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Re: Request for delay in implementation of Section 1446(f) for non-publicly traded partnerships

Gentlemen:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ requests that the relief from withholding under new Section 1446(f) of the Internal Revenue Code² (the “Code”) that was

¹ SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over \$2.5 trillion for businesses and municipalities in the U.S., serving clients with over \$18.5 trillion in assets and managing more than \$67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

² Except as otherwise expressly provided herein, all references to “Section” are to sections of the Internal Revenue Code of 1986, as amended (the “Code”), and all references to “Treas. Reg. §” or “Regulations” are

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provided to sales of publicly traded partnership interests in Notice 2018-08³ be extended to partnership interests that are not publicly traded. Notice 2018-08 requested comments on whether the challenges that apply to transfers of publicly-traded partnerships under Section 1446(f) also apply to non-publicly traded partnerships; the members of SIFMA confirm that such relief is warranted. The new withholding requirement raises many issues of both procedure and substance, making compliance impractical with respect to sales of both publicly traded and non-publicly traded partnerships until the Department of Treasury (“Treasury”) and the Internal Revenue Service (“IRS”) publish guidance for implementing this provision. Further, we would underscore the need for immediate guidance under Section 864(c)(8) for taxpayers to determine their tax liability with respect to a sale of a partnership interest.

By way of background, Public Law 115-97, the “Tax Cuts and Jobs Act”,⁴ added two new provisions to the Code concerning sales of partnership interests by foreign persons. New Section 864(c)(8) treats a foreign partner’s gain (or loss) from the disposition of an interest in a partnership as effectively connected income subject to US net income tax to the extent that the partner would have had effectively connected gain (or loss) had the partnership sold all of its assets at fair market value on the disposition date. New Section 1446(f) requires that a buyer of a partnership interest from a foreign person withhold 10 percent of the “amount realized” by the outgoing partner “if any portion of the gain (if any) on any disposition of an interest in a partnership would be” subject to tax under Section 864(c)(8). If the transferee fails to withhold the correct amount of tax under Section 1446(f), the obligation to collect is shifted to the partnership itself, which is required to withhold from future distributions to the transferee partner. Section 1446(f) applies to transfers of partnership interests after December 31, 2017.

Notice 2018-08 requested comments on the guidance that may be needed to assist taxpayers in applying new Sections 864(c)(8) and 1446(f). SIFMA intends to submit a letter including specific substantive recommendations for that guidance, however, our members believe the numerous questions that must be addressed in that guidance are ample reason for a temporary suspension of withholding for dispositions of interests in non-publicly traded partnerships. These questions include:

- How is the “amount realized” to be determined? As acknowledged in Notice 2018-08, it is uncertain whether the amount realized comprises only cash and other property exchanged for the partnership interest, or whether partnership liabilities need to be taken into account under Section 752(d). What are the rules for withholding if the partnership interest is exchanged for non-cash property?
- How precisely does a seller demonstrate to a buyer it is not a foreign person? Section 1446(f)(2) refers to a “non-foreign affidavit” containing the seller’s taxpayer identification number (“TIN”), but what else must the affidavit contain? The Form W-9, which is used for

to Treasury Regulations issued pursuant to the Code. Furthermore, all references to the “IRS” or the “Service” are to the Internal Revenue Service.

³ Notice 2018-08, 2018-5 IRB.

⁴ The Tax Cuts and Jobs Act was the short title of H.R. 1 prior to adoption of the last Senate amendment on December 20, 2017 when the short title was stricken from the bill.

collecting TINs and contains a certification that the signer is “a US citizen or other US person,” appears to meet the statutory requirements of a “non-foreign affidavit”. However, confirmation is requested that a Form W-9 is sufficient.

