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OECD/G20 Inclusive Framework on BEPS
Reports on the Pillar One and Pillar Two Blueprints
Public Consultation Document

The Alternative Investment Management Association (AIMA)[1] and the Alternative Credit Council (ACC)[2] would like to provide comments in response to the public consultation document relating to the Reports on the Pillar One and Pillar Two Blueprints.

AIMA and the ACC have responded to the OECD's previous public consultation documents concerning Pillar One and Pillar Two. We note that the Reports set out measures which might more effectively limit the scope of the Pillar One and Pillar Two regimes to those multinational enterprises (MNEs) at which they are aimed. In the case of Pillar One, those are MNEs which as Automated Digital Services (ADS) or Consumer Facing Businesses (CFB) carry on significant economic activity in a market jurisdiction without a substantial business presence, while Pillar Two seeks to impose a minimum global effective tax rate (ETR) on MNEs.

[1] AIMA is the global representative of the alternative investment industry, with more than 1,900 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

[2] The ACC currently represents over 170 members that manage over $400bn of private credit assets. The ACC is an affiliate of AIMA and is governed by its own board which ultimately reports to the AIMA Council. ACC members provide an important source of funding to the economy, providing finance to mid-market corporates, SMEs, commercial and residential real estate developments, infrastructure as well the trade and receivables business. The ACC's core objectives are to provide direction on policy and regulatory matters, support wider advocacy and educational efforts, and generate industry research with the view to strengthening the sector's sustainability and wider economic and financial benefits.

Two principles are important in the case of the asset management industry:

- It is not appropriate to categorise financial services activity as ADS or CFB, given the unavoidable complexity of the commercial and regulatory environments in which they operate. These require MNEs to maintain and capitalise business establishments in the markets in which they operate. This holds for the asset management sector, for which regulation is more fragmented across jurisdictions but is appropriate to the level of activity carried out in each jurisdiction;

- Tax neutrality is a necessary attribute for investment funds and institutional investors and is consistent with BEPS principles. Savings and pension provision are socially desirable, and collective investment should be encouraged as a means of spreading risk while increasing opportunity and reducing costs while gaining the benefits of managerial expertise. It is not appropriate to impose a tax charge within an investment structure which would not be imposed directly on investors.

If these principles are not respected, the ability of the asset management industry to raise capital around the world and invest it through investment funds across jurisdictions will be restricted, to the detriment of the investors who provide the capital and the businesses seeking equity and credit finance.

By way of illustration, recently published ACC research[3] shows that private credit managers expect to lend over $100bn to SMEs and mid-sized businesses during 2020. This is broadly similar to their total lending volume in 2019, the sector remains optimistic about its prospects and it is likely that similar amounts of capital will be deployed during 2021. Investor appetite for private credit remains undiminished: there is demand for assets that can generate income, provide diversification or act as a hedge during equity bear markets. Private credit is an attractive way for investors to address these requirements at a time when traditional fixed income assets are offering either minimal or negative rates, while supporting the flow of credit to parts of the economy underserved by traditional banking or public markets. Non-bank lenders have important sources of finance to borrowers during 2020, particularly those who are outside the typical risk appetite of banks or were unable to access government liquidity schemes.

We therefore welcome the recognition of these principles in the Reports. Their adoption within the eventual political agreement on Pillar One and Pillar Two is essential.

We have these comments on the proposals set out in the Reports:

Pillar One

The Report on Pillar One makes clear that a substantial amount of work is required before political agreement is possible on Pillar One. This should not be at the cost of compromising the integrity of the Pillar One building blocks. It should seek to deliver a targeted but functioning system which addresses Amount A in respect of a limited number of the largest MNEs which carry on clearly defined ADS and CFB activities. The nexus rules should balance the taxing right of the market jurisdiction with the compliance burden. Financial services, including asset management, should be clearly and expressly exempted, and their exemption should not depend upon an interpretation of whether a financial services provider undertakes CFB activities.

[3] *Financing the Economy 2020* https://acc.aima.org/resources/research/financing-the-economy-2020.html

The work on Amount B demonstrates that a uniform approach may benefit MNEs and tax authorities, but this should be broad enough to accommodate the many variations of distribution arrangements that exist.

Dispute prevention and resolution measures in respect of both Amount A and Amount B will be necessary if the Pillar One measures are to function effectively.

Pillar Two

We believe that Pillar Two continues to carry the risk of unjustified or double taxation in situations where the GloBE rules do not reflect the nature of the MNE structure.

Very many investment funds will fall outside the scope of Pillar Two as they will not have subsidiaries or permanent establishments in another jurisdiction for which consolidated accounts are prepared, and therefore are not MNEs. However, there is a significant number of complex funds which would be classed as MNEs. We welcome the exemption for Investment Funds but note defects in the definition:

- The pooling requirement (paragraph (a)) does not recognise that an investment fund may have an initial period ("seeding") where there is only one investor. This may be necessary to demonstrate the viability of the investment strategy to outside investors;

- The regulation requirement (paragraph (e)) appropriately recognises that either the investment fund or the fund management should be regulated where it is established but the commentary at paragraph 80 additionally makes this a requirement of the fund's jurisdiction. In practice, many fund jurisdictions do not impose this requirement in respect of certain types of professional investor funds;

- It is not clear that the extension of the definition to special purpose vehicles and other fund-owned entities would enable the entity to qualify as an Excluded Entity because of the requirement that an Excluded Entity must itself be an Ultimate Parent Entity (UPE). Rather, it would be a Constituent Entity. Paragraph 82 suggests that this is not the intended effect of the extension but the language of the definition should be clearer.

In the case of a fund-owned vehicle with minority third party ownership by persons that are not an Excluded Entity, the GloBE rules may apply a tax charge. This will be levied in respect of the whole amount of the relevant income rather than the portion not attributable to Excluded Entities.

It is important to appreciate that tax incurred – or the possibility of tax being incurred – within a tax neutral fund structure would render the fund unmarketable. The tax would be an additional cost to investors since they would not otherwise bear it.

We understand that a proposal is under consideration that entities which would be Investment Funds but for the fact that they are not a UPE may be treated as tax transparent entities and therefore "stateless entities". This would have the effect of treating income as arising to investors rather than the fund and could therefore maintain the fund's tax neutrality. This would resolve the issue in many cases. It would be essential that this treatment applies whether or not the entity is actually tax transparent and only for the purposes of Pillar Two.

We would be pleased to provide any further explanation required.

Yours sincerely

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AIMA