

## BEPS: Eliminate Double Non-Taxation Without Impeding Cross-Border Investment

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BlackRock supports the international community's attempt to curb aggressive tax planning. However, we are concerned that this Economic Co-operation and Development (OECD) project, called Base Erosion and Profit Shifting (BEPS), will have inadvertent consequences that in the long run will prove damaging to economic growth. In this *ViewPoint*, we explain the impact of the newly proposed rules and suggest recommendations consistent with the BEPS project's main goals while minimizing potentially adverse side effects.

*...many of the BEPS proposals will inadvertently affect cross-border investment flows, impacting both the ability for capital markets to contribute to economic growth and the investment opportunities of end-investors.*

The goal of the BEPS project is "to create a single set of consensus-based international tax rules to address BEPS, and hence to protect tax bases while offering increased certainty and predictability to taxpayers."<sup>1</sup> However, asset owners and asset managers<sup>2</sup> are concerned that many of the BEPS proposals will inadvertently affect cross-border investment flows, impacting both the ability for capital markets to contribute to economic growth and the investment opportunities of end-investors. Assuming the current BEPS proposals are not modified to address commingled investment vehicles (i.e. mainstream and alternative funds), the outcome would contradict the OECD's mission of encouraging cross-border investment and BEPS's stated goal of eliminating double non-taxation<sup>4</sup> while not creating new rules that "result in double taxation, unwarranted compliance burdens or restrictions to legitimate cross-border activity."<sup>5</sup>

Commingled investment vehicles perform an increasingly important role in capital formation and allocation. They provide non-bank finance on a long-term basis by matching the investment needs of asset owners with companies and projects seeking capital. As currently proposed, funds making cross-border investments, such as mainstream funds (e.g. mutual funds and UCITS), which the OECD refers to as 'collective investment vehicles', and alternative funds (e.g. the EU's Alternative Investment Funds and the proposed European Long Term Investment Funds) will be significantly impacted by the BEPS project.<sup>6</sup> Funds investing in infrastructure, renewable energy, real estate, and other real assets as well as private equity and venture capital funds are likely to be hit hardest.

### BLACKROCK RECOMMENDATIONS

1. Maintain the principle of tax neutrality between direct and indirect investing through commingled investment vehicles
2. Link the three OECD global tax transparency initiatives (BEPS, CRS and TRACE) impacting cross-border investment
3. Build on the OECD 2010 CIV Report and the TRACE project to address mainstream funds
4. Engage with asset owners and alternative fund managers to address issues associated with cross-border investments in alternative asset classes. We detail 4 specific suggestions to provide short-term and long-term solutions for alternative funds.

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These unintended consequences of BEPS appear to counter efforts to stimulate market finance, including the European's Commission's initiative for a European Capital Markets Union and the OECD's initiative on Institutional Investors and Long-Term Investment to promote private investment in infrastructure projects.<sup>7</sup>

The BEPS project is to be completed in 2015, which makes this an urgent matter to be addressed. Given the cross-border nature of the issues raised by BEPS, national solutions implemented after the BEPS recommendations have been finalized will result in differing and conflicting measures across markets which will impact cross-border investment and lead to double taxation and market inefficiencies. Recognizing the complexity of the issues and the importance of the BEPS project, we recommend a series of solutions to reinforce the international tax framework without undermining capital flows. In the Appendices, we describe the effect BEPS may have on mainstream and alternative funds, and provide a detailed analysis of the OECD proposals to date together with a glossary of key terms.

### Unintended Consequences

- ▶ Reduction of capital flows to investment projects, companies and governments
- ▶ Reduced investment choice and returns for savers and end-investors as funds become less attractive
- ▶ Pricing volatility in certain asset classes where significant private investment is sought
- ▶ National fragmentation of funds

### Background

In July 2013, the G20 governments agreed that multinational enterprises were using aggressive cross-border tax planning strategies resulting in double non-taxation (i.e. zero or reduced taxation in the source country, even where the recipient is not taxed in its residence country) and therefore asked the OECD to develop new international tax standards to tighten the international tax regime. The BEPS program consists of the 15 Actions listed in Figure 1.

