referring to tax laws and regulation in its country of establishment rather than referring to taxation. Our comments are based on the general assumption that the beneficiaries of pension fund, i.e. the pensioners, are individually taxed on their pensions when received. This is fundamental to our objective to have pension funds be recognized as eligible tax treaty residents of a contracting state, as that would result in the desired situation that additional taxes are generally not imposed on pension funds. Otherwise, if additional taxes were to be imposed, the mere purpose of pension funds, i.e. to provide pension payments, would be undermined.

Our comments are specifically based on the Dutch pension fund environment.

The four specific questions are:

**A) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognized pension fund” in proposed Art. 3(1) j): does that phrase deal adequately with pension funds established in your state? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?**

The reference to a “separate person” does not raise concerns. It would deal adequately with pension funds established in the Netherlands.

**B) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?**

Yes, the word “exclusively” would be too restrictive and we would therefore suggest to use the phrase: “exclusively or almost exclusively”. The suggested wording would provide alignment with the wording in Dutch tax law. According to Dutch tax law, a pension fund is an entity that “exclusively or almost exclusively” has as purpose the care of employees and ex employees in case of invalidity and old age by means of pensions under a pension scheme or of distributions under an early retirement scheme. Dutch tax law therefore provides some leeway in the core activities of a pension fund. Two examples that we can mention in this respect are:

- If a pension fund is investing its assets in such a way that it goes beyond “normal, passive, investing by a pension fund to safe guard its pension obligations” and this investing has features of an “active trade or business”, this would not be a core activity of a pension fund. Within limitations, this does not automatically lead to a breach of the pension fund status.

- Dutch tax law describes the specific products/benefits that pension funds should offer to pensioners and / or workers. There is however leeway for *pension fund alike* products/benefits. See also our response to question C).

**C) As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(i) j): Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits.**

As mentioned above, the products/benefits offered to pensioners and / or workers can be broad; the main requirement is that it can be regarded as “a pension arrangement”. In our experience, examples include financial coverage for financial risk as a result of invalidity and products / services in order to have workers re-integrate in the labour process.

**D) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements included in subdivision ii) of the definition of “recognized pension fund” in proposed Art. 3(i) j): Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?**

Yes, the word ‘exclusively’ would be too restrictive and we would therefore suggest to use the phrase: “exclusively or almost exclusively”.

In the Dutch context, an intermediary that invests on behalf of pension funds, *and* that meets the requirement of “a separate person” as described in Art. 3(i) j) would typically be a fiscally non transparent fund for mutual account. In most cases such a fund would opt for the tax neutral status of a fiscal investment institution, provided for by Dutch corporate tax law. The most important element that would be covered if the term “exclusively” would be extended to “exclusively or almost exclusively”, is the participation of non-resident pension funds in an intermediary. If Art. 3(i) j) has to be interpreted in the way that an intermediary in State X can “exclusively” invest funds for the benefit of pension funds resident in State X,

then that restriction to State X is not in line with business reality and potentially EU freedoms of movement of people and capital.

Extending the scope to “exclusively or almost exclusively” would permit an intermediary to also invest funds of pension funds resident in other Contracting States, to the extent they would meet the general “recognized pension fund” definition.

Attn: Tax Treaties, Transfer Pricing and Financial Transactions Division  
OECD / CTPA  
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75775 Paris Cedex 16  
France

**Re Discussion Draft on changes to the OECD Model Tax Convention concerning the treaty residence of pension funds**    Date 29 March 2016

Dear Sir or Madam,

NN Investment Partners appreciates the opportunity to provide comments with respect to the discussion draft on treaty residence of pension funds. With this letter NN Investment Partners seeks to provide comments on the questions raised in the discussion draft and to reiterate its concerns with respect to the wider issue of treaty entitlement of CIVs.

**NN Investment Partners**

NN Investment Partners is the investment management business of NN Group. NN Group is an insurance and asset management company with a strong, predominantly European presence in more than 18 countries. With around 11,500 employees the group offers retirement services, insurance, investments and (in the Netherlands) banking services to more than 15 million customers. NN Group is registered in the EU Transparency Register under public ID number: 493416718971-18. NN Investment Partners offers a wide variety of actively managed investment products and advisory services to institutional and retail customers. NN Investment Partners currently manages CIVs and non-CIVs domiciled in Benelux, Poland, France, Japan and the Cayman Islands. As of December 2015, NN Investment Partners manages approximately €187 billion for institutional and retail clients worldwide.