- What will be the deadline for depositing tax, and which tax forms are required to be filed by the buyer to report the withholding tax liability? When are those forms due?
- Is the buyer required to provide an information return to the IRS or to the seller, and if so, on what form and by what deadline?
- Is withholding required when the seller has no gain?
 - Can the buyer avoid withholding if it receives a statement from the seller certifying that no “portion of the gain (if any) on any disposition of an interest in a partnership would be” subject to tax under Section 864(c)(8)? If so, what evidence would the seller need to demonstrate this? How would the seller be expected to obtain such evidence in the absence of detailed information from the underlying partnership (which may be reluctant to provide such information to the seller given its own secondary liability in the event the buyer fails to withhold)?
 - In a partial redemption of the partnership interest which does not result in any gain under Section 731(a), does the partnership have to withhold?
- In the case of tiered partnerships, what are the obligations for an upper-tier partnership to determine whether any of its lower-tier holding partnerships have potential US trade or business assets?
- Section 1446(f)(3) allows the Secretary of the Treasury to reduce the amount of withholding upon a determination that “such reduced amount will not jeopardize the collection of the tax.” What is the procedure to apply for such a reduction? What must the buyer or seller show, and what is the standard of proof, given that the buyer and the seller may not have direct knowledge of the assets of the partnership connected to the US trade or business or their value?
- Section 1446(f)(4) provides that if a buyer fails to withhold, the partnership itself must withhold from future distributions to the buyer as a new partner. How do the buyer and the partnership establish that the correct amount was withheld by the buyer, particularly if an exception to withholding or a reduced amount of withholding is authorized? Who, if anyone, gets a tax credit for withholding by the partnership?

- Section 1446(f)(6) provides a broad grant of regulatory authority to the Treasury to implement the withholding tax, “including regulations providing for exceptions from the provisions of this subsection.” Section 864(c)(8)(E) provides a similarly broad grant of authority for regulations to implement the substantive tax, “including with respect to exchanges described in section 332, 351, 354, 355, 356, or 361.” When, if ever, is withholding excused in a non-recognition transaction?
- Confirmation that a loan of a partnership interest is not a disposition for purposes of Section 1446(f).

Until these questions are answered, we are concerned that withholding cannot be done correctly, if at all, and the risk of over and under withholding is significant. Accordingly, our members believe the IRS should extend the relief provided in Notice 2018-08 to all sales of partnership interests, not just sales of publicly traded partnership interests.

Further, due to the significant practical problems referenced in Notice 2018-08, SIFMA believes that the Treasury should use its regulatory authority under Section 1446(f)(6) to extend the relief granted in Notice 2018-08 for dispositions of publicly traded partnership interests indefinitely or at least until such practical problems can be overcome and market participants have had an appropriate period of time to adjust. Otherwise, our members would support *de minimis* rules to enhance the administrability of Section 1446(f). If the partnership’s US trade or business assets make up less than a specified percentage of the value of the partnership’s total assets, an exception analogous to the one that applies under Section 1445 would prevent withholding in cases where it is likely to be excessive.⁵ Similarly, if the partnership interest being sold is a minor interest in the partnership, rules analogous to those under Section 897(c)(3) and (k)(1)(A) should apply to prevent withholding on the sale.


Conclusion

We very much appreciate your consideration of our members’ concerns, and we would appreciate the opportunity to discuss the issues in this submission with you and your colleagues. As discussed above, we intend to submit a follow up letter addressing the substantive points in order to make constructive recommendations for regulatory guidance.

⁵ Withholding under Section 1445 is required upon the transfer of a partnership interest only if: (i) 50% or more of the value of the gross assets of such partnership consists of US real property interests (USRPIs); and (ii) 90% or more of the value of the gross assets of the partnership consists of USRPIs plus any cash or cash equivalents.

Please do not hesitate to contact me at (202) 962-7333 or ppeabody@sifma.org, or SIFMA members' outside consultants Tara Ferris or Jonathan Jackel at Ernst & Young. Tara can be reached at (212) 360-9697 or tara.ferris@ey.com and Jonathan can be reached at Jonathan.Jackel@ey.com (202) 327-5725.

Sincerely,



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SIFMA