

26 CFR § 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.

(Also: Part 1, § 1091)

Rev. Proc. 2014-45

SECTION 1. PURPOSE

This revenue procedure describes the circumstances in which the Internal Revenue Service (Service) will not treat a redemption of shares in a money market fund (MMF) as part of a wash sale for purposes of section 1091 of the Internal Revenue Code. This revenue procedure responds to Securities and Exchange Commission (SEC) rules that change how certain MMF shares are priced. See Money Market Fund Reform; Amendments to Form PF, Securities Act Release No. 33-9616, Investment Advisers Act Release No. IA-3879, Investment Company Act Release No. IC-31166, Financial Reporting Codification No. FR-84 (SEC MMF Reform Rules). As described in section 2.03 of this revenue procedure, the Service previously published Notice 2013-48, 2013-31 I.R.B. 120, proposing a revenue procedure that would have excepted from the wash

sale rules certain *de minimis* losses realized in redemptions of MMF shares. This revenue procedure includes revisions responding to comments received regarding that proposal.

SECTION 2. BACKGROUND

.01 Money Market Funds

(1) An MMF is a type of investment company registered under the Investment Company Act of 1940 (1940 Act) and regulated as an MMF under Rule 2a–7 under the 1940 Act (17 CFR §270.2a–7). Unlike other types of mutual funds, MMFs have historically sought to keep stable (typically at \$1.00) the prices at which their shares are distributed, redeemed, and repurchased.

(2) To hold itself out to investors as an MMF, an investment company must meet the requirements specified in Rule 2a–7, which, among other things, establishes limitations as to the maturity, quality, diversification, and liquidity of an MMF's investments. Generally, an MMF must hold a diversified portfolio of short-term, low-risk, liquid securities. The securities that an MMF holds generally result in no more than minimal fluctuations in the MMF's net asset value per share (NAV).

(3) Until the SEC MMF Reform Rules change how certain MMFs price their shares, Rule 2a–7 permits any MMF meeting the other requirements of Rule 2a–7 to compute its price per share for purposes of distribution, redemption, and repurchase by using either or both of (a) the amortized cost method of valuation, and (b) the penny-rounding method of pricing. Under the amortized cost method, an MMF's NAV is determined by valuing the fund's portfolio securities at their acquisition cost, adjusted for amortization

of premium or accretion of discount. Under the penny-rounding method, an MMF's NAV is rounded to the nearest one percent in computing the price per share for purposes of distribution, redemption, and repurchase. These methods have enabled MMFs to maintain constant share prices except in situations in which the "deviation [of the current net asset value per share calculated using available market quotations] from the money market fund's amortized cost price per share exceeds ½ of 1 percent" (commonly called "breaking the buck"). 17 CFR §270.2a-7(c)(8)(ii)(B).

(4) The perceived safety and simplicity of MMFs have led to their widespread use for cash management purposes. It is therefore common for investors to purchase and redeem MMF shares frequently. An MMF is often used as an account into which, or from which, cash is automatically deposited, or withdrawn, on a daily basis (commonly referred to as a sweep arrangement). MMFs generally declare dividends daily and distribute them monthly. MMF shareholders typically reinvest these distributions automatically in the MMF.

(5) In June 2013, the SEC proposed rules that would change how certain MMF shares are priced. See Money Market Fund Reform; Amendments to Form PF, Securities Act Release No. 33-9408, Investment Advisors Act Release No. IA-3616, Investment Company Act Release No. IC-30551, 78 FR 36834 (June 19, 2013) (SEC MMF Reform Proposal). The SEC MMF Reform Rules adopt the general approach of the SEC MMF Reform Proposal, but include various modifications in response to

comments and combine the two principal reform alternatives.¹ The SEC MMF Reform Rules generally bar the use of the amortized cost method of valuation and the use of the penny-rounding method of pricing, except by government MMFs and retail MMFs.² In the case of an MMF that is neither a government MMF nor a retail MMF, the SEC MMF Reform Rules require the MMF to value its portfolio securities using market-based factors and to “compute its price per share for purposes of distribution, redemption and repurchase by rounding the fund’s current net asset value per share to a minimum of the fourth decimal place in the case of a fund with a \$1.0000 share price or an equivalent or more precise level of accuracy for money market funds with a different share price (e.g. \$10.000 per share, or \$100.00 per share).” *Id.* §270.2a–7(c)(1)(ii). (This method of computing the price per share is referred to hereafter as “basis point rounding.”)³

(6) An MMF that uses market factors to value its securities and uses basis point rounding to price its shares for purposes of distribution, redemption, and repurchase (floating-NAV MMF) has a share price that is expected to change regularly, or “float.” Floating-NAV MMFs therefore resemble in some respects other mutual funds that are

¹ These alternatives were Floating Net Asset Value and Standby Liquidity Fees and Gates. See SEC MMF Reform Proposal at 36849 and 36878. The proposal included a number of other possibilities, including a combination of these two.

² A government MMF is an MMF that “invests 99.5 percent or more of its total assets in cash, government securities, and/or repurchase agreements that are collateralized fully.” SEC MMF Reform Rules, §270.2a–7(a)(16). A retail MMF is an MMF that “has policies and procedures reasonably designed to limit all beneficial owners of the fund to natural persons.” *Id.* §270.2a–7(a)(25).

³ The SEC has also amended Rule 2a–7 to require every MMF to disclose daily the fund’s current NAV rounded to the nearest basis point, but government and retail MMFs are not required to use basis point rounding to distribute, redeem, and repurchase shares.

not MMFs, but they remain subject to the risk-limiting conditions in Rule 2a-7 and are expected to continue to fulfill MMFs' unique role.

(7) Stable share prices simplify the taxation of transactions in MMF shares because a shareholder does not realize gain or loss when a share is redeemed for an amount equal to its basis. Shareholders typically will realize gain or loss, however, on redemptions of floating-NAV MMF shares. In certain circumstances, a loss realized on the redemption of an MMF share may implicate the wash sale rules of section 1091, as discussed in section 2.02 of this revenue procedure.

(8) The Treasury Department and the Service have proposed regulations to simplify the recognition of gain or loss on floating-NAV MMF shares. Shareholders of floating-NAV MMFs may rely on the proposed regulations before final regulations are issued. See §1.446-7 of the proposed Income Tax Regulations. Under the permissible method of accounting described in those proposed regulations, aggregate gain or loss is determined for each computation period, and no gain or loss is determined for any particular redemption of a taxpayer's shares in a floating-NAV MMF. Without a determination of loss, a particular redemption does not implicate the wash sale rules. If a shareholder of a floating-NAV MMF, however, does not use this method of accounting, then that shareholder will typically experience frequent wash sales. This revenue procedure provides relief for such a shareholder.

(9) Sections 6045, 6045A, and 6045B establish certain reporting requirements relating to securities. