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BVCA response to the OECD consultation – Pillar Two Blueprints

The British Private Equity and Venture Capital Association ("BVCA") welcomes the OECD's efforts to develop a consensus solution to the tax challenges arising from the digitalisation of the economy and are pleased to have the opportunity to comment on its public consultation document, 'Reports on the Pillar One and Pillar Two Blueprints' (the "Condoc") and, specifically in relation to the Report on the Pillar Two Blueprint (the "Pillar Two Blueprint"), in respect of the Global Anti-Base Erosion Proposal ("GloBE"). We write under separate cover in relation to our comments on the Report on Pillar One Blueprint.

The BVCA is the industry body for the private equity and venture capital industry in the UK. With a membership of over 700 firms, the BVCA represents the vast majority of all UK based PE/VC firms, as well as their professional investors and advisers. BVCA members invested over £43bn into nearly 3,230 UK businesses in the period 2015-19, the majority being SMEs, and companies backed by PE/VC currently employ around 972,000 people in the UK.

As we explained in our previous submission (see Appendix), what differentiates private equity and venture capital funds (PE/VC funds) from many other sources of financing is the active involvement of the manager in advising on the running of the businesses invested in, strengthening management expertise, delivering operational improvements and/or helping companies to expand into new markets. This active approach is also employed in helping underperforming companies to survive, protecting jobs and delivering successful businesses with a strong future. In this way they provide a crucial pillar of the economy, providing access to capital for businesses as they grow.

We also explained, in our prior submission, that a significant proportion of private equity and venture capital funding comes from pension funds and insurance companies who invest the pensions or savings of millions of citizens across the world.[1] Private equity and venture capital is a key asset class for these long-term investors, as it generates capital gains on a consistent basis over the long-term. We described the key principle of investment funds being that an investor should not be in a worse tax position through investing via a collective investment vehicle than if they had invested directly in the underlying asset.

Against this backdrop, we very much welcome the fact that, the Pillar Two Blueprint design includes a list of expressly excluded entities that will not fall within the scope of the regime, including a specific category for 'Investment Funds'. We also appreciate the ongoing engagement of the OECD with us as representatives of the industry and believe the proposal appropriately reflects the

[1] The five largest investor categories in EU28 private equity funds between 2014-2018 (% by amount): Pension funds (29%), Fund of funds (13%), Insurance companies (10%), Sovereign wealth funds (9%), Government agencies (7%).

extensive technical work that has been undertaken so far in this area. We have provided some further comments in this regard in section 1 below.

We have also provided further comments, in section 2 below, in respect of the application of the Pillar 2 regime to the portfolio companies in which investment funds invest, in relation to which we are largely in agreement with the proposals.

Finally we would like to reiterate our prior comments in relation to timing of the implementation of the proposals, set out in section 3 below.

1. **Exclusion for Investment Funds (ref. Pillar Two, Section II (Chapter 2: Scope of the GloBE rules) of the ConDoc)**

We fundamentally agree with the principle that it is appropriate to carve out investment funds through a targeted exemption from the GloBE proposals, which would otherwise cut across national regimes that ensure tax neutrality for investment funds and potentially significantly deter those institutional investors who would otherwise provide capital for investment. We welcome the fact that previous submissions on these points have been taken into consideration in designing the proposal, particularly in the discussions in section 2.3.1 of Pillar Two Blueprint, and are satisfied that that the concerns we have noted in prior submissions have, accordingly, been largely addressed.

Continued engagement with refining the definitions

As the OECD moves forward from the Blueprint stage to implementation, and the drafting of the exclusions are refined in more detail, we would very much welcome a continued engagement in that process. We think it is important that the lines of communication with key stakeholders remain open, so that as refinements are made no unintended consequences emerge.

We would like to be involved in particular with any further technical work regarding the treatment of investment funds to identify whether further rules are needed, as referred to in paragraph 83 of the Pillar Two Blueprint, to ensure that the overall principle of tax neutral outcomes for investment funds is preserved.

Consistency between Pillar One and Pillar Two Regimes

We acknowledge that, as Pillars One and Two develop, it may be that different pressure points may arise in each, but in our view it is essential that these regimes work cohesively, to provide a comprehensive and unified strategy for tackling the tax challenges arising from a digital economy.
As such it is important that Pillars One and Two take a consistent approach with regards to their application to investment funds. This implies that Pillars One and Two must both employ the same carve out for investment fund arrangements, so as to ensure that the application of these regimes overall is coordinated, coherent and robust.

We will be writing under separate cover in respect of the Pillar One Blueprint accordingly, to recommend that the Pillar One proposals adopt the Pillar Two framework for excluding investment fund arrangements from their scope.

2. **Portfolio companies for separate investments**

As we noted in our prior submission, it is recognised that the investee businesses (portfolio businesses) of PE/VC funds are likely to themselves be MNEs that are within the scope of Pillar Two where they meet the threshold requirement.

We note the further detail and clarification that has been included in the Pillar Two Blueprint and that the definition of MNE Group under the GloBE rules will be aligned with that of the CbCR, in relying on the UPE's applicable financial accounting standard to determine whether a subsidiary's accounts are consolidated and thus whether it is a Constituent Entity. We also support the inclusion of some explanation regarding the application to portfolio companies of investment funds detailed in section 2.4.3 of the Pillar Two Blueprint, and example 2.4.3 in Annex A.

In this regard we would like to again note that we feel this is a helpful clarification in the development of Pillar 2, which reflects productive interactions with the PE/VC industry generally.

3. Timing

Given that many portfolio companies in which PE/VC funds invest are likely to themselves be MNEs that are within the scope of Pillar Two where they meet the threshold requirement, our stakeholders continue to have significant interest in the regime being implemented in a clear and coherent manner.

As such we reiterate our prior concerns as regards timing of the implementation of the proposals. The introduction of the OECD's Pillar One proposal for a new taxing right will be a fundamental change to the taxation regime for MNEs and will undoubtedly have unforeseen impacts on the nature and application of international taxation. The introduction of the GloBE proposal will be just as fundamental a reform. Simultaneously introducing both proposals would lead to huge uncertainty and confusion given the massive scope of the changes to the global tax system that would be introduced.

We therefore recommend that the GloBE proposal is not introduced until an appropriate amount of time has passed after the introduction of the Pillar One new taxing right. We would suggest at least five years. As well as reducing the uncertainty and confusion described above, this staggered introduction would provide time for the changes made by the implementation of the Pillar One proposal to bed in, during which problems that arose from such introduction could be addressed.

Representatives from our industry would be happy to discuss this in further detail at a time that is convenient for you. Please contact Chris Elphick for further information.

Yours faithfully,

Mark Baldwin
Chairman of the BVCA Tax Committee