

MEMO# 11171

August 9, 1999

CONGRESS PASSES TAX CUT BILL

[11171] August 9, 1999 TO: BOARD OF GOVERNORS No. 51-99 FEDERAL LEGISLATION
MEMBERS No. 21-99 PRIMARY CONTACTS - MEMBER COMPLEX No. 75-99 PUBLIC
INFORMATION COMMITTEE No. 34-99 RE: CONGRESS PASSES TAX CUT BILL

Both the Senate and the House of Representatives approved on August 5 a tax relief package that contains a number of provisions of interest to the mutual fund industry. H.R. 2488, the "Financial Freedom Act of 1999," includes the following: Increased IRA and Retirement Plan Contribution Limits. The annual IRA contribution limit is raised in stages to \$5,000 by 2006. The 401(k), 403(b) plan and 457 plan annual contribution limits are increased in stages to \$15,000 by 2005. The annual SIMPLE plan limit is raised in stages to \$10,000 by 2004. Expanded IRA and Roth IRA Eligibility. Income limits on eligibility to make Roth IRA contributions are increased from \$95,000 to \$100,000 for individuals and from \$150,000 to \$200,000 for couples, beginning in 2003. Also in 2003, the income limit on eligibility to convert a regular IRA to a Roth IRA is increased from \$100,000 to \$200,000 for couples. (There is no change in eligibility limits for deductible IRAs.) New After-tax "Plus" Accounts. 401(k) and 403(b) plans are permitted to allow participants to make after-tax contributions whose eventual distributions are taxed similar to Roth IRA distributions. "Catch-up" Contributions. Persons 50 and older are eventually permitted to contribute an additional 50 percent more than the standard limit to IRAs and salary deferral pension plans. The "catch-up" amount is phased in over five years in 10 percent increments. Other Pension Provisions. Portability is enhanced among the various types of defined-contribution plans and IRAs, top-heavy rules are modified and regulatory burdens are reduced under other provisions. "Flow-through" Provision. A provision is included that eliminates a tax barrier discouraging foreign investors from investing in U.S. securities through U.S. mutual funds. Foreign investors are allowed to receive the same tax treatment for interest and short-term received capital gains from U.S. mutual funds as they would receive if they invested either directly or through a foreign mutual fund. Capital Gains Tax Reduction. The maximum rate of tax on net capital gains realized by individuals after December 31, 1998 is reduced from 20 percent to 18 percent; gains currently taxed at a 10-percent rate will be taxed at an 8 percent rate. In addition, the basis of assets acquired after December 31, 1999 is indexed for inflation. Education IRAs. The annual limit on contributions to Education IRAs is increased from \$500 to \$2,000, and withdrawals are permitted for elementary and secondary education expenses. Corporations are also permitted to contribute to Education IRAs. President Clinton has indicated that he will veto the tax cut bill. We will keep you informed of further developments. Matthew P. Fink

abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.