

110 Bishopsgate
19th Floor, Suites 19-06 and 19-07
London EC2N 4AY, UK
+44 (0) 207 961 0830
www.iciglobal.org

Suite 715–717, Level 7
Two Exchange Square
8 Connaught Place
Central, Hong Kong
+852 2168 0882

1401 H Street, NW
Suite 1200
Washington, DC 20005, USA
+001 202 326 5800
www.ici.org

+001 202 326 5832
MOBILE: +001 202 957 7226
lawson@ici.org

By Electronic Delivery

9 December 2015

Philip Kerfs
Head of Unit (International Cooperation)
International Cooperation and Tax Administration Division
Centre for Tax Policy and Administration
Organisation for Economic Co-operation and Development
2, rue André Pascal - 75775 Paris Cedex 16

RE: *Controlling Persons of CIVs –
Recommendations for Practical
Implementation of the CRS*

Dear Philip:

ICI Global¹ respectfully requests Common Reporting Standard (CRS)² guidance clarifying two issues involving “controlling persons” of collective investment vehicles (CIVs). The requested guidance, as discussed below, is entirely consistent with both the CRS’ objectives and the application to CIVs of the Financial Action Task Force (FATF) Recommendations.³

Financial institutions (FIs) that otherwise might be uncertain about who should be treated as a CIV’s controlling person(s) will benefit from the requested guidance. While FIs with a full understanding of the facts independently will come to the answers we recommend, and adopt them in the absence of guidance, resolving the uncertainty for all FIs would be most welcome.

¹ The international arm of the Investment Company Institute, ICI Global serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US\$19.4 trillion. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC.

² <http://www.oecd.org/tax/automatic-exchange/common-reporting-standard/standard-for-automatic-exchange-of-financial-information-in-tax-matters.htm>.

³ FATF Recommendation 10 is the basis for interpreting the CRS. See CRS Commentary (page 198, paragraph 132).

The guidance requested in this letter is limited to CIVs as defined in the OECD's CIV Report (hereafter "the OECD Report").⁴ Specifically, we request guidance only for CIVs that are widely-held, hold a diversified portfolio of securities, and are subject to investor-protection regulation in the country in which they are established.

CIVs have constantly changing and very large shareholder bases. Interests in the typical CIV may be acquired or disposed of every day. CIVs, as noted in the OECD Report,⁵ have "thousands" of individual investors. In the US, the typical CIV has tens of thousands (or more) of individual investors.

CIV investors around the globe may acquire their shares either directly or through an intermediary that holds the shares in "street name" or "nominee" accounts. The identities of investors holding shares through street name accounts is "highly valuable proprietary information"⁶ belonging to the intermediary; as such, this information generally is not shared with the CIV.

This letter focuses specifically on CIVs established in the US as "registered investment companies" (RICs) under the Investment Company Act of 1940.⁷ RICs are legal entities under US law and taxed under Subchapter M of the US Internal Revenue Code as corporations.⁸ The day-to-day operations of a RIC are performed by an investment management firm; the typical fund manager has several employees, some of whom also are officers of the RIC, with significant management responsibilities. Each RIC has a board of directors or trustees that provides oversight.

RICs, like CIVs of other countries, are treated as investment entities under Section VIII.A(6)(b) of the CRS. Assuming that the US is treated under the CRS as a nonparticipating jurisdiction, RICs will be treated as "nonparticipating professionally-managed investment entities" and therefore as "passive nonfinancial entities" (passive NFEs) under Section VIII.D(8) of the CRS. Consequently, the "controlling person(s)" of these CIVs presumably will be subject to CRS reporting.

The Controlling Person(s) of a US CIV (In General)

The CRS provides that, in the case of an entity that is a legal person, the controlling person is the natural person (or persons) who exercises control over the entity. If no one natural person controls the entity through an ownership interest (*e.g.*, 25 percent), the controlling person is the natural person who controls the entity through other means. If no natural person is identified as exercising control over the entity, the controlling person is the "senior managing official."

While we recognize that the CRS Commentary cannot be changed immediately, we submit that CIVs should not report as controlling persons anyone not owning a controlling interest in the CIV.

⁴ The CIV Report's official title is "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles" and is found here: <http://www.oecd.org/tax/treaties/45359261.pdf>.

⁵ See CIV Report (para 37).

⁶ See CIV Report (para 18).

⁷ 15 United States Code (USC) §§ 80a-1 *et seq.*

⁸ 26 USC §§ 851 *et seq.*

In the context of money laundering – a primary purpose of the FATF Recommendations – it seems entirely appropriate, absent comparable protections, to identify a controlling person. When the senior managing official has no tax liability associated with managing the CIV, however, no CRS benefit is gained by requiring such reporting. Indeed, the useless information that is collected, maintained, and reported burdens the FIs and makes it harder for tax authorities to find taxpayers who are not reporting their income properly. We would welcome a change to this requirement.

The Senior Managing Official Ambiguity

CIVs established in the US are so large,⁹ and held so widely, that it is impossible as a practical matter for any individual to own 25 percent or more of such a CIV. Because the management of the typical CIV is shared by many individuals, the CRS Commentary effectively requires CIVs to report a senior managing official as the controlling person.

