Internal Revenue Service

Department of the Treasury

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Person to Contact:

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LEGEND:

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Fund =

Year A =
Year B =
Year C =
Year D =

State =

This is in reply to a letter dated October 26, 1998, seeking consent to revoke, for Year A and subsequent calendar years, a previous election made by the Fund under § 4892(e)(4)(A) of the Internal Revenue Code of 1986, as amended (the "Code"). Additionally, the Fund requests that the calculation of its required distribution of capital gain net income under § 4982(e)(2) for the calendar year ending December 31, Year A, be determined on the basis of capital gains and losses realized and recognized during the ten-month period from January 1, Year A, through October 31, Year A.

FACTS

The Fund is organized as a State corporation and has elected to be treated as a business development company under the Investment Company Act of 1940, 15 U.S.C. § 80a-1 et seq. The Fund has elected and intends to continue to qualify for treatment as a regulated investment company ("RIC") under subchapter M of the Code.

The Fund uses the accrual method of accounting for tax and financial accounting purposes, and uses a calendar year end for tax purposes. For the tax years ending after December 31, Year B, the

Fund elected pursuant to § 4982(e)(4)(A) to use its tax year of 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).

The Fund's experience has been that the § 4982(e)(4)(A) election created additional administrative complexities primarily due to time constraints in declaring required excise tax distributions. The Fund has historically paid its dividends in additional shares of the Fund's common stock or in cash at the specific election of the shareholder. The use of a December 31 year-end requires the Fund to estimate capital gains through December 31. The Board of Directors declares dividends (based on estimated capital gains) by early December and sets a record date at least ten days after the declaration date. The Fund pays the dividend prior to January 31 pursuant to § 852(b)(7).

The Fund's transfer agent requires approximately 45 days between the record date and the pay date. This period is used to mail cash election forms to the shareholders and to calculate the number of shares to be issued, based on the number of shareholders electing to receive cash dividends. Because the record date typically occurs in mid-December, the payment date has historically occurred in January. The distribution in January of income of a prior year results in confusion for the shareholders of the fund, many of whom are cash basis taxpayers.

If the estimates used for the distribution of capital gains prove to be incorrect, the Fund may need to distribute additional funds that must be characterized as § 855 dividends to avoid disqualification of the Fund as a RIC. This additional distribution results in additional administrative complexity.

The promulgation of regulations coordinating the excise tax and subchapter M provisions has greatly reduced the administrative burden of having a tax year different from the period used for determining the required distributions under § 4982. Accordingly, the Fund seeks consent to revoke its election to use its taxable year (the calendar year) for purposes of sections 4982(b)(1)(B) and 4982(e)(2).

The Fund represents that:

1. The desire to revoke its § 4982(e)(4)(A) election is due to administrative and non-tax related financial burdens caused by the election.

2. It is not seeking to revoke its election for the purpose of preserving or securing a tax benefit.

3. It will neither benefit through hindsight nor prejudice the interests of the government as a result of being permitted to revoke its election.

4. It will not make a subsequent election under § 4982(e)(4)(A) for five calendar years following the year of the grant of revocation.

LAW and ANALYSIS

Section 4982(a) of the Code, which was enacted as part of the Tax Reform Act of 1986 and is effective for tax 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 the term "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 its capital gain net income for the 1-year period ending on October 31 of such calendar year.

Section 4982(b)(2) provides that the amount determined under § 4982(b)(1) for any calendar year shall be increased by the excess (if any) of the "grossed up required distribution for the preceding calendar year," over the distributed amount for such preceding year.

Section 4982(b)(3) defines "grossed up required distribution" for any calendar year to mean the required distribution for such year determined by applying § 4982(b)(2) to such year but substituting "100 percent" for each percentage set forth in § 4982(b)(1).

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 its 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 in § 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 section 988 transaction and which is properly taken into account for the portion of the calendar year after October 31 will not be taken into account in determining the amount of the ordinary income of the RIC for such calendar year but will be taken into account in determining the ordinary income of the RIC for the following calendar year. In the case of any company

making an election under section 4982(e)(4), the preceding sentence shall be applied by substituting the last day of the company's taxable year for October 31.

Based upon the information submitted and the representations made, we conclude that the Fund's desire to revoke its election under § 4982(e)(4)(A) of the Code is because of administrative burdens and not because of any federal tax-related financial burden caused by the election. The Fund does not seek to revoke its election for the purpose of preserving or securing a federal tax benefit. Additionally, the Fund will neither benefit through hindsight nor prejudice the interests of the government as a result of being permitted to revoke its election.

CONCLUSION

Accordingly, pursuant to § 4982(e)(4)(B), the Secretary consents to the revocation of the election made by the Fund under § 4982(e)(4)(A) effective for calendar Year A and subsequent years. In addition, in calculating the "required distribution" for calendar Year A, for purposes of § 4982(b)(1) and (2), the capital gain net income and foreign currency gains and losses of the Fund will be determined on the basis of the capital and foreign currency gains and losses taken into account during the 10-month period from January 1, Year A, through October 31, Year A.

As a condition to the Secretary's consent to the revocation pursuant to § 4982(e)(4)(B), the Fund may not make a subsequent election under § 4982(e)(4)(A) for a period of 5 calendar years following the year to which the grant of revocation applies, that is Year C through Year D.

Except as specifically ruled upon above, no opinion is expressed or implied as to the federal excise or income tax consequences regarding the Fund.

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

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

Sincerely,

Assistant Chief Counsel
(Financial Institutions and Products)

By: _____
Alice M. Bennett
Chief, Branch 3

enclosures: Copy of letter for § 6110 purposes