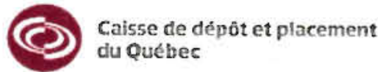

April 12, 2018

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Re: Comments Addressing Section 897(l) Qualified Foreign Pension Fund Requirements

Caisse de depot et placement du Quebec, PGGM, the New Zealand Super Fund, Pension Denmark, and the Future Fund thank you for the opportunity to provide written comments on section 897(l), which exempts qualified foreign pension funds ("**QFPFs**") from the application of section 897 (also known as FIRPTA). Section 897(l) was enacted and signed into law on December 18, 2015 under the Protecting Americans From Tax Hikes Act ("**PATH Act**")[1] and as amended by the Consolidated Appropriations Act of 2018 ("**Appropriations Act**"), signed into law on March 23, 2018. We respectfully request that Treasury consider the

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[1] P.L. 114-113.

following comments and proposed recommendations before issuing regulations under section 897(l).

We are a group of government and public pension funds from Canada, the Netherlands, New Zealand, Denmark and Australia, respectively, invested across multiple asset classes throughout the world, with a significant number of investments in the United States, including U.S. infrastructure and real estate assets. We invest and manage funds for public pension, retirement, disability and employee benefit plans. Each of us, or investors we represent, believe that we should qualify as QFPFs and, where relevant, qualify as retirement, pension or employee benefit funds under income tax treaties with the United States; some of us also qualify as foreign governments under section 892. Collectively, we manage over USD 650 billion in assets as at September, 2017.

We anticipate significant growth in our U.S. infrastructure and real estate investments over the next several years, especially if we would qualify as QFPFs. We therefore welcome the enactment of section 897(l) and view it as a clear expression of U.S. policy to encourage investment in U.S. real estate by foreign pension funds. Consistent with this policy, it will be necessary that Treasury and the IRS provide regulatory guidance regarding the definition of a QFPF that is sufficiently clear and inclusive of foreign pension funds that have the types of characteristics that make evident they should be included from a policy perspective. There are many different pension regimes in the world, each with its unique rules and it is somewhat unclear as to how the statutory definition of a QFPF applies in certain cases.

We recommend that regulations be issued to provide rules that permit a sufficiently broad set of foreign pension funds to qualify for the benefits of section 897(l) – and for pension funds to easily determine their status – while ensuring that entities that may not be within the intended reach of section 897(l) cannot inappropriately benefit from section 897(l). In that, we welcome the amendments to the QFPF definition enacted as part of the Appropriations Act. These amendments reflect a broad definition of QFPFs and suggest that Congress and the Administration intend an expansive definition and application of the QFPF rules. Nevertheless, we believe there remain a number of issues with respect to the QFPF definition that regulations ought to clarify.

This comment letter suggests several ways in which regulations can clarify the specific rules of section 897(l) and that we believe will give foreign pension fund investors greater certainty, directly leading to increased investment in U.S. infrastructure and real estate assets by such investors. This letter first provides a brief overview of the relevant statutory rules (as amended by the Appropriations Act), followed by our proposals and recommendations regarding several of the specific requirements of the definition of a QFPF under section 897(l)(2).

General Overview of Section 897

Section 897 of the Internal Revenue Code ("**Code**") was enacted as part of Foreign Investment in Real Property Tax Act ("**FIRPTA**"). Section 897 provides that gain or loss of a foreign corporation (or a non-resident alien individual) from the disposition of a U.S. real property interest ("**USRPI**")[2] must be taken into account under section 881(a)(1) (or section 871(b)(1) for individuals) (*i.e.*, as if the foreign person were engaged in the conduct of a U.S. trade or

[2] A USRPI includes any interest (other than solely as a creditor) in real property located in the United States or the Virgin Islands, including land and unsevered natural products of the land, improvements on land, personal property associated with the use of real property, certain valuable leases, interests in mines, well, and other natural deposits. Section 897(c)(1)(A)(i).

business and such gain or loss from the disposition of USRPI is effectively connected with such U.S. trade or business). A USRPI includes both a direct interest in real property located in the United States and an interest in a U.S. corporation that is (or was during a testing period) a U.S. real property holding corporation ("**USRPHC**").

In 2015, the PATH Act, in part, modified the application of FIRPTA regarding interests held by foreign retirement and pension funds by adding new statutory exceptions under section 897.

As a result of these amendments, section 897 does not apply to any USRPI held directly or indirectly through one or more partnerships, or to any distribution received from a real estate investment trust ("**REIT**"), by a QFPF or by a foreign entity all of the interests of which are owned by a QFPF.[3] This means that QFPFs generally will be exempt from U.S. federal income tax on gains from the disposition of a USRPHC, distributions from a USRPHC that are characterized as capital gains under section 301(c)(3), and REIT distributions that are attributable to the sale of USRPIs. QFPFs may also be exempt from U.S. federal income tax on sales of direct interests in U.S. real property, although in practice such holdings frequently would be taxable if the real property is actually used in the conduct of a U.S. trade or business.

A QFPF is defined as any trust, corporation, or other organization or arrangement (collectively, a "**Fund**") that meets each of the following five requirements:[4]

(A) It is created or organized under the law of a country other than the United States;

(B) Which is established (the "**Employee/Employer Requirement**")-

   i. by such country (or one or more political subdivisions thereof) to provide retirement or pension benefits to participants or beneficiaries that are current or former employees (including self-employed individuals) or persons designated by such employees, as a result of services rendered by such employees to their employers, or

   ii. by one or more employers to provide retirement or pension benefits to participants or beneficiaries that are current or former employees (including self-employed individuals) or persons designated by such employees in consideration for services rendered by such employees to such employers;

(C) It does not have a single participant or beneficiary with a right to more than five percent of its assets or income;

(D) It is subject to government regulation and with respect to which annual information about its beneficiaries is provided, or is otherwise available, to the relevant tax authorities in the country in which it is established or operates; and

(E) Under the laws of the country in which it is established or operates, either (i) contributions to such Fund which would otherwise be subject to tax under

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[3] *See* JCX-144-15, Technical Explanation Of The Protecting Americans From Tax Hikes Act Of 2015, House Amendment #2 To The Senate Amendment To H.R. 2029 (Rules Committee Print 114-40). Specifically, pursuant to the amendments enacted as part of the Appropriations Act, a QFPF, and any entity wholly owned by a QFPF, shall not be treated as a non-resident alien individual or foreign corporation for purposes of section 897 (*i.e.*, for FIRPTA purposes) (see amended section 897(l)(1)).

[4] Section 897(l)(2)(A)-(E) (as amended by the Appropriations Act).

such laws are deductible or excluded from the gross income of such entity or arrangement or taxed at a reduced rate, or (ii) taxation of any investment income of Fund is deferred or such income is excluded from the gross income of such entity or arrangement or is taxed at a reduced rate.

Effective December 18, 2015, QFPFs are exempt from FIRPTA by virtue of section 897(l). Furthermore, QFPFs are exempt from FIRPTA withholding under section 1445.[5]

In the next sections, we recommend an expansive interpretation of the definition of a QFPF (as evidenced by the recently enacted Appropriations Act), in particular: (1) further clarification of the "Employee/Employer" requirement; (2) clarification of the term "arrangement"; (3) clarification of annual information reporting requirement; (4) extending the definition of QFPF to pension funds treated as controlled pension trusts of foreign governments under Temp. Treas. Reg. Sec. 1.892-2T(c); and (5) clarification of qualification for section 897(l) benefits for entities wholly owned by multiple QFPFs, as well as in multi-tiered structures. We also recommend further clarifications be made to the section 1445 FIRPTA withholding regulations, namely with respect to U.S. real property interests held by QFPFs through foreign partnerships.

1. Clarification of the "Employee/Employer" requirement and the benefits QFPFs may provide

We welcome the amendment to section 897(l)(2)(B) enacted in the Appropriations Act which clarified that government-sponsored pension funds established to provide public retirement or pension benefits, including with respect to self-employed persons should satisfy this condition.

However, we recommend further guidance be provided in regulations as to how to satisfy the Employee/Employer requirement. The Joint Committee on Taxation's 2015 Bluebook provided that a government-sponsored pension fund that is established for the general public of a foreign country should be included within the definition of a QFPF and should be treated as satisfying the Employer/Employee requirement. In other words, funds such as social security funds should qualify, notwithstanding that they are not organized for a specified employer or employers.

Amended section 897(l)(2)(B) provides that government sponsored pension funds satisfy the condition where they provide retirement or pension benefits to participants that are current or former employees as a result of services rendered. While such government sponsored retirement funds typically provide pension benefits to recipients as a result of their employment (in the public and/or the private sector), a number of these government funds also extend pension and retirement benefits to recipients who are not current or former employees of a given employer (*e.g.*, because of disability, inability to work, etc.).

Further, amended section 897(l)(2)(B) does not explicitly address pension or retirement funds that also provide certain ancillary benefits. In that, the regulations should clarify the impact of ancillary benefits that may be paid by a QFPF. Section 897(l)(2)(B) (as amended) requires that a QFPF be established to provide retirement or pension benefits, but it does not provide whether such retirement or pension benefits must be the exclusive benefits that may be

[5] *See* section 1445(f)(3)(B). The JCT Report explains the changes made to section 1445 are "conforming changes" which eliminate withholding on sales by qualified foreign pension funds, as well as by their wholly-owned foreign subsidiaries, of USRPIs. *See* JCX-144-15.

provided or must only be the primary benefits. Thus, clarification as to the provision of ancillary benefits is needed. Similarly to U.S. pension funds, foreign pension funds almost always pay ancillary benefits, such as disability, death, survivor, or health benefits. In certain cases, such funds may also provide other ancillary benefits, such as employee savings provisions that are not the types of benefits U.S. retirement funds typically offer. We suggest clarifying the level and type of ancillary benefits a QFPF may offer.

Recommendations

We recommend that regulations clarify that a government-sponsored pension fund established to provide public retirement or pension benefits will satisfy the Employee/Employer requirement even where some of its recipients are not current or former employees.

We also recommend that regulations clarify the retirement benefit requirement of section 897(l)(2)(B) will be satisfied if a fund is established primarily to pay retirement or pension benefits.

Treasury and the IRS may also provide in regulations that certain types of ancillary benefits will not cause a fund to fail the retirement benefits requirement. In such a case, we would recommend that Treasury and the IRS provide a list of types of benefits that will be deemed to be in the nature of retirement benefits (*e.g.*, survivor benefits, disability benefits) and provide a *de minimis* rule that permits a certain amount of the fund's benefits (*e.g.*, 25 percent of total benefits, over a three or five year averaging period) to be other benefits not specifically deemed to be retirement or pension benefits. Such a *de minimis* rule would be needed because it is unlikely that regulations can include a list of permitted ancillary benefits that is sufficiently inclusive of the various additional benefits that retirement and pension funds around the world offer.

2. Interpret the term "arrangement" expansively

Section 897(l)(2) defines a QFPF to mean any Fund – i.e., trust, corporation, or other organization or arrangement. The section 897(l) regulations should clarify and take an expansive view of the term "arrangement" for the purposes of section 897(l) taking into account that pension funds in certain jurisdictions may, for example, be constituted without a defined legal form or as multiple legal entities. The JCT Bluebook, in discussing section 897(l), stated that "[f]oreign pension funds may be structured in a variety of ways and may comprise one or more separate entities. The word 'arrangement' encompasses such alternative structures."

For example, the New Zealand Superannuation fund, being a governmental pension fund, is not organized as a separate entity, but rather as a separate account of the government of New Zealand set aside to fund its pension liabilities.

In other situations, a pension trust may be established to administer a retirement plan, but the funds of the trust not required to satisfy current requirements to pay benefits are contributed to a separate entity that invests on behalf of the pension trust. Finally, a single employer may maintain separate trusts for different employees (*e.g.*, working in different countries, or having different roles within the company that is the employer) but have these

trusts invest together.

In each of the above examples, we believe that, consistent with the JCT's language, a single arrangement exists, and we recommend that regulations provide clarification in this regard.

Recommendation

We recommend that regulations under section 897(l) clarify that the reference in section 897(l)(2) to any Fund – i.e., to "any trust, corporation, or other organization or arrangement" is intended to be interpreted broadly so that a QFPF can take any legal or contractual form, including consisting of multiple legal entities or no legal entities (such as a separate account set aside to fund pension benefits, provided that such account is appropriately ring-fenced to ensure that its purpose is to primarily provide retirement or pension benefits).

3. Clarify Annual Information Reporting Requirements

We welcome the amendment to the information reporting requirement of section 897(l)(2)(D) enacted in the Appropriations Act, namely that the requirement can be satisfied where the QFPF (in addition to being subject to government regulations) provides annual information about its beneficiaries, or such information is otherwise available, to the relevant tax authorities (emphasis added).[6]

We recommend that regulations clarify how a foreign pension fund can satisfy this requirement, namely around circumstances where information about a QFPF's beneficiaries would be considered available to the relevant tax authorities. Again, this requirement should be interpreted broadly.

Further, the regulations should take into account that, where the fund is a governmental pension fund, the government would generally already have, or be able to obtain, the requisite information regarding beneficiaries.

Recommendation

We recommend that regulations clarify that, if the fund is a governmental pension fund, it would be deemed to have satisfied the information reporting requirement.

4. Other simplifying rules - Pension funds that are section 892 Foreign Governments Should Qualify as QFPFs

Section 897(l)(3) gives Treasury and the IRS broad regulatory authority to prescribe such regulations as are necessary or appropriate to carry out the purposes of section 897(l), *i.e.*, to encourage investment in U.S. real estate and infrastructure by foreign pension funds. Accordingly, Treasury and the IRS may consider identifying certain types of entities that primarily provide pension type benefits, in other contexts relevant to U.S. tax law and that would therefore have already determined whether they satisfy the requisite definitions under such laws. For example, under Temp. Treas. Reg. Sec. 1.892-2T(c), a separately organized pension trust of a foreign government qualifies for exemption from U.S. federal income tax on

[6] Section 897(l)(2)(D), as originally enacted, provided that QFPFs need to provide annual information reporting about their beneficiaries to the relevant tax authorites in the country in which they are established or operate.

certain investment income. Similarly, a number of U.S. income tax treaties provide enhanced benefits (*e.g.*, an exemption from U.S. tax on dividend income) for pension, retirement or employee benefit plans resident in certain countries. In each of these cases, Congress or Treasury has made a determination that these plans, if they satisfy the relevant conditions, are appropriate candidates for beneficial treatment under U.S. tax laws compared to other foreign investors. Treating such entities as QFPFs would be an appropriate exercise of Treasury's broad regulatory authority and would greatly increase the certainty and efficiency with which such pension funds can ascertain their status under section 897(l).

Recommendation

Regulations should provide that any pension fund that satisfies the requirements of Temp. Treas. Reg. Sec. 1.892-2T(c) and any pension, retirement or employee benefit fund that satisfies the requirements of an income tax treaty between its country of residence and the United States (including the residence requirement, the applicable limitation on benefits requirement, and the requirements to be eligible for enhanced benefits under such treaty) is treated as a QFPF.

5. Qualification for section 897(l) benefits for entities owned by QFPFs

Section 897(l)(1) provides that a QFPF, and any entity wholly owned by a QFPF (emphasis added), shall not be treated as a non-resident alien individual or foreign corporation for purposes of section 897 (*i.e.*, for FIRPTA purposes). Accordingly, QFPFs and any entity wholly owned by a QFPF are exempt from FIRPTA, including on any capital gain REIT distributions they receive.

We believe several clarifications to the rule applying to entities that are wholly owned by QFPFs are warranted, each of which is consistent with the purposes of section 897(l). First, without clarification, arguably the exemption applies only to entities that are directly wholly owned by a QFPF, and not if the QFPF holds the entity through another wholly owned intermediate entity. We do not believe such a strict interpretation to be consistent with the intent of the statute, but we urge Treasury and the IRS to clarify this in regulations.

Second, it is unclear whether the provision applies only to entities wholly owned by a single QFPF or also to entities wholly owned by multiple QFPFs. We recommend the latter interpretation as giving effect to the purposes of section 897(l). That is, if two QFPFs each seek to invest in the same USRPHC, if they do so directly, then each benefits from section 897(l). The same result obtains if they pool their investment through a partnership. The result should not be different if they pool their investment through an entity that is treated as a corporation for U.S. federal income tax purposes (for example, the use of a per se corporation may be warranted if the pooling vehicle also invests in real estate assets in other countries and legal or tax considerations in such countries mandate the use of a particular entity type).

Recommendations

We recommend that regulations clarify that section 897(l) applies to multi-tiered structures, *i.e.* that an entity that is indirectly wholly owned by QFPFs through other entities qualifies for section 897(l) benefits.

We further recommend that regulations clarify that an entity that is wholly owned by multiple QFPFs qualifies for section 897(l) benefits.

6. Clarifications to the section 1445 regulations for USRPI investments held through foreign LPs

Section 1445 provides rules for determining the appropriate U.S. withholding tax applicable to dispositions of a USRPI by a foreign person ("**FIRPTA Withholding**"). Broadly, transfers of USRPIs by "foreign persons" (as defined for purposes of the section 1445 regulations) are subject to FIRPTA Withholding generally equal to 15% of sale proceeds in case of a direct sale of a USRPI by a foreign person and 35% of the gain in case of sales through a U.S. partnership or REIT capital gain dividend distributions.[7]

As stated, however, section 897(l) provides that QFPFs are exempt from FIRPTA Withholding. In that respect, the section 1445 regulations dealing with FIRPTA Withholding were amended in 2016.

Specifically, the section 1445 regulations provide that no FIRPTA Withholding is required if the transferor of a USRPI is not "a foreign person", as defined for purposes of section 1445.[8] Mechanically, in order to establish that it is not a foreign person, a transferor needs to provide a "certificate of non-foreign status" to the transferee /FIRPTA Withholding agent (as provided in the section 1445 regulations).

The 2016 amendments to the section 1445 regulations amended the definition of a "foreign person" to exclude a QFPF, or an entity wholly owned by a QFPF, both with respect to direct disposition of USRPIs by QFPFs, as well as dispositions of USRPIs by U.S. partnerships with QFPF partners and REIT capital gain dividend distributions made to QFPFs.[9]

However, there is uncertainty where a QFPF invests in USRPIs through a foreign partnership. A "foreign person" for purposes of the FIRPTA Withholding rules includes a foreign partnership.[10] Therefore, under general principles, proceeds from the sale of a USRPI by a foreign partnership should be subject to 15% FIRPTA Withholding (to be applied by the transferee).

While there is a mechanism in place for a QFPF to certify that it is not a "foreign person" and therefore not subject to FIRPTA Withholding on its proportionate share of income arising from the sale of a USRPI by a U.S. partnership, no similar mechanism exists in the case of QFPFs that hold USRPIs through a foreign partnership.

The general mechanism through which a QFPF can certify its non-foreign person status to the relevant FIRPTA Withholding agent is also not available in case of USRPIs held through a foreign partnership because, as stated, a foreign partnership seller is, itself, treated as a "foreign person" for these purposes and therefore is subject to FIRPTA Withholding.

Recommendation

We recommend that the section 1445 regulations, specifically Treas. Reg. sec. 1.1445-2, are amended to provide for a mechanism that would permit a QFPF investing in

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[7] See sections 1445(a) and (e).

[8] Treas. Reg. secs. 1.1445-2(b) and 1.1445-5(b)(3).

[9] See, for example, (amended) Treas. Reg. sec. 1.1445-2(b)(2) which provides that a foreign person is a "non-resident alien individual, foreign corporation, foreign partnership, foreign trust or foreign estate, but not a QFPF or an entity all of the interests of which are held by a QFPF".

[10] *Id.*

USRPIs through a foreign partnership to certify its QFPF status such that its proportionate share of sale proceeds are not subject to FIRPTA Withholding. In particular, we would recommend that consideration is given to amending the regulations to allow a foreign partnership (e.g., its general partner) to provide the FIRPTA Withholding agent with its QFPF partners' certificates of non-foreign status and their respective capital and profits interest percentages in the partnership. The FIRPTA Withholding agent should then be able to rely on the QFPF partner's certificate of non-foreign status and the percentage breakdown of partnership interests provided by the general partner,[11] and effectively not be obligated to apply FIRPTA Withholding on the QFPF partners' proportionate share of the sale proceeds.

Conclusion

We welcome the enactment of section 897(l) and the recently enacted amendments to the definition of a QFPF. Nevertheless, we recommend Treasury and the IRS to exercise the broad discretion granted by section 897(l)(3) to prescribe "such regulations as may be necessary or appropriate to carry out the purposes" of section 897(l) to clarify certain outstanding issues with respect to the QFPF definition and the FIRPTA Withholding Rules. As Treasury and the Service consider the content of such regulations, we ask that the preceding comments and proposed recommendations be considered.

We appreciate the Treasury's and Service's efforts to issue any future guidance in respect to section 897(l). We would be happy to discuss these comments at your convenience. Thank you again for your time and kind consideration.

Please feel free to contact us with any questions.

Sincerely,

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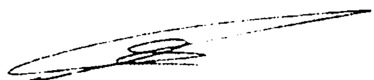
[11] Subject to actual knowledge that the provided QFPF certificates or partnership percentage interest breakdown of non-foreign status are false – i.e., substantially similar reliance standards as the ones already provided in the FIRPTA Withholding regulations (see, for example, Treas. Reg. sec. 1.1445-2(c)(ii)(A)).



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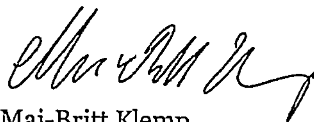

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