MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

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Via Electronic Filing:

CC:PA:LPD:PR (REG – 121647 – 1)
Internal Revenue Service
Room 5205
P.O. Box 7604
Ben Franklin Station
Washington D.C. 20044

Re: MFA Comments REG-121647-10, Proposed Regulations to Implement FATCA

Dear Ladies and Gentlemen:

Managed Funds Association ("MFA")[1] welcomes this opportunity to comment on proposed regulations (the "Proposed Regulations") issued by the Internal Revenue Service (the "IRS") and the Department of the Treasury ("Treasury") to implement that portion of the Foreign Account Tax Compliance Act of 2010 ("FATCA") set forth in sections 1471-1474 of the Internal Revenue Code of 1986, as amended (the "Code"). MFA supports the broad anti-tax evasion objectives underlying FATCA and we support efforts by Treasury and the IRS to establish an appropriate regime to obtain the information needed for U.S. tax enforcement purposes in a manner that does not impose unnecessary administrative burdens, particularly on those foreign financial institutions ("FFIs") that present little or no opportunity for U.S. taxpayers to evade their U.S. tax obligations.

MFA has participated actively in the process undertaken by the IRS and Treasury following the enactment of FATCA to develop a regulatory framework that is consistent with the statutory objective to deter tax evasion by U.S. persons and that establishes consistent, clear, and efficient compliance requirements for the non-U.S. financial and

[1] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and all other regions where MFA members are market participants.

non-financial institutions to which the legislation is applicable.[2] MFA believes that the Proposed Regulations represent a major step toward these dual policy objectives, particularly when considered in connection with the simultaneous announcement by the IRS and Treasury of an initiative to develop a framework of agreements with non-U.S. governments that would provide an alternative approach to the implementation of FATCA.

MFA looks forward to continuing its dialogue with the IRS and Treasury as the regulatory process moves forward and submits the comments below, which focus on the application of FATCA to non-U.S. investment funds, the interests in which are not publicly traded and, in contrast to bank accounts and publicly traded funds, generally have restricted redemption rights. In the case of MFA members, these non-U.S. investment funds provide a vehicle through which non-U.S. investors access the U.S. capital markets and typically have few, if any, U.S. persons as investors, other than U.S. tax exempt investors such as pension funds and university endowment funds.

Deemed Compliant FFIs

Under section 1471(a), FFIs, including non-U.S. private investment funds, are subject to a special withholding tax unless they comply with section 1471(b), which in turn generally requires an FFI to enter into an agreement with the IRS to provide information with respect to its U.S. account holders and to withhold U.S. tax on certain payments they make to recalcitrant account holders. Section 1471(b)(2) provides an exception to this general rule under which certain categories of FFIs may be "deemed compliant" with section 1471(b), subject to the requirements outlined in section 1471(b)(2).

Section 1.1471-5(f) of the Proposed Regulations provides rules under which FFIs will be deemed compliant with the requirements of section 1471(b)(2) and thus exempt from withholding under sections 1471(a) and (b). Deemed compliant status is provided for "qualified collective investment vehicles" and "restricted funds" if the requirements of section 1.1471-5(f)(1)(i)(C) or (D) respectively are satisfied. Both of these categories require that a fund be "regulated as an investment fund in its country of incorporation or organization." The Proposed Regulations do not provide guidance regarding what it means to be regulated as an investment fund. Because of differences in regulation in different jurisdictions, we believe it is important for the IRS to develop a clear standard that can be applied across jurisdictions. MFA recommends that the IRS and Treasury revise the provisions in section 1.1471-5(f)(1)(i)(C)(1) and (2), or otherwise provide clear guidance, such that this requirement will be met if a fund is *registered* as an investment fund in its country of incorporation or organization, provided that the country of

[2] MFA submitted comments letters in November 2010 and June, 2011 in response to earlier notices on implementation of FATCA. MFA's comment letters are available at the following links: http://www.managedfunds.org/wp-content/uploads/2010/11/MFA-Response-to-IRS-Notice-2010-60.pdf (November 2010 letter), and http://www.managedfunds.org/wp-content/uploads/2011/06/6.7.11-MFA-letter-on-FATCA-notice-2011-34.pdf (June 2011 letter).

incorporation or organization is FATF compliant. To provide clarity, we encourage the IRS to define a FATF compliant jurisdiction to include FATF member jurisdictions and FATF associate member jurisdictions, as posted on the FATF website.