**Comments**

As a preliminary remark, we would like to note that we support the OECD in its commitment to develop sound tax policies, to promote the uniform and equitable enforcement of the tax laws, and to reduce the cost and burden of administration and compliance to the benefit of taxpayers and government alike. We specifically agree with the general terms of this initiative, that we believe will facilitate and harmonise treaty access for pension funds and positively affect pension savers.

We would like to share with you our comments on specific questions raised in the discussion draft:

- a) *As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognized pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?*

In certain jurisdictions pension funds may be established under contractual form and may therefore not be regarded as separate persons under the taxation laws of that jurisdiction. While it is true that, technically speaking, investors in such pension funds should be entitled to treaty benefits we also note that in practice this may not always be the case especially when the pension fund is widely-held (due to the disproportionately high administrative burden associated with claiming treaty benefits for each individual investor). We therefore suggest



removing the phrase “that is treated as a separate person under the taxation laws of that State” in order to facilitate treaty access to pension funds irrespective of their legal form and tax treatment in their home jurisdiction. We also recommend putting appropriate safeguards in place so to prevent investors from claiming treaty benefits on top of those already claimed by the pension funds.

- b) *As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?*

We note that the proposed wording departs from the text initially proposed under BEPS Action 6. For consistency purposes we recommend to fully align the proposed wording with the text from BEPS Action 6 in order to not restrict the activities that may be performed by pension funds.

- c) *As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?*

No comments.

- d) *As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognized pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?*

We note that the proposed wording departs from the text initially proposed under BEPS Action 6. For consistency purposes we recommend to fully align the proposed wording with the text from BEPS Action 6. This is particularly important as pension funds increasingly invest through intermediaries (such as CIVs) along with other types of investors, i.e. such intermediaries are not constituted and operated *exclusively* to invest funds for the benefit of pension funds. We therefore recommend adding back the phrase “almost exclusively” in subdivision ii) of the definition of “recognized pension fund”. Additionally, we suggest clarifying that “almost exclusively” means to cover situations where at least 75% of investors in the intermediary vehicle are recognized pension funds.

Furthermore, we believe that the requirement for an entity or arrangement acting as an intermediary for the benefit of a pension fund to be resident in the same state as that pension fund is too restrictive. For operational efficiency reasons such intermediary vehicles are often set up in well-established fund domicile countries while the pension funds investing through such intermediaries may be established elsewhere. We therefore suggest to delete the phrase “that are residents of the same State” from the proposed paragraph 10.8 to the Commentary on Article 3.

We would like to take the opportunity to reiterate our concerns about the wider issue of treaty entitlement of CIVs under BEPS Action 6. We strongly believe that widely-held funds present a low risk of tax evasion or avoidance and should

therefore be considered as residents of contracting states in which they are established for the purposes of accessing treaty benefits.

**Conclusion**

NN Investment Partners appreciates the opportunity to offer its views on the recently released discussion draft dealing with the treaty residence of the pension funds. Please do not hesitate to contact Nenad Ilic ([nenad.ilic@nnip.com](mailto:nenad.ilic@nnip.com)) should you have any additional questions.

Respectfully submitted,

NN Investment Partners,

A handwritten signature in blue ink, consisting of a stylized 'N' followed by a horizontal line and a diagonal stroke.

Nenad Ilic  
Senior Tax Specialist

**To:**  
**Tax Treaties, Transfer Pricing and Financial**  
**Transactions Division**  
**OECD/CTPA**

Sent via e-mail: [taxtreaties@oecd.org](mailto:taxtreaties@oecd.org)

01 April 2016

Dear Sirs,

**PUBLIC DISCUSSION DRAFT – TREATY RESIDENCE OF PENSION FUNDS**

PensionsEurope<sup>1</sup> and EFAMA<sup>2</sup> are grateful for the opportunity to comment on the OECD Public Discussion Draft on changes to the OECD model tax convention concerning the treaty residence of pension funds. We agree with the aim of the discussion draft to ensure that a pension funds is considered to be a resident of the state in which it is constituted for the purposes of tax treaties.