In September 2014, the OECD published recommendations on seven of the 15 Actions, and the remaining recommendations are due by December 2015. Forty four countries are contributing to the BEPS initiative (all of the OECD and G20 countries) and the recommendations released generally represent a consensus view across participating countries. Although multinational enterprises are the primary targets of these Actions, commingled investment funds are implicated because of the cross-border nature of both asset owners and fund investments. Appendix B on page 5 contains a detailed analysis of the implications of the BEPS Actions on both mainstream and alternative funds.

The OECD had started considering the international tax treatment of funds well in advance of BEPS – not, however, because investment funds raised particular tax avoidance concerns. Three funds-related OECD work streams are described below:

- ▶ In 2010, the OECD published a report on Collective Investment Vehicles ((CIVs), i.e. mainstream funds) which sought to better define and improve the tax treaty entitlement of mainstream funds. The OECD 2010 CIV Report<sup>8</sup> offered countries various options of model treaty provisions to choose from in addressing CIVs in their bilateral tax treaties. This optionality has led, however, to divergences in practices between countries.
- ▶ Consequently, the OECD decided to develop such work via the Tax Relief and Compliance Enhancement (TRACE) Project, which had first started in 2006.<sup>9</sup> The 2013 TRACE report recommended that countries implement a system to allow intermediaries to claim treaty benefits on behalf of investors on a 'pooled' basis. It also required intermediaries to report beneficial owner information directly to source countries.<sup>10</sup>
- ▶ The third OECD work stream which touches fund investors is the Automatic Exchange of Information (AEOI) initiative.<sup>11</sup> In July 2014, the OECD published Common Reporting Standards (CRS) for AEOI to provide that countries obtain tax information from their financial institutions and automatically exchange it with other jurisdictions (so far, 51 jurisdictions will adopt). The CRS are of particular relevance to financial institutions as, once enacted into national laws, they set out a regime for financial institutions resident in a signatory country to provide information on cross-border accounts to their residing tax authority.

### Figure 1: THE 15 ACTIONS OF THE BEPS PROJECT

- |           |   |
|-----------|---|
| Action 1  | Address the challenge of the digital economy  |
| Action 2  | Neutralize the effects of hybrid mismatch arrangements  |
| Action 3  | Strengthen Controlled Foreign Corporation rules   |
| Action 4  | Limit base erosion via interest deductions  |
| Action 5  | Counter harmful tax practices more effectively, taking into account transparency and substance      |
| Action 6  | Prevent treaty abuse  |
| Action 7  | Prevent the artificial avoidance of Permanent Establishment status                                  |
| Action 8  | Assure that transfer pricing outcomes are in line with value creation: Intangibles                  |
| Action 9  | Assure that transfer pricing outcomes are in line with value creation: Risk and capital             |
| Action 10 | Assure that transfer pricing outcomes are in line with value creation: Other high risk transactions |
| Action 11 | Collect and analyze data on BEPS  |
| Action 12 | Disclosure of aggressive tax planning   |
| Action 13 | Re-examine transfer pricing documentation   |
| Action 14 | Make dispute resolution mechanisms more effective   |
| Action 15 | Develop a multilateral instrument   |

## Key Recommendations to Eliminate Double Non-Taxation without Impeding Cross-Border Investment

### **BlackRock recommends that the longstanding principle of tax neutrality between direct and indirect investing through commingled investment vehicles be maintained.**

The G20's mandate to the OECD was not driven by international tax issues of double non-taxation arising from commingled investment vehicles. Thus, the BEPS Actions should not result in unintended consequences to commingled investment vehicles and asset owners.

**We recommend that policy makers seize the unique opportunity to link all three OECD global tax transparency initiatives impacting cross-border investment.** BEPS, CRS and TRACE<sup>12</sup> each contain important rules that address commingled investment vehicles. Combining these initiatives would facilitate the development of solutions that meet the objectives of policy makers whilst retaining the viability of commingled investment funds for a variety of asset classes.