Unlike a "registration" standard, the term "regulated" has an uncertain meaning and, to the extent that it contemplates regulation of investment strategies and other matters similar to the manner in which domestic investment companies are regulated under the Investment Company Act of 1940, such regulation does not appear to have relevance to the goals of FATCA to prevent tax evasion. Further, adopting a standard whereby a fund must be "regulated" as described above would create an unlevel playing field by preventing many private investment funds from being deemed compliant FFIs, even though many private funds have limited redemption rights and thus do not present the tax-related risks of FFIs with immediate or short term redemption rights, such as those granted by many publicly traded funds that would likely be deemed compliant FFIs. Adopting a "registration" requirement, particularly if this requirement were limited to registration in an FATF-compliant jurisdiction, would be better tailored to identify legitimate investment funds that do not pose significant risks of tax evasion.

In the case of a "qualified collective investment vehicle," section 1.1471-5(f)(1)(i)(C)(2) also requires that investors (other than certain debt holders) be limited to participating FFIs, registered deemed compliant FFIs, certain U.S. persons and exempt beneficial owners. MFA recommends that the list of permitted investors be expanded to include persons such as certified deemed compliant FFIs, active Non-Financial Foreign Entities and non-U.S. individuals who do not present the potential for tax evasion at which FATCA is directed.

In the case of a "restricted fund," section 1.1471-5(f)(1)(i)(D)(3) further requires that all distribution agreements used by the fund prohibit sales to "U.S. persons." MFA believes this definition is too broad and encompasses classes of U.S. entities that do not present the potential for tax evasion. The limitation on sales to U.S. owners is particularly onerous given that many offshore funds, directly or indirectly, are sold to tax-exempt U.S. persons. Specifically, as defined in section 7701(a)(30), the term U.S. person includes all U.S. citizens and residents; all domestic partnerships; all domestic corporations; and certain estates and trusts. The use of the term "U.S. person" which employs the 7701(a)(30) definition rather than "specified U.S. person" would impose an unnecessarily significant limitation on the use of the "restricted fund" category. MFA recommends that the disqualified investor category be limited to "specified U.S. persons" as defined in section 1473(3), which applies to all U.S. persons other than those entities that fall within one of nine enumerated categories such publicly traded corporations; tax-exempt organizations; governments and their agencies and instrumentalities; banks; real estate investment trusts; regulated investment companies; common trust funds; and certain other trusts. We believe limiting this provision to "specified U.S. persons" is consistent with the intended purpose of prohibiting sales to those U.S. persons that present a risk of tax evasion. We further note that the definition of "restricted distributor" in section 1.1471-5(f)(4)(vii), unlike the definition of "restricted fund," references the

concept of "specified U.S. persons" rather than "U.S. persons" in outlining the types of investors to whom a restricted distributor may not distribute interests in a fund.

The IRS also should clarify paragraph (f)(1)(i)(D)(1) to make clear that interests in a restricted fund may be sold through a combination of distributors described in paragraph (f)(1)(i)(D)(2) and directly by the restricted fund. Many private funds are sold through a combination of direct sales by the fund and the use of distributors. Further, because private funds typically do not have employees, the fund retains service providers, including investment managers and administrators, to perform services on behalf of the fund. We encourage the IRS to clarify that administrators and investment managers for private funds are not distributors and that interests sold and redeemed by a fund will be deemed sold and redeemed directly by the fund, notwithstanding the services provided by investment managers and administrators.

In section 1.1471-5(f)(4)(iii), the Proposed Regulations provide that a "restricted distributor" must operate "solely in its country of incorporation or organization." Based on our members' discussions with their distributors, MFA believes that this limitation will preclude many distributors from meeting the "restricted distributor" definition given that many distributors distribute fund interests within defined regions. MFA recommends that the definition of "restricted distributor" should be amended to provide that a distributor that operates within the European Union ("EU") will be deemed to operate "solely in its country of incorporation or organization". This proposal would mirror the ability of a "local FFI" that is organized in an EU Member State to treat all of its account holders in the EU as being resident in a single country per section 1.1471-5(f)(1)(i)(A). We further encourage Treasury and the IRS to consider incorporate similar concepts for other regions (*e.g.*, ASEAN).

