

MEMO# 31841

July 9, 2019

ICI Proposes Guidance Permitting Pass-Through of Interest under Section 163(j)

[31841]

July 9, 2019 TO: ICI Members

Tax Committee SUBJECTS: Tax RE: ICI Proposes Guidance Permitting Pass-Through of Interest under Section 163(j)

ICI recently submitted to the Internal Revenue Service (IRS) draft proposed regulations (attached) that would permit regulated investment companies (RICs) to pass through interest income to corporate shareholders for purposes of determining such corporations' interest expense limitation under section 163(j). We originally suggested this guidance in our 2019-2020 Guidance Priority List recommendations.[\[1\]](#) Absent such guidance, corporate shareholders in fixed income or money market funds could be limited in their ability to use interest-related dividends from those funds to offset any interest expense under section 163(j) as amended by the 2017 tax legislation.[\[2\]](#)

The draft proposed regulations would permit RICs to pay "section 163(j)-related interest dividends," which is the amount of a dividend distribution reported to the RICs' shareholders as a section 163(j)-related interest dividend and as determined under the draft regulations. A taxpayer that receives a section 163(j)-related interest dividend would be permitted to treat that dividend as interest income for purposes of section 163(j). The draft regulations also include examples illustrating how such reporting would work.

ICI also submitted to the IRS the attached examples. The first illustrates the example in Rev. Rul. 2005-31,[\[3\]](#) which clarifies the designation of qualified dividend income (QDI) under section 854 and qualified interest income (QII) and net short-term capital gain under section 871(k), where the reported amounts may exceed 100 percent of the distributions. The principles contained in the draft proposed regulations are based upon those set forth in Rev. Rul. 2005-31. Examples 2 and 3 in the attached document illustrate the first two examples in ICI's draft proposed regulations.

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[Attachment No. 1](#)

[Attachment No. 2](#)

endnotes

[1] See Institute Memorandum No. 31797 dated June 10, 2019, which can be found at: https://www.ici.org/my_ici/memorandum/memo31797.

[2] See Institute Memorandum No. 30991 dated December 21, 2017, which can be found at: https://www.ici.org/my_ici/memorandum/memo30991.

[3] See Institute Memorandum No. 18831 dated May 4, 2005, which can be found at: <https://www.ici.org/pdf/memo18831.pdf>.

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