

**MEMO# 1004**

February 22, 1989

## **VIRGINIA PASS-THROUGH REQUIREMENTS**

- 1 - February 22, 1989 TO: TAX MEMBERS NO. 6-89 MONEY MARKET FUND CHIEF EXECUTIVE OFFICERS NO. 2-89 RE: VIRGINIA PASS-THROUGH REQUIREMENTS

\_\_\_\_\_ Last spring, the Virginia Department of Taxation announced that Virginia would permit pass-through treatment for federal obligations and for certain state obligations. (See Institute Memorandum to Tax Members No. 25-88 and Money Market Chief Executive Officers No. 24-88, dated May 31, 1988.) The Announcement provided that "in order that taxpayers may have sufficiently detailed information upon which they can substantiate the exempt interest claimed, they should be furnished with a breakdown of the dividends on a monthly basis." The State's instructions for preparing 1988 Virginia income tax returns (attached) provide that pass-through treatment will not be permitted unless you attach a statement to your return from the fund which: (1) details the amount of dividends you earned from the fund; and (2) summarizes the prorations between exempt and taxable dividends on a monthly basis. If the company only provides a statement that a certain percentage of the income from the fund is from exempt obligations, this is not sufficient for exempting this income from Virginia income taxation. The instructions provide similar requirements for passing through income derived from certain state obligations. Upon learning of these instructions, the Institute contacted the Virginia Tax Commissioner and indicated that the Virginia reporting requirements would be extremely burdensome for funds and could not be met, in many instances, before - 2 - shareholders would be required to file their State income tax returns. The attached response from the State Tax Commissioner provides that it is not "the [State Department of Taxation's] policy to deny a subtraction for exempt mutual fund interest if the fund's report to the taxpayer, whether on a monthly or less frequent basis, segregates taxable and exempt interest on a percentage or average percentage basis." The letter further provides that the instructions are "only intended to be a general guide" and that they "are not intended to require taxpayers to provide the department with information that is not available to them from the mutual fund in which they invest." We will keep you informed of developments. Keith D. Lawson Assistant General Counsel Attachments

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