Mexico City, April 22, 2016

Via email

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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 consultation document on issues and suggestions on the tax treaty entitlement of non-CIV (Collective Investment Vehicle) funds. Comments appear in *italics* following the questions.

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

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

We suggest following Australia's "widely held rules" for Managed Investment Trusts which state, for instance, that if one of the criteria below is satisfied, the fund should be deemed widely held:

- *The fund is listed on an approved market stock exchange;*
- *The fund has at least 50 members; or,*
- *One or more specified 'widely held' entities together hold more than 25% of the participation interests in the fund, and no other type of single entity holds more that 60% of the 'participation interests' in the fund.*

2. What types of regulatory frameworks would be acceptable in order to conclude that a fund is "regulated" for the purposes of such a proposal?

The AIFMD was aimed to increase investor's protection and reduce systemic risk by establishing a harmonized regulatory framework in the European Union for Alternative Investment Funds managers. These provisions include:

risk management requirements, depositary requirements, compensation requirements and prudential capital requirements.

This regulatory framework results applicable when managing or marketing alternative funds in or from the European Union, regardless of the fund's domicile and involves disclosure, transparency and private equity requirements, among others.

Therefore, we believe that any type of regulatory framework that contains disclosure provisions, transparency and private equity requirements that are substantially similar to those included in the Alternative Investment Fund Managers Directive (AIFMD) should be acceptable in order to conclude that a fund is "regulated".

Other regulatory frameworks that would be acceptable to conclude that a fund is "regulated" for the purposes of such a proposal could be the following:

- *Genuine diversity of ownership principle*
- *UCITS Directive*
- *CB UCITS Regulations in Ireland*
- *REITs Regulatory Framework in the US, Singapore, etc.*
- *ASEAN CIS fund passport mechanism*
- *Regulation of managed investment schemes in Australia*
- *Hong Kong/China mutual fund recognition platform*
- *Etc.*

For instance, would these include the types of regulatory requirements described in paragraph 16 of the 2010 CIV report (i.e. "regulatory requirements relating to concentration of investments, restricting a CIV's ability to acquire a controlling interest in a company, prohibiting or restricting certain types of investments, and limiting the use of leverage by the CIV") as well as disclosure requirements relating to distribution of interests (e.g. "know your customer" rules)?

Yes

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

It is worth mentioning that investors are usually not motivated by tax-driven reasons when deciding to invest in non-CIVs. Their main driver is usually to diversify risk across international markets and benefit from reduced costs and

economies of scale as well as the market experience of professional managed funds. These non-tax reasons generally outweigh any tax-motivated purpose.

Moreover, a significant ratio of non-CIVs' investors are institutional investors that are resident in treaty countries and usually tax exempt.

In order to address treaty-shopping concerns we recommend setting a threshold of ownership by equivalent beneficiaries. The threshold could be established and agreed to in each treaty (e.g., ranging between 80% and 90%).

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

Investors in a non-CIV are usually in for long-term investments, such as in pension funds; therefore, we believe that mandatory distribution requirements for a fund to be eligible for the proposed exception would not be feasible. However, we believe that since non-tax reasons generally outweigh any tax-motivated purpose in these types of investments, a bona fide clause should be set in place.

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

By incorporating more requirements for a non-CIV to qualify for the exemption, such as "widely held rules" and being subject to an AIFMD-like regulatory framework. Incorporating a "Bona fide clause" could also be helpful.

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

No comment.

NON-CIV FUNDS SET UP AS TRANSPARENT ENTITIES

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

Considering that regulated non-CIVs must meet disclosure provisions and transparency requirements, and considering the global trend to adopt anti-laundering provisions and "know your customer" rules, we believe that there should not be material problems that could prevent the application of the new transparent entity provision.

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

Questions related to certain aspects of the proposal

8. The rationale that was given for the above proposal refers to the fact that "investors in Alternative Funds are primarily institutional investors, and are often entitled to benefits that are at least as good as the benefits that might be claimed by the Alternative Fund". What is the meaning of "institutional investors" in that context?

We deem fit to define institutional investors as non-bank persons or organizations that trade securities in large enough share quantities. Examples of "institutional investors" could be the following: public and private pensions, retirement plans, insurance companies, university endowment funds, health care endowment funds, sovereign wealth funds and charitable investment funds, among others. It is worth mentioning that these represent the primary investors in non-CIV funds.

