

Independent Agent Exemption

—Minimizing the PE risk of fund managers—



Financial Services Agency



The “Independent Agent Exemption”

FY2008 Tax Reform

The **“Independent Agent Exemption”** was introduced into domestic tax legislation.

Agents of an independent status
(“independent agents”) are excluded
from the scope of the **“Agent PEs”**



Requirements of an “Independent Agent”

- **Legal Independence**
- **Economical Independence**
- **Ordinary Course of Business**

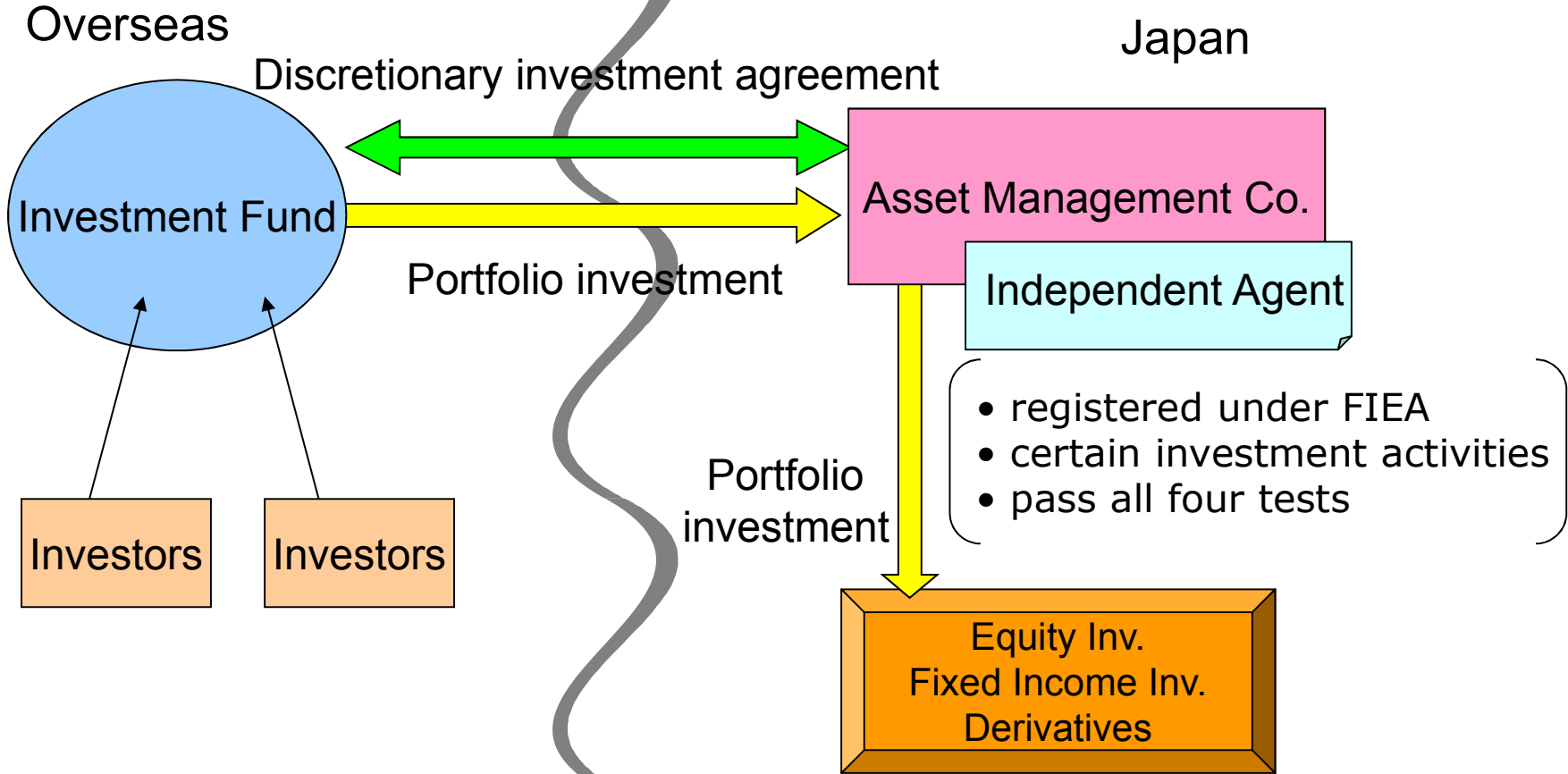
The applications of the “Independent Agent” provision of domestic laws are basically consistent with the commentaries to the OECD “Model Tax Convention on Income and on Capital.”



