

MEMO# 13720

July 12, 2001

SWITZERLAND AGREES TO REFUND TAX RECLAIMS TO REGULATED INVESTMENT COMPANIES UNDER US-SWITZERLAND INCOME TAX TREATY

[13720] July 12, 2001 TO: BOARD OF GOVERNORS No. 33-01 ACCOUNTING/TREASURERS MEMBERS No. 16-01 BANK AND TRUST ADVISORY COMMITTEE No. 9-01 CLOSED-END INVESTMENT COMPANY MEMBERS No. 23-01 INTERNATIONAL MEMBERS No. 10-01 SECURITIES OPERATIONS SUBCOMMITTEE No. 8-01 TAX MEMBERS No. 18-01 TRANSFER AGENT ADVISORY COMMITTEE No. 49-01 UNIT INVESTMENT TRUST MEMBERS No. 27-01 RE: SWITZERLAND AGREES TO REFUND TAX RECLAIMS TO REGULATED INVESTMENT COMPANIES UNDER US-SWITZERLAND INCOME TAX TREATY We are pleased to inform you that the Swiss Federal Tax Administration (FTA) has agreed to begin processing tax reclaims¹ filed by regulated investment companies (RICs) under the US-Switzerland Income Tax Treaty (Treaty), payment of which has been suspended since 1998. The agreement was reached following a collective effort of the Institute and five global custodians who jointly retained US and Swiss counsel and met twice in Switzerland with the FTA, most recently on June 21, 2001. Certain conditions and procedures for receiving refunds of withheld amounts were described in a letter provided by the FTA to Swiss counsel.² The agreement applies both to reclaims filed with respect to tax withheld during calendar years 1998 through 2001 and prospectively. If the FTA decides to modify the agreed procedures, any such change would apply only to tax withheld after the modification is announced. Pursuant to the agreement, a RIC will be entitled to a full refund of all withheld amounts if more than 95 percent of its direct shareholders are citizens or residents of the United States.³ For this purpose, a "tax reclaim" represents a receivable owed to a regulated investment company (RIC) by the Swiss tax authorities in an amount equal to the difference between the 35 percent Swiss withholding tax rate on dividends and the lower withholding tax rate of 15 percent to which the RIC is entitled under the Treaty. ² The FTA's letter is being translated into English and will be distributed after the translation is complete. If you would like to receive a copy of the FTA's original letter, in German, please contact the Institute's Ezella Wynn at 202 218-3560. ³ If a RIC has 5 percent or more non-US direct shareholders, the RIC will be entitled to a proportionate refund.⁴ These ownership percentages would be determined as of March 31, 2001 for reclaims attributable to calendar years 1998 through 2001, and each March 31 for reclaims attributable to subsequent years (e.g., March 31, 2002 for reclaims attributable to calendar year 2002). While the Institute maintains its position that RICs are entitled to full refunds under the Treaty because they beneficially own the income, the FTA's letter acknowledges that the Institute and the FTA have agreed to disagree on this point in the interest of resolving this issue. The Institute and the global custodian group

are continuing to discuss with the FTA the precise procedures for filing RIC reclaims. The FTA has indicated, however, that they will require a RIC to certify, to the best of its knowledge and belief, both (1) the percentage of the RIC's total shares held directly by investors (i.e., not through broker or other intermediary accounts) and (2) the percentage of the RIC's shares held by US persons, extrapolated from shares held directly in the RIC.⁵ Where a RIC had no direct shareholders, the RIC could apply for refunds, on a case-by-case basis, by providing other evidence to the FTA regarding the percentage of the RIC's shares held by US persons. The FTA reserves the right to audit information provided by the RIC. Deanna J. Flores Associate Counsel 3 Data collected by the Institute during the discussions with the FTA indicate that essentially all RICs will satisfy this 95 percent threshold and, therefore, will receive full refunds of their Swiss tax reclaims. 4 For example, if a RIC certified that 92 percent of its direct shareholders were US citizens or residents, the RIC would receive 92 percent of outstanding tax reclaims from Switzerland. 5 Under the agreement, the FTA will respect this extrapolation, without regard to the percentage of a RIC's total shares held directly by investors (e.g., whether a RIC has 1 percent or 99 percent of its shares held directly in the RIC).

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