



All that's hot in the mutual fund industry

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## Tax Deferral Proposal Reaches Senate

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Legislation allowing mutual fund investors to defer income tax on reinvested capital gains got a boost last week, when the first Senate bill addressing the issue was introduced.

Proponents of the bill say they hope that despite budget crunches due to hurricane repairs, the new show of support will advance the proposal.

"Senate support is terrifically important," says Leslie Kramerich, a government affairs officer for retirement and tax policy with the Investment Company Institute. "It's great to have support in both bodies of Congress. There's a real possibility of this bill moving forward."

Kramerich says that although Congress has been paying close attention to disaster relief in the wake of mounting bills related to Hurricanes Katrina and Rita, the lawmakers also realize that they need to tackle retirement issues.

Although the bill isn't a magic bullet for everyone's retirement needs, she says, it's nonetheless significant because it encourages people to save who don't have access to employer-sponsored savings plans like 401(k)s. Kramerich says tens of millions of U.S. workers would benefit.

The bill, known as the Growth Act, was proposed by Senators Michael Crapo (R-Id.), Tim Johnson (D-S.D.) and Jim Bunning (R-Ky). It would level the playing field, tax-wise, between mutual funds and other investments like stocks and bonds by allowing shareholders to pay taxes on their holdings only when they sell, says Alison Aikele, a spokeswoman for Crapo.

Currently, investors in taxable mutual funds must pay yearly capital gains taxes on trades executed in the portfolio even if they sell no shares and simply reinvest capital gains distributions back into fund shares.

That extra tax burden turns many potential investors away from mutual funds, says Aikele. It also results in some investors' selling holdings each year to pay their tax bills.

With rising concerns about how the huge population of aging baby boomers will fund their golden years, a raft of proposals has been put forward to encourage greater savings. Many of them, including efforts to reform the Social Security system, have not gained enough traction to advance to the president's desk.

But observers say that Senate support of a capital gains deferral bill could add to the momentum that's been building in the House. During the past several sessions, Reps. Jim Saxton (R-N.J.) and Paul Ryan (R-Wis.) have each put forward separate bills addressing the issue. Ryan reintroduced his bill this past May. As of late last week, it had 37 co-sponsors.

"It really helps that Senator Crapo is on the Finance Committee," says **McGuinness & Holch** partner Niels Holch. "That means that he's in a position to move this legislation along when a tax bill comes around." Provided there's enough support, it's not unusual for bills to be combined when they pertain to a similar subject.

However, Holch also points out that now isn't a good time to introduce bills that impact Treasury income. With \$200 billion earmarked for New Orleans hurricane repairs, an expensive war in Iraq and other spending issues, he says, lawmakers aren't feeling overly generous on handing out tax breaks now.

"It's very difficult for a bill that defers revenue now," he says. "The leaders in Congress haven't pulled all the tax cut proposals off the table yet but they're facing increasing pressure to do so. Some of that will depend on what happens with Hurricane Rita over the next few days."

During each two-year legislative session, says Holch, some 10,000 bills are introduced but only about 300 pass.

On the other hand, he notes, introducing a tax deferral bill even in this environment is a way to stake out turf and establish interest in an issue. It's a common strategy, particularly in tax areas, to build support slowly, then argue for

inclusion in a broader tax bill when the time is right.

The ICI's Kramerich says the timing of the introduction is a further indication that lawmakers continue to be interested in helping Americans save for retirement.

The trade group is trying to encourage mutual fund shareholders as well as consumer groups to become more involved in retirement planning. To that end, says Ed Giltenan, head of ICI's media relations group, it is embarking on a broad public information campaign that includes an informational website, [fundingyourfuture.org](http://fundingyourfuture.org).<sup>1</sup> The site contains details on retirement plan rules, tips on saving and updates on legislative proposals.

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