The FATF Recommendations do not provide any guidance regarding who should be identified by the CIV as a senior managing official. The customer due diligence rule proposed in the US in August 2014 provides FIs with “flexibility” in identifying controlling persons.¹⁰ Specifically, the proposed rule notes that the reported controlling person would be any individual with “significant managerial control;” individuals identified in the proposed rule include “an executive officer or senior manager (*e.g.*, a Chief Executive Officer, Chief Financial Officer, Chief Compliance Officer, . . . Vice President, or Treasurer) or any other individual who regularly performs similar functions.”¹¹ The CIVs established in the US comply with the FATF Recommendations by using their best judgment to identify this person.

Recommended Clarification

We recommend that a frequently asked question (FAQ) be issued clarifying that a CIV treated as a passive NFE is to use its best judgment to determine who, in the absence of a 25 percent owner, should be identified as its controlling person.

The Controlling Person(s) of a US CIV Organized as a Business/Statutory Trust

The Entity vs. Trust Ambiguity

The CRS Commentary does not provide clear guidance regarding who should be treated as the controlling person of a CIV organized as a trust that is a legal person in its country of establishment. We submit, for the reasons discussed below, that the CIV should apply the entity standard for determining its controlling person(s).

⁹ The 7,923 US mutual funds (the most common form of RIC) had total net assets at 31 December 2014 of \$15,852 billion (for an average size of \$2 billion). See page 173 of the ICI's 2015 Investment Company Fact Book, found here: http://www.icifactbook.org/pdf/2015_factbook_1.pdf.

¹⁰ See page 45158 of <http://www.gpo.gov/fdsys/pkg/FR-2014-08-04/pdf/2014-18036.pdf>.

¹¹ *Id.*, at page 45170.

CIVs may be established under the laws of one of the United States as either corporations or business/statutory trusts.¹² Business/statutory trusts have essentially all of the relevant characteristics of corporations and essentially none of the relevant characteristics of trusts.¹³ Consequently, CIVs organized in the US as business/statutory trusts (*e.g.*, Massachusetts business trusts) are legal persons; for US federal income tax purposes, they are entities taxed as corporations.

The FATF Recommendations are applied to US CIVs by treating them as entities.¹⁴ Moreover, the OECD, in its CIV Report, recognized the tax policy rationale for treating a trust as a person for treaty purposes when it is treated as a taxpayer and resident for domestic tax purposes.¹⁵

The distinction between “entity” and “trust” status for CRS purposes¹⁶ is extraordinarily significant. If a CIV organized as a business/statutory trust is treated as an entity that is a legal person, the only individual likely to be identified as a controlling person would be the senior managing official. In contrast, if such a CIV is treated as a trust, *every* investor in the CIV would be treated as a beneficial owner and therefore as a controlling person; many others, including portfolio managers, also might be treated as controlling persons.

A CIV, as a practical matter, cannot provide FIs with a list of its investors. First, unlike a family trust or a closely-held partnership, a CIV’s investor base changes constantly. Second, unlike family trusts or closely-held partnerships, a CIV’s investor base typically includes many thousands of individual investors. Third, a substantial portion of investor interests are held in nominee/street name accounts; the CIV, therefore, does not know the investors’ identities. Even trying to provide information regarding those investors whose interests are registered directly on a CIV’s books would be difficult; the information also most likely would become immediately inaccurate as individuals dispose of their CIV interests and/or become investors.

Requiring a CIV to provide all FIs with which it does business a list of its investors – were it even possible – would lead to redundant reporting. The FI that maintains the client account, whether it is a broker or the CIV itself, would have tax reporting responsibilities. While redundant reporting might be useful in some situations, no benefit would seem apparent were reporting even possible in the context of a CIV with many thousands of investors with small investments.

¹² Others will provide details regarding their own locally-established CIVs that, despite being organized as trusts, are legal entities under domestic law.

¹³ The relevant factors include: management powers of trustees comparable to those of corporate directors; status as an association; regulation by statute; perpetual existence; capacity to be sued; transferable shares; ability to issue multiple classes of shares; shareholder voting rights; amendment of governing document; and the right to liquidate.

¹⁴ See page 45160 of <http://www.gpo.gov/fdsys/pkg/FR-2014-08-04/pdf/2014-18036.pdf>. See also page 45170, which treats all RICs as legal entities.

¹⁵ See CIV Report (para 26).

¹⁶ See CRS Commentary (page 198, paragraphs 133 and 134).

Recommended Clarification

The CRS should be implemented by requiring that a CIV established in the US as a business/statutory trust be treated as an entity for purposes of determining its controlling person(s). Thus, in general, all US CIVs would treat as controlling persons only a senior managing official.

Clarifying this result – which is consistent with the FATF Recommendations – will save FIs and CIVs from the unnecessary burden arising from an incorrect test being applied. Moreover, this result would prevent CIVs from potentially being precluded from opening financial accounts because they cannot satisfy a totally unworkable requirement to identify all investors.

We suggest two actions that, taken together, would provide the requisite clarification. First, an FAQ should be issued clarifying that a CIV organized as a trust and treated as a legal entity in its country of establishment is a legal person for CRS purposes; hence, such a CIV would not treat all of its investors as controlling persons. Second, each country in which a CIV may be organized as a trust with legal personality should be encouraged to indicate this treatment on the OECD's AEOI portal. FIs then could consult the AEOI portal to determine whether CIVs established as trusts should report their investors or only a senior managing official.

* * *

Many thanks in advance for considering these recommendations. Please feel to contact me at your convenience to discuss further any of the points raised in this letter.

Sincerely,

/s/ Keith Lawson

Keith Lawson
Deputy General Counsel – Tax Law