

MEMO# 8081

July 25, 1996

INSTITUTE SUBMISSION TO IRS ON MULTIPLE-CLASS FUNDS

1 See Institute Memoranda to Tax Committee No. 23-95 and Accounting/Treasurers Committee No. 22-95, dated June 16, 1995, and to Tax Committee No. 33-95 and Accounting/Treasurers Committee No. 45-95, dated November 2, 1995. July 25, 1996 TO: ACCOUNTING/TREASURERS COMMITTEE No. 30-96 TAX COMMITTEE No. 27-96 RE: INSTITUTE SUBMISSION TO IRS ON MULTIPLE-CLASS FUNDS

As you know, the Institute has asked the IRS to issue published guidance setting forth the circumstances under which the IRS will not assert that dividends paid by a multiple-class mutual fund are preferential.¹ In connection with this request, the Institute submitted to the IRS the attached letter, which was accompanied by (1) a draft of a revenue procedure on multiple-class funds that was prepared by the Institute, and (2) a memorandum on expense limitation arrangements (e.g., waivers and reimbursements) in a multiple-class context. The letter reminds the IRS that issues relating to multiple-class funds are particularly important to our members and that we would like to resolve these issues as soon as possible. The draft revenue procedure sets forth "safe harbor" circumstances under which the IRS will (1) respect the separate classes of a multiple-class fund, thus allowing dividends to differ among the classes, and (2) permit expense limitation arrangements with respect to a fund's expenses. The criteria set forth in the draft revenue procedure for respecting the separate classes generally are based on the requirements imposed by the Securities and Exchange Commission pursuant to Rule 18f-3, with an additional requirement that each class is bona fide, which means that each class is either publicly offered or has at least 500 beneficial owners. The draft revenue procedure specifies three types of expense limitations that will not be treated as giving rise to preferential dividends. The three types are as follows: (1) limitations that reduce the expenses of a distribution arrangement and/or shareholder service arrangement for a particular class or classes; (2) limitations that reduce management fees, or any other fund-wide expenses, for all classes; and (3) limitations that reduce class-specific expenses for a particular class or classes. The Institute's proposal on expense limitations would significantly reduce the inconsistencies between the tax and securities law treatment of expense limitations and would relieve the industry from the unwarranted restrictions currently imposed by the IRS on expense limitations. We will keep you informed of developments. Anne M. Barr Assistant Counsel - Tax Attachment