

MEMO# 20910

March 2, 2007

California Revises Mutual Fund Service Provider Apportionment Regulations; Comments Requested

[20910]

March 2, 2007

TO: ADVISER DISTRIBUTOR TAX ISSUES TASK FORCE No. 3-07
TAX COMMITTEE No. 5-07 RE: CALIFORNIA REVISES MUTUAL FUND SERVICE PROVIDER
APPORTIONMENT REGULATIONS; COMMENTS REQUESTED

The California Franchise Tax Board ("FTB") has released an explanation and amendments (attached) to its proposed regulation on apportionment for mutual fund service providers ("MFSPs"). These amendments include changes suggested by the Institute. [\[1\]](#) The FTB will accept written comments regarding these amendments until 5:00 p.m. on March 12, 2007. The Institute plans to submit a letter reiterating our concerns regarding the regulation's "throw-back" rule. Please contact the undersigned by 5:00 p.m. on Wednesday, March 7, 2007 to provide additional comments regarding the amendments to the proposed regulation.

As requested by the Institute, the revised regulation provides greater flexibility to MFSPs regarding the permissible sources of information and methods for approximating the domiciles of shareholders in omnibus accounts (subsection (b)(1)(A)) and underlying beneficiaries of pooled assets such as pension plans (subsection (b)(1)(B)). Specifically, the proposed regulation no longer requires a MFSP to develop a reasonable method of assigning shares based solely on information received from the shareholder of record. A MFSP may use information derived from other sources.

Also as requested by the Institute, the proposed amendments permit a MFSP to compute the shareholder ratio in subsection (b)(1)(A) by using the taxable year of the principal member of the MFSP's combined reporting group (as an alternative to using the RIC's taxable year that ends during the taxable year of the principal member of the MFSP's combined reporting group), provided that the method chosen is used consistently in later years.

The FTB amendments address other issues, including clarifying that:

- the shareholder ratio calculation in subsection (b)(1)(A) should be performed for all states and not just for California;
- the definition of "domicile" in subsection (a)(4) presumes that the domicile of a beneficial owner of assets managed by a MFSP is the beneficiary's mailing address on the records of the entity for whom asset management services are rendered or the MFSP, unless either entity has actual knowledge that the beneficiary's address is different;
- the definitions of management, distribution or administrative services apply to "asset management services," as defined in subsection (a)(7);
- subsection (b)(1)(C)'s apportionment rules applicable to non-taxpayer members and subsection (b)(1)(D)'s "throw-back" provision apply to both services to RICs and asset management services; and
- the special apportionment rules in subsection (b)(1)(C) do not preclude MFSP sales not addressed by the proposed regulation from being included in the MFSP's sales factor.

The proposed regulation, including amendments, would apply to tax years beginning on or after January 1, 2007.

Lisa Robinson
Associate Counsel

[Attachment](#)

endnotes

[1] See Institute [Memorandum](#) (20318) to Adviser Distributor Tax Issues Task Force No. 9-06 and Tax Members No. 31-06, dated August 25, 2006.