**We recommend that policy makers build on the OECD 2010 CIV Report and the TRACE project to address mainstream funds.** The enhanced level of investor data provided by these OECD tax transparency initiatives can be used to define a framework for globally consistent reporting to both source and residence countries.<sup>13</sup> By using this data, policy makers could develop an administrable tax reporting platform in which mainstream vehicles can raise and invest capital cross-border such that source countries would only apply withholding at source where fund investor information does not conform to global standards. Such a framework would allow governments to tighten the appropriate collection of tax and significantly reduce government and private resources devoted to the process of tax withholding while maintaining the viability of cross-border investing.

**We recommend that the OECD engage with national governments, asset owners and alternative fund managers to address some fundamental policy issues associated with cross-border investments in alternative asset classes** (such as infrastructure, renewable energy and real estate). The OECD CIV 2010 Report explicitly excludes private equity funds, hedge funds, and trusts from the definition of 'CIVs' making it necessary to separately address alternative funds. In addition, as highlighted in Appendices A and B, alternative funds are impacted by a far larger number of the BEPS Actions resulting in more complex issues and a more severe impact on asset owners. We recommend four key deliverables to address the BEPS treatment of alternative funds:

1. Well-crafted OECD commentary and examples to guide source countries in how to apply the proposed Principle Purpose Test<sup>14</sup> (PPT) for tax treaty access by alternative funds.

2. A 'qualified investment fund' approach with the presumption that funds meeting defined criteria have not been created for the purpose of tax avoidance. Using this approach it would still be open for tax authorities to challenge abusive structures or transactions.
3. Effective transparency whereby underlying taxation within alternative funds is driven by the identity and nature of the end-investor. Providing such transparency to governments must be consistent and administrable by the industry.
4. A comprehensive solution to address the multiple issues raised by the various BEPS Actions (such as Treaty Relief, Hybrid Mismatches, Interest Deductibility and Transfer Pricing Documentation). This comprehensive solution must be workable for fund investors and provide comfort to tax authorities that appropriate taxes are being paid in the source country and the countries in which the investors are resident. As with mainstream funds, we believe this can be achieved by taking advantage of the vastly increased available investor data, enabling a package that both facilitates investment flows and combats tax avoidance and evasion.

BlackRock understands that the complexity of the BEPS project makes it challenging to develop a comprehensive solution in the available time. We firmly believe, however, that short-term solutions that avoid the unintended consequences on alternative funds are realistic, including guidelines from the OECD on how to apply the PPT clause and the 'qualified investment fund' approach detailed above. With regards to mainstream funds, we recommend that governments create a consistent investor tax reporting platform by taking advantage of the other international tax initiatives, such as TRACE.

The data flows created by CRS, TRACE and the US's FATCA make more holistic solutions feasible for both mainstream and alternative funds. To provide tax certainty to fund investors and minimize undue tax friction between investing directly or via commingled investment vehicles, we support the creation of a multilateral instrument, as outlined in Action 15 (see Figure 1), if it provides a holistic solution for all commingled investment vehicles.

## Conclusion

Fund investors value certainty. We are concerned that the tax uncertainties associated with BEPS, for both mainstream and alternative funds, will negatively impact the allocation of capital. Larger investors may be forced away from investing in commingled investment funds and towards direct investing and thus achieve less diversification. Smaller investors may not be able to make cross-border investments at all if the tax efficiencies caused by BEPS make investing in funds unattractive.

Unless there is direct relief from BEPS's unintended impact on funds, we believe serious consequences will follow:

- ▶ Reduction of capital flows to investment projects, companies and governments;
- ▶ Reduced investment choice and returns for savers and end-investors as funds become less attractive;
- ▶ Pricing volatility in certain asset classes where significant private investment is sought; and
- ▶ National fragmentation of funds.

