



November 24, 2022

Via Electronic Submission: investmentmanagerexemption@hmrc.gov.uk

Investment Manager Exemption Team
HMRC
B8.22 Stratford Regional Centre
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NE88

Re: Expanding the Investment Transactions List for the Investment Management Exemption and other fund tax regimes

Managed Funds Association¹ (“MFA”) appreciates the opportunity to provide additional feedback, to His Majesty’s Revenue and Customs (“HMRC” or “**HM Revenue & Customs**”) on the above-captioned consultation regarding its intention to expand the Investment Transactions List (“ITL”) used for purposes of the Investment Management Exemption (“IME”) to include cryptoassets.² We write again in support of the measure to expand the ITL to include certain types of cryptoassets for purposes of the IME. However, we respectfully urge you reconsider certain recommendations submitted by the investment management industry in response to the initial consultation which were not adopted in the *draft* Investment Manager (Investment Transactions) (Cryptoassets) Regulations 2022 (“**Draft Regulations**”).

First, we urge you to modify paragraph (2)(a) of the Draft Regulations to reflect the industry consensus that the definition of “cryptoasset” in regulation 14A(3) of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (SI 2017/692) (“**AML Regulation**”) should serve as the definition of “cryptoasset” for purposes of the IME.³ Investment managers are subject to and comply with the AML Regulation and its familiar definitions. Although the definition of “cryptoasset” in the “Crypto-Asset Reporting Framework” (“**CARF**”) published by the Organisation for Economic Co-operation and Development (“**OECD**”) in March 2022 has since been finalized,⁴ we see no

¹ Managed Funds Association (“MFA”) represents the global hedge fund and alternative asset management industry and its investors by advocating for regulatory, tax, and other public policies that foster efficient, transparent, and fair capital markets. MFA’s more than 150 member firms collectively manage nearly \$2.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, Brussels, London, and Asia. www.managedfunds.org.

² “Expanding the Investment Transactions List for the Investment Management Exemption and other fund tax regimes,” HM Revenue & Customs, <https://www.gov.uk/government/consultations/expanding-the-investment-transactions-list-for-the-investment-management-exemption-and-other-fund-tax-regimes/expanding-the-investment-transactions-list-for-the-investment-management-exemption-and-other-fund-tax-regimes> (last updated May 23, 2022)

³ See Letter from Managed Funds Association to Investment Manager Exemption Team (July 18, 2022) (attached); Letter from Sidley Austin LLP to Investment Manager Exemption Team (July 18, 2022); Letter from Alternative Investment Management Association to Investment Manager Exemption Team (July 18, 2022); see also Letter from Simmons & Simmons LLP to Investment Manager Exemption Team (July 18, 2022) (indicating the AML Regulation as an alternative starting point where finalization of the CARF definition is pending and may delay reforms to the IME).

⁴ OECD (2022), Crypto-Asset Reporting Framework and Amendments to the Common Reporting Standard, OECD, Paris, <https://www.oecd.org/tax/exchange-of-tax-information/crypto-asset-reporting-framework-and-amendments-to-the-common-reporting-standard.htm>.

principled basis on which a defined term should incorporate an intergovernmental organization's definition rather than a comparable definition in domestic law. The CARF definition may be varied in the future in a manner which is neither suitable nor appropriate for purposes of the IME.

Moreover, the Draft Regulations use terminology identical to the CARF but selectively depart from the definitions of such terminology. For example, the definitions of "cryptoasset" are identical by virtue of the Draft Regulations' incorporation of the CARF definition, whereas the definition of "relevant cryptoasset" is tailored to the purposes of the IME. Indeed, the CARF definition of "relevant cryptoasset" may *include* the categories enumerated in paragraph (2)(b) which the Draft Regulations intend to *exclude*. We are concerned that taxpayers may inadvertently conflate the CARF and Draft Regulations' definitions of "relevant cryptoasset" because of the earlier incorporation of the CARF definition of "cryptoasset." Accordingly, we recommend that HMRC adopts the substantially similar definition of "cryptoasset" in the AML Regulation. At a minimum, we recommend that HMRC reproduces, but not incorporates by reference, the CARF definition of "cryptoasset" in the text of paragraph (2)(a) of the Draft Regulations to avoid any confusion.

