



Asset Management – Top 10 Things You Didn't Know You Should Know

2019 Financial Services Tax Conference

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Today's Presenters

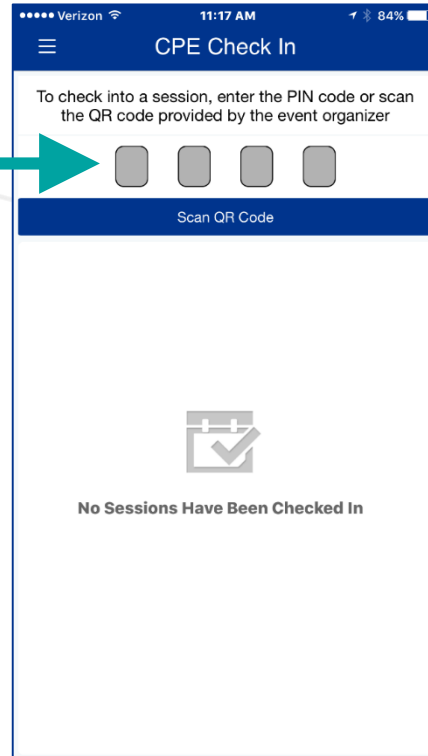
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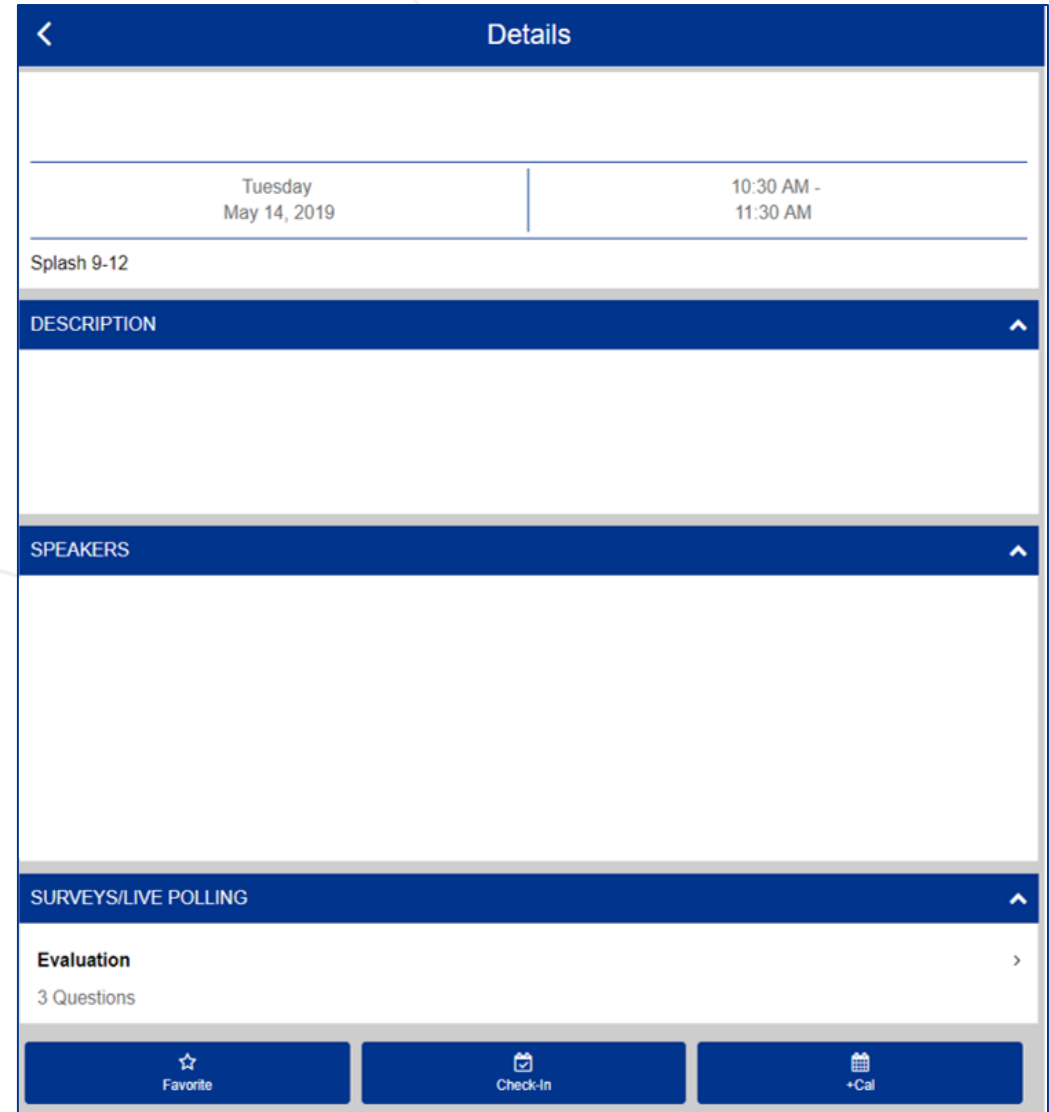
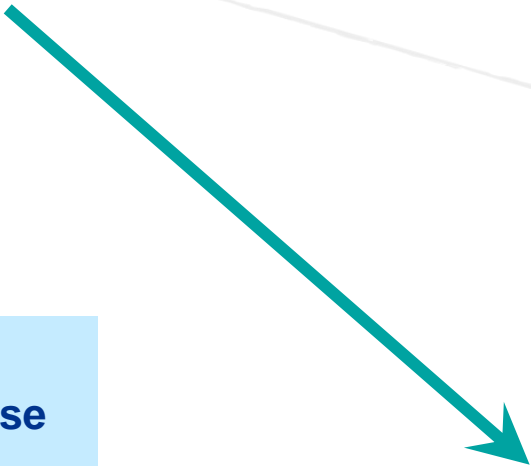
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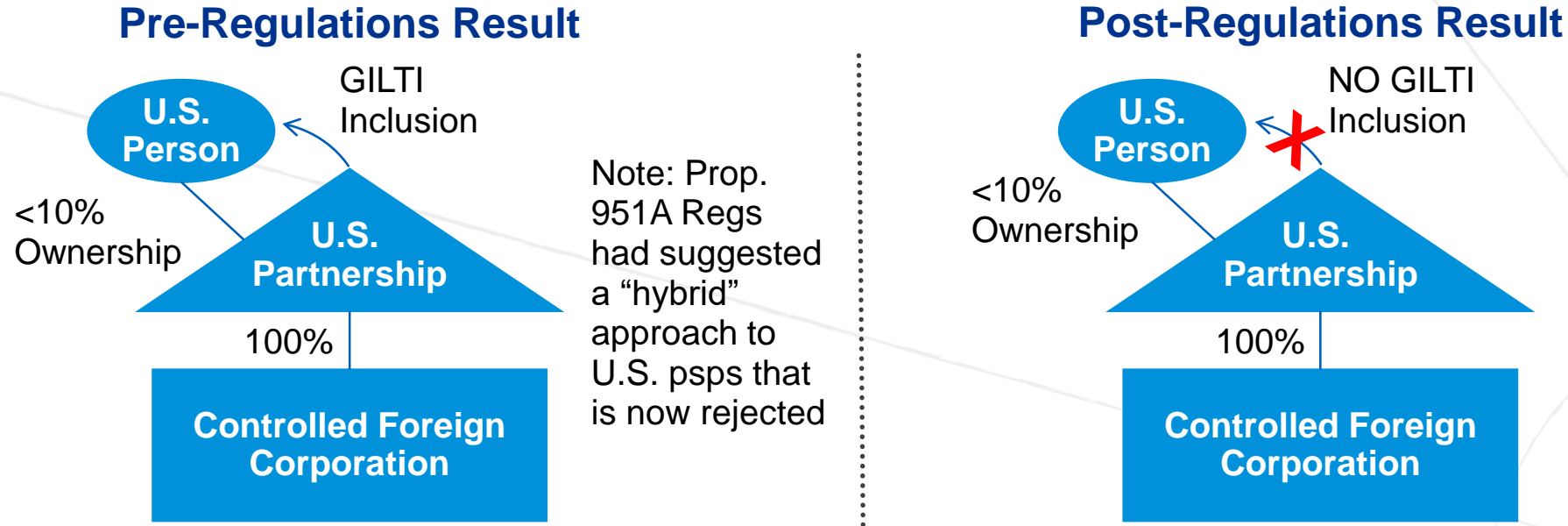