BlackRock appreciates the attention given by the OECD and member governments to cross-border investment issues following the release of the initial discussion drafts. A great deal of detailed work is still needed, however, to address the important issues outstanding for fund investors and governments. We encourage the OECD to actively engage with both asset owners and asset managers to develop short-term and long-term solutions that facilitate cross-border investing via commingled vehicles.

## APPENDIX A: Unintended Consequences on Commingled Investment Vehicles

### Mainstream Funds ('CIVs' as per the OECD 2010 Report)

Tax treaties are intended to reduce double taxation, but governments are increasingly concerned that they are being misused to create double non-taxation. In the future, many tax treaties will state that they are not intended to facilitate double non-taxation, and will include rules that deny treaty benefits when obtaining those benefits was a principal purpose of the structure. These proposed changes to tax treaties are constructive, however, the issues presented where tax treaties are applied to investment funds are different and highly specialized. These must be specifically considered to avoid unintentional impacts on end-investors and cross-border investment flows.

Tax treaty access is important to funds as taxes incurred by funds are generally not recoverable or creditable by fund investors. BlackRock was encouraged by the recent Public Discussion Document "Follow-up Work on BEPS Action 6: Preventing Treaty Abuse" which suggests a path forward for mainstream funds.<sup>15</sup> We are hopeful that momentum is developing behind allowing treaty access for mainstream funds, and putting in place practical mechanisms to enable treaty benefits to be delivered to mainstream funds.

Some source countries have expressed concern that funds may enable income to be rolled up income tax-free and argue that in these circumstances tax treaty relief should be denied on the fund's income. Consequently, a growing number of residence countries require funds to provide investor tax reporting (information on the fund's income) so that their residents can be taxed on their share of the fund's income. If such data is not available, investors usually suffer some form of punitive taxation. Investor tax reporting is complex for residence countries, and exceedingly challenging for funds. Funds now have to meet multiple, significantly different, country reporting requirements as greater numbers of countries adopt reporting and this can vary enormously from country to country.

We recommend that governments consider creating a consistent investor tax reporting platform. Were standardized reporting available, more residence countries would be able to tax their residents on rolled up income, and the concerns of source countries would thereby be addressed. We believe this platform can be achieved by taking advantage of the vastly increased available investor tax data as a result of several other international taxation initiatives, including the OECD's CRS, which has also been adopted by the EU.

### Alternative Funds (or 'non-CIVs')

Alternative funds include funds investing in tangible assets such as infrastructure, renewable energy and real estate (such as AIFs and, in the future, ELTIFs). The need to encourage such market-based finance is acute in Europe, something which the EU is seeking to reinforce with the Capital Markets Union and the European Fund for Strategic Investments. However, the proposed BEPS framework will apply to alternative funds with difficulty.

Institutional investors such as retirement plans, insurance companies, sovereign wealth funds and endowments represent the primary investors in alternative funds. They are, typically, tax-exempt (or bear a reduced rate of tax) in their residence country. Where they invest directly, many bilateral treaties respect their tax-exempt status, and will often reduce or eliminate withholding and other taxes.

In addition to direct investment, institutional investors also frequently invest through alternative funds for a variety of non-tax reasons, including gaining access to certain asset classes, professional management, oversight and diversification or because of regulatory constraints. Alternative funds are frequently structured in a complex manner using multiple subsidiary entities for a wide variety of (non-tax) commercial reasons, making it essential that tax treaty access is preserved through complex structures. In the case of investment via a commingled vehicle, taxes incurred within the fund structure will *not* be recoverable in the jurisdiction of residence of these institutional investors since they generally bear no taxes in the first place.