Second, for similar reasons, we urge you to modify paragraph (2)(b)(ii) of the Draft Regulations to clarify that cryptoassets which are in the nature of commodities⁵ are not excluded from the definition of "relevant cryptoasset." Paragraph (2)(b)(ii) excludes from the definition of "relevant cryptoasset" any cryptoasset which represents rights in respect of "property a transaction in which would not fall within regulation 2(2) of [the Investment Transactions (Tax) Regulations 2014], unless that property is another relevant cryptoasset." Because transactions in physical commodities are not investment transactions for purposes of the IME, it is unclear whether cryptoassets which are in the nature of commodities (e.g., Bitcoin, Ether, etc.) are excluded under paragraph (2)(b)(ii) by virtue of representing rights in respect of property not included within regulation 2(2) of the Investment Transactions (Tax) Regulations 2014. We do not believe HMRC intended such a result; rather, we believe that the better reading is that paragraph (2)(b)(ii) excludes cryptoassets which represent rights in respect of *separate* or *underlying* property a transaction in which would not fall within regulation 2(2) of the Investment Transactions (Tax) Regulations 2014. Otherwise, we are concerned that the Draft Regulations may exclude the most common transactions in cryptoassets—precisely those transactions which the Draft Regulations were intended to encourage. Accordingly, we recommend that HMRC clarifies that cryptoassets which are in the nature of commodities are not excluded from the definition of "relevant cryptoasset."

Third, we respectfully request additional interpretive guidance concerning the anti-avoidance provision in paragraph (3) of the Draft Regulations. Paragraph (3) seemingly excludes from the IME transactions in cryptoassets created or issued by the non-UK resident, an investment manager acting on behalf of that non-UK resident, or a person connected with either. We are concerned that, without additional guidance, this anti-avoidance provision may stifle future innovation, for example, in tokenized structured products.⁶ The private credit industry (as distinguished from bank-intermediated credit), including closed-end direct lending funds, may find a use case for security tokens in the reselling or securitizing of loans. The potential benefits of security tokens in private credit include the creation of secondary security token markets for increased liquidity, accessibility, and transparency and more effective price discovery and automated administration (e.g., yield distributions) and compliance (e.g., anti-money laundering/know your

⁵ We use the term "commodity" generically to mean "an article of trade or commerce," *Commodity*, Black's Law Dictionary (10th ed. 2014), or "[a]n economic good...[or] an article of commerce..." *Commodity*, Merriam-Webster Dictionary, <https://www.merriam-webster.com/dictionary/commodity> (last visited Nov. 22, 2022).

⁶ For a broad discussion of tokenization of assets, see OECD (2020), The Tokenisation of Assets and Potential Implications for Financial Markets, OECD Blockchain Policy Series, www.oecd.org/finance/The-Tokenisation-of-Assets-and-Potential-Implications-for-Financial-Markets.htm.

customer processes) via smart contracts. In such use cases, an investment manager or person connected with the investment manager may be considered the creator or issuer of the security token (cryptoasset), and paragraph (3) may exclude from the IME transactions in that security token. By contrast, a sale of the underlying loan or traditional asset-backed security would not be transactions excluded from the IME notwithstanding that such transactions bear no meaningful difference from the sale of a security token which represents rights in respect of the same property. We, therefore, request interpretive guidance clarifying that the scope of the anti-avoidance provision in paragraph (3) permits the tokenization of property a transaction in which would fall within regulation 2(2) of the Investment Transactions (Tax) Regulations 2014.

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We appreciate the opportunity to submit additional feedback to HMRC, and we would be pleased to meet with the Investment Manager Exemption Team to discuss our comments. If the Investment Manager Exemption Team have questions or comments, please do not hesitate to contact Joseph Schwartz, Director and Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Jennifer W. Han

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July 18, 2022

Via Electronic Submission: investmentmanagerexemption@hmrc.gov.uk

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I. Tax Certainty

We agree that expanding the ITL to include certain types of cryptoassets for purposes of the IME would “provide certainty of tax treatment to U.K. investment managers and their non-U.K. resident investors who are seeking to include cryptoassets within their portfolios.” As correctly noted, U.K. investment managers are unable to provide discretionary investment management services to offshore fund vehicles which are undertaking investment strategies involving trading spot cryptoassets without bringing such investments within the charge, and subjecting their non-U.K. resident investors, to U.K. tax. Instead, U.K. investment managers generally have limited such strategies to exchange-traded futures and options contracts on cryptoassets or otherwise have foregone the strategies altogether. As such, we do not expect the measure to result in a negative impact for the exchequer.

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³ We generically refer to “cryptocurrency,” “crypto,” “cryptoassets,” and “digital assets” interchangeably.

⁴ We further endorse the submission of Sidley Austin LLP, which addresses certain questions for which the consultation solicits responses.

