

[TEXT OF THE FATCA COMMENT LETTER SUBMITTED BY
ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION]

CC:PA:LPD:PR (NOT-121556-10)

Room 5203

Internal Revenue Service

PO Box 7604

Ben Franklin Station

Washington, DC 20044

USA

Sent by email to: Notice.Comments@irs.counsel.treas.gov

6 June 2011

Dear Sir/Madam,

The Foreign Account Tax Compliance Act ('FATCA')

The Alternative Investment Management Association Ltd (AIMA) is the trade body for the hedge fund industry globally. We represent all constituencies within the sector - including hedge fund managers, fund of hedge funds managers, prime brokers, fund administrators, accountants and lawyers. Our membership comprises over 1,200 corporate bodies, of whom approximately 65% are managers, in 45 countries.

We refer to previous submissions we made to you on 29 June and 1 November 2010 in respect of the main provisions of FATCA and Notice 2010-60, issued in August 2010. Both submissions are copied with this letter and main points we made in each of them are summarised in the appendix here.

In this submission, we would like to provide further comments on the application of FATCA to funds and to make some submissions in respect of *Notice 2011-34* (issued on 8 April), which considers some priority concerns raised in previous comments made to you by industry stakeholders.

Application of FATCA to funds

We are aware of previous submissions in relation to the application of FATCA to funds made to you by other industry bodies (most notably, the submission of the European Fund and Asset Management Association (EFAMA)). The potential implementation issues from FATCA are faced by funds of all types and we believe, therefore, that changes to the regime should be scoped so as to apply to all relevant funds. We would like to point out that hedge funds managed by our members are regulated, as collective investment vehicles, in all the main jurisdictions in which they are active and, in the case of corporate vehicles, they are also subject to company law and regulation.

We wish to refer, in particular, to the position of funds which exclude US persons from investment.

Position of restricted funds

We suggest that the Department of Treasury and the Internal Revenue Service consider recognition of a category of funds, which we term here ‘restricted funds’, namely funds restricted to low risk investors ~ such as funds that prohibit investment by US persons. We believe that, if a restriction is properly operated, “deemed-compliant” status should apply for FATCA purposes to all funds, recognising that the objectives of the Department and the Service must be met, while making the compliance burden of meeting those objectives more proportionate to the potential for avoidance of US tax.

We believe that a combination of (i) a contractual prohibition imposed by the fund against any direct US taxable or US tax-exempt investor (determined under US Federal tax principles, a “U.S. Person”), including a contractual representation on the part of the investor of its non-U.S. status, (ii) covenants to maintain such non-US Person status and for investors who are not individuals, covenants to (A) exclude any US Persons from maintaining any interest in such investor (“Exclusion Covenant”) and (B) secure the same Exclusion Covenant from any of its own interest holders who are not individuals and (iii) related contractual indemnities from the investor for any breach of representation or covenant will address the twin objectives of precluding the presence of US persons seeking to avoid US taxation in such fund structures and preserving administrative feasibility, particularly for funds which do not specifically target US investors in the first place. Such funds should be viewed as adequately restricted.

AIMA therefore proposes that restricted funds should be able to apply for ‘deemed-compliant’ status, as a result of which the fund would:

- register with the IRS and obtain an employer identification number (‘EIN’) to provide to withholding agents;
- confirm continued compliance every three years;
- notify the IRS of any material changes in this information within 180 days (on this point, we recommend that the IRS and Treasury provide guidelines in terms of when information changes are deemed to be material for updated reporting);
- maintain suitable procedures to verify direct and indirect account holders;
- not be subject to withholding obligations under FATCA; and
- be subject only to limited reporting requirements.

We believe that AIMA members would find such restricted fund proposals both acceptable and proportionate, while still meeting the objectives of FATCA.

We also recommend that additional guidance be issued:

(a) on specific factors that will enable an FFI to determine the status of a foreign entity (e.g., as an FFI versus a non-financial foreign entity (“NFFE”), among others) under circumstances where that foreign investor entity has not entered into an agreement with the IRS and has not secured an FFI EIN, including forms of self-certifications that the foreign entity can provide that the FFI can rely on;

(b) in connection with guidance on a centralized option for funds:

(i) considering simplified procedures to be followed by asset managers for master-feeder structures where partnership returns are already being filed with the IRS, to avoid duplicative reporting. Generally, master funds will also have US tax return (Form 1065) filing requirements. We request that the Department and the Service consider a centralized option for master-feeders, with simplified additional reporting procedures such as reporting PPPs on Schedule K-1, given that a significant amount of reporting is already provided through Form 1065.