1. Foreign Portfolio Companies

Recent change for less than 10% U.S. Investors

- Recent final 951A regulations provide that a U.S. partnership is treated as an aggregate entity for **GILTI inclusion** purposes, meaning that a U.S. person that is not itself a U.S. shareholder of a CFC does not have GILTI as a result of ownership of a CFC through a U.S. partnership.
- Likewise, recent 951 proposed regulations provide that a U.S. partnership is treated as an aggregate entity for **subpart F inclusion** purposes

Illustrated: GILTI Pickup <10% U.S. Owner



- Before Final 951A Regulations, a U.S. person would include their proportionate share of GILTI tested income or loss through a U.S. partnership, even if that U.S. person were not themselves a U.S. shareholder, because they own their CFC interests through a U.S. partnership that is itself a U.S. shareholder
- Following Final 951A Regulations, a U.S. partnership is treated as an aggregate entity for GILTI inclusion purposes, meaning that a U.S. person that is not itself a U.S. shareholder of a CFC does not have GILTI tested income or loss as a result of ownership of a CFC through a U.S. partnership

2. PFIC and CFCs—Collateral Effects

Implication of change for funds

- Less impetus to restructure funds to eliminate domestic partnership
- Are there still benefits to avoiding domestic partnerships? Don't forget about 1248.

More on PFICS

- Pop-up PFICs and bad inclusion (2018) = non basis?

Where do we see things headed?

- Consider the 962 election!

NEW!! PFIC Regulations

- Last week, new PFIC regs dropped clarifying many long-standing uncertainties, including the PFIC insurance exception, rules for related party income, long-through rules for partnership investments (taxpayer unfavorable ☹️) and, as discussed below, PFIC testing.
 - Ownership attribution (taxpayer favorable 😊). Confirmation of top-down approach to ownership attribution through partnerships (particularly favorable to private equity and asset management structures)

3. Carried Interest

Carry Waivers

- Do they work?
- How do they work?
- Are people doing them?
- Multiple realizations in a single year—do special allocations work the way people think?
- Fiduciary issues

4. Holding Period—Follow on Investments.

Funds may make follow on investment calls for subsequent contributions into portfolio companies.

Partnerships

Partners have one capital account and one basis in their partnership interest.

Partners can have a bifurcated holding period.

- Portion of interest issued for cash and hot assets = ST holding period starts.
- Portion of interest issued for long term capital and section 1231 assets = HP tacks.
- Cash contributions start a new holding period for the portion of the interest acquired with cash.

Corporations

Shares of stock newly issued for contributed property in a section 351 transaction take a holding period based on the holding period of the contributed property (may be divided between short- and long-term).

- Shares of stock newly issued for cash have a holding period that begins on the date of the contribution/issuance

Although not entirely clear, a cash contribution by a shareholder without the issuance of new shares will likely result in a segmented holding period for the shareholder's pre-existing shares.

Carried Interest—Follow on Investments

HoldCo wants to acquire an additional business as an add on to its investment in OpCo.

— Fund I and AIV want to acquire an add on to its initial investment in OpCo.

Fund I and AIV invested in HoldCo 4 yrs prior to acquisition of Target.

— A sale of HoldCo interests doesn't trigger section 1061 gain.

How should Fund I and AIV fund the acquisition of Target?

— Holding period concerns with contributions of capital.

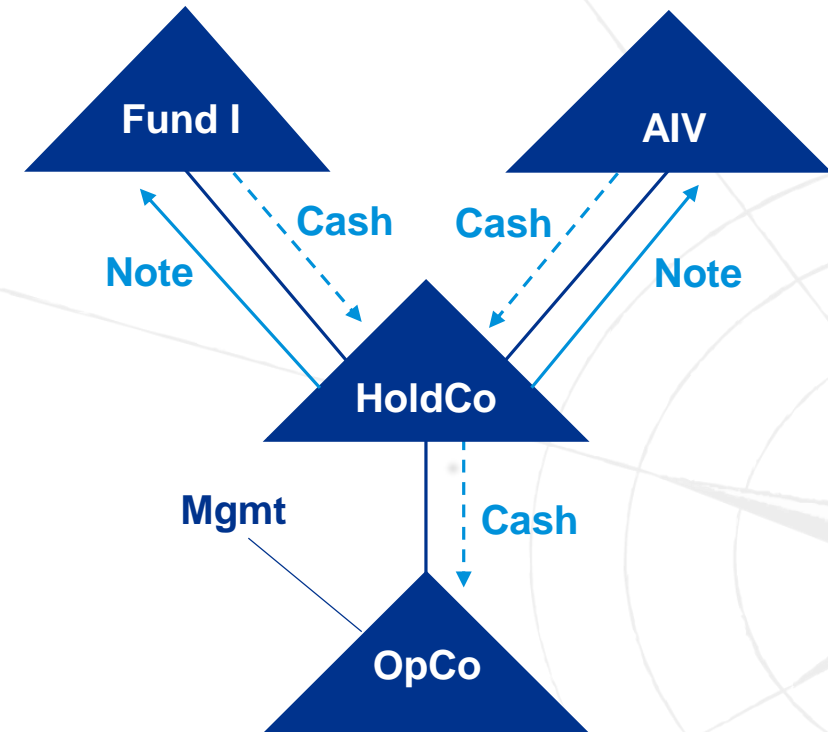
— Potential taint of holding period in HoldCo if cash is contributed in a capital call

Consider funding with debt.

