

MEMO# 35410

August 18, 2023

ICI Submission on Liquidity Fee-Related Tax Issues for Money Market Funds

[35410]

August 18, 2023

TO:
ICI Members
Investment Company Directors
Money Market Funds Advisory Committee
Tax Committee

SUBJECTS: Money Market Funds
Tax RE: ICI Submission on Liquidity Fee-Related Tax Issues for Money Market Funds

ICI has requested guidance, in the attached letter, from the Treasury Department and Internal Revenue Service (IRS) on two liquidity fee-related tax issues for money market funds (MMFs). These issues arise from the Securities and Exchange Commission's (SEC's) recently adopted [final rule](#) for MMFs.^[1] This SEC guidance provides rules for both mandatory and discretionary liquidity fees, effective October 2, 2023,^[2] for redemptions in stable net asset value (NAV) MMFs available to retail investors.

We first request an exemption from the wash sale rule for redemptions on which a liquidity fee is imposed. This request would allow the amount of the loss on the redemption (equal to the liquidity fee amount) to be taken into account immediately.

This guidance is necessary to prevent investors from experiencing tax reporting complexities that otherwise would arise. Specifically, without the requested exemption, an investor who incurs liquidity fees on a redemption and purchases shares (such as by dividend reinvestment) within 30 days before or after the redemption will have a wash sale. Under the wash sale rule, the loss (attributable to the liquidity fee) will be disallowed and instead added to the cost basis of the shares acquired. Thus, the cost basis of the acquired shares would exceed the stable NAV price; every subsequent redemption at the stable NAV price would result in a small capital loss. As MMFs today do not report gains and losses on MMF share redemptions, significant investor confusion could arise.

Second, we request guidance on various issues related to the treatment of liquidity fees received by a MMF. Specifically, we request that: (1) MMFs treat receipt of the liquidity fee as a non-taxable event; (2) shareholders treat the liquidity fee as a reduction of gross

proceeds; and (3) liquidity fees distributed by a fund (to avoid breaking the buck on the upside) be deemed to be taxable income to the extent that the distribution otherwise would be a return of capital. These requests all relate to the industry's objective of keeping consistent (e.g., at \$1.00) the stable NAV price and the cost basis of these shares.

Keith Lawson
Deputy General Counsel - Tax Law

Notes

[1] See, [ICI Memo #35375](#), dated July 13, 2023.

[2] Discretionary liquidity fees may be imposed by retail money funds after October 2, 2023; these funds are required to have a framework for implementing discretionary fees on April 2, 2024. The mandatory liquidity fee framework for institutional prime and institutional tax-exempt MMFs goes into effect on October 2, 2024.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.