

## Internal Revenue Service

## Department of the Treasury

Number: **200130014**

Release Date: 7/27/2001

Index Number: 4982.00-00

Washington, DC 20224

Person to Contact:

Telephone Number:

(202) 622-4122

Refer Reply To:

CC:FIP:1/PLR-111943-01

Date:

April 26, 2001

### Legend:

Fund A =

Fund B =

Fund C =

Fund D =

Trust =

Advisor =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Year 1 =

Year 2 =

Dear :

This is in response to a letter dated February 22, 2001, requesting rulings on behalf of Fund A, Fund B, Fund C, and Fund D (individually, a Fund). Each Fund seeks consent to revoke an election previously made under § 4982(e)(4)(A) of the Internal Revenue Code effective for the calendar year 2001 and subsequent years.

Additionally, each Fund requests that in calculating its required distributions under § 4982 for the year ending December 31, 2001, for purposes of §§ 4982(b)(1)(B), 4982(e)(2), 4982(e)(5) and 4982(e)(6), the capital gain net income, foreign currency gains and losses, and gains and losses recognized under § 1296 for each Fund be determined on the basis of capital gains and losses, foreign currency gains and losses, and gains and losses recognized under § 1296 during the ten-month period from January 1, 2001, through October 31, 2001.

## **FACTS**

Fund A is a State Business Trust formed on Date 1. Fund A is registered with the Securities and Exchange Commission as a diversified, open-end management investment company under the Investment Company Act of 1940, 15 U.S.C. § 80a-1, et seq. (the “1940 Act”). Fund B, Fund C, and Fund D are each a series of Trust, a State Business Trust formed on Date 2. Trust is registered with the Securities and Exchange Commission as a diversified, open-end management investment company under the 1940 Act. Advisor has been the investment manager of Fund A since Year 1 and Fund B, Fund C, and Fund D since Year 2.

Each Fund has qualified and elected to be treated as a regulated investment company (RIC) under subchapter M, part I, of Chapter 1 of the Code. Each Fund operates in a manner intended to continue to qualify it as a RIC, and the policy of each Fund is to distribute all or substantially all of its income so that each Fund and its shareholders will be taxed in accordance with § 852.

Each Fund is treated as a separate corporation for tax purposes under § 851(g). Each Fund uses the accrual method of accounting for tax and financial reporting purposes. Each Fund has historically had a tax year ending on December 31. In order to coordinate the income tax provisions applicable to a RIC and the provisions of § 4982, each Fund elected (on Form 8613) under § 4982(e)(4)(A) to use its tax year ending December 31, in lieu of the 1-year period ending on October 31, for purposes of calculating the required distribution amount under §§ 4982(b)(1)(B) and 4982(e)(2). Fund A first made an election pursuant to § 4982(e)(4)(A) for the calendar year ended Date 3. Fund B, Fund C, and Fund D first made an election pursuant to § 4982(e)(4)(A) for the calendar year ended Date 4.

At the time it originally made the election, each Fund believed that the election under § 4982(e)(4)(A) would relieve the administrative burden associated with dual calculations of capital and foreign currency gains and losses under the excise tax and subchapter M regimes. Each Fund’s experience, however, has been that the election has created additional administrative burdens and complexities, primarily due to increasingly strict market-driven time constraints in declaring required excise tax distributions. Each Fund must estimate its total net realized capital gains for the calendar year in order to declare its capital gain distributions in early December. These gains and losses cannot be predicted with any reasonable degree of accuracy. Therefore, each Fund may have to limit its trading activities involving capital gains and

losses. Such a situation can result in missed trading opportunities as dictated by market price fluctuations and may run contrary to each Fund's fiduciary responsibility to its shareholders. Further, the promulgation of Treasury regulations coordinating the excise tax and subchapter M rules has greatly reduced the administrative burden referred to above.

Each Fund represents that:

- (a) The desire to revoke its election is due to administrative and non-tax related financial burdens caused by the election;
- (b) It is not seeking to revoke its election in order to preserve or secure a tax benefit;
- (c) It will neither benefit through hindsight nor prejudice the interests of the government as a result of being permitted to revoke its election; and
- (d) It will not make a subsequent election under § 4982(e)(4) for at least five calendar years following the year of the grant of revocation.

## **LAW AND ANALYSIS**

Section 4982(a), which was enacted as part of the Tax Reform Act of 1986 and is effective for calendar years beginning after December 31, 1986, imposes an excise tax on every RIC for each calendar year equal to 4 percent of the excess (if any) of the "required distribution" for the calendar year over the "distributed amount" for the calendar year.

