United States Senate
WASHINGTON, DC 20510

September 21, 2015

The Honorable Jack Lew
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

Dear Secretary Lew,

We write to applaud the Treasury Department and the Internal Revenue Service's recent efforts to crack down on the use of so-called "management fee waivers" by private equity fund managers.[1] For over a decade, many private equity fund managers have used these waivers to disguise payments for services as capital gains. This sort of tax cheating must be stopped.

Fund managers should not be allowed to alter the character of their salary income simply by inserting into their fee arrangements a few magic words that lack meaningful economic effect. As your guidance recognizes, Congress enacted section 707(a)(2)(A) of the Internal Revenue Code precisely to combat this sort of abuse.[2] Your guidance appropriately provides that the tax treatment of a fee waiver arrangement depends on whether the manager bears significant entrepreneurial risk. In many current fee waiver arrangements, there is no such risk.

We were especially heartened to see that the preamble of your guidance makes clear that the proposed regulations should not be read as a change in the IRS's position on this issue. Rather, this guidance is consistent with the Treasury and IRS's longstanding view of current law.

We urge the Treasury and the IRS to finalize the regulations as quickly as possible. The abuse of fee waivers has been ongoing for years at the expense of middle-class taxpayers who do not use similar gimmicks. Section 707(a)(2)(A) was enacted over 30 years ago, and management fee waivers have been used in the private equity industry for at least 15 years. There is no reason to delay the finalization of these regulations.

In addition, we expect swift enforcement of these long-awaited proposed regulations. Billions of dollars of tax revenue has already been permanently lost as a result of abusive fee waivers. The IRS must ensure that full taxes, interest, and penalties be paid with respect to all abusive fee waivers. We expect this to be a high priority for the agency.

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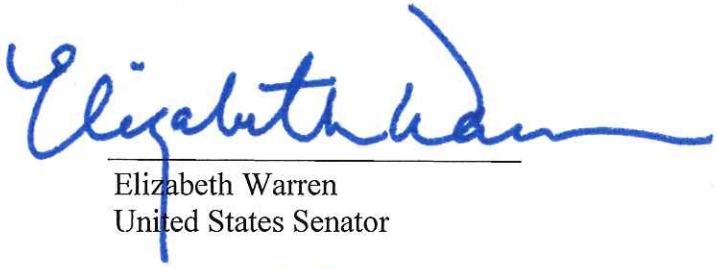
[1] REG–115452–14, 2015-32 I.R.B. 158.
[2] H.R. Rep. No. 432 (Pt. 2), 98th Cong., 2d Sess. 1216–21 (1984); S. Prt. No. 169 (Vol. 1), 98th Cong., 2d Sess. 223–32 (1984).

Just like teachers, firefighters, police officers, and all other hard working taxpayers, wealthy fund managers must pay ordinary income tax on their salaries. We will be watching your enforcement of these rules closely and look forward to your vigilance on this issue.

Sincerely,

Al Franken
United States Senator



Elizabeth Warren
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CC: Internal Revenue Service (IRS) Commissioner John Koskinen

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