“Reference Cases”

- **Clarify the meaning of “Independent Agent” in the context of investment management business**

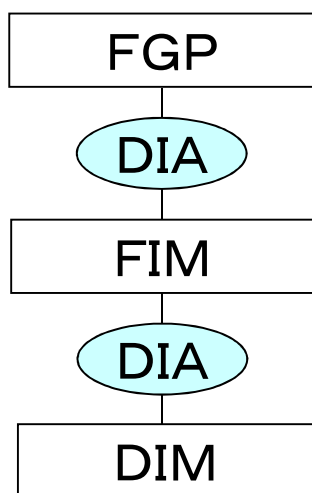
Summary



Investors are subject to taxation on their investment incomes in their residence, but are not in Japan.

Asset Management Co. is subject to taxation on the fees it received in Japan.

Applying the Provision of the “Independent Agent” to Certain Investment Activities



- Registered under the FIEA
- Conducts certain investment activities

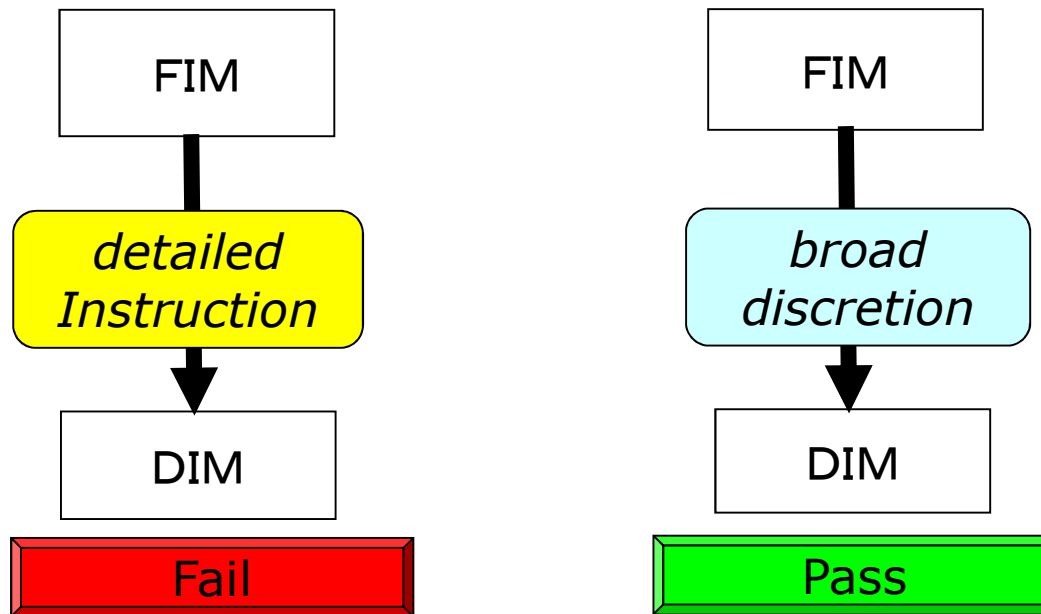
When a Foreign General Partner (FGP) or Foreign Investment Manager (FIM) of an offshore fund enters into a Discretionary Investment Agreement (DIA) with a Domestic Investment Manager (DIM) registered under the Financial Instruments and Exchange Act (FIEA)*, and the DIM conducts Certain Investment Activities (i.e. Portfolio Investment),

the DIM will be treated as an “Independent Agent” of the partners of the offshore fund if it passes all of the following tests;

- (A) **“Detailed instruction” test**
- (B) **“Shared officers” test**
- (C) **“Remuneration” test**
- (D) **“Diversification capacity” test**

* including a person approved by the commissioner of the FSA (the Article 16(x vii) of the Cabinet Office Ordinance on Definitions under Article 2 of the FIEA)

“Detailed instruction” test

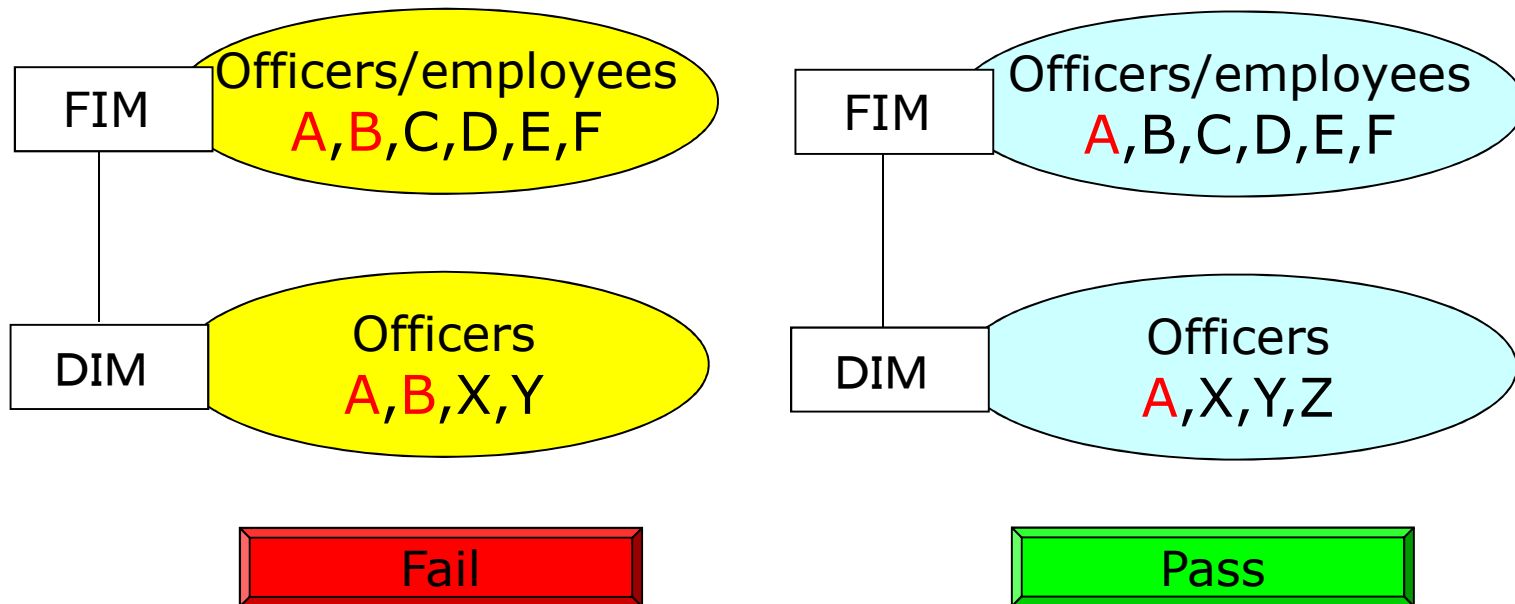


FSA’s “Q&A” is to clarify the points that are still unclear from the perspective of practical applications

“Reference cases”

“As the investment decisions that the DIM is delegated to make under the DIA are extremely limited, the partners of the offshore fund or a FIM is considered to be directly conducting investment activities in Japan.”

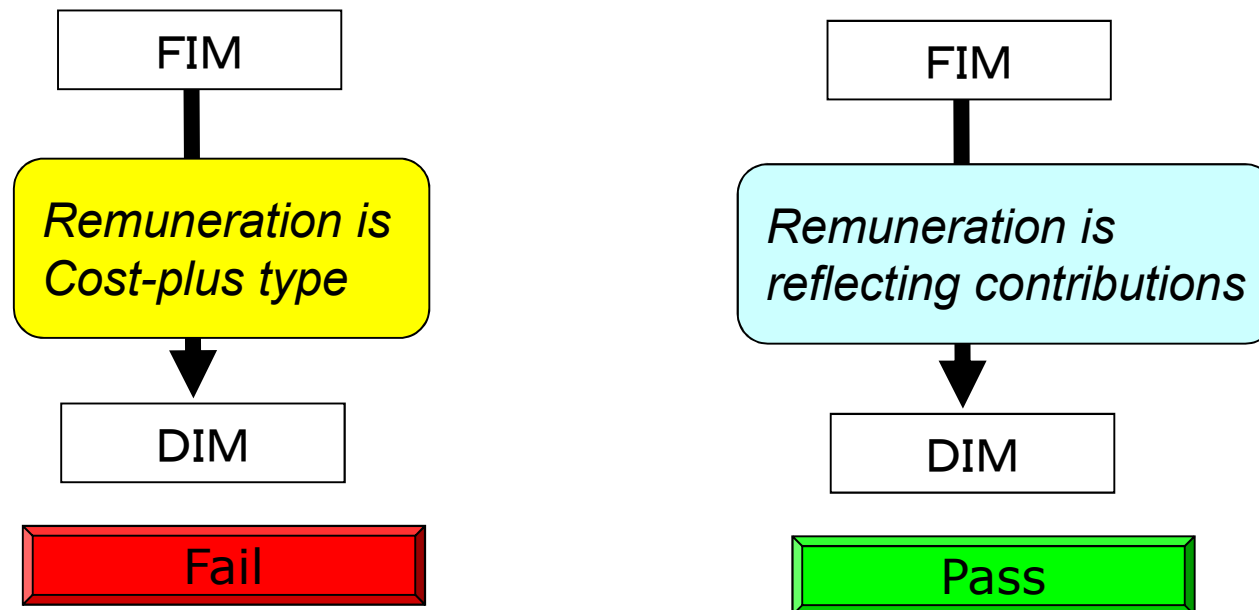
“Shared officers” test



“Reference cases”

“One half or more officers of the DIM concurrently serve as the officers or the employees of the FGP or the FIM.”