In a survey of investment managers not currently invested in cryptoassets, “[r]egulatory and tax uncertainty continues to be the greatest barrier to investing (cited by 83% of respondents).”⁵ Likewise, among “[t]he top five challenges cited by hedge fund managers who currently invest in digital assets as being very significant or significant...[l]ack of regulatory and tax regime clarity (90%)” far surpasses other concerns.⁶ We believe that uncertainty regarding the status of trading spot cryptoassets under the IME and other comparable safe harbors is a substantial factor contributing to the prevailing view that tax uncertainty is the most significant barrier to investing in cryptoassets. Expanding the ITL to include certain types of cryptoassets for purposes of the IME would reduce tax uncertainty and encourage further investment in cryptoassets. Indeed, “[a]round a third of respondents not currently investing say that if the main barriers were to be removed, they would actively accelerate their involvement/investment in digital assets.”⁷

II. National Competitiveness

We equally agree that expanding the ITL to include certain types of cryptoassets for purposes of the IME would “encourage new cryptoasset investment management businesses to base themselves in the U.K.” As discussed further in the survey, the distribution of crypto-native investment managers located in the U.K. decreased year-over-year,⁸ with other highly developed nations, namely, the United States, offshore jurisdictions, and emerging nations accounting for the largest proportion of jurisdictions in which crypto-native investment managers are located.⁹ The authors of the report indicated that “the expectation is that these results would remain constant, unless particular governments or authorities enact policies that are more attractive (or restrictive) to crypto hedge funds and their respective managers.”¹⁰ We believe that expanding the ITL to include certain types of cryptoassets for purposes of the IME would encourage existing U.K. investment managers to adopt investment strategies in relation to cryptoassets and newly-formed crypto-native investment managers to locate in the U.K. We expect this measure to directly result in the retention and creation of highly qualified and compensated jobs located in the U.K. rather than other jurisdictions in which similarly expanded safe harbors may be considered.¹¹

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⁵ PricewaterhouseCoopers Ltd., “4rd Annual Global Crypto Hedge Fund Report,” at 3, 41, 49 (June 2022), <https://www.pwc.com/gx/en/financial-services/pdf/4th-annual-global-crypto-hedge-fund-report-june-2022.pdf>.

⁶ *Id.* at 46.

⁷ *Id.* at 41.

⁸ We note that, “[t]his year, the methodology for evaluating where investment teams are physically located changed slightly, and [survey administrators] limited each crypto hedge fund to choose a single answer instead of providing every location a manager may have been based throughout the year...This practice will...allow results to actually represent locations with pools of crypto hedge fund talent.” *Id.* at 34.

⁹ Compare *id.* with PricewaterhouseCoopers Ltd., “3rd Annual Global Crypto Hedge Fund Report,” at 32 (May 2021), [https://www.pwc.com/gx/en/financial-services/pdf/3rd-annual-pwc-elwood-aima-crypto-hedge-fund-report-may-2021\).pdf](https://www.pwc.com/gx/en/financial-services/pdf/3rd-annual-pwc-elwood-aima-crypto-hedge-fund-report-may-2021).pdf).

¹⁰ *Id.*

¹¹ We have requested that the United States Department of the Treasury and Internal Revenue Service prioritize comparable guidance. See Managed Funds Assoc., “Re: Notice 2022-21, Public Recommendations Invited on Items to be Included on the 2022-2023 Priority Guidance Plan” (June 3, 2022), https://downloads.regulations.gov/IRS-2022-0007-0085/attachment_1.pdf.

Although the path to enactment is uncertain, we note that Members of Congress similarly have given thought to legislatively expanding comparable safe harbors. For example, on June 7, 2022, bi-partisan co-sponsors introduced the “Lummis-Gillibrand Responsible Financial Innovation Act,” which would expand the Section 864(b) trading safe harbors to include “digital assets,” defined as “a natively electronic asset that—(i) confers economic, proprietary, or access rights or powers; and (ii) is recorded using cryptographically secured distributed ledger technology or any similar analogue...” S.4356, 117th Cong. (2022).

We appreciate the opportunity to submit a consultation response to HMRC, and we would be pleased to meet with the Investment Manager Exemption Team to discuss our comments. We also welcome the opportunity to discuss our views on related issues including, among others, whether certain yield-generating activities in relation to cryptoassets (*e.g.*, staking, liquidity mining, yield farming) should be in scope of the IME. If the Investment Manager Exemption Team have questions or comments, please do not hesitate to contact Joseph Schwartz, Director and Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Jennifer W. Han

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