Section 4982(b)(1) defines "required distribution" to mean, with respect to any calendar year, the sum of 98 percent of the RIC's ordinary income for such calendar year, plus 98 percent of the RIC's capital gain net income for the 1-year period ending on October 31 of such calendar year.

Section 4982(e)(2)(A) provides that for purposes of § 4982, in general, the term "capital gain net income" has the meaning given to that term by § 1222(9), but determined by treating the 1-year period ending on October 31 of the calendar year as the RIC's tax year.

Section 4982(e)(2)(B) reduces the RIC's capital gain net income, but not below the RIC's net capital gain, by the amount of the RIC's net ordinary loss for the calendar year. Section 4982(e)(2)(C)(i) provides that, for purposes of § 4982, the term "net capital gain" has the meaning given that term by § 1222(11), but determined by treating the 1-year period ending on October 31 of the calendar year as the RIC's tax year.

Section 4982(e)(4)(A) provides that if the tax year of a RIC ends with the month of November or December, the RIC may elect to have the capital gain net income for its tax year applied in lieu of the 1-year period ending on October 31 of the calendar year for purposes of satisfying the required distribution defined under § 4982(b)(1). Section

4982(e)(4)(B) provides that, once made, such election may be revoked only with the consent of the Secretary.

Section 4982(e)(5) provides that any foreign currency gain or loss which is attributable to a § 988 transaction and which is properly taken into account for the portion of the calendar year after October 31 shall not be taken into account in determining the amount of the ordinary income of the RIC for such calendar year but shall be taken into account in determining the ordinary income of the RIC for the following calendar year. In the case of any RIC making an election under § 4982(e)(4), the preceding sentence shall be applied by substituting the last day of the RIC's taxable year for October 31.

Section 4982(e)(6)(A) provides that for purposes of determining a RIC's ordinary income, notwithstanding § 4982(e)(1)(C), § 1296 shall be applied as if the RIC's taxable year ended on October 31. Section 4982(e)(6)(B) provides that any ordinary gain or loss from an actual disposition of stock in a passive foreign investment company during the portion of the calendar year after October 31 shall be taken into account in determining the RIC's ordinary income for the following calendar year. However, if a RIC has made an election under § 4982(e)(4), the preceding two sentences shall be applied by substituting the last day of the RIC's taxable year for October 31.

Based on the information submitted and the representations made, we conclude that each Fund desires to revoke its election under § 4982(e)(4)(A) because of administrative burdens and not because of any federal tax-related financial burden caused by the election. Each Fund does not seek to revoke its election to preserve or secure a federal tax benefit. Additionally, each Fund will neither benefit through hindsight nor prejudice the interests of the government by being permitted to revoke the election.

## **CONCLUSIONS**

Accordingly, pursuant to § 4982(e)(4)(B), the Secretary consents to the revocation of the election made by each Fund under § 4982(e)(4)(A) effective for the calendar year 2001 and subsequent years. Additionally, in calculating each Fund's "required distribution" under § 4982 for the year ending December 31, 2001, for purposes of §§ 4982(b)(1)(B), 4982(e)(2), 4982(e)(5) and 4982(e)(6), the capital gain net income, foreign currency gains and losses, and gains and losses recognized under § 1296 for each Fund shall be determined on the basis of capital gains and losses, foreign currency gains and losses, and gains and losses recognized under § 1296 during the ten-month period from January 1, 2001, through October 31, 2001.

As a condition to the Secretary's consenting to the revocations pursuant to § 4982(e)(4)(B), each Fund may not make a subsequent election under § 4982(e)(4)(A) for a period of five calendar years following the year to which the grant of revocation applies, that is, the years 2002 through 2006.

Except as specifically ruled upon above, no opinion is expressed or implied as to the treatment of each Fund for federal excise or income tax purposes other than as

specified herein. In particular, no opinion is expressed concerning each Fund's qualification as a RIC.

This ruling is directed only to the taxpayers that requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

It is important that a copy of this letter be attached to the federal income and excise tax returns filed by each Fund for the first tax year to which this letter applies.

Sincerely,  
Acting Associate Chief Counsel  
(Financial Institutions & Products)  
By: Alvin J. Kraft  
Chief, Branch 1

Enclosures:  
Copy of this letter  
Copy for 6110 purposes