MEMO# 7878

May 21, 1996

INSTITUTE STATEMENT ON NEW TAX PROVISIONS IN PRESIDENT CLINTON'S BUDGET PROPOSAL

1 See Institute Memorandum to Closed-End Fund Committee No. 7-96, Operations Members No. 12-96, Pension Members No. 15-96, Tax Members No. 13-96, Transfer Agent Advisory Committee No. 15-96, and Unit Investment Trust Committee No. 10-96, dated March 26, 1996. 2 See Institute Memorandum to Accounting/Treasurers Members No. 54-95, Closed-End Fund Committee 57-95, International Committee No. 38-95, Operations Committee No. 34-95, Tax Members No. 52-95, Transfer Agent Advisory Committee No. 60-95, and Unit Investment Trust Committee No. 82-95, dated November 21, 1995. 3 See Institute Memorandum to Tax Members No. 20-96, dated April 25, 1996. May 21, 1996 TO: TAX COMMITTEE No. 15-96 RE: INSTITUTE STATEMENT ON NEW TAX PROVISIONS IN PRESIDENT CLINTON'S BUDGET PROPOSAL

____ President Clintons budget proposal for the fiscal year beginning October 1, 1996 includes several tax provisions of interest to regulated investment companies ("RICs") and their shareholders.1 The House Ways and Means Committee requested written comments on tax provisions included in the President's budget proposal that were not included in the Balanced Budget Act of 1995,2 which was approved by Congress last November and vetoed by President Clinton. In the attached statement submitted to the Committee, the Institute commented on proposals to (1) require securities investors to use the average cost basis method, (2) increase information reporting penalties, and (3) require gain recognition on conversions of large C corporations to S corporations (this proposal indirectly relates to RICs). The Institute*s comments are summarized below. Average Cost Basis. The Institute strongly opposes the proposal to require taxpayers to calculate gains and losses on dispositions of substantially identical securities, including shares of a RIC, using an average cost basis. The proposal would increase taxes on securities investors, and thus reduce incentives to save and discourage capital investment. In addition, requiring the use of the average cost basis method would substantially complicate basis calculations for millions of securities investors. (The Institute previously submitted letters to members of the Senate Finance Committee and the House Ways and Means Committee expressing opposition to the average cost basis proposal.3) Information Reporting Penalties. The Institute opposes the proposal to increase the penalty for failure to file correct information returns. The RIC industry maintains a high level of information reporting compliance, and the current penalty structure provides powerful incentives for RICs to promptly correct any errors made. Conversions of Large C Corporations to S Corporations. Should the Congress adopt this proposal, the Institute recommends that the legislative history for the proposal, which would require current gain recognition on the conversion of a large C corporation to an S corporation, include a statement making it clear that the proposal would not impact Notice 88-96, which provides a safe harbor from gain recognition for RICs that temporarily fail to qualify under Subchapter M. We will keep you informed of developments. Anne M. Barr Assistant Counsel - Tax Attachment

---