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State X =

Dear

This is in reply to a letter of November 8, 1999, and subsequent correspondence submitted on behalf of P1, P2, P3, P4, P5, P6, P7, P8, S1, S2, S3, S4, S5, S6, S7, S8, S9, and S10, by their authorized representative requesting certain rulings relating to the master-feeder investment fund structure between P3 through P8 (the "Series") and S1 through S10 (the "Funds").

P1 and P2 are each trusts (the "Trusts") formed under the laws of State X, pursuant to Declarations of Trust ("Declaration(s)"). P1 and P2 are each registered with the Securities and Exchange Commission (the "SEC") under the 1940 Act as open-end diversified management investment companies. P3, is a series of P1. P4, P5, P6, P7, and P8 are each a series of P2.

P3 through P8 represent that they are each a partnership in which S1 through S10 are partners in their respective partnership. S1 invests in P3. S2 invests in P4. S3, S4, and S5, invest in P5. S6 and S7 invest in P6. S8 invests in P7. S9 and S10 invest in P8.

Each Series has distinct investment objectives and will invest in a portfolio of securities in which no other Series will have an interest. A Fund will invest in one or more Series, and its interest in each Series in which it invests will be determined by reference to its capital account in that Series and without regard to its capital account in any other Series. The interest of a Fund is limited to the net assets of the Series in which it invests and does not extend to the assets of any other Series established under the Declaration. In addition, the rights of the Funds investing in each Series are limited in redemption and liquidation or termination to the assets of that particular Series.

The Declaration provides that the Trustees will administer the affairs of the Trusts. In accordance with the Declaration, the Trustees for P1 and P2 have adopted Capital Account Establishment and Maintenance Procedures ("Procedures"). The Declaration and the Procedures are collectively referred to as the "Agreement."

The Declaration provides that, consistent with its investment objectives, each Series will be managed so as to comply with the requirements applicable to regulated investment companies (RICs) under § 851 _et_ _seq_. of the Internal Revenue Code as though such requirements were applied at the Series level.

The Declaration provides that no Series will be liable for the debts and obligations of any other Series. Further, the Declaration provides that the expenses, fees, charges, taxes, and liabilities incurred or arising in connection with a particular Series, or in connection with the management thereof, are payable out of the assets of that Series and not out of the assets of any other Series. Certain general items, such as Trustee fees and 1940 Act registration expenses, for example, are allocated among the Series based upon the relative net asset values of each.

Matters affecting only one Series will be voted on only by the investors of that Series. To the extent required by the 1940 Act, a single vote of all investors will be held for the election of Trustees and the approval of accountants.

Subject to specific provisions of the Declaration, the Trustees will have exclusive and absolute control over the assets and activities of each Series.

Holders of interests in Series will be limited to certain institutional investors ("Holders"), and will not include individuals, S corporations, partnerships, or grantor trusts that are beneficially owned by any individual, S corporation or partnerships.

Each Series will invest their assets in a manner that complies with the requirements specified in § 851(b) of the Code as though they were each a RIC subject to § 851(b).

The Declaration, which governs the rights, obligations and liabilities of the Holders, provides that the Holders' interests in the Series are not transferable. Increases and decreases in the size of a Holder's investment will be accomplished by adjustments to that Holder's capital account balance, not by a transfer of interests in the Series or capital accounts between the various Holders.

The Series represent that, except as required by § 704(c) of the Code and § 1.704-1(b)(4) of the Income Tax Regulations, each Holder's allocable share of that Series's income will be comprised of a proportionate share of each item of income includ able in that Series's gross income. The Series further represent that the organization of the Series in a manner to enable them to be classified as partnerships under § 301.7701-2 of the Procedure

and Administration Regulations was not done to enable a Holder that is a regulated investment company to make distributions that would be prohibited under Rev. Rul. 89-81, 1989-1 C.B. 266, had the regulated investment company invested directly in the assets of the Series.

The Series also represent that each is and will continue to be registered with the SEC under the 1940 Act as a management company; and that it will make all of its book allocations in proportion to the Holders' relative book capital accounts.

Section 7704(a) of the Code provides that a publicly traded partnership shall be treated as a corporation.

Section 7704(b) of the Code provides that, for purposes of § 7704, the term "publicly traded partnership" means any partnership if (1) interests in such partnership are traded on an established securities market, or (2) interests in such partnership are readily tradable on a secondary market (or the substantial equivalent thereof).

Section 1.7704-1(h)(1) of the regulations, concerning private placements, provides that except as otherwise provided in § 1.7704-1(h)(2), interests in a partnership are not readily tradable on a secondary market or the substantial equivalent thereof if (i) all interests in the partnership were issued in a transaction (or transactions) that was not required to be registered under the Securities Act of 1933 (15 U.S.C. 77a et seq.); and (ii) the partnership does not have more than 100 partners at any time during the taxable year of the partnership.