“Remuneration” test



“Reference cases”

“The DIM does not receive remuneration which corresponds to the amount of the total assets to be invested or investment income.”



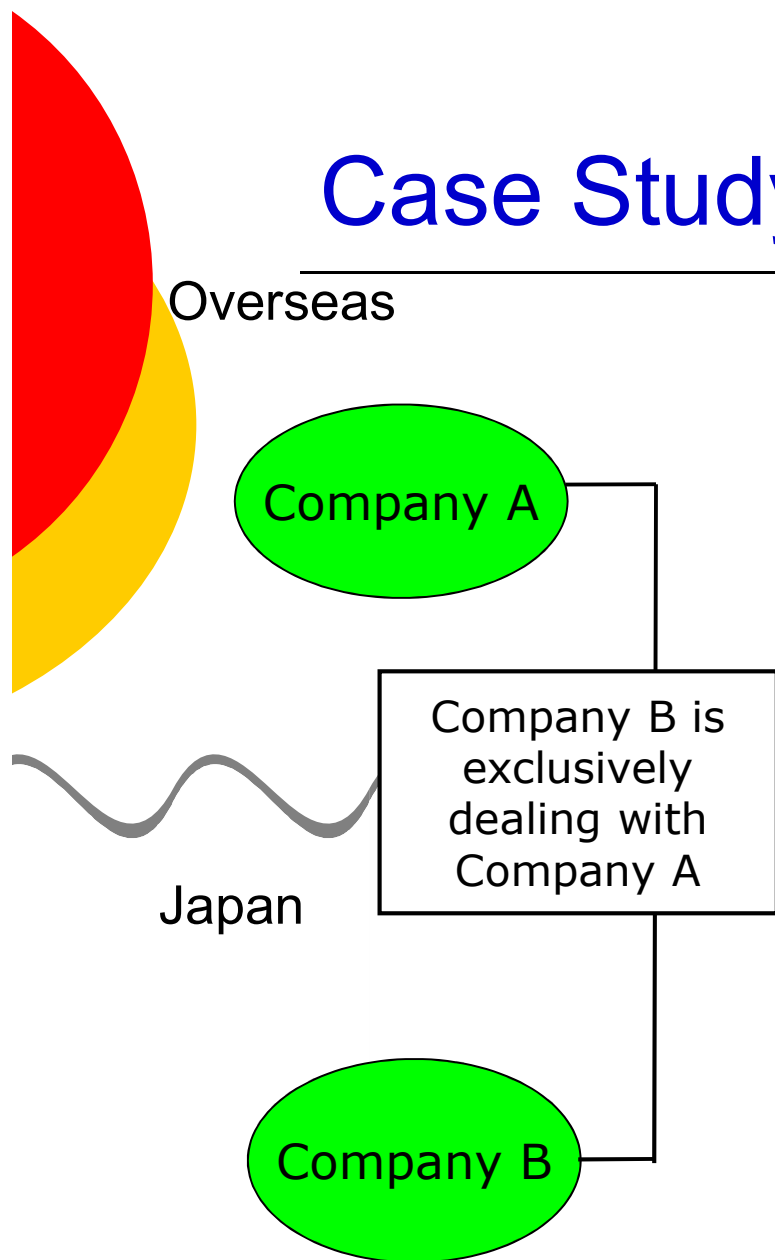
“Diversification capacity” test

Refer the next “Case Study”

“Reference cases”

“The DIM **does not have a capacity to diversify its business or to acquire other clients**, without fundamentally altering the way the DIM conducts its business or losing economic rationality for its business, in cases where the DIM **exclusively** or **almost exclusively** deals with the offshore fund or the FIM,

Case Study



Even though **exclusively** dealing with Company A, the Company B described below will be considered “Independent” from Company A.

Company B

(i) has special skills and knowledge
and

(ii) bears entrepreneurial risks.

Remuneration corresponding to
(a) the assets under management or
(b) the investment income,
indicates Company B bears entrepreneurial risk.

※ See Case 5 of “Reference cases”