— How does sharing impact decision whether to debt finance?

— Debt-equity considerations – consider Holdco leverage capacity

— Section 163(j) concerns? Fund I and AIV receive interest income. Can HoldCo deduct interests expense?



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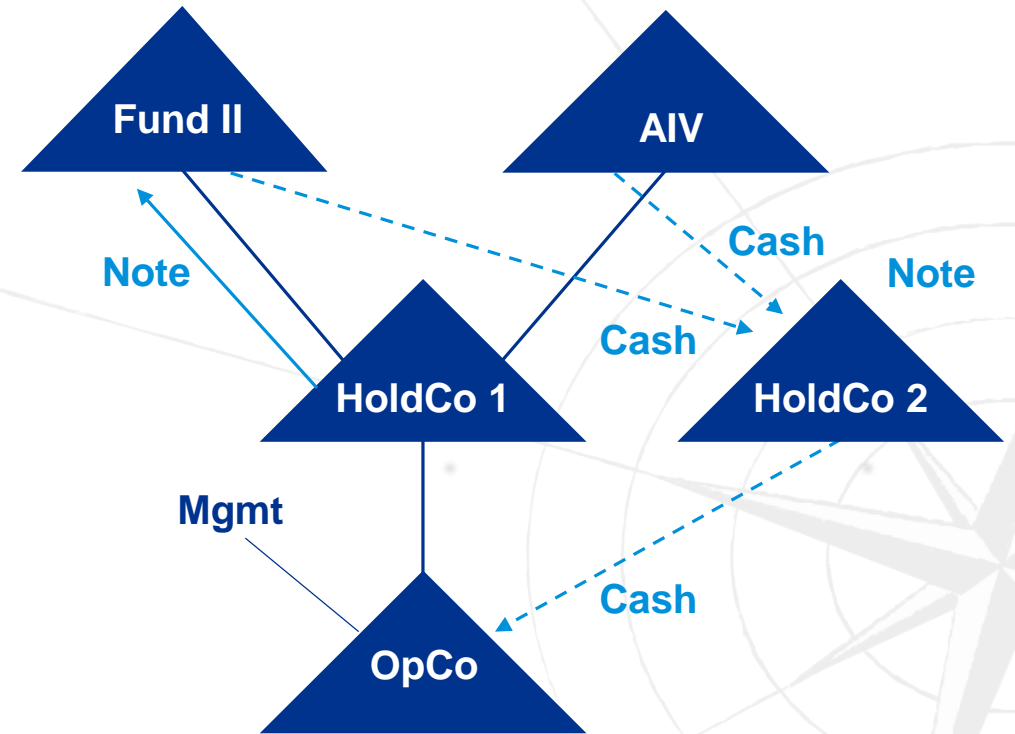
- A sale of HoldCo interests doesn't trigger section 1061 gain.

How should Fund I and AIV fund the acquisition of Target?

- Holding period concerns with contributions of capital.
- Potential taint of holding period in HoldCo 1 if cash is contributed to HoldCo 1 in a capital call.

Consider funding sister entity

- Structuring complexity
- Administrative complexity



5. REITs—Should they be used more?

REIT for Carry?

- Section 1061 applies to “applicable partnership interests” which does **not** include a REIT
- Fund as a REIT or a REIT carry-vehicle?
 - Funny class of stock and the closely held requirement...