In particular, does it include taxable entities or other non-CIVs? Absent a clear definition of "institutional investors", how can it be concluded that institutional investors "are often entitled to benefits that are at least as good as the benefits that

might be claimed by the Alternative Fund"? Also, is it suggested that "institutional investors" are less likely to engage in treaty-shopping and, if yes, why?

Yes, since their non-tax reasons generally outweigh any tax-motivated purpose.

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

The main types of non-CIV Funds are Alternative Investment Funds, Real Estate Investment Trusts, Sovereign Wealth Funds, pension funds, private equity funds, hedge funds, among others.

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

No comment.

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

Making investments to diversify risk across international markets and benefit from reduced costs and economies of scale.

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

By meeting rules similar to the genuine diversity of ownership condition (GDO).

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

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

No comment.

14. How would the proposal address the concern, expressed by some commentators, that many non-CIV funds would be unable to determine who their

ultimate beneficial owners are and, therefore, would not know the treaty residence and tax status of these beneficial owners?

No comment.

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

No comment.

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

No comment.

Questions related to the prevention of treaty-shopping

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

Consideration should be given to including a subject-to-tax test applicable for the beneficial owner.

18. The proposal would grant treaty benefits if a certain high percentage of a non-CIV is beneficially owned by investors entitled to similar or better benefits. Even a percentage as high as 80% would leave substantial room for treaty-shopping as a

20% participation in a very large fund could represent a significant investment. How could this concern be addressed?

Consideration should be given to providing treaty benefits solely to the investors that are deemed equivalent beneficiaries (without the need of establishing an ownership threshold).

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

No comment.

Questions related to the prevention of deferral

20. According to the proposal, acceptable ultimate beneficial owners would include persons who would "include their proportionate share of the fund's income on a current basis". How would a State of source be able to determine when this requirement is met?

By including a subject-to-tax test (i.e., a sworn statement by the legal representative).

Also, what would be considered an acceptable anti-deferral regime? In particular, would a regime under which a taxpayer is taxed on a deemed amount of income or deemed return on investment be considered as an anti-deferral regime even if the amount that is taxed is significantly lower than the actual return? Would the United States PFIC regime be an example of an acceptable anti-deferral regime?

No comment.

21. As regards the application of the proposal in the case of indirect ownership, who will be tested in relation to the condition that an ultimate owner is either tax exempt or taxed on a current basis?

The beneficial owner.

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

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

We believe that this provision should be removed and solely rely on the equivalent beneficiaries test.

SUGGESTION THAT A "SUBSTANTIAL CONNECTION" APPROACH BE ADOPTED

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

No comment.

SUGGESTION OF A "GLOBAL STREAMED FUND" REGIME

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

- Whether the approach would create difficulties for non-CIV funds that do not currently distribute all their income on a current basis?
- Whether the approach would create difficulties for non-CIV funds that cannot, for various reasons, determine who their investors are?

- Whether the suggestion that tax on distributions be collected by the State of residence and remitted to the State of source would create legal and practical difficulties?
- What should be the consequences if, after a payment is made to a GSF, it is subsequently discovered that the fund did not meet the requirements for qualifying as a GSF or did not distribute 100% of its income on a current basis?

No comment.

ADDITIONAL EXAMPLES FOR THE COMMENTARY ON THE PPT RULE

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

No comment.

CONCERNS WITH RESPECT TO CONDUIT ARRANGEMENTS

26. Commentators who share the concern described above in relation to conduit arrangements are invited to provide one or more examples where the PPT rule could apply to legitimate types of arrangements that are commonly entered into by non-CIV funds because these could be seen as conduit arrangements in the light of the examples already included in paragraph 19 of the Commentary on the PPT rule included in paragraph 26 of the Report. These examples should be brief and should focus on common transactions that do not raise concerns related to treaty-shopping or inappropriate granting of treaty benefits.

No comment.

CONCERNS RELATED TO THE "SPECIAL TAX REGIMES" PROPOSAL

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

No comment.

OTHER SUGGESTIONS

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

No comment.

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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 of comments you may have.

Sincerely,

IFA Grupo Mexicano, A.C.