

**MEMO# 2229**

September 27, 1990

## **STATUS OF BUDGET NEGOTIATIONS**

September 27, 1990 TO: MEMBERS - ONE PER COMPLEX NO. 42-90 RE: STATUS OF BUDGET NEGOTIATIONS

The negotiations over the Federal Budget for fiscal 1991 have reached a critical point because, without a budget agreement, automatic government spending cuts take effect October 1. As you know, under consideration are two proposals that would have a significant impact on investment companies: a securities transaction excise tax ("STET") and the indexing of capital assets for inflation ("indexing"). Securities Transaction Excise Tax - STET The Institute and others have actively opposed a STET. In particular, we have expressed our concern regarding the adverse impact of 1) a STET imposed on shareholder transactions in money market funds and 2) the double layer of tax resulting from a STET imposed on both portfolio and shareholder transactions in all funds. At the moment, the STET does not appear to be part of any budget agreement. (See Institute Memoranda to Board of Governors No. 58-90, Members - One Per Complex No. 32-90, Federal Legislation Committee No. 5-90 and Tax Committee No. 21-90, dated August 13, 1990; and to Members - One Per Complex No. 29-90, dated August 1, 1990.) However, we will continue to monitor the negotiations for a possible STET proposal.

Indexing of Capital Assets It appears that President Bush has failed again in his attempts to secure a preferential capital gains tax rate. Budget talks have been deadlocked for weeks over this issue. Late last night, it was reported that indexing of capital gains is under very serious consideration as an alternative to the Administration's capital gains proposal. As you know, indexing would create substantial complexity for investment companies and their shareholders. Over the past year, the Institute has informed both Congress and the Administration of the burdens imposed on funds and their shareholders under various indexing proposals. Last year, when indexing was included in the House version of the 1989 tax bill, the Institute succeeded in obtaining several provisions clarifying the application of indexing to investment companies and their shareholders. (See Institute Memorandum to Tax Members No. 32-89, Closed-End Fund Members No. 43-89, Unit Investment Trust Members No. 49-89, Accounting/Treasurers Committee No. 38-89, Operations Committee No. 17-89 and Transfer Agent Advisory Committee No. 24-89, dated September 27, 1989.) However, the inherent complexity of indexing as applied to investment companies and their shareholders is not resolved by the 1989 amendments and, in fact, cannot wholly be resolved under any indexing proposal. While tax practitioners recognize the inherent pitfalls of any indexing proposals, practical issues may not be resolved in a final budget compromise, and may have to await administrative action. We will continue to inform Congress and the Administration of our concerns about indexing and will keep you advised of developments. David Silver

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