

COMMENT LETTER

October 19, 2007

ICI Comment Letter Regarding California's Proposed Withholding Regulation (pdf)

By Electronic Delivery October 19, 2007 Mr. Bruce Langston Legal Department Franchise Tax Board P.O. Box 1720 Rancho Cordova, CA 95741-1720 Re: Proposed Changes Clarify Exclusion of RIC Income from Withholding Regulation Dear Mr. Langston: The Investment Company Institute¹ requests that the Franchise Tax Board ("FTB") amend its proposed withholding regulation to clarify that regulated investment company ("RIC") distributions are not California source income subject to withholding. Specifically, we request that the FTB make two changes to the proposed regulation: (1) Add a new subsection 18662-4(b)(12), which reads: (12) Income excluded from "taxable income of a nonresident or part-year resident" under Revenue and Taxation Code section 17955. (2) Amend the last sentence of subsection 18662-7(b) to read: It also does not include income excluded from "taxable income of a nonresident or part-year resident" under Revenue and Taxation Code section 17955. Section 17955 of the Revenue and Taxation Code generally provides that for purposes of computing taxable income of a nonresident or part-year resident, gross income of a nonresident from sources within California shall not include dividends, interest or gains and losses from certain qualifying investment securities, including RIC distributions. The proposed regulation excludes from withholding payments from intangible personal property, such as interest and dividends, unless the 1 ICI members include 8,889 open-end investment companies (mutual funds), 675 closed-end investment companies, 471 exchange-traded funds, and 4 sponsors of unit investment trusts. Mutual fund members of the ICI have total assets of approximately \$11.339 trillion (representing 98 percent of all assets of US mutual funds); these funds serve approximately 93.9 million shareholders in more than 53.8 million households. property has acquired a business situs in California or the payee has failed to provide a valid taxpayer identification number. (Prop. Reg. § 18662-4(b)(8)). The regulation states that California source income does not include income earned by partners in "investment partnerships" within the meaning of Code sections 17955 or 23040.1 (Prop. Reg. § 18662-7(b)). We understand that, consistent with the California Code, the FTB does not intend to treat income earned by RICs as California source income or require RICs to withhold on distributions to nonresidents under the proposed regulation. By incorporating only section 17955's exclusion for investment partnerships, the proposed regulation does not make clear that RIC income is excluded from the definition of "California source income." Our suggested changes clarify that RIC income from qualifying investment securities, like income from investment partnerships, is excluded from the definition of "California source income" and not subject to withholding

under the regulation. We look forward to ongoing discussions with your office as the regulation is finalized. Please contact the undersigned at 202-326-5835 or lrobinson@ici.org if we can provide you with any additional information. Sincerely, /s/ Lisa Robinson
Lisa Robinson cc: Colleen Berwick

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