Many governments recognize that investing via funds should not lead to a worse result for investors than investing directly (this is called the ‘tax neutrality’ principle) but, at the same time, are also seeking to avoid any softening for alternative funds for fear that this might allow their use for ‘treaty shopping’.<sup>16</sup> This, in reality, will rarely be the principal purpose of an alternative fund which invests pursuant to specified non-tax investment objectives (as explained in fund offering documents).<sup>17</sup> It is also true, however, that the fund structures involved have become increasingly more complex over time, mirroring the legal and geographic complexity of these investment projects and channeling end-investors’ capital in global markets. We recognize that it is challenging to achieve tax neutrality for a wider range of investors investing simultaneously through a single fund structure into assets located in many different countries. Perhaps this has tended to make the functioning of these structures less transparent to the tax authorities involved.

The impact of BEPS on the structures used to invest in real asset classes (infrastructure, real estate, etc.) is also more complex as a result of the broad scope of the overall BEPS project. Alternative funds will be impacted by more Actions than mainstream funds (for instance Actions 2, 4, 5, 6, 8 and 13) because they employ additional mechanisms such as

loan instruments and levered acquisition of assets, covered by various BEPS Actions, which mainstream funds do not use. While there may be room for source country tax authorities (i.e. where investments are located) to tailor the OECD framework, leaving implementation of BEPS for alternative funds to individual countries to work out as they apply anti-avoidance rules, as has been suggested by the OECD, is likely to result in piecemeal reform that will hurt both end-investors and economies.

As set forth in our Recommendations on page 3, in order to stay true to the tax neutrality principle, we suggest that alternative funds, whose overall purpose is to channel genuine investment flows on a cross-border basis, receive the protection of a ‘qualified investment fund’ regime, provided they meet a number of strong and objective criteria. In addition, other BEPS Actions affecting alternative funds need to be addressed holistically. Within this construct, our Recommendations do take into consideration the concerns of tax authorities, notably that any solution adopted should also provide greater transparency as to the identity of the fund investors in such structures, and comfort that the tax outcomes being achieved within the fund structures are appropriate.

## APPENDIX B: Detailed Analysis of the OECD Recommendations published in September 2014

Recommendations for seven of the 15 Actions were released in September 2014, and follow up discussion documents covering a number of the issues raised by the recommendations continue to be published. The following recommendations are of particular relevance to fund investors:

### Treaty Relief (Action 6)

Tax treaties are bilateral agreements between countries which are intended to facilitate cross-border flows in a fashion that respects the taxing rights of the countries while mitigating potential double taxation. In most instances, tax treaties provide for withholding tax rates lower than domestic withholding rates on items of income such as dividends, interest and certain capital gains. However, tax treaties have significant limitations in the context of commingled investment funds:

- ▶ Fund investors will often be residents of many different countries, and not tax resident in either the fund’s domicile or the source country, which does not fit well within the bilateral nature of a tax treaty.
- ▶ The definitions within tax treaties are often not sufficiently clear to ensure that funds (which are not typically themselves liable to tax) are entitled to the benefits of the tax treaty as they should be.

These problems were recognized in the OECD 2010 CIV Report. This Report acknowledged that it is appropriate that a mainstream fund based in the particular country should be given treaty benefits as a local resident. It also stated that funds should not insert an additional layer of taxation between investments and investors, and so the absence of taxability of the fund in principle should not prevent tax treaty access.

The current BEPS recommendation on treaty relief is to clarify that tax treaties are not intended to be used to generate double non-taxation and to propose to governments to include in tax treaties a Limitation of Benefits (LOB)<sup>18</sup> or Principle Purpose Test clause (or potentially both). However, either have the potential to deny treaty benefits to mainstream and alternative funds, and to their subsidiaries. Subsidiaries of alternative funds will generally fail the LOB clause – and the PPT clause may prevent ‘treaty shopping’ irrespective of whether or not it results in a reasonable outcome, given the identity of the investors and the taxing aspirations of the source country.

The OECD has signaled that it is willing to build on its 2010 CIV Report and the TRACE project to address treaty access for mainstream funds. An outline solution has largely been identified although its building blocks have yet to be defined for this to be operational. In addition, the discussion draft contains an optional suggestion that countries should consider making exceptions for mainstream funds, with little

guidance on how such relief should operate. This is significant because in practice, withholding tax relief at source has worsened since 2010. Many source country tax administrations have substantially eroded treaty benefits by imposing stringent administrative requirements upon mainstream funds that are often impossible to satisfy. Such actions have led to double taxation contrary to established treaty principles and rules.

