

MEMO# 1238

July 3, 1989

MARYLAND TAX DEVELOPMENTS

- 1 - July 3, 1989 TO: TAX MEMBERS NO. 20-89 MONEY MARKET FUND CHIEF EXECUTIVE OFFICERS NO. 5-89 RE: MARYLAND TAX DEVELOPMENTS

1. Pass-Through of Federal
Obligation Interest As you know, the Institute has been working for some time to eliminate state taxation of investment company dividends derived from interest on federal obligations. We are pleased to inform you that Maryland has now become a "pass-through" state with its recent enactment of legislation providing pass-through treatment for federal obligation interest. The Maryland statute, a copy of which is attached, provides that individuals shall subtract from federal adjusted gross income, in determining Maryland adjusted gross income, "state tax exempt interest" received from a regulated investment company (RIC) so long as at least 50 percent of the interest received by the RIC during its taxable year is from U.S. Government obligations.

2. Trustee Allocations of RIC Capital Gain Distributions For the past two years, the Institute has supported legislation in Maryland to amend its law requiring that all realized and unrealized capital gains of a trust accrue to the benefit of remaindermen rather than income beneficiaries. This legislation is intended to broaden the investment opportunities available to trustees seeking to maximize total return to income beneficiaries and remaindermen without violating their fiduciary obligation not to benefit either class over the other. Under the existing statute, many investments with attractive returns might not have been suitable for trusts, because the investments might be deemed to favor either current income distributions or capital appreciation. Funds that invest primarily in growth stocks, for example, might be deemed to be more beneficial to the remaindermen of a trust than to its income beneficiaries.

- 2 - We are pleased to inform you that this legislation has now been enacted. The new statute, a copy of which is attached, permits trustees to irrevocably elect to treat as income eligible to be paid to an income beneficiary a portion of the capital gain dividend paid to a trustee by a mutual fund. The portion of the capital gain dividend subject to this election will be limited so that the total distribution to income beneficiaries cannot exceed the annual federal mid-term rate. All remaining capital gain dividend amounts, plus all unrealized capital gains, will accrue to the benefit of the remaindermen. We will keep you informed of developments. Keith D. Lawson Assistant General Counsel Attachments

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