**1. Questions raised by Working Party 1 on Tax Conventions and Related Questions**

In the following PensionsEurope and EFAMA are happy to answer the questions raised by Working Party 1 on Tax Conventions and Related Questions in the course of above mentioned Public Discussion Draft:

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<sup>1</sup> PensionsEurope represents national associations of pension funds and similar institutions for workplace pensions. Some members operate purely individual pension schemes. PensionsEurope has 24 member associations in EU Member States and other European countries with significant – in size and relevance – workplace pension systems<sup>1</sup>. Through its Member Associations PensionsEurope represents around € 3.5 trillion of assets managed for future pension payments. For more information about PensionsEurope, please visit [www.pensionseurope.eu](http://www.pensionseurope.eu)

<sup>2</sup> EFAMA is the representative association for the European investment management industry. EFAMA represents through its 26 member associations and 61 corporate members EUR 21 trillion in assets under management of which EUR 12.6 trillion managed by 56,000 investment funds at end 2015. Just over 30,000 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 25,900 funds composed of AIFs (Alternative Investment Funds). For more information about EFAMA, please visit [www.efama.org](http://www.efama.org)

- a.) As regards the phrase “that is treated as a separate person under the taxation laws of that State” included in the definition of “recognised pension fund” in proposed Art. 3(1) j): Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?**

Although this is already mentioned in the OECD commentaries on article 4 we believe that the definition proposed in article 3 (1) j) should expressly mention that a “recognized pension fund” will cover an entity irrespective of the fact that this entity is generally exempt from income taxation in that Contracting State.

In addition, we have some concerns regarding the wording “that is treated as a separate person under the taxation laws of that state”. A clarification should be added stating that contractual trust arrangements, notwithstanding not constituting a separate legal person, will meet the definition of “recognized pension scheme” if these are established by an employer or employers to hold assets set aside to fund the employers’ sponsored pension plans (e.g. occupational pension scheme, defined benefit pension scheme, etc.). Besides, some countries (e.g. Luxemburg) have pension funds that are part of the state itself and therefore public establishments. As a result these funds might not be treated as separate persons under national tax law. In the UK, the most common form of defined contribution pension funds are in the form of contractual arrangements within insurance companies. Those companies are subject to a special pensions tax regime only in relation to that part of their business (which is treated as a Registered Pension Scheme), but the pensions business is not considered a separate person for tax purposes.

The rationale for requiring a recognised pension fund to be a separate person for tax is to distinguish recognised pension funds that are entitled to treaty benefits from fiscally transparent entities that are not themselves persons under the treaty.

The definition should be extended to include pension funds that are **part of a** separate person under the taxation laws of that State, **or of the State itself**.

Besides, the term recognized pension fund should also comprise tax transparent pension funds where only the pension funds (or the management company) according to their home country are allowed to make claims on behalf of the investors/employees (compare 6.28-6.30 OECD CIV report, 2010).

- b.) As regards the phrase “that is constituted and operated exclusively to administer or provide retirement or similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j): Is the word “exclusively” too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to “retirement benefits” but also to “similar benefits”?**

We noticed that the scope of pension funds covered by the BEPS 6 final report referred to entities providing “exclusively or almost exclusively” retirement benefits, while the discussion draft only refers to the exclusive purpose of providing such benefits. We believe that the initial wording should be kept.

The word “exclusively” could be too restrictive and we would therefore suggest using the wording of “exclusively or almost exclusively”: *“that is constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits”*.

This addition would guarantee that a fund should be a recognised pension funds when the purpose is to administer or provide retirement or similar benefits, while other activities would be allowed and subordinated to the main activity of retirement provision.

- c.) As regards the phrase “similar benefits” included in subdivision i) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Are there examples of “benefits” that are typically granted by pension funds that would not be covered by the phrase “similar benefits”? If yes, please describe these benefits?