**In terms of treaty relief for alternative funds, the OECD has indicated that it is willing to work with member countries and the industry to craft a solution. However, the BEPS timetable is challenging and significant commitment will be required from all participants to deliver a viable solution for these funds. This remains a significant concern for fund investors and cross-border investment flows.**

### Hybrid Mismatches (Action 2)

Central to BEPS is action on cross-border tax planning that either creates a deduction in one country without corresponding taxation of such income in another country, or a deduction for the same expense in two jurisdictions simultaneously. In order for alternative funds to transfer cash distributions to fund investors more effectively, loan instruments are frequently used (for non-tax reasons) that would be categorized under Action 2 as 'hybrid instruments'. Alternative funds use similar instruments to ensure that tax is not inappropriately paid at the fund level. This is driven by the principle of tax neutrality between commingled investment vehicles (both mainstream and alternative funds) and direct investment in the underlying assets. The Action 2 report recommends that hybrid mismatches used in this way would result in the loss of tax deductibility in the source country. This would penalize fund investment compared to direct investment, thereby countering the principle of tax neutrality.

### Transfer Pricing Documentation (Action 13)

Action 13 includes a new requirement for taxpayers, including related parties (where ownership exceeds 25%), to provide substantive intercompany pricing and other information to participating countries. Where this applies to funds (e.g., private equity or infrastructure) it will be difficult for alternative funds to comply and may also not, ultimately, be relevant to tax authority concerns.

### Multilateral Instrument (Action 15)

Recognizing that changes to individual tax treaties through bilateral negotiation would be extremely slow and, in the interim, unilateral adoption of BEPS recommendations, either by legislation or practice, could lead to greater double taxation, the OECD recommends that a multilateral instrument be created through which jurisdictions could modify pre-existing bilateral treaties on a single agreed basis. If adopted, this approach would expedite a more appropriate global response to the BEPS recommendations. We are supportive of a multilateral instrument *if* it provides a holistic solution for *both mainstream and alternative funds*. This would provide tax certainty to fund investors and minimize undue tax friction between investing directly or via commingled investment vehicles.

### Further Actions Expected

The recommendations for the other eight BEPS Actions (Actions 3, 4, 7, 8, 10, 11, 12 and 14) remain to be published through December 2015.

The preliminary Action 4 (limiting interest deductions) Public Discussion Draft was issued in December 2014. Action 4 has particular potential to impact alternative funds. Levered acquisition of assets, involving both external and shareholder debt, is common in tangible asset classes. The OECD recognizes that the global interest restriction rules proposed in the Public Discussion Draft sit badly with such funds holding such investments. It remains unclear how funds might be adequately accommodated. If Action 4 recommends that a taxpayer's global external interest expense be attributed to each source location (and / or otherwise capped), many institutional investors will be disadvantaged as they are likely to have little (or no) external debt. This contrasts with the ability of multinational enterprises to take on external debt and outbid alternative funds in acquisition contexts, thus creating an un-level playing field and market inefficiencies. This highlights the benefits of a comprehensive solution as opposed to patchwork 'fixes' for funds within each BEPS Action.

## RELATED CONTENT

[ViewPoint – The European Capital Markets Union: An Investor Perspective – February 2015](#)

[BlackRock and JP Morgan Chase co-signed letter to OECD consultation: "Follow-Up Work on BEPS Action 6: Prevent Treaty Abuse" – January 2015 \(page 123-146\)](#)

[Collective letter responding to the consultation: "Proposals with respect to the BEPS Action Plan, Including Action 6 \(Prevent Treaty Abuse\)" – April 2014 \(page 71-75\)](#)

