

MEMO# 7416

November 14, 1995

CONFEREES ACT ON TAX PROVISIONS

November 14, 1995 TO: BOARD OF GOVERNORS No. 75-95 FEDERAL LEGISLATION
MEMBERS No. 25-95 PUBLIC INFORMATION COMMITTEE No. 41-95 30% REPEAL WORKING
GROUP TAX ISSUES WORKING GROUP PENSION SIMPLIFICATION WORKING GROUP RE:
CONFEREES ACT ON TAX PROVISIONS

The House-Senate conferees have agreed to a compromise between the House and Senate versions of the tax cut provisions of the budget reconciliation bill. From the standpoint of the Institute's legislative agenda, the results are quite favorable. The 30% test (the "short-short" rule) would be repealed. A bank common trust fund would be allowed to transfer its assets to one or more mutual funds without being subject to taxation. The income limits on eligibility for full deductibility of IRA contributions would be increased by \$5,000 a year for 12 years, from the present \$40,000 for couples and \$25,000 for individuals ultimately to \$100,000 for couples and \$85,000 for individuals. (These limits would be subsequently indexed for inflation in \$5,000 increments.) Penalty-free IRA withdrawals would be provided for first-home purchases, higher education expenses, financially devastating medical expenses, and during periods of unemployment. Present-law nondeductible IRAs would be replaced with new American Dream Savings Accounts which would not have an income limit on eligibility. Contributions to an American Dream Savings Account would not be tax-deductible. Withdrawals from an American Dream Savings Account would not be includible in income or subject to a 10 percent early withdrawal tax if attributable to contributions that had been held in the American Dream Savings Account for at least five years and were either (1) made after the individual attained age 59½ or (2) made for one of the special early withdrawal purposes, or on account of death or disability, or in the form of an annuity. Other withdrawals would be taxable to the extent of earnings on contributions. Each spouse in a married couple would be eligible to make an annual IRA contribution of up to \$2,000. The total annual contribution by an individual to both an IRA and an American Dream Savings Account could not exceed \$2,000. The \$2,000 limit would be indexed for inflation in \$500 increments. A new simplified retirement plan (called a SIMPLE plan) would be created for small businesses with 100 or fewer employees. A SIMPLE plan could be either an IRA for each employee or part of a 401(k) plan. Employees could contribute up to \$6,000 of their wages; employers would generally have to match employee contributions up to 3% of the employee's pay. SIMPLE plans would not be subject to nondiscrimination or top-heavy rules. All contributions to an employee's account would be fully vested. Simplified nondiscrimination rules would be provided for 401(k) plans. The Institute has advocated enactment of all the above items. Other features of the conference action: The conferees' bill does not include a provision requiring mutual funds to report the basis of shares redeemed by shareholders (though such a provision has been included in tax simplification legislation in the past). The Institute has advocated not requiring mandated shareholder

basis reporting. The conferees' bill does not include a provision in the Senate-passed bill which would have expanded the coverage of the special rules limiting the deductibility of compensation above \$1,000,000 per year. The conferees' bill would provide a 50% exclusion for capital gains of individuals, effective for dispositions on or after January 1, 1995. The basis of certain assets acquired after 2000 (or marked to market in 2001) would be indexed for inflation if held for at least three years after 2000. The conferees' bill would permit the establishment of tax-favored medical savings accounts. Following approval by the House and Senate, the bill will be sent to the President, where a veto is likely. We will keep you informed as this matter develops. For additional information, please contact the Legislative Affairs Department (202) 326-5890. For those members with access privileges, this memo can be found in ICINet. Julie Domenick Senior Vice President Public Affairs

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