The benefits offered to pensioners and / or workers can be broad; the main requirement is that it can be regarded as “a pension arrangement”.

Pension funds may perform activities outside the strict scope of their main purpose of administering or providing retirement benefits, and such activities are often relatively small in size compared to the main activity of providing retirement benefits. The addition of the term “almost exclusively” would provide for proper scope to capture the majority of the pension funds that currently exist. The addition of “almost exclusively” would also ensure that pension funds should only fall within the scope of the definition of a recognized pension fund if the primary purpose is indeed to administer or provide retirement or similar benefits, whereby only activities that would be relatively small in size and clearly subordinated to the main activity of providing retirement benefits would be permissible.

Considering that the definition is intended to cover many different forms of pension funds, the term “similar benefits” should be interpreted broadly. In relation to paragraph 10.5 of the draft Commentary, we suggest to replace to term “invalidity” as mentioned in the final sentence of this paragraph by the term “disability”. The term disability may be considered more appropriate to address the consequences of impairments of a physical or mental nature.

- d.) As regards the phrase “that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements” included in subdivision ii) of the definition of “recognised pension fund” in proposed Art. 3(1) j):** Is the word “exclusively” too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

We are of the opinion that the word “exclusively” is too restrictive.

We support the recognition of the OECD that also investment vehicles that are wholly owned entities or arrangements of more than one recognized pension funds are covered by the OECD comments in 10.8. Pension funds often invest together with other pension funds pooling their assets in certain arrangements or entities, or may for example invest via wholly owned entities or arrangements for commercial, legal or regulatory reasons.

However, we disagree with stating 10.8 that pension funds “invest via wholly owned entities or arrangements that are residents of the same State”. If our reading is correct the requirement “that are residents of the same State” means that the investment vehicles and arrangements and the investing pension funds are residents of the same State. This would imply great practical disadvantages, as those (wholly owned) vehicles are not always residents of the same State as the investing pension funds (i.e. German pension funds investing in an investment structure in Luxembourg).

Thus we suggest to delete “that are residents of the same State” from the wording of 10.8. The intermediary may invest funds on behalf of resident and non-resident funds and should not be restricted to an entity that is resident in the same state as the pension fund.

We would therefore propose the following wording:

“(ii) that is constituted and operated exclusively **or almost exclusively** to invest funds for the benefit of entities or arrangements **either** referred to in subdivision i) **or resident in another States that has equivalent benefits and fulfills the requirements provided in subdivision i)**”

## 2. Additional comments regarding the treaty entitlement of pension funds

### The reciprocal recognition of pension funds

The reciprocal recognition of pension funds is an important objective not only at EU-level, to which we referred to in PensionsEurope’s draft “*position paper on the withholding tax refund barriers to cross-border investment in the EU*”, March 2016) but also at OECD level.

### CIVs

In Europe, many pension funds invest through dedicated collective investment vehicles which are regulated, i.e. constituted under the European UCITS or AIF directives and authorised and controlled by Financial Market Regulators.

To make sure that CIVs will benefit from paragraph 10.8, we would suggest adding the following words to Paragraph 10.8:

“Pension funds (...) often invest via wholly owned entities or arrangements, such as Collective Investment Vehicles, that are resident of/ are regulated by/ the same State as the pension fund or a

State that has signed a tax treaty (including a non-discriminatory clause) with the Pension fund's state of residence".

## **Non-CIVs**

We welcome the OECD's recognition of the economic importance of non-CIV funds and the need to ensure that treaty benefits be granted where appropriate (see BEPS Action 6). Our main concern for non-CIV investments is that non-CIV's themselves will not be able to claim treaty benefits under the LOB and PPT provisions (even if a derivative benefits test is introduced, this will remain an issue due to the different types of investors and/or number of investors in these funds. For indirect (fund) investments, this would result in a higher tax burden which ultimately impacts the pension benefits. In addition, third country wholly owned vehicles (SPVs) or joint-venture vehicles may also not be able to claim treaty benefits. Pension funds should not become the unintended victims of disallowing treaty benefits to non-CIVs. In this respect, we suggested that a look-through provision could be introduced as a result of which income derived by a pension fund through an intermediate (non-CIV) fund should be subject to the withholding tax rate that would have applied to the pension fund in case of a direct investment.

