

MEMO# 30788

July 20, 2017

ICI Letter on EU Reclaims and Closing Agreement Methodology

[30788]

July 20, 2017 TO: ICI Members

ICI Global Members SUBJECTS: Fund Accounting & Financial Reporting

International/Global

Tax RE: ICI Letter on EU Reclaims and Closing Agreement Methodology

The attached letter proposes procedures by which regulated investment companies (RICs) take into account previously-withheld foreign taxes that are recovered from European jurisdictions based upon the European Union (EU) treaty's free movement of capital article.[\[1\]](#) Last year, as you know, the IRS issued Notice 2016-10[\[2\]](#) and provided a "netting" approach based upon the credit-offset methodology advanced by the ICI.[\[3\]](#)

This letter first suggests a methodology for calculating the "compliance fee" required by any RIC seeking a closing agreement. The letter also urges reconsideration of the treatment of interest under the Notice's netting procedure. Finally, although not discussed at length in this letter, the letter reiterates our proposal that RICs be permitted to use netting even when netting can be achieved only by carrying forward excess tax recoveries for some limited number of years.

The closing agreement methodology suggested in the letter involves five steps for calculating the compliance fee. They are:

Step 1: Determine the portion of taxable versus tax-exempt investors.

Step 2: Multiply the amount of the recovered ("refunded") taxes by the taxable shareholder percentage. The product of this calculation is the "unadjusted fee amount."

Step 3: To determine the "compliance fee" that the RIC will pay pursuant to the closing agreement, multiply the unadjusted fee amount (as determined in Step 2) by a factor that reflects the additional tax that will be collected when the RIC distributes to shareholders the portion of the refunded tax that is not paid over to the US Treasury pursuant to the closing agreement.

Step 4: The RIC will treat as investment company taxable income the excess of the refunded amount over the compliance fee. The RIC will then distribute this excess to shareholders in order to satisfy the general RIC distribution requirements and avoid a RIC-

level tax on the income.

Step 5: The excess refund distribution will be characterized as “qualified dividend income” (or not), as discussed in our April 2016 submission, based on the nature of the previously-included income on which the tax was paid.

These steps, and the rationale on which they are based, are discussed in detail in the letter.

Keith Lawson
Deputy General Counsel - Tax Law

[Attachment](#)

endnotes

[1] See Institute Memorandum No. [26165](#), dated May 18, 2012.

[2] See Institute Memorandum No. [29650](#), dated January 15, 2016.

[3] See Institute Memoranda No. [27211](#), dated May 1, 2013; and No. [28219](#), dated June 19, 2014.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.