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By Electronic Delivery

September 11, 2020

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Associate Chief Counsel (International)
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Helen Hubbard
Associate Chief Counsel (Financial Institutions & Products)
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

RE: Notice 2016-10 and Closing agreements

Dear Mr. Blessing and Ms. Hubbard:

The Investment Company Institute¹ requests a meeting with you and your colleagues at the Internal Revenue Service (IRS) to discuss issues arising from Notice 2016-10 and a closing agreement template for regulated investment companies (RICs) receiving reclaim amounts from European Union countries.² Resolution of these issues and finalization of a standard closing agreement are of increased urgency because France has conceded claims made by US RICs. Most funds with international investments have filed claims in France; we thus estimate the amount of money that will be returned to US RICs to be several billion euros. At least two funds already have received refunds from France (equal to about €300 million), and we expect others to receive refunds imminently.

Specifically, ICI requests:

¹ The [Investment Company Institute](http://www.ici.org) (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US\$26.0 trillion in the United States, serving more than 100 million US shareholders, and US\$7.9 trillion in assets in other jurisdictions. ICI carries out its international work through [ICI Global](http://www.ici.org), with offices in London, Hong Kong, and Washington, DC.

² Specifically, RICs have filed reclaims under Article 63 of the Treaty on the Functioning of the European Union (TFEU) which prohibits certain restrictions on the free movement of capital. The Court of Justice of the European Union (CJEU) has held that Article 63 is violated if a Member State exempts its resident funds from withholding tax on dividends paid by resident country companies while imposing tax on "comparable" non-resident funds.

- (1) RICs be permitted to “carry forward” the amount of any refunded taxes that cannot be offset in the year refunded under Notice 2016-10;
- (2) Finalization of a standardized closing agreement; and
- (3) Development of a mechanism for RICs to make payment to the IRS upon receipt of any reclaims, to prevent the accrual of post-refund interest.

Carryovers

As described in our 2016 letter,³ the netting method permitted in Notice 2016-10 provides RICs with an administrable mechanism for compensating the US government for foreign tax credits previously claimed in good faith by the RICs’ shareholders. This mechanism, however, is useful only to the extent that a RIC has sufficient foreign tax credits in the year in which the refund is received to fully offset that refund. For the reasons outlined in our previous letter, we urge the IRS to permit RICs to carryover any amounts that cannot be fully netted in the first year.

We recognize that the IRS may have concerns about permitting an unlimited carryover. We agree that it would be reasonable to limit the carryover period. A period of eight years generally should permit RICs to fully offset any refunded amounts, but a shorter carryover period still would be preferable to requiring these funds to enter into a closing agreement.

Given the size of the French reclaim amounts, we understand that many funds will be unable to use the credit offset approach as set forth in Notice 2016-10 because they will not have sufficient foreign tax credits in the year in which the refund is received. Absent additional guidance, this means that an exponential number of funds will be forced to enter into closing agreements with the IRS to resolve the issue. We believe that permitting a carryover would reduce greatly the burden on both the IRS and funds, while ensuring that the government is properly compensated for foreign tax credits previously taken.⁴

Standardized Closing Agreement

Providing standard terms for a closing agreement would reduce significantly the administrative burden to the IRS and RICs. Even if funds are permitted to carryover refund amounts, they still may need to come in for a closing agreement for a number of reasons, including: (1) the fund may not expect to have sufficient foreign tax credits to offset the refunded amounts, even over some number of years; (2) the fund and its board may determine that it is in the best interests of the fund shareholders to enter into a closing agreement; or (3) the RICs may be held predominantly by insurance companies, for whom netting is not permitted under Notice 2016-10.

³ See ICI Letter to Bob Stack, Marjorie Rollinson and Helen Hubbard, dated April 1, 2016 (attached).

⁴ As discussed in the 2016 comment letter, we believe it would be appropriate to impose an interest toll charge on any amounts carried forward.

ICI has seen the draft closing agreement sent to several of our members. As we have not been involved in the closing agreement discussions, we have some questions about the terms.⁵ Overall, however, we believe the agreement is workable for refunds received in the year that the closing agreement is sought. Standardized terms similar to those in the draft will provide RICs receiving refunds in future years a framework for dealing with such amounts when received (i.e., the refunded amounts should not be included in income, in whole or in part), which should simplify and shorten the closing agreement process.

Nevertheless, the IRS will need to separately negotiate closing agreements with funds that already included refunds into income, in whole or in part, or for other special circumstances (e.g., the RIC has liquidated). Some number of funds have received refunds since 2016 but have not been able to enter discussions with the IRS regarding those amounts. To mitigate the time needed to finalize these closing agreements, the IRS also could provide standardized terms for RICs in these situations.

We also would like to discuss the rationale for including the “excess refund” in the RIC’s income in the year the compliance fee is paid.⁶ We believe this amount should not be included in the fund’s income because it already was included in the gross-up when the tax credit was passed through to shareholders under section 853(b)(2). This amount effectively would be taxed twice under the current draft closing agreement.

If the excess refund is included in the RIC’s income, we ask that the IRS clarify that such amount is qualified dividend income (QDI) to the extent that the dividend when received was QDI. This would ensure that existing shareholders are not unfairly taxed on these amounts.

Payment Mechanism

Finally, we urge the IRS to create a mechanism by which RICs can make payments to the IRS when refunds are received, to prevent the accrual of post-refund interest.⁷ A standard closing agreement should diminish somewhat the need for this in the future, by reducing the amount of time it takes to finalize an agreement. Nevertheless, allowing for payment would lessen the imperative that the IRS conclude closing agreements as quickly as possible.

Funds that have received refunds already would like to pay a deposit but thus far have not been able to do so. The post-refund interest may be significant for some of these RICs, and we would like to avoid this going forward. Allowing RICs to make a deposit when a refund is received would ensure fair administration of the tax law. This is especially important as France

⁵ Because we are not involved in the individual negotiations, we would like to include in the meeting representatives from the accounting firms, to ensure that everyone in the industry is on the same page.

⁶ The “Excess Refund” is the amount of the foreign tax adjustment (the refund amount and interest in US dollars) in excess of the amount paid to the IRS as part of the compliance fee.

⁷ Because RICs generally do not have tax liabilities, they cannot prepay or post a deposit for the anticipated compliance fee liability. Any amounts paid by the fund would be refunded to them because there is no future tax liability against which to credit the payment.

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and other countries concede and begin to make payments. The number of RICs that will need closing agreements will multiply exponentially, especially if carryover is not permitted.

* * *

We appreciate your time and attention to these issues. We emphasize the need to resolve these issues as quickly as possible, given the imminent refund of French reclaims. We will contact your offices soon to arrange a time to further discuss our requests. In the meantime, please do not hesitate to contact Keith Lawson (202-326-5832 or lawson@ici.org) or me (202-371-5432 or kgibian@ici.org) if you have any questions or concerns.

Sincerely,



Karen Lau Gibian
Associate General Counsel, Tax Law

Attachment