### **The limitation on Benefits" (LOB) clause for pension funds**

We noticed that a couple of treaties that became recently effective include a "Limitation on Benefits" (LOB) clause for pension funds (e.g. Germany – France, Netherlands – Germany). As a result a certain percentage of pension holders / retirees are required to be resident of either contracting state. In this respect, we believe that pension funds qualifying as "recognized pension funds" should automatically be granted treaty access without regard to the residence of their investors.

A LOB clause not only leaves too much flexibility to contracting states during their bilateral negotiations as to the conditions under which pension funds can qualify for treaty benefits, but is also setting conditions which may be difficult to comply with in practice. This leads to high compliance costs for the pension funds, delays in accessing treaty reliefs as well as to legal uncertainties.

It is essential that the small investors are encouraged to make appropriate provision through pension funding arrangements to obtain the necessary long term financial security for workers into their retirement years. The massive global pension under-provisioning (including the underfunding by governments of basic social welfare pensions) has been well documented and cannot afford to be ignored. It is crucial that their role is not lost in the treaty debate.

Significantly, US Foreign Account Tax Compliance Act and related Intergovernmental Agreements and the Common Reporting Standard have given them appropriate "deemed compliant" status. The BEPS Action 6 agenda should follow that lead and recognize Pension Funds as qualifying residents in their home jurisdiction (country of establishment), without restriction under LoB or Principal Purpose Test.

In addition, it has to be kept in mind that most of the treaties provide for treaty relief for individuals, if resident in European or third countries. In rare circumstances where the actual tax residence of the ultimate beneficial owners is known by the investment fund, the industry can see that most of them would qualify as "equivalent beneficiaries". Thus looking through the chain of ownership would hardly bring any additional certainty and revenue to the tax authorities. For the pension fund industry, however, the costs of implementing any look-through is likely to be huge and has the



potential to change the entire business model at a significant cost that ultimately will be passed on to investors.

We would also highly recommend that the multilateral instrument of BEPS Action 15 should not contain a LOB clause due to the reasons mentioned above. A wider adoption of an LOB approach would just mean more cases where the lack of data about underlying beneficial owners is problematic.

We are grateful in advance for your attention to the concerns expressed in this letter and we welcome the opportunity to discuss these with you. In case there is any additional information that we can provide, please contact PensionsEurope at [info@pensionseurope.eu](mailto:info@pensionseurope.eu) or +32 (0) 2 289 14 14 and EFAMA at [info@efama.org](mailto:info@efama.org) or +32 (0) 2 513 39 69.

Kind regards,

**Matti LEPPÄLÄ**  
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1 April 2016

Dear sir/ madam,

***BEPS Discussion Draft: Treaty Residence of Pension Funds***

PricewaterhouseCoopers International Limited (PwC) welcomes the opportunity to comment on the OECD's *Public Discussion Draft on the Treaty Residence of Pension Funds*.

We commend the Working Party for its efforts to date in reaching agreement over many of the recommendations. We set out in this document our concerns over some areas and our responses to the OECD's specific questions.

We appreciate your consideration of our comments on the Discussion Draft and we would be pleased to assist the OECD further in its efforts in this area.

The response in the pages that follow reflects the views of the PwC network of firms.

**Overview comments on the Discussion Draft**

We recognise the OECD's endorsement of the explicit recognition of pension funds as tax treaty residents and greatly appreciate that the draft Commentary now formalises a lot of what is current practice by acknowledging that most states already view such entities as residents for purposes of the Model Tax Convention.

It is important in some circumstances that a recognised pension fund is considered 'liable to tax', even if it benefits from an exemption from corporate income tax. The OECD could make this even clearer in the Commentary beyond saying that "In many States, a person is considered liable to comprehensive taxation even if the Contracting State does not in fact impose tax".

It is important to note the potential for double taxation for pension funds and pension beneficiaries, so a reciprocal exemption from source taxation for pension funds should also be considered.