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## Glossary

TERM	DEFINITION
<b>Alternative Fund</b>	For the purpose of this <i>ViewPoint</i> , any fund that is not a mainstream fund including those investing in real asset classes such as infrastructure, renewable energy, real estate, and other real assets. They also include private equity and venture capital funds.
<b>BEPS</b>	Base Erosion and Profit Shifting
<b>CIV</b>	Collective Investment Vehicle. They are called 'mainstream' investment funds for the purpose of this <i>ViewPoint</i> . Defined in the OECD CIV 2010 Report as "funds that are mainstream, hold a diversified portfolio of securities and are subject to investor-protection regulation in the country in which they are established". The term explicitly excluded private equity funds, hedge funds, trusts or other entities.
<b>Commingled Investment Vehicles</b>	Comprise of mainstream investment funds (so-called CIVs by the OECD) and alternative funds or non-CIVs, i.e. any fund that is not a CIV as defined in the OECD CIV 2010 Report.
<b>CRS</b>	Common Reporting Standards A key outcome from the OECD's Automatic Exchange of Information (AEOI) project. A standard regime (to be enacted in national laws) under which financial institutions resident in a signatory country must provide information on cross-border accounts of other signatory countries' residents to their local tax authority.
<b>Double Non-Taxation</b>	A reduction (or elimination) of tax in the source country (typically generated by tax treaty access) even where the income or gain is not subject to tax in the residence country (or elsewhere).
<b>FATCA</b>	Foreign Account Tax Compliance Act A US law which aims to improve information reporting on US taxpayers to prevent tax evasion. It requires foreign financial institutions, including CIVs and non-CIVs, to identify and declare US account holders, and withhold on certain payments to the US authorities. It covers US-domiciled funds held by non-US investors and non-US funds that invest in the US, as well as segregated accounts.
<b>Investor Tax Reporting</b>	Commingled Investment Vehicles generate income and gains on their investments. A growing number of countries mandate the reporting of such income and gains, on which they then tax their residents, and funds that do not provide such reporting may lead to penal taxation for residents of those countries.
<b>LOB</b>	Limitation of benefits constrain tax treaty access under BEPS. The US has addressed the need to define which entities should be entitled to treaty access by including within its tax treaties an LOB clause, which includes a detailed list of qualifying persons.
<b>OECD CIV 2010 Report</b>	Report issued by the OECD in 2010 entitled "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles". This Report sought to better define (and thereby improve) the tax treaty entitlement of CIVs. In practice, it worsened the position for CIVs as it offered little by way of agreed practical solutions, and ultimately led to the TRACE Project.
<b>PPT</b>	Principal Purpose Test necessary for tax treaty access under BEPS. By contrast with the US (which applies a LOB), many jurisdictions allow tax treaty access to a wide definition of residents, but have separate clauses that deny relief where it can be shown that a principal purpose of the structure was to obtain that relief.
<b>Residence Country</b>	The country where the person owning the asset is resident for tax purposes.
<b>Source Country</b>	The country where the asset generating the income or gain is located.
<b>Tax Treaties and Tax Treaty Relief</b>	Tax treaties are generally bilateral agreements between two countries, intended to encourage cross-border investment by residents of one country into the other. Tax treaty relief is the process whereby a resident of one country is granted a reduced level of taxation in a source country. For example, a source country might charge 30% withholding tax on dividend payments made by companies in that country under domestic law, but its tax treaty with the residence country might reduce this withholding tax to 15%.
<b>Tax Treaty Access</b>	Tax treaties are bilateral agreements between two states. They are intended to define and limit the level of taxation of a resident of one of the states on income or gains earned in the other state. Access to provisions of the tax treaty is essential in order to reduce double taxation on cross-border investment.
<b>TRACE</b>	Tax Relief and Compliance Enhancement Project Proposed form of authorised intermediary system for claiming withholding tax relief at source on portfolio investments. Seeks to reduce the administrative barriers that currently affect the ability of portfolio investors to effectively claim the reduced rates of withholding tax to which they are entitled pursuant to tax treaties or to domestic law of the country of investment.
<b>Treaty Shopping</b>	A resident of State A with an asset in State B might route the investment via State C if the tax treaty between States B and C is more favorable than that between States A and C.
<b>UCITS</b>	Undertakings for Collective Investment in Transferable Securities, as provided in EU law.
<b>Withholding Tax</b>	A source country tax levied on payments being made in respect of assets located in that country.