Section 1.1471-5(f)(4)(v) requires that a restricted distributor must have no more than $175 million in total assets under management ("AUM") and no more than $7 million in gross revenue on its income statement for the most recent accounting year and, if the distributor belongs to an affiliated group, the entire group must have no more than $500 million in total AUM and no more than $20 million in gross revenue for its most recent accounting year on a combined or consolidated income statement. Based on our members' discussions with their distributors, MFA believes that these requirements will preclude many distributors from meeting the definition of "restricted distributor." Accordingly, MFA recommends that the thresholds should be raised to $500 million in total AUM and $20m in gross revenue. Similarly, if the distributor belongs to an affiliated group, the thresholds for the entire group should be raised to $1 billion in total AUM and no more than $60m in gross revenue.

Compliance and Certifications

Under the Proposed Regulations, FFIs will be required to make certain certifications to the IRS. Because non-U.S. private investment funds do not typically have employees, guidance is needed as to which entities and persons acting on behalf of an FFI investment fund have responsibilities for carrying out the compliance

responsibilities of such funds, including making any required certifications. Given the myriad differences in structure and delegation of responsibilities in the investment fund industry, we believe that the governing body of an FFI fund, or any person or entity the governing body decides to delegate responsibility to, should have responsibility for the fund's FATCA compliance, including making any required certifications. Even when the governing body elects to delegate such responsibility, of course, the FFI fund will continue to have ultimate responsibility for its FATCA compliance.

We further encourage the IRS to provide guidance that investment fund FFIs with a common asset manager or agent may choose to centralize their FATCA compliance obligations under a single agreement with the asset manager or agent. In considering this issue, it is important to recognize that investment funds, even when managed by the same adviser, are legally distinct entities which often have different investors and can engage in entirely distinct trading activities in different assets and markets. Any losses at one fund are borne exclusively by the investors in and counterparties to that fund and do not subject other funds managed by the same adviser directly to losses. Notwithstanding this structure, we believe that it would efficient for both market participants and regulators to allow for this centralized option. It also should be noted that the entity responsible for the compliance function should not be required to be an FFI individually. For example, many funds are commonly managed by U.S. resident investment advisers, which should be permitted to have responsibility for the compliance function.

Many private funds are structured as master-feeder or other similar multi-tier structures. For these structures, the outside investors invest directly at the feeder or sub-fund level, and that fund, in turn, invests substantially all of its assets into a master or umbrella fund. Given that the outside investors are at the feeder or sub-fund level, we believe this is the appropriate level at which to apply the FATCA provisions. To provide greater clarity and promote consistency in applying FATCA, we encourage the IRS to provide guidance that the regulations will apply at the feeder or sub-fund level.

Government-to-Government Agreements

The government-to-government agreements are intended to provide an alternative means of compliance with FATCA under which an FFI, organized in a jurisdiction with an intergovernmental agreement in place, that is not exempt from FATCA as a deemed-compliant FFI or otherwise, may comply with FATCA by providing the required information to its home country government which would thereafter provide the information to the IRS. While these agreements will likely have the most relevance to depository and similar institutions, MFA recommends that the model agreement that is expected to emerge from the government-to-government consultation process now underway be structured to permit the alternative compliance regime to be used by private investment funds.

Conclusion

MFA appreciates the opportunity to provide comments on the Proposed Regulations. We support the anti-tax evasion goal underlying FATCA and we believe the Proposed Regulations are an important step toward achieving that goal in a manner that establishes consistent, clear and efficient compliance requirements for FFIs. We believe the suggestions discussed above will further achieve those dual goals.

MFA and its members would welcome an opportunity to meet with the staff from the IRS and Treasury to discuss these and any other issues in connection with implementation of the Proposed Regulation. If you have any questions regarding any of these comments, or if we can provide further information with respect to these or other issues, please do not hesitate to contact Stuart J. Kaswell or me at (202) 730-2600.

Respectfully submitted,

/s/ Richard H. Baker

Richard H. Baker
President and CEO