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Home > Businesses > Help & Resources > Legal Library > Letter Rulings > Letter Rulings - By Year(s) > (2000-2004) Rulings >

Letter Ruling 03-2: Financial Services for Offshore Investment Funds

April 15, 2003

You request a letter ruling on behalf of ***** ("Company"). You ask whether the provision of Company's services in Massachusetts for its clients, which include various unrelated offshore investment funds ("Funds"), would subject the Funds to Massachusetts taxation.

I. Facts

The following is your representation of the facts upon which we base this letter ruling. Company is based in ***** Massachusetts and recently reorganized as a Delaware corporation. The Company will file Massachusetts corporate excise tax returns annually with the Massachusetts Department of Revenue.

***** ("Parent"), a Delaware corporation listed on the New York Stock Exchange, owns 100% of the Company's stock. The Parent has numerous other affiliates, including a wholly owned ***** corporation, ***** ("Corporation"), through which the Parent indirectly conducts international operations. Corporation wholly owns an offshore financial services company, which, in turn, wholly owns an offshore management company, ***** ("Affiliate 1"). Affiliate 1 directly and through an offshore ***** subsidiary wholly owns another management company, ***** ("Affiliate 2"), located in a different offshore location. Similarly, Affiliate 2 wholly owns another management company, ***** ("Affiliate 3") in yet another offshore location. Affiliate 1, Affiliate 2, and Affiliate 3 (each, an "Affiliate", and together, the "Affiliates") were organized outside of the U.S., conduct all of their direct operations outside of the U.S., and have no property located in the U.S. Each of the Affiliates provides administrative services to Funds from offshore locations as described below.

The Company currently provides administrative services primarily to investment funds structured as partnerships for U.S. tax purposes. In general, the Company derives the majority of such business from unrelated sources and contracts directly with, and holds itself out as available to provide services for, such funds. The Company intends to provide similar services to Funds that are typically organized outside of the United States either as (1) corporations, limited liability companies, or other entities that are classified as foreign corporations within the meaning of G.L. c. 63, § 30(2), (2) partnerships, limited liability companies, or other entities that are treated as partnerships for federal and/or Massachusetts income tax purposes, or (3) in limited circumstances, common law business trusts, partnerships, or other entities with transferable shares within the meaning of G.L. c. 62, § 1(j). The Funds in question will conduct all of their operations outside of Massachusetts, except that they may engage the Company and the Affiliates as described below.

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It is anticipated that the Company also will make presentations, which may or may not be made in Massachusetts, to various investment managers of Funds as to the administrative services that can be provided by the Affiliates and the Company to such Funds. In order to increase its business, the Company may refer such investment managers to the Affiliates in the expectation that the Company may be awarded a subcontract for the provision of certain services to such Funds. The investment managers then are expected to approach the various Funds with the services and fees proposed by the Affiliates and the Company, and, if a Fund accepts the proposal, it will enter into an administration agreement with one of the Affiliates. Authorized officers of the Fund and the Affiliate will execute the administration agreement outside of Massachusetts.

In accordance with the terms of the administration agreement, the Affiliate generally will agree to provide the following services to a Fund:

1. calculating and publishing the net asset values per share for each class and series of shares issued by a Fund and the subscription and redemption prices per share for each class and series of shares issued by a Fund;
2. if requested, providing the services of an officer or employee to act as secretary for a Fund who will attend board meetings and prepare corporate documents;
3. providing and maintaining a registered office for the Fund at an offshore location;
4. maintaining the share register;
5. preparing offshore regulatory registrations and filings;
6. preparing financial statements, reconciling accounting issues, and receiving, generating, and maintaining records and books of account of the Funds;
7. processing subscription and redemption requests of shareholders of the Funds, sending notices, financial statements, and other correspondence to shareholders, and acting as proxy agent for shareholders; and
8. establishing and maintaining bank, brokerage, custodian, and other accounts, and paying all expenses and liabilities of a Fund due to service providers of a Fund.