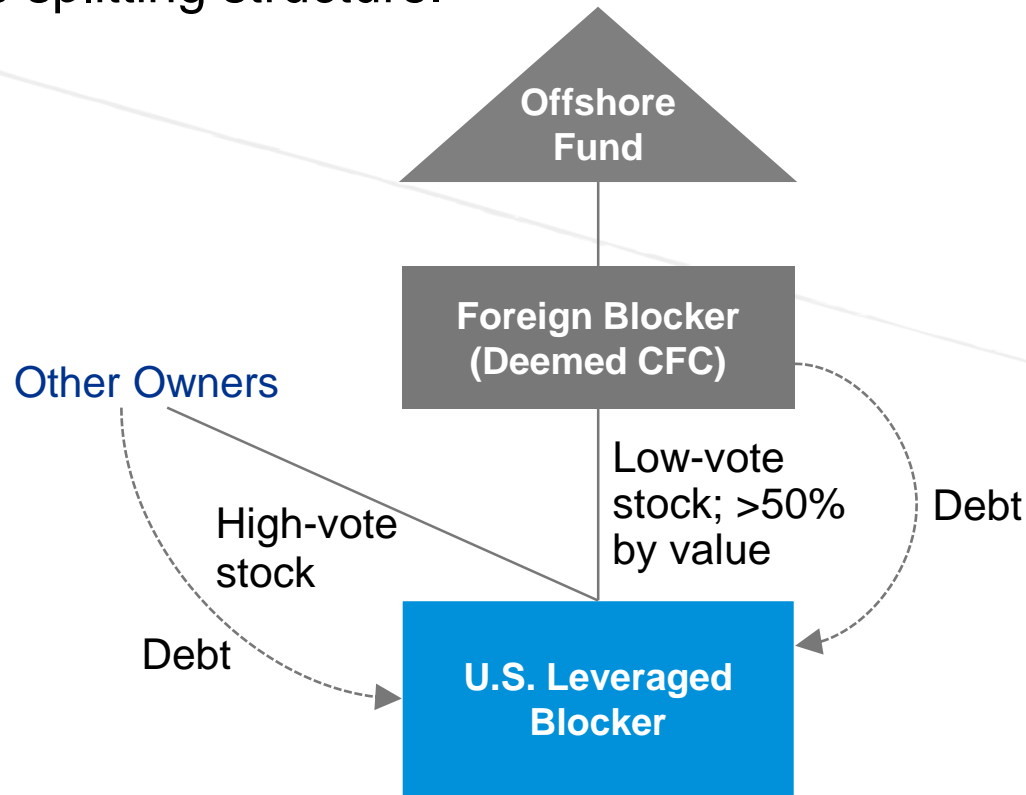
REIT for 199A deductions

- Basic observation is that there is no payroll/basis limitation for REIT dividends
- Play for real estate based lending? Mortgage REITs!
 - Good for investors?
 - Foreign and tax exempt investors have special issues to consider

6. Portfolio Interest

Downward Attribution 881(c)(3)(C) trap

— Example of a vote splitting structure.



7. Family Offices

Management fees deductible?

— Lender's Bagel

- Paradigm shift of just great facts?

— Converting fee income into partnership allocations—variations on a theme!

- Entrepreneurial risk the right standard?
- Questions regarding application of the standard in the family context

8. Credit funds

Loan Guidelines

- How has the syndication market changed?
- Commitment before the bank?
- Is there a new emerging market consensus for guidelines that work?

Trade Claims

- FDAP vs ECI
 - Interest?
 - Source?

9. Workout Activities

Are workout activities a trade or business?

- Buying distressed debt with a view towards working it out is a long-standing trade or business issue
- Differing views but perhaps a building consensus?
 - Not ETB provided no fees/loans vs. an intent-based, value-add test
 - Whipple? Sun Capital? Safe harbor?
 - Careful what your PPM says!

Collection activities a trade or business?

- Related questions also arise on whether collection activities may rise to the level of a trade or business.
 - No clear answer but consistency (212/162 vs 864) is a factor in this context

10. Update on Self-Employment Tax Campaign

Asset Managers and SECA

- Asset Managers are often structured so as to take advantage of an exemption from self-employment tax for limited partners in limited partnerships.
- The IRS has made challenging these structures a national campaign.

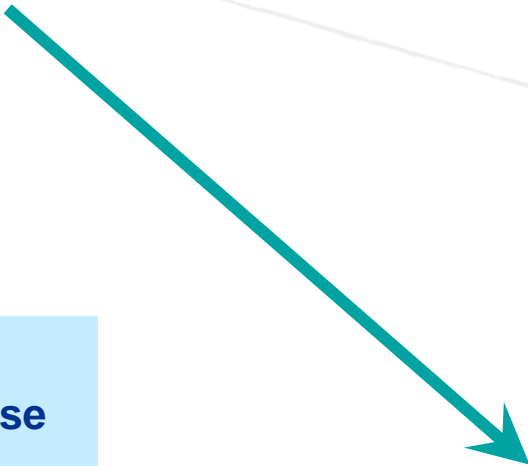
Current Status of IRS Campaign

- Low Hanging fruit or principled attack?

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