The Series represents that each Series will have no more than 100 partners (Holders), and that no interests in a Series have been, or will be traded on an established securities market or issued in a transaction registered under the Securities Act of 1933. Based on the information provided and the representations made, we conclude that the Series will each be treated as a separate entity for federal income tax purposes and that no Series will be a publicly traded partnership for purposes of § 7704 of the Code.

Section 851(a) of the Code defines a RIC, in part, as a domestic corporation registered under the 1940 Act as a management company.

Section 851(b) of the Code limits the definition of a RIC to a corporation meeting certain election, gross income, and diversification requirements.

Section 851(b)(2) of the Code provides that, to qualify as a

RIC, 90 percent of a corporation's gross income must be derived from dividends, interest, payments with respect to securities loans (as defined in § 512(a)(5)), gains from the sale or other disposition of stocks, securities, foreign currencies, or other income derived with respect to the business of investing in such stocks, securities, or currencies.

Section 851(b)(3)(A) of the Code requires that, to qualify as a RIC, at the close of each quarter of the taxable year, at least 50 percent of the value of a corporation's total assets must be represented by cash and cash items (including receivables), Government securities, securities of other RICs, and other securities generally limited in respect of one issuer to an amount not greater in value than 5 percent of the value of the total assets of the corporation and to not more than 10 percent of the outstanding voting securities of such issuer.

Section 851(b)(3)(B) of the Code provides that to qualify as a RIC, not more than 25 percent of the corporation's total assets may be invested in the securities (other than Government securities and securities of other RICs) of any one issuer, or two or more issuers which the corporation controls and which are determined, under regulations, to be engaged in the same or similar trades or businesses or related trades or businesses.

Section 853(a) of the Code provides that a RIC more than 50 percent of the value (as defined in § 851(c)(4) of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations and which meets the requirements of § 852(a) for the taxable year may elect to treat its shareholders as if they had paid certain foreign taxes incurred by the RIC for purposes of determining a shareholder's foreign credit under § 901.

Section 702(b) of the Code provides that the character of items stated in § 702(a) that are included in a partner's distributive share shall be determined as if such items were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership. Section 702(c) provides that where it is necessary to determine the amount or character of the gross income of a partner, such amount shall include that partner's distributive share of the gross income of the partnership.

Section 1006(n)(1) of the Technical and Miscellaneous Revenue Act of 1988 added a sentence to the flush language of § 851(b) of the Code that states that income derived from a partnership or trust shall be treated as satisfying the 90 percent test of § 851(b)(2) only to the extent that such income is attributable to items of income of the partnership or trust which

would be described in § 851(b)(2) if earned directly by the RIC. The legislative history of that sentence indicates that it was intended to clarify the general rule used to characterize items of income, gain, loss, deduction, or credit includable in a partner's distributive share, as applied to RICs that are partners. It therefore explains the relationship of § 702 to the 90 percent test under § 851(b)(2). See S. Rep. No. 445, 100th Cong., 2d Sess. 93 (1988).

Under subchapter K of the Code, a partnership is considered to be either an aggregate of its members or a separate entity. Under the aggregate approach, each partner is treated as an owner of an undivided interest in partnership assets and operations. Under the entity approach, the partnership is treated as a separate entity in which partners have no direct interest in partnership assets and operations. See S. Rep. No. 1622, 83d Cong., 2d Sess. 89 (1954) and H.R. Rep. No. 2543, 83d Cong., 2d Sess. 59 (1954).

In order for Holders to qualify as RICs under the diversification tests of § 851 of the Code, the aggregate approach will have to be applied to each Holder's partnership interest in a Series. As an aggregate, each Holder will be entitled to take into account its share of the individual items of income and assets of the Series it invested in.

Rev. Rul. 75-62, 1975-1 C.B. 188, concerns a life insurance company that contributed cash to a partnership in exchange for a 50 percent interest in the partnership. The partnership held real estate as its principal asset. For the taxable year in question, § 805(b) of the Code required life insurance companies to value their assets each taxable year. For this purpose, § 805(b)(4) required that shares of stock and real estate be valued at their fair market values, and that other assets be valued at their adjusted basis. The issue presented in the ruling is whether, for purposes of § 805(b)(4), the life insurance company's interest in the partnership is considered to be an investment in the real estate held by the partnership (an aggregate approach) or an investment in other property (an entity approach).

Rev. Rul. 75-62 holds that the partnership interest held by the life insurance company must be accounted for as other property for purposes of § 805(b)(4) of the Code. The ruling cites §§ 705 and 741, both of which generally treat an interest in a partnership as an interest in an entity, as evidence of an intent in subchapter K to take the entity approach in questions concerning the nature of an interest in a partnership. The ruling states that the legislative history of § 805(b)(4) does not indicate that application of the entity approach to the facts of the

ruling is inappropriate, and that there is no compelling reason to take the aggregate approach.