(ii) making express provision for the appropriate person (or persons) to certify compliance, given that the funds themselves do not have their own compliance officers. Section I.A.3 of *Notice 2011-34* proposes that the chief compliance officer or another equivalent-level officer of the FFI will certify completion of procedures for preexisting individual accounts (among other things). Accordingly, guidance is requested on how this section will apply to investment fund FFIs and other FFIs that do not have their own employees but contract with agents for management, administration, custody, transfer agency and other services.

(c) on funds structured as umbrella (or series) type funds, whereby each umbrella fund has a number of

sub-funds (or compartments) with its own investor base, asset portfolio and possibly different investment managers and distributors. Guidance is required as to whether FATCA compliance should be at a sub-fund level or at the umbrella fund level as a whole. We request that it should be at sub-fund level because, if it were at the level of the whole fund, that will not reflect the practical reality of the sub-funds operating as individual funds and will make reporting all the more difficult in respect of passthru payments;

(d) to clarify how off-balance sheet transactions or positions (such as swaps, futures, forwards among others) will be valued;

(e) on whether certain derivative contracts constitute 'US assets' and whether payments thereunder constitute 'withholdable payments'. In particular, we would draw your attention to the fact that a large number of non-US investment managers enter into derivative contracts with US counterparties which have no connection with US income-generating assets. For example, a non-US hedge fund and a US bank may enter into a swap contract under which the US bank, in performance of the contract, makes a payment, the value of which is linked to a basket of foreign securities. As the term 'withholdable payment' is currently drafted, that payment may be caught within such definition; we request that such payment be outside the scope as a US tax withholding in such a case would be inequitable and could inevitably result in a significant shift in business away from US investment banks; and

(f) to clarify that the determination of a passthru payment should be done in a manner that does not result in double-counting a US asset held by the FFI (when calculating the passthru percentage) to the extent that the asset gives rise to amounts that are already treated as withholdable payments made by that FFI.

Notice 2011-34

We note that specific categories of deemed-compliant FFIs have been and are still being considered by the Department and the Service, which is welcomed. AIMA considers that the categories of deemed-compliant FFIs that are investment vehicles, as currently proposed in Section III.C of *Notice 2011-34*, are so narrowly drawn as to be of very limited practical use to our members. We therefore request that you continue to consider our proposals above and the previous submissions of AIMA and other industry bodies in relation to other categories of deemed-compliant FFIs that are investment vehicles, such as exchange traded funds and funds which allow investment only from investors that pose a low risk of tax evasion.

AIMA is also concerned about the potential impact of FATCA on funds that do not invest (either directly or indirectly) in the US and have no US source income. A fund which does not make or receive any 'withholdable payments' or 'passthru' payments would in practice not be subject to the rules relating to withholding of taxes; however, under the current rules it would not be a participating FFI or deemed-compliant FFI. We understand that such funds are likely to be viewed as 'non-participating FFIs' in FATCA terms and this could lead to unintended consequences.

For example, global custodians are likely to ask for representations in relation to compliance with FATCA from all FFIs, whether or not they invest in the US. Funds that have no direct or indirect US source income, and would not normally require US tax advice, are therefore likely to have to take US legal and tax advice in relation to these FATCA representations, and could face difficulties in engaging custodians, or other external service providers, if they cannot make the required representations.

We also ask that the implementation and calculation of PPPs be reconsidered or, preferably, that the application of the concept be deferred beyond 2012, until a reasonably practical methodology is found, which could include the exclusion of equity or debt interests in a publicly traded or widely-held Participating FFIs.

AIMA considers that, as currently drafted, the scope of FATCA could be considerably wider than is required to achieve its objectives and we therefore request that FFIs that are able to demonstrate that they do not invest (either directly or indirectly) in the US and have no US source income, be outside the scope of FATCA. Such FFIs could, for example, be exempted from, or deemed to comply with the requirements of *section 1471(b)*. In order for any such system to be accessible to those who most need it, the requirements to be met by any such FFI wanting to fall outside the scope of FATCA should not run off concepts that in themselves require an understanding of US tax law, so that this relief can be used without obtaining specific US tax advice.

If you would like to discuss any aspects of this submission, please contact me. As you may be aware, our Director of Government & Regulatory Affairs will meet members of the Department and the Service in Washington DC on 9 June, to discuss our members' concerns in relation to FATCA.

Yours faithfully,

Mary Richardson
Director, Head of Tax Affairs

Alternative Investment Management
Association
London

cc:

Mr Steven Musher, Associate Chief Counsel, International IRS
Ms Manal Corwin, International Tax Counsel, Department of the
Treasury