## Endnotes

1. OECD/G20Base Erosion and Profit Shifting Project, "Explanatory Statement: 2014 Deliverables". Available at: <http://www.oecd.org/tax/beps-2014-deliverables-explanatory-statement.pdf>
2. Asset owners include individuals, pension funds, insurers, sovereign wealth funds, foundations, endowments and family offices. They can manage their money directly and/or outsource this function to asset managers. Asset managers act as agent on behalf of their clients, the asset owner. We also refer to asset owners as end-investors in this *ViewPoint*. Asset managers are required to act as a fiduciary and invest according to the investment guidelines set out in the legal documentation of the mandate set out, or the product selected, by the asset owner.
3. Commingled investment vehicles comprise of both mainstream funds (which the OECD qualifies as 'collective investment vehicles') and alternative investment funds ('non-CIVs' in the OECD literature).
4. Double non-taxation is a reduction (or elimination) of tax in the source country (typically generated by tax treaty access) even where the income or gain is not subject to tax in the residence country (or elsewhere).
5. OECD/G20Base Erosion and Profit Shifting Project, "Explanatory Statement: 2014 Deliverables".
6. UCITS stand for Undertakings for Collective Investment in Transferable Securities, as provided in EU law. According to the EU's Alternative Investment Fund Managers Directive, Alternative Investments Funds (AIFs) include funds for commodities, real estate and infrastructure as well as private equity and hedge funds. The European Long-term Investment Fund (ELTIF) is a new EU vehicle restricted to invest in certain asset classes providing fund investors with long-term, stable returns.
7. The G20 in their Brisbane Communiqué put emphasis on long-term financing, focusing on infrastructure investment. The OECD, with its project on Institutional Investors and Long-Term Investment, is participating in this work. To read more: <http://www.oecd.org/daf/fin/private-pensions/g20-oecd-long-term-financing.htm>
8. The report is called "Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles", available here: A source country is where the asset generating the income or gain is located. It sought to better define (and thereby improve) the tax treaty entitlement of mainstream funds.
9. Available here: [http://www.oecd.org/ctp/exchange-of-tax-information/TRACE\\_Implementation\\_Package\\_Website.pdf](http://www.oecd.org/ctp/exchange-of-tax-information/TRACE_Implementation_Package_Website.pdf)
10. A source country is where the asset generating the income or gain is located.
11. Available here: <http://www.oecd.org/ctp/exchange-of-tax-information/automaticexchange.htm>
12. The OECD's CRS initiative and the TRACE project require funds and their investors to deliver significant information to tax authorities in both source and residence countries.
13. A residence country is defined as the country where the person owning the asset is resident for tax purposes.
14. PPT stands for Principal Purpose Test for tax treaty access. By contrast with the US which applies an LOB provision, many jurisdictions allow tax treaty access to a wide definition of residents, but have separate clauses that deny relief where it can be shown that a principle purpose was to obtain that relief.
15. Available here: <http://www.oecd.org/ctp/treaties/discussion-draft-action-6-follow-up-prevent-treaty-abuse.pdf>
16. Treaty shopping in this context is the case where A resident of State A with an asset in State B might route the investment via State C if the tax treaty between States B and C is more favorable than that between States A and C.
17. A fund whose purpose is to conduct tax arbitrage transactions would need to reflect this in its investor information material.
18. LOB stands for limitation of benefits for tax treaty access. The US has addressed the need to define which entities should be entitled to treaty access by including within its tax treaties an LOB clause, which is a detailed list of qualifying persons. Any entity that does not specifically qualify can apply to the US for discretionary relief, a process that is complex, time consuming and rarely attempted.

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