IN FOCUS –
Trust, but verify.
The Treaty Eligibility Challenges of Revenue Ruling 81-100 Group Trusts

When investing in foreign markets, group trusts often experience issues obtaining tax treaty benefits. Foreign tax authorities oftentimes are not assured that the underlying pension plan participants within the group trust are treaty eligible, and therefore require proof in the form of documentation at the underlying participant level. This is a burdensome requirement for the group trust and getting compliance is often difficult to impossible. In this edition of In Focus, we aim to summarize issues experienced by group trusts in various markets of investment as well as review potential solutions being explored by market participants.

Markets of Investment That Present Tax Treaty Challenges

AUSTRIA

81-100 group trusts are receiving rejections on their treaty based reclaims filed in Austria. The Austrian Tax Authority’s reluctance to view the 81-100 group trust as a treaty eligible investor in its own right is a common theme among various markets of investment.

An “81-100 Group Trust” refers to a collective investment trust, group trust or collective investment fund that is a commingled pool governed by ERISA. It qualifies for tax-exempt treatment under Internal Revenue Service (IRS) Revenue Ruling 81-100 (as modified by Revenue Ruling 2004-67 and Revenue Ruling 2011-1) because all of its assets are derived from either qualified plans or certain governmental plans (group trust) pools that are exempt from U.S. taxation under Section 501(a) of the Internal Revenue Code (IRC).
The French Tax Authorities (FTA) issued a statement of practice on September 12, 2012 outlining relief at source requirements for “simple collective trusts of pensions” that automatically transfer dividends of French origin to U.S. pension funds in the year in which they are received. According to the statement of practice the simple collective trusts of pensions may apply for the benefit of the relief at source procedure on behalf of their members by providing the following information/documentation:

1. A list of members of the trust
2. A list of members that are:
   a. IRC Section 401(a) Qualified Retirement Plans;
   b. IRC Section 401(b) Tax Deferred Annuity Contracts;
   c. IRC Section 457 Deferred Compensation Plans; all of which are established and managed exclusively for the purpose of providing retirement benefits and hold less than 10 percent of the voting shares of the French distributing entity;
3. Each member must provide an attestation issued by the U.S. authorities or any other supporting documents stating that they have been established and operate in accordance with the referenced IRC Sections
4. an attestation stating the percentage of rights to French dividends received by the collective trust attributable to pension funds that come under the referenced IRC Sections

81-100 group trusts receive IRS Determination Letters which certify the following:

1. that the trust is a “group trust arrangement as described in Revenue Ruling 81-100…” “This means that the trust is exempt from federal income tax under Internal Revenue Code section 501(a) for the funds that equitably belong to its participating trusts that qualify under Section 401(a)”
2. that the participants of the group trust are limited to the pooling of assets of only certain types of qualifying specified trusts

The Determination letter in combination with Form 6166, certifying that “the fund is a group trust arrangement described in Revenue Ruling 81-100, and to the best of our knowledge, each participant is a resident of the United States” is deemed insufficient proof of eligibility of each participant in the group trust.

The tax treaty between the U.S. and Japan provides for a withholding tax exemption for qualifying pension funds. In order to avail of the exemption, the investor must satisfy residency criteria under Article 4 and the Limitations on Benefits (LoB) provisions under Article 22.

Documentation requirements for relief at source in the case of investors domiciled in countries whose tax treaty with Japan contains an LoB provision, are Form 17 and Form 6166. The Form 17 allows the investor to make representation of its ability to satisfy the LoB provisions of the tax treaty between Japan and the U.S.

Additionally, U.S. pensions are required to provide a disclosure that includes the total number of the fund’s individual participants, as well as the number of participants that are U.S. residents. This disclosure is required as proof that U.S. resident participants meet the 50 percent threshold of the LoB provision. This declaration is required in addition to the Form 17 LoB statement.

1. These documents must be produced annually
2. The tax treaty does not extend its benefits to pension funds established in the U.S. Territories (Puerto Rico, the U.S. Virgin Islands and Guam)
A self certification from the pension attesting that more than 50 percent of its beneficiaries are U.S. residents is deemed insufficient. The declaration must be provided annually, immediately after the end of the pension fund’s fiscal year.

