

MEMO# 20077

May 26, 2006

Draft ICI Comment Letter Regarding Reporting and Backup Withholding Requirements for Exempt-Interest Dividends

©2006 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. [20077] May 26, 2006 TO: TAX COMMITTEE No. 21-06 TRANSFER AGENT ADVISORY COMMITTEE No. 36-06 RE: DRAFT ICI COMMENT LETTER REGARDING REPORTING AND BACKUP WITHHOLDING REQUIREMENTS FOR EXEMPT-INTEREST DIVIDENDS Attached is the ICI's draft comment letter requesting clarification of reporting and backup withholding requirements applicable to exempt-interest dividends as a result of changes enacted by the Tax Increase Prevention and Reconciliation Act (the "Act"). 1 As we previously informed you, the Act amends section 6049's requirement for information reporting of interest by striking a provision that excluded tax-exempt interest from the definition of "interest." While the Act does not amend expressly the backup withholding rules of section 3406, the Act's changes to section 6049 effectively make tax-exempt interest a "reportable payment" under section 3406. Because the backup withholding rules of section 3406 apply to reportable payments, an extension of the definition of "reportable payment" to include tax-exempt interest appears to bring these payments within the backup withholding regime retroactive to January 1, 2006. First, the draft letter requests guidance clarifying that RICs report exempt-interest dividends on a new box to Form 1099-DIV, which is preferable because all RIC distributions (other than exempt-interest dividends) already are reported on Form 1099-DIV. Second, with respect to backup withholding, the Institute requests guidance (i) clarifying the first future date (allowing adequate time for implantation) on which payors are required to impose backup withholding; and (ii) providing extensive interest and penalty relief until a date later in 2006 that provides payors with sufficient time to modify their systems to comply with the new rules. 1 See ICI Memorandum (20024) to Adviser Distributor Tax Issues Task Force No. 6-06, International Members No. 8-06, Operations Members No. 12-06, Pension Members No. 36-06 and Tax Members No. 15-06, dated May 12, 2006. 2 Please provide any comments or suggested to Lisa Robinson (202-326-5835 or lrobinson@ici.org) by 4:00 p.m. EDT on Tuesday, May 30, 2006. Lisa Robinson Associate Counsel Attachment (in .pdf format)

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