

MEMO# 14532

March 13, 2002

TREASURY LETTER TO ICI ON CAPITAL GAINS DEFERRAL

[14532] March 13, 2002 TO: BOARD OF GOVERNORS No. 10-02 FEDERAL LEGISLATION MEMBERS No. 4-02 PRIMARY CONTACTS - MEMBER COMPLEX No. 21-02 PUBLIC INFORMATION COMMITTEE No. 9-02 TAX COMMITTEE No. 8-02 RE: TREASURY LETTER TO ICI ON CAPITAL GAINS DEFERRAL On October 12, 2001, Terry Glenn as Chairman of the Institute's Board of Governors wrote to Treasury Secretary O'Neill and recommended that the economic stimulus package then under consideration include the proposal to allow mutual fund shareholders to defer taxes on reinvested capital gain distributions until they redeem mutual fund shares. (A copy of Mr. Glenn's letter is attached.) On March 4, 2002, Mark Weinberger, Treasury Assistant Secretary for Tax Policy, responded to Mr. Glenn. The letter raises a tax policy objection to the proposal and notes as follows: "Under current law, as financial intermediaries the income of mutual funds is taxed under the general principle that such income is currently taxable to either the intermediary or the investor, but not both. Although mutual funds are theoretically subject to the corporate income tax, no corporate level tax is imposed on income that is passed through (and taxed) to the investor. In contrast to current law, the proposal would give preferable tax treatment to a portfolio held inside a RIC relative to an identical portfolio held directly by an individual or by other financial intermediaries, such as a trust, partnership, or REIT. The proposal also raises issues about how to allocate and account for basis." While not favorable, the letter articulates the pure tax policy objections we anticipated. As we have discussed, in order for us to succeed it will be necessary to overcome pure tax 2 policy theory by emphasizing broader social policy benefits, as the tax code does in many other instances. We will keep you informed of further developments. Matthew P. Fink President Attachments Note: Not all recipients receive the attachments. To obtain copies of the attachments, please visit our members website (<http://members.ici.org>) and search for memo 14532, or call the ICI Library at (202) 326-8304 and request the attachments for memo 14532. Attachment no. 1 (in .pdf format)