Common Contractual Fund

Investment managers awakening to the possibilities of Institutional Asset Pooling

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The Common Contractual Fund (CCF) is a vehicle introduced in Ireland aimed at enabling institutional investors to pool investments in a tax efficient manner.

Originally introduced in 2003 for pension funds the CCF is a contractual arrangement between investors similar to a Luxembourg FCP. Under Irish tax law the CCF is explicitly treated as tax transparent, a feature lacking in other types of fund structure. The regulations for the CCF were updated in 2005 and allow for a UCITS and non-UCITS version of the CCF. Amended tax rules extended the scope of transparency to all forms of institutional investor including pension funds. Significantly, there has been an increase in interest recently by investment managers in the use of this asset pooling vehicle.

Why the need for an asset pooling vehicle?

The interest in creating larger asset pools is driven by a desire to improve asset performance through a combination of improved reporting and elimination of duplicated costs. While previously asset pooling was primarily of interest to institutional money managers and multinational companies with multiple occupational pension plans, their appeal is widening to investment managers.

Asset pooling has long assisted institutional money managers and multinationals to achieve investment management, administration and custody efficiencies by pooling the investments of their different pension funds into a single fund.

Now, investment managers are viewing these transparent vehicles as a way to gain from economies of scale and lower administrative and accounting costs. This increased appeal stems from the investment managers' pursuit of tax optimisation, increased risk management oversight and improved governance and control.

The CCF can be the right solution for investment managers who wish to pool any type of investments which are sensitive to withholding tax. It helps to overcome the tax drag frequently resulting from higher withholding taxes being applied at pooled portfolio level than where assets are held directly.

What should be the tax attributes of an asset pooling vehicle?

Institutional investors, especially pension funds, generally benefit from reduced rates of withholding taxes under double taxation agreements. It is vital that this treatment is retained when the assets of separate institutional investors are pooled in a single intermediate vehicle.

For asset pooling to work the investment decision must be tax neutral. In other words investors. must get the same tax result through pooling as if they had invested directly. This neutrality requires the agreement of the tax authorities in the investor's home domicile and in the country of the investments and requires them to apply treaty benefits as if the intermediate asset pooling vehicle did not exist

To achieve full tax neutrality the vehicle and its institutional investors must be exempt from all local taxes in the jurisdiction where the vehicle is domiciled and the vehicle must be considered to be tax transparent by the tax authority;

- of the investor's home jurisdiction,
- which imposes withholding taxes on the investment flows and
- ideally, of the country where the vehicle is domiciled

The benefits

There are a number of important benefits for an investment manager in using this pooling vehicle, such as;

- reduced administration and accounting costs for pooled assets
- consistent investment management across a larger pool of assets
- a greater level of oversight and control
- an increased level of risk management
- tax transparency should not compromise the tax profile of the assets.

Establishing tax transparency for the CCF?

The first CCF was launched in 2004 and since then PwC has reviewed the tax transparency of the CCF in many major OECD and EU countries. Our conclusion is that the CCF would generally be regarded as a tax transparent vehicle by the vast majority of tax authorities. In some cases the transparent position has been reinforced by local Revenue rulings. In general it can be said that the CCF should be treated as tax transparent in most countries but each situation must be examined carefully and a case by case approach is necessary.

What is the VAT position?

The management of a CCF is exempt from VAT and this may confer an advantage over the management of assets in segregated accounts. The comparison of VAT costs will depend on the mix of exempt and taxable, management, custody and administrative activities and the level of VAT recovery.

The future

With a number of CCFs having been successfully launched since its introduction in 2004, the pooling of institutional investors' assets in a tax efficient way is now a reality rather than a possibility, putting Ireland to the forefront as a jurisdiction of choice for asset pooling vehicles. Moreover, investment managers are now awakening to the significant opportunities and benefits that are afforded by the CCF.

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