Some of the services contracted for in an administration agreement then may be subcontracted out by the Affiliate to the Company pursuant to the terms of a services agreement between the Affiliate and the Company. However, the Affiliate will not subcontract out all of the services in the administration agreement to the Company, but instead will provide some of the services itself, including (1) shareholder services, (2) the services of a secretary, (3) providing and maintaining a registered office at an offshore location, and (4) preparing regulatory registrations and filings in compliance with local offshore jurisdiction laws. The Affiliate, for example, will itself provide the following shareholder services to the Funds: (1) processing and recording subscription and redemption requests; (2) maintaining the share register; (3) preparing investor account statements; (4) receiving and responding to investor inquiries; and (5), acting as proxy agent for the shareholders.

Moreover, the Affiliate will not subcontract out to the Company the provision of secretarial services. Instead, if requested by a Fund, the Affiliate will provide an employee or officer of the Affiliate, or it will procure one from one of the other Affiliates, to act as a secretary for a Fund. It is anticipated that only approximately three employees or officers of the Affiliates will serve as secretaries for all of the Funds and that all required secretarial duties for a Fund will be performed outside of Massachusetts. The individuals that are appointed as secretaries also will have other regular duties

as employees of the Affiliate that employs them, including general compliance responsibilities. It is anticipated that these three or so employees or officers will act as secretaries for approximately 250 Funds over the course of one year and that the time required to perform the secretarial duties for any one Fund will be relatively nominal. The Affiliate will charge a Fund a flat fee for the secretarial services provided. The employees or officers that act as secretaries will not receive any additional compensation from a Fund and instead will only receive their regular salaries from the Affiliate in an amount that will be substantially less than the flat fee charged by the Affiliate to the Fund.

In addition, an Affiliate may provide additional services to a Fund under the administration agreement. It may (1) assist with a Fund's formation and review its inception documents, and/or (2) safekeep original contracts, agreements and board minutes of a Fund offshore. None of these services will be contracted out to the Company. Instead, if provided, these services will be performed by an Affiliate at an offshore location. Also, if requested, an Affiliate may provide the services of an employee or officer to act as a director for a Fund under the administration agreement.

The Affiliate then will subcontract out to the Company the obligation to perform certain services listed in the administration agreement in accordance with the terms of the services agreement. The services agreement generally will provide that the Affiliate can subcontract out to the Company the obligation to provide services such as (1) the calculation and publication of net asset values and subscription and redemption prices; (2) the preparation of financial statements; and (3) the payment of expenses. It is anticipated that pursuant to the terms of the services agreement, the following duties will be required to be performed by the Company on behalf of the Funds:

1. Calculation and publication of net asset values and subscription and redemption prices for a Fund, together with related financial and accounting services;
2. Investor recordkeeping/reporting;
3. General administration and accounting; and
4. Management reporting.

In conducting these duties, the Company will generate and maintain corporate records and books of account for the Funds solely for its use in providing the above listed services to the Funds. Each Fund will be responsible for keeping and maintaining its own principal corporate records and books of account (whether or not with the assistance of an Affiliate) at an offshore location outside of Massachusetts. However, because the Company will be providing comprehensive portfolio accounting and recordkeeping services to the Funds, it is likely that many Funds will not themselves maintain certain corresponding records relating to those services.

On occasion, the Company also may provide an employee or officer to act as a director of a Fund. However, no board of director meetings or shareholder meetings of a Fund will be conducted in Massachusetts. In addition, the Company will not execute any contracts on behalf of the Funds, except for certain contracts related to the purchase, sale, or management of Fund investments.

In accordance with the terms of the administration agreement, neither the Company nor any Affiliates will be subject to the supervision or control of a Fund in its day to day performance of its obligations under the agreement. Instead, as set forth in the administration agreement, a Fund will only be able to control the scope of the duties required under the administration agreement, the performance benchmarks required to be achieved, and any systems and control changes required after reviewing performance reports received from the Affiliate, for example, with regard to the prevention of fraud and money laundering.

