MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

November 12, 2019

Via email: TFDE@oecd.org

Tax Policy and Statistics Division
Centre for Tax Policy and Administration
Organisation for Economic Co-Operation and Development
2, rue André Pascal
75775 Paris Cedex 16
France

Re: Managed Funds Association Comments on Secretariat Proposal for a "Unified Approach" under Pillar One

Dear Sir / Madam:

The Managed Funds Association[1] appreciates the opportunity to submit comments regarding the Organisation for Economic Co-Operation and Development's ("OECD") consultation document – Secretariat Proposal for a "Unified Approach" under Pillar One (the "Consultation Paper"). MFA supports the OECD's objective of developing a framework that allocates taxing rights fairly among countries to address the tax challenges of the digitalization of the economy and that avoids double taxation or distorting investment activities. We believe a key aspect of achieving this objective is clearly defining the appropriate scope of operating businesses and business profits that should be subject to the Unified Approach of Pillar One.

Asset managers and pooled investment funds play a critical role in providing investors with expert investment advice when they invest capital on a cross-border basis in global markets. We are concerned that applying the Unified Approach to the asset management industry would impair this important activity by increasing risks of double taxation and creating additional friction for cross-border investments, to the detriment of investors and capital markets. Given the policy rationale underlying Pillar One, we do not believe that there is a policy basis to impose the Unified Approach on the asset management industry and its investors, particularly in light of these costs.

[1] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

In considering the relevance of the asset management industry to Pillar One, we understand that the OECD is contemplating the application of the Unified Approach to a wider range of multinational enterprises ("MNEs") than just digital businesses. We believe, however, that asset managers and the pooled investment funds they manage are not the types of businesses that give rise to the policy issues the OECD is intending to address in Pillar One. In that regard, we appreciate the OECD's recognition that "[f]urther discussion should take place to consider whether other sectors (e.g. financial services) should also be carved out, taking into account the tax policy rationale as well as other practicalities."[2] The financial services industry is comprised of a wide range of business entities and business models. The focus of this letter is on privately offered pooled investment funds, such as alternative investment funds, and the asset managers to those investment funds, though we believe that many of the policy considerations would also apply to other parts of the asset management industry and the financial services industry more broadly. As such, we encourage the OECD to consider a broad-based exemption from Pillar One for the financial services industry that includes the asset management industry. If the OECD decides not to adopt a broad-based exemption, we believe it should at a minimum provide an exemption for the asset management industry.

<u>The OECD Should Exempt Pooled Investment Funds from Pillar One</u>

It is important to recognize that pooled investment funds, both "collective investment vehicles" ("CIVs") as defined in paragraph 22 of the Commentary on Article 1 of the 2017 OECD Model Tax Convention on Income and Capital and privately offered investment funds that do not meet the OECD's definition of CIVs, are not operating businesses. Pooled investment funds are formed to facilitate investment by underlying investors such as pension plans and charitable foundations. Notably, the investor rationales for investing in CIVs, as recognized by the OECD,[3] apply equally to privately offered investment funds (*e.g.*, risk diversification and economies of scale). As such, pooled investment funds are fundamentally different than the operating MNEs relevant to the policy rationale underlying Pillar One.

Pooled investment funds fulfill their function by buying, holding, and selling assets such as securities and commodities on behalf of investors who are the owners of the investment fund. In this regard, pooled investment funds are similar to securities accounts or other types of accounts that allow investors to invest in global capital markets while obtaining the benefits of a professional adviser, the asset manager. Pooled investment funds themselves generally do not have employees, "customers," or "consumers." These funds have owners (the underlying investors) who realize gains or losses based on the performance of the investments made by the fund.

