**SwissBanking**

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**Public Discussion Draft – BEPS Action 3: Strengthening CFC Rules**

Dear Mr. Pross,

The Swiss Bankers Association (SBA) is the leading professional organisation of the Swiss financial centre. Its main purpose is to maintain and promote the best possible framework conditions for the Swiss financial centre both at home and abroad. The SBA was founded in 1912 in Basel as a trade association and today has 317 institutional members and approximately 18'500 individual members.

The SBA thanks the OECD for the opportunity to provide comments on its discussion draft on Action 3 (Strengthening CFC Rules) of the Base Erosion and Profit Shifting (BEPS) Action Plan issued on 3 April 2015 ("discussion draft").

We generally agree with the comments provided by the BIAC but would like to stress the following points, which reflect a financial sector perspective.

**General comments**

The SBA believes that the discussion draft attempts to address a number of competing objectives, which (partly) conflict with other action items. This is in particular valid with regard to transfer pricing rules. We are of the opinion that effective transfer pricing rules address BEPS concerns more effectively than CFC rules and should not be undermined by conflicting rules resulting in the re-allocation of profits, which were already allocated through transfer pricing and arm's length rules. The discussion draft lacks any analysis and proposal on how such conflicts (and other conflicts with respect to other action items, in particular 2, 4, 5, and 8-10, 11, 14 and 15) shall be addressed.

Since no clear objective has been identified in the discussion draft for implementing CFC rules, we are of the opinion that these do not cover the initial objective of the BEPS action plan. We furthermore believe that any CFC rule (if adopted) should be introduced as a best practice rule and not as a minimum standard.

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## Secondary Rules

The SBA is concerned about the idea to introduce secondary rules that apply "to income earned by CFCs that did not give rise to sufficient CFC taxation in the parent jurisdiction". From our point of view such rules cut against the original intention of the BEPS action plan and would lead to a re-allocation of taxing rights purely based on the level of taxation in a particular country. Such an approach would have a significant impact on the cross-border business and as a consequence countries applying lower tax rates might loose tax revenues and hence their overall competitiveness only because they are not high tax countries.

## Sector specific Rules

If CFC rules are adopted in the BEPS context, the SBA is of the opinion that there is a need for sector specific rules. The discussion draft does not address this possibility and does not make any suggestion for rules in this regard. In particular with respect to the definition of CFCs, income specific rules for the financial industry might need to be taken into consideration. It is for example obvious that interest income in case of regulated banks should not generally be considered as passive (and therefore as CFC) income. Banks have many different types of interest income which need to be analyzed in more detail and which might require special rules (e.g. interest income on client positions vs. positions of the bank).

## Substance Analysis

The SBA has concerns regarding substance analysis based on employees. In the current international business environment such criteria might not be adequate in all situations. Applying such rules would lead in particular in case of outsourcing to results that do not reflect the value chain adequately. Usually the outsourced activities are of a preparatory or auxiliary nature (e.g. production of reports) and do not contribute significantly to the value of a certain product/service. On the other hand, such auxiliary work is typically performed by a large number of employees located abroad; the number of these employees can be much higher than the amount of employees contributing effectively to the value of the product/service provided. In this context, one should rather focus on where the functions and risks are located or assets are booked instead of on employee headcounts. This being said, we recognize that countries might have different interpretations in this respect. A substance analysis based only on the number of employees would nevertheless lead to a situation where more profits than justified are allocated abroad and where the contribution to the value chain is not correctly reflected in such an allocation.

## Final comments / Summary

The discussion draft lacks addressing clearly enough the aims of the CFC rules and conflicts with other action items. It is also missing an analysis and discussion of the existing (and up and running) CFC systems (these are only mentioned at some points as examples). In addition the excessive profit approach and the secondary rule are not embedded in the CFC rules but are somehow isolated as a separate building block.

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Finally, no suggestion is made how the complexity of CFC rules can be reduced. If CFC rules are nevertheless to be adopted in the BEPS context, these should constitute best practices and not minimum standards.

The SBA thanks the OECD for taking due account of these comments.

Yours sincerely,
Swiss Bankers Association

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