We note that it is also important to recognise certain pension business written by life insurance companies as able to benefit from reliefs and exemptions available to pension funds. It is important that the drafting does not inadvertently impact on the status quo in this regard.

### **Treatment as a separate person**

The form of entity or arrangement which constitutes a pension fund for the purposes of the Model Tax Convention should include, under the laws of a state, any legal framework for establishing a procedure that is treated as a person for tax purposes. In a particular state that could include the trustees of a trust, a body which may include beneficiaries, a contractual arrangement, sponsors or others potentially regarded as owners or stakeholders. We note that the Discussion Draft states that “Consultation with stakeholders will be necessary to ensure that the definition and its Commentary cover the main forms of pension funds that currently exist” and, in that regard, the status quo for the life insurance companies with pension business that currently qualify will need to be maintained. Such pension business is a separate contractual arrangement which is regulated and which is part of that insurance company. We refer for example to the competent authority agreement between the United States and the United Kingdom qualifying it as a pension scheme pursuant to the UK-US double tax treaty.

The current wording of Article 3 and Article 4 of the Model Tax Convention and Article 3 of the 2016 US Model Tax Convention do not require the existence of a separate person and the addition of the words ‘treated as a separate person’ potentially puts at risk qualification under the legal frameworks of some states. It is sufficient that the entity or arrangement is recognised within the context of the taxation laws of the state.

### **Retirement or similar benefits an exclusive purpose**

The discussion draft posed two questions that appears to be closely related. The first is as regards the purpose of the fund having to relate to the provision or administration of retirement or similar benefits. The second is that the purpose is the exclusive reason it was constituted or operates. There is also a connected point about the fund having to be regulated as such.

A recognised pension fund should be constituted, and required to operate, essentially with the purpose of providing retirement or similar benefits. But it does not seem necessary for this to be an exclusive purpose such that, as is relatively common, such funds cannot carry out relatively small activities that would not be described as similar to retirement often serve a social or public purpose.

A number of states currently allow for some leeway in the activities that can be performed by pension funds through an ‘exclusively or almost exclusively’ test. This was also the wording used in paragraphs 12 and 13 of the final version of the Report on Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances), which was presented to the G20 in October 2015, as regards the follow-up work required. We also refer to the 2016 US Model Tax Convention which contains ‘exclusively or almost exclusively’ in the activities test for pension funds.

Activities that may be performed by pension funds that may or may not be considered similar to providing retirement benefits might include, for example, certain health products (such as screening), financial advice (such as in relation to savings) or certain housing-related benefits (such as mortgage advice). Australia, for example, legislated criteria which allow superannuation funds to release accumulated benefits to members facing conditions of financial hardship. If it were decided necessary for the arrangement to be exclusively for the provision or administration of retirement or similar benefits, it would be critical for the description of what is similar to include these examples and a description of the nature of other benefits now existing or which might be created in future.



Having discussed the purposes of the fund, the additional reference to the fund being “regulated as such by that state or one of its political subdivisions or local authorities” could be problematic. Removal of the words ‘as such’ would still be sufficient to refer to adequate regulation of a fund’s pension arrangements. An example of this would be where a state-owned fund had appropriate constitutional review.

#### **Inclusion of entities or arrangements exclusively to invest funds for recognised pension funds**

Pension funds often pool their invested monies in certain joint arrangements or entities and it is appropriate to treat these investment intermediaries in the same way as the pension funds that invest through them.

It is also common for pension funds to invest via wholly-owned entities or arrangements for commercial, legal or regulatory reasons. There does not seem to be any particular reason for such arrangements to have to be within the same state and this is not mentioned in relation to the pooling of monies by pension funds. In some cases, where a pension is investing through a wholly-owned subsidiary, it may be advisable to establish the subsidiary in the same jurisdiction as the situs of the investment as a local entity may have more ready access to the courts should litigation develop. In other cases, a third jurisdiction may sometimes be used because the third jurisdiction has strong creditor protections.

The exclusivity of the arrangements to investment of monies for recognised pension funds and not for wider investment intermediaries seems in keeping with the treatment of the funds themselves.

We hope that the comments we make above are helpful to the Working Party and we remain available to provide any assistance that the OECD may require.

Yours faithfully,

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