The flush language of § 851(b)(3) of the Code (formerly § 851(b)(4) for taxable years of a RIC that began before August 5, 1997) and its legislative history indicate that here, unlike the situation described in Rev. Rul. 75-62, Congress intended that an aggregate approach be taken in determining the nature of the partnership interests held by the Holders. The flush language of § 851(b) mandates an aggregate approach in applying the 90 percent gross income test of § 851(b)(2) to RICs that hold partnership interests. It would be anomalous to suggest that Congress intended that a RIC's interest in a partnership be viewed as a direct investment in the partnership's assets for purposes of the § 851(b)(2) test but not be viewed as a direct investment in those assets for purposes of the test set out in, _inter_ _alia_, § 851(b)(3).

The tax treatment accorded real estate investment trusts (REITs) lends further support to applying the aggregate approach to the present case. REITs were created to provide an investment vehicle similar to the RIC for small investors to invest in real estate and real estate mortgages. _See_ H.R. Rep. 2020, 86th Cong., 2d Sess. 3 (1960). Like RICs, REITs are subject to restrictions on the type of assets they can hold if they want to retain the benefits accorded them under subchapter M and are subject to certain gross income source tests. REITs and RICs also have similar distribution and holding period requirements.

Section 1.856-3(g) of the regulations provides that:

> In the case of a real estate investment trust which is a partner in a partnership, as defined in section 7701(a)-(2) and the regulations thereunder, the trust will be deemed to own its proportionate share of each of the assets of the partnership and will be deemed to be entitled to the income of the partnership attributable to such share. For purposes of section 856, the interest of a partner in the partnership's assets shall be determined in accordance with his capital interest in the partnership. The character of the various assets in the hands of the partnership and items of gross income of the partnership shall retain the same character in the hands of the partners for all purposes of section 856. Thus, for example, if a trust owns a 30-percent capital interest in a partnership which owns a piece of rental property the trust will be treated as owning 30 percent of such property and as being entitled to 30 percent of the rent derived from the property by the partnership. Similarly, if the partnership holds any property primar-

> ily for sale to customers in the ordinary course of its trade or business, the trust will be treated as holding its proportionate share of such property primarily for such purpose. Also, for example, where a partnership sells real property or a trust sells its interest in a partnership which owns real property, any gross income realized from such sale, to the extent that it is attributable to the real property, shall be deemed gross income from the sale or disposition of real property held for either the period that the partnership has held the real property or the period that the trust was a member of the partnership, whichever is the shorter.

Thus, the regulation adopts the aggregate "look-through" approach in determining how a REIT should account for its partnership interests for purposes of all of the income and asset qualification tests under § 856 of the Code.

The legislative purpose underlying the creation of both RICs and REITs was to provide small investors a means of pooling their resources to invest in a particular type of asset without the imposition of corporate income tax. The qualification tests are similar for each. Therefore, although the RIC regulations do not specifically address the issue herein, it is appropriate to adopt an approach for RICs that parallels that set forth for REITs.

Accordingly, each of the Holders, as partners in a Series, will be deemed to own a proportionate share of the assets of the applicable Series and will be deemed to be entitled to the income of the Series attributable to that share for purposes of determining whether that Holder satisfies the requirements of §§ 851(b)(2), 851(b)(3), and 853(a) of the Code. For purposes of these sections, the interest of a Holder in a Series shall be determined in accordance with the Holder's capital interest in that Series.

Section 704(a) of the Code provides that a partner's distributive share of income, gain, loss, deduction, or credit shall, except as otherwise provided in Chapter 1 of the Code, be determined by the partnership agreement.

Section 704(b) of the Code provides that a partner's distributive share of income, gain, loss, deduction, or credit (or item thereof) shall be determined in accordance with the partner's interest in the partnership (determined by taking into account all facts and circumstances), if (1) the partnership agreement does not provide as to the partner's distributive share of income, gain, loss, deduction, or credit (or item thereof), or (2) the allocation to a partner under the agreement of income,

gain, loss, deduction, or credit (or item thereof) does not have substantial economic effect.

Section 1.704-1(b)(2)(ii) of the regulations provides that in order for an allocation to have economic effect, it must be consistent with the underlying economic arrangement of the partners. This means that in the event there is an economic benefit or economic burden that corresponds to an allocation, the partner to whom the allocation is made must receive the economic benefit or bear the economic burden. Generally, an allocation has economic effect if (1) the partnership capital accounts are maintained in accordance with § 1.704-1(b)(2)(iv), (2) upon liquidation of the partnership (or any partner's interest in the partnership) liquidating distributions will be made to the partners in accordance with their positive capital account balances, and (3) partners are unconditionally required to restore the negative balance of their capital accounts to the partnership upon the liquidation of their interests in the partnership.