Further complications are experienced by 81-100 group trusts, where in order to qualify for treaty relief at source, the Japanese Tax Authorities require that each pension participating in the 81-100 group trust provide the referenced declaration. In these instances, the following self certification from each member of the 81-100 group trust was also deemed insufficient:

“… the pool is exempt from U.S. federal taxation under section 401(a) of the U.S. Internal Revenue Code and qualifies as a group trust under applicable Internal Revenue Service rules and regulations …” and that “…the Pool is established and operated exclusively for the collective investment of pension, profits sharing or stock bonus trust or custodial accounts qualifying under section 401(a) of the Code that are U.S. tax-exempt under section 501(a) of the Code or Code section 401(a)(24) governmental plans providing pension benefits or other employee benefits for retirees ….” Further confirming that “all participants are considered US residents and that more than 50 percent of the participants’ beneficiaries are considered United States residents.”

Often times the group trust is not able to produce the declaration, especially since it requires detailed information pertaining to all participants’ beneficial owners, which must be updated upon participants’ subscription/redemption.

SWITZERLAND

Pursuant to the U.S-Switzerland tax treaty, qualifying pensions are eligible to avail of a withholding tax exemption on dividend and interest income. Group trusts filing reclaims pursuant to the tax treaty with Switzerland must complete Form 82E, where among other questions, they are asked, “were you a tax exempt recognized United States pension trust?” and if the answer is yes, “were more than 50 percent of the beneficiaries, members or participants residents of the United States or Switzerland?” These questions intend to confirm that the LoB provisions of the tax treaty are met.

Following submission of the reclaim, group trusts receive request for additional information from the Swiss Tax Authorities. The request seeks to establish beneficial ownership and also asks for the following:

- For each due date a supplement 20XX client list that shows names, complete address, the Taxpayer Identification Number (TIN) and the proportionate share of each participant in the group trust;
- A Form 6166 (relating to tax year 20XX for each participant figuring on the 20XX client list attached to the claim for refund). As the Competent Authority Agreement provided that a group trust described in RIF Revenue Ruling 81-100 qualified for benefits under Article 10(3) of the Swiss-US Income Tax Treaty only with respect to participants that are trusts mentioned under subparagraph 3. a), b) or c) of the Competent Authority Agreement. This additional documentation is needed in order to verify if all participants meet these requirements;
- Detailed information about the participants’ possibilities to invest in the Group Trust. Is it possible that participants will contribute securities as well?
As a matter of background, in 2015, Switzerland and the U.S. entered into a Mutual Agreement Procedure (MAP), whereby group trusts must confirm that participants fall into one of the below categories:

- A U.S. resident tax-exempt trust providing pension benefits or retirement benefits under an IRC plan or stock bonus plan (including IRC section 401(k) arrangements);
- A U.S. resident tax-exempt trust described in IRC Section 457(g) providing pension or retirement benefits under an IRC section 457(b) plan;
- A U.S. resident tax-exempt trust providing pension or retirement benefits under a Code section 403(b);
- a group trust described in IRS Revenue Ruling 81-100 (as modified by IRS Revenue Ruling 2004-67) with respect only to the participants that are trusts mentioned under the subparagraphs above;
- the Thrift Savings Fund (Code Section 7701(j))

The MAP further confirmed that individual retirement accounts under Code section 408 or Roth IRAs under Code section 408A are excluded from treaty benefits.

According to the MAP, in order to claim treaty benefits, the U.S. pension or other retirement arrangement must provide:

a. a certification letter (Form 6166) issued by the IRS for the taxable year(s) in question; and
b. a Swiss Form 82E to which the U.S. pension or other retirement arrangement has attached a statement that it does not control the company paying the dividends and that it satisfied the requirements of the relevant treaty article.

Although the MAP lays out the criteria for treaty benefits as agreed by the contracting parties, the requests for additional information from the Swiss Tax Authorities are seeking to look through the group trusts by requiring that each participant in the group trust provide their own Form 6166, as well as a client list disclosing detailed information pertaining to each participant.

