Response of the Commercial Real Estate Finance Council Europe to the OECD's Public Discussion Draft "Follow Up Work on the Report on BEPS Action 6 (*Prevent Treaty Abuse*)" dated 21 November 2014

Submitted by email: taxtreaties@oecd.org
FAO Marlies de Ruiter, Head, Tax Treaties, Transfer Pricing and Financial Transactions Division
OECD/CTPA

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Dear Ms de Ruiter

Public Discussion Draft: Follow-up Work on the Report on BEPS Action 6 (Prevent Treaty Abuse)

We are grateful for the opportunity to comment on this important aspect of the OECD's work.

CREFC Europe is the voice of the commercial real estate (**CRE**) finance industry in Europe, representing banks, insurers, fund managers and others providing or intermediating the provision of debt to real estate businesses, as well as advisers, consultants and others with a stake in this sector. We seek to promote transparency and liquidity in CRE finance markets by developing and disseminating best practice and engaging with regulators and policymakers, so that our industry can flourish while playing its part in supporting the real estate sector and the wider economy and delivering returns to investors.

We set out below some high-level comments and state our support for the more detailed submissions of two other organisations whose membership and interests overlap in relevant ways with our own.

High-level comments

Past submissions. We would generally reiterate the points made in previous submissions regarding Action 6, independently on 9 April 2014 (referencing submissions by INREV[1] and the BPF[2]), and jointly with a number of other European real estate industry associations on 23 May 2014.

Support for policy aims. We remain supportive of the OECD's broad policy objectives in relation to preventing treaty abuse. We support efforts to develop internationally consistent solutions to address policymakers' concerns in this area.

Concern about the treatment of investment funds... However, we are concerned that the evolving proposals continue to deal inadequately and inappropriately with the investment fund structures through which substantial international capital (both equity and debt) is channelled into investment in CRE and the built environment.

…and especially about the treatment of non-CIVs. We are especially concerned about the position of non-CIV funds, which are very widely used in the CRE sector for good (non-tax) commercial reasons flowing from the mostly institutional and international investor profile and the large-scale, long-term and illiquid nature of the underlying asset class invested in.

[1] INREV is the European Association for Investors in Non-listed Real Estate Vehicles.

[2] The BPF is the British Property Federation.

No policy case for penalising investors in CRE debt funds. CRE debt funds typically attract capital from institutional investors including pension and insurance firms, which would qualify for treaty benefits if they invested directly, but choose to invest indirectly and collectively. Good (non-tax) reasons for that choice are a lack of the requisite resources or infrastructure to invest in CRE debt directly, or a preference for the risk diversification offered by collective investment. We see no policy justification for restricting treaty benefits in a way that disturbs such structures.

No policy case for penalising CRE debt funds' use of subsidiaries. CRE debt funds typically use subsidiary companies to segregate the risks presented by different loans they invest in, and to facilitate joint venture investments or appropriate transaction-specific financing. In some cases, operational considerations (such as a desire to limit the number of subsidiaries used by a fund) lead to the use of cell/compartment and multi-issue vehicles by alternative investment funds. Given that the existence of such holding structures is not tax-driven, we do not consider that it should be regarded as objectionable for their location to be selected having regard to tax neutrality alongside other legal, practical and financial considerations. There is no particular reason for them to be located in the same jurisdiction as the fund, fund manager or underlying assets.

Risk of unintended consequences for financial stability. In the aftermath of the financial crisis, many countries, particularly in Europe, recognise the resilience that a more diversified financial system could offer. Given the feedback loops between property and credit cycles, CRE debt is one sector in which excessive reliance on the banking sector to provide finance seems very clear. Europe's CRE debt market has experienced a strong, and very welcome, flowering of non-bank finance supply in the last few years, largely thanks to fund vehicles. These vehicles almost invariably fall within the regulatory scope of the Alternative Investment Fund Managers Directive (albeit the subsidiaries through which they invest usually won't), but they typically fall outside the OECD's CIV definition. Denying treaty benefits to such vehicles could have far-reaching adverse consequences for financial stability.

Risks to competition and to the flow and cost of credit for the real economy. Denying treaty benefits for (largely non-CIV) CRE debt funds would also have an adverse impact on the flow and cost of credit for borrowers and thus also for investment flows more generally in the built environment and the real economy. CRE loan documentation typically imposes a grossing up obligation on the borrower in the event of withholding taxes being imposed. The OECD's current proposals risk both increasing the effective cost of borrowing for businesses under existing loans, and reducing effective competition in the debt market by placing market-based finance provision (through such funds) at an unjustifiable tax disadvantage relative to more traditional sources of finance.

Support for INREV and BPF submissions. As we did in our April 2014 submission, we would like to express our agreement with and support for the more detailed representations being made by INREV and the BPF, which identify the key issues arising from the current proposals for the flow of international capital into CRE, and make constructive suggestions for how those issues might be addressed.

Yours sincerely

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