Section 1.704-1(b)(2)(iv)(b) of the regulations provides that the partners' capital accounts will be considered to be determined and maintained in accordance with the rules of paragraph (b)(2)(iv) if, and only if, each partner's capital account is increased by (1) the amount of money contributed by him to the partnership, (2) the fair market value of property contributed by the partner to the partnership (net of liabilities secured by such contributed property that the partnership is considered to assume or take subject to under § 752 of the Code), and (3) allocations to the partner of partnership income and gain (or items thereof), including income and gain exempt from tax and income and gain described in paragraph (b)(2)(iv)(g), but excluding income and gain described in paragraph (b)(4)(i); and decreased by (4) the amount of money distributed to the partner by the partnership, (5) the fair market value of property distributed to the partner by the partnership (net of liabilities secured by such distributed property that such partner is considered to assume or take subject to under § 752), (6) allocations to the partner of expenditures of the partnership described in § 705(a)(2)(B), and (7) allocations of partnership loss and deduction (or item thereof), including loss and deduction described in paragraph (b)(2)(iv)(g), but excluding items described in (6) above and loss or deduction described in paragraphs (b)(4)(i) or (b)(4)(iii).

Section 1.704-1(b)(2)(ii)(h) of the regulations provides that the partnership agreement includes all agreements among the partners, or between one or more partners and the partnership concerning affairs of the partnership and responsibilities of the partners.

Section 3.4 of Article III of the Procedures provides that the provisions contained in the Procedures, relating to the maintenance of book capital accounts and tax capital accounts, are intended to comply with § 1.704-1(b) of the regulations, and shall be interpreted and applied in a manner consistent with such regulations.

Section 3.4 of the Procedures further provides that the Trustees shall make any appropriate modifications in the event unanticipated events might otherwise cause the Procedures not to comply with § 1.704-1(b), including the requirements described in §§ 1.704-1(b)(2)(ii)(b)(1) and 1.704-1(b)(2)(iv) of the regulations.

Section 4.3 of Article IV of the Procedures provides that upon liquidation of the Series, the proceeds will be distributed to the Holders as provided in Article VII of the Procedures.

Section 5.6 of Article V of the Procedures provides that if a redemption occurs prior to the end of a fiscal year, Series will treat the fiscal year as ended for the purposes of computing the redeeming Holder's distributive share of the Series items and allocations of all items to such Holder will be made as though each Holder were receiving its allocable share of Series items at such time.

Section 7.1 of Article VII of the Procedures provides that subject to § 7.4 of the Procedures, upon the dissolution of Series, the Trustees shall liquidate the assets of Series, apply and distribute the proceeds as follows:

(a) first to the payment of all debts and obligations of Series to third parties, including without limitation the retirement of outstanding debt, including any debt owed to Holders or their affiliates, and the expenses of liquidation, and to the setting up of any reserves for contingencies which may be necessary; and

(b) then in accordance with the Holders' positive book capital account balances after adjusting book capital accounts for allocations provided in Article V of the Procedures and in accordance with the requirements described in § 1.704-1(b)(2)(ii)(b)(2) of the regulations.

Section 7.4 of Article VII of the Procedures provides that if a Holder has a negative balance in its book capital account following the liquidation of its interest, as determined after taking into account all capital account adjustments for the fiscal year during which the liquidation occurs, then such Holder shall restore the amount of such negative balance to Series by

the later of the end of the fiscal year or 90 days after the date of such liquidation so as to comply with the requirements of § 1.704-1(b)(2)(ii)(b)(3) of the regulations. Such amount shall, upon liquidation of Series be paid to creditors of Series or distributed to other Holders in accordance with their positive book capital account balances.

Based on the foregoing, the allocations provided for in the Procedures meet the requirements for economic effect set forth in § 1.704-1(b)(2)(ii) of the regulations. Accordingly, the allocations contained in the Procedures have economic effect within the meaning of § 704(b) of the Code. No opinion is expressed or implied regarding whether the allocations of profits and losses contained in the Procedures satisfy the requirements for substantiality as set forth in § 1.704-1(b)(2)(iii).

Except as specifically ruled upon above, no opinion is expressed on the federal tax consequences of the transactions described above under any other provisions of the Code. Specifically, no opinion is expressed as to whether any of the Holders qualifies as a RIC that is taxable under subchapter M, part 1 of the Code.

This ruling is directed only to the taxpayers who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to P1's authorized representative.

Sincerely yours,
. THOMAS HINES
Acting Branch Chief, Branch 2
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures: 2
Copy of this letter
Copy for § 6110 purposes