**SWEDEN**

Historically, 81-100 group trusts were able to avail of a withholding tax exemption pursuant to the tax treaty between Sweden and the U.S. However, recently investors have seen similar requests for additional information from the Swedish Tax Authorities. Group trusts are requested to provide Form 6166 for each participating pension plan.

**Is the Current Language on Form 6166 Causing Treaty Eligibility Issues?**

The language on the Form 6166 issued to group trusts has undergone some changes in the past years. An older version of the 6166 issued to group trusts used to state “I certify that, to the best of our knowledge, the above named entity is a trust forming part of a pension, profits sharing, or stock bonus plan qualified under 401(a) of the US Internal Revenue Code, which is exempt from U.S. taxation under section 501(a), and is a resident of the United States for the purposes of US taxation.”

Over time the contents of the Form 6166 have changed to state the following “I certify that the above named fund is a group trust arrangement described in Revenue Ruling 81-100, and to the best of our knowledge, each participant is a resident of the United States.”

The current wording on the 6166 may imply to the foreign tax authorities that the group trust is not eligible for treaty benefits in its own right, but only to the extent of its participants being treaty eligible.

The IRS has expressed its willingness to consider proposals for revisions of the wording of the 6166. Such proposals are being provided and reviewed by the Association of Global Custodians (AGC), of which BBH is an active participant.
OECD/BEPS Considerations

On February 29, 2016, the Organization for Economic Co-operation and Development (OECD) published a discussion draft titled, Proposed Changes to the OECD Model Tax Convention Concerning the Treaty Residence of Pension Funds. The Discussion Draft builds on the final version of the OECD’s Base Erosion Profit Shifting (BEPS) Report, Action 6 (Preventing and Granting of Treaty Benefits in Inappropriate Circumstances) where it was concluded that work needs to be done so that “…pension funds should be considered to be a resident of that State in which it is constituted regardless of whether the pension fund benefits from a limited or complete exemption from taxation in that State.”

Under the current version of the U.S. Model Tax Treaty, the definition of a pension fund requires that the fund be “operated exclusively or almost exclusively”:

a. To administer or provide pension or retirement benefits; or

b. To earn income from the benefit of one or more persons established in the same Contracting State that are generally exempt from income taxation in that Contracting State and that are operated exclusively or almost exclusively to administer or provide pension or retirement benefits;

The proposed definition of a “recognized pension fund” under Article 3, paragraph j), subparagraph (ii) of the OECD Model Tax Convention includes specific reference to group trusts, which may help in alleviating some treaty accessibility issues being experienced by group trusts or similar arrangements.

(iii) That is constituted and operated exclusively to invests funds for the benefit of entities or arrangements referred to in subdivision (i)

The commentary to Article 3, further expends on the term “arrangement” to include vehicles such as trusts.

The reference to an “arrangement” is intended to cover cases where pension benefits are provided through vehicles such as a trust, which under the relevant trust law, would not constitute an entity: the definition will apply as long as the trust or the body of trustees is treated for tax purposes, as a separate entity recognized as a separate person.

Another potential consideration is that group trusts can include Puerto Rican pension funds. While the US Model Tax Treaty requires the that the group trust be operated “exclusively or almost exclusively to administer or provide pension or retirement benefits,” which may be interpreted to allow participation by Puerto Rican pension funds in the group trust, the OECD Model Tax Convention does not make such reference in its definition of a “recognized pension fund.”

If adopted, the Model Tax Convention will be reflected in future bilateral tax treaties, as well as multilateral instruments that would be implemented to facilitate BEPS. It is anticipated that OECD will issue additional commentary with an intended implementation for the 2017 Model.

BBH Perspective

BBH is an active participant in the Association of Global Custodians (AGC) which provides a forum for addressing issues which create impediments for our clients seeking treaty benefits and local law reduction opportunities.

At a recent meeting that took place between the AGC participants and the United States Competent Authority (USCA), the participants requested that the IRS confirm its position regarding treaty eligibility of 81-100 group trusts. Since many markets are seeking to look through the group trust to its underlying participants, it’s imperative that the IRS confirm whether its position is that an 81-100 group trust is a treaty eligible U.S. resident in its own right and the same must be reflected in the language of Form 6166.

For more information please contact your relationship manager or the Global Tax Services Group.