The asset manager is a separate entity that employs the investment professionals who make investment decisions on behalf of the pooled investment fund. In most jurisdictions, the asset manager to a pooled investment fund is a regulated entity. For example, in the United States, asset managers to pooled investment funds, including privately offered funds, are regulated by the Securities and Exchange Commission, the Commodity Futures Trading Commission, or both, and

[2] Paragraph 20 of the Consultation Paper.
[3] See section 2.1 of the OECD's Report on "The Granting Of Treaty Benefits With Respect To The Income Of Collective Investment Vehicles" dated 23 April 2010.

in the European Union they are regulated by national competent authorities under the Alternative Investment Fund Managers Directive, as well as applicable national laws.

Because pooled investment funds are not operating businesses and do not have consumers or customers, we believe the gains and losses investor earn should not be treated as business "profits" for purposes of Pillar One. Moreover, the profits earned by pooled investment funds and their investors already are subject to a comprehensive international tax framework that allocates taxes among the source countries of a fund's portfolio investments, the countries of the investors in the pooled investment fund, and the country of the pooled investment fund itself, as applicable. Because a robust tax framework already exists to allocate the gains of pooled investment funds, there is not a regulatory gap that needs to be addressed by Pillar One. Indeed, we are concerned that overlaying the Unified Approach of Pillar One to the existing framework will create additional complexity and uncertainty and increase the risk of double taxation for investors in pooled investment funds. Accordingly, we encourage the OECD to exempt pooled investment funds form the scope of Pillar One.

The OECD Should Exempt Asset Managers from Pillar One

As discussed above, asset managers are distinct from the pooled investment funds they manage. While asset managers are operating businesses, we believe that they also are not the types of entities that raise the policy issues underlying Pillar One. To establish the appropriate scope of Pillar One, we encourage the OECD to focus the proposed "Unified Approach" on consumer-facing businesses that are not well addressed by existing international tax standards when those businesses generate profits from user participation, marketing intangibles, or significant economic presence in countries other than where the business is conducted.

With respect to asset managers to pooled investment funds and other institutional clients, those asset managers are not consumer-facing, as defined in the Consultation Paper, because the clients are not individuals who are acquiring services for personal purposes. While investors in pooled investment funds receive the benefits of the investment advice an asset manager provides to the pooled investment fund, it is the fund itself that is the client (we also note that many of the underlying investors in privately offered investment funds themselves are institutions such as endowments, foundations, and pensions). This important distinction is highlighted by the fact that an asset manager's regulatory obligations and contractual agreements generally apply to the pooled investment fund and not directly to the underlying investors. For example, the asset manager enters into its management contract with the fund, not with underlying investors. Under that contract, it is the fund, not the investors, that pays the manager any fees for the manager's investment advice. The manager makes investment decisions based on the interests of the fund as a whole, not based on individual underlying investors. Because asset managers to pooled investment funds and other institutional clients are not consumer-facing businesses, they should be exempted from the scope of Pillar One.

Some asset managers do have individual clients, such that a portion of their business may be considered consumer-facing. However, asset managers, even those with individual clients, do not generate profits from user participation or marketing intangibles. Asset managers generate profits from the investment advice they provide to clients under their contractual agreements with clients.

Specifically, a manager generates profits from its ability to provide clients with investment advice that achieves a specified investment objective and risk-adjusted investment returns. Further, the profits earned by asset managers already are subject to comprehensive tax rules to allocate taxing rights among the countries where a manager has a significant economic presence. Because asset managers are not the types of businesses and do not generate the types of profits that raise the policy rationale underlying Pillar One, the OECD should exempt them from the scope of Pillar One.

Conclusion

We appreciate the OECD's work to develop a framework to address the tax challenges arising in a digitalized economy. We support the OECD's recognition that certain sectors, such as the financial services industry, can appropriately be exempted from the scope of Pillar One. In considering the appropriate scope of Pillar One, we believe the most compelling policy outcome is to exempt the financial services industry, in particular asset managers and pooled investment funds. We look forward to continuing to engage with the OECD on these important topics. If you have any questions regarding any of the issues discussed in this letter, please do not hesitate to contact us at (202) 730-2600.

Respectfully submitted,

/s/ Mark D. Epley

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/s/ Benjamin Allensworth

Benjamin Allensworth
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