The Company and the Affiliates each intend to advertise regularly their services to the public in published marketing materials and through Web sites. The Company currently has approximately ***** of assets under administration for approximately 120 investment funds.

II. Ruling

For the reasons discussed below, we rule that the provision of accounting, pricing, information, and other administrative services, as detailed above, by the Company for the Funds will not cause the Funds to be subject to Massachusetts taxation. The provision of shareholder, accounting, pricing, information, and other administrative services, and maintenance of records and reports and the maintenance of registered offices for the Funds in offshore locations by the Affiliates, as detailed above, will not cause Funds to be subject to Massachusetts taxation. Finally, the solicitation by the Company of sales of all of the above detailed services to be provided by the Affiliates and the Company will not cause the Funds to be subject to Massachusetts taxation.

III. Discussion of Law

The determination of whether the provision of administrative services by a Massachusetts company to offshore investment funds has previously been ruled on in Letter Ruling 01-04. In that ruling, the Commissioner determined that the provisions of accounting, custodial, investment, management, shareholder and other administrative services as well as the receipt, generation and maintenance of relevant electronic and paper records and reports for various unrelated offshore investment funds^[1] by a Massachusetts service provider would not cause the funds to be subject to Massachusetts taxation, since the service provider was acting as an independent contractor for the funds.^[2]

The facts presented here are somewhat analogous to those in LR 01-04. Company is a service provider providing administrative and other services on behalf of the Funds. In this regard, Company is acting as an independent contractor for the Funds. The majority of the services to be provided by the Company to a Fund are explicitly delineated as permissible activities of an independent contractor in Massachusetts in TIR 98-6. Other than occasionally providing the services of a director to a Fund, which we consider to be a type of administrative service, the remaining activities of the Company are either accounting services, or services directly related to accounting, that appear to be within the general scope of permissible activities listed in TIR 98 6.

The Company will not perform on behalf of a Fund any of the activities that TIR 98-6 indicates may expose a Fund to Massachusetts' tax jurisdiction. In addition, while the Company may, on occasion, at the request of a Fund, provide an employee or officer to act as a director for a Fund, no director or shareholder meetings will be conducted in Massachusetts.

In addition, it is our opinion that the Affiliates are also acting as independent contractors for the Funds, rather than as representatives of the Funds. While an Affiliate will, upon request, provide an employee or officer to act as a secretary for a Fund, these employees are not considered to be employees of a Fund, since they will work in this capacity for numerous Funds, will only spend a few hours per year per Fund on such duties, will not be directly compensated by a Fund, and will have other regular duties in their employment by an Affiliate. See, e.g., Treas. Reg. § 31.3121(d) 1(b); *Marshall Durbin Food Corp. v. U.S.*, 79 1 U.S.T.C. (CCH) ¶ 9273 (N.D. Ala. 1979); and Rev. Rul. 74-390, 1974 2 C.B. 331.

Therefore, we rule that the service activities of Company and Affiliates are not enough, standing alone, to cause the Funds, whether organized as a foreign corporation, limited liability company, partnership, or trust to be doing business in Massachusetts.^[3]

Very truly yours,

/s/Alan LeBovidge

Alan LeBovidge
Commissioner of Revenue

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LR 03-2

[\[1\]](#) As the facts in LR 01-04 indicate, the funds at issue therein were or could be organized as corporations, limited liability companies, partnerships, and corporate trusts.

[\[2\]](#) A person is an independent contractor only if the criteria listed in Massachusetts regulation 830 CMR 63.39.1(7) are met. A service provider providing administrative and/or other services on behalf of an offshore investment company is generally considered to be an independent contractor. TIR 98-6. Moreover, service providers are allowed to utilize copies of books and records of the offshore investment company in Massachusetts without creating nexus for the offshore investment company so long as the principal books and records of the offshore investment company are kept outside of Massachusetts. See *also* LR 97-2, 91-2.

[\[3\]](#) This ruling makes no determination as to whether any of the Funds would have nexus with Massachusetts if their activities exceed those discussed herein.