

Client Advisory

October 6, 2008

Congress Passes Legislation Eliminating Offshore Fund Deferrals by Investment Managers

On Friday, October 3, 2008, the Emergency Economic Stabilization Act of 2008 (the "Act") was enacted into law. The Act includes a provision that effectively eliminates the ability of cash method investment managers to defer their recognition of income by electing to defer their receipt of fees earned for performing investment management services for offshore funds.

Under the Act, an investment manager must currently include in income, management and performance fees payable by an offshore fund even if payment is deferred. (The Act does not change the tax law rules applicable to compensation which is subject to a meaningful possibility of being forfeited if certain events occur before the applicable payment date, but as a practical matter we would not expect fund managers to be willing to accept any meaningful possibility of having to forfeit their fees in order to be able to defer their recognition of income.)

The Act applies to amounts payable for services performed after December 31, 2008. Therefore, calendar year managers will not be eligible to make any future fee deferral elections for 2009 and later years. Also, so-called side pocket arrangements, under which the payment of fees is deferred until the investment becomes capable of being valued, will be subject to these rules after 2008.

Fees for services performed before 2009 that were deferred pursuant to previously made deferral elections, together with all amounts earned on the notional investment of the deferred fees, are grandfathered, provided that all of the deferred amounts (including amounts earned on the notional investment of deferred fees) are paid to the investment manager before January 1, 2018. Investment managers who previously made deferral elections should determine whether any of such elections would require payment dates after 2017, in which event such elections will need to be amended. The procedure for making such amendments will depend, in part, on whether their existing agreements permit prior deferral elections to be amended. Also, investment managers whose prior deferral elections specify payment dates before 2018 and whose deferral agreements allow them to do so, should consider amending their prior deferral elections to provide for a later payment date (provided the revised payment date is not later than December 31, 2017), inasmuch as future deferrals will no longer be possible. The Act directs the Treasury Department to issue, within 120 days of enactment of the Act, guidance providing a limited period of time during which prior deferral elections may be amended to accelerate the payment date to December 31, 2017 if the previously elected payment date was subsequent to 2017.

If you have any questions regarding this Advisory, please contact your relationship partner or Jill Darrow (212.940.7113), Edward Rayner (212.940.8515) or William Duff (212.940.8532).

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