Impact of OECD withholding tax proposals cross border and on UCITs funds (Ireland)

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Withholding tax proposals likely to impact cross-border and UCITS funds

While the Organisation for Economic Co-operation and Development (OECD) and European Union (EU) proposals are likely to clarify withholding tax treaty benefits, this may come at a cost to funds distributed in several countries.

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New proposals emerging from the OECD and the EU will have a major impact on international funds. If implemented, they will lead to a streamlining of procedures and clarification of treaty benefit entitlements. But these benefits may well come at a cost. It is very likely that new reporting procedures will accompany any improvement in treaty benefits and funds currently in receipt of benefits might lose out. Funds domiciled in locations such as Dublin and Luxembourg will be especially impacted.

Withholding taxes on cross-border investment flows can be a major cost to investors. Tax treaties and other procedures are designed to mitigate these costs by eliminating double taxation. Tax treaties often do not operate as they should, particularly when the investments are held through a chain of intermediaries, and especially when held through the medium of a collective investment fund. Procedures for obtaining tax reliefs are often cumbersome, paper-driven and can differ widely between jurisdictions. All of this results in significant cost to investors, either as a result of tax reliefs foregone or costs of compliance. Very important proposals to alleviate these problems will emerge in the next 12 to 18 months. Within OECD and the EU, groups consisting of government and industry representatives have been meeting to examine the problems and make recommendations for solutions.

The OECD consultative group has held a series of meetings over the last two years, most recently in April 2008. Substantial agreement exists between the governments and industry on what the major problems are. This is likely to result in important clarification on how treaties should operate in the context of investment funds and recommendations for improvements to cross-border withholding tax procedures.

Without derivative benefits, funds distributed in a single country could have a significant advantage over funds distributed in many countries. This would have major implications for widely distributed funds such as UCITS. The OECD and EU have joined forces to ensure that internationally agreed measures conform to the recommendations of the EU sponsored group of experts (known as FISCO), who issued a report in November 2007 recommending a new streamlined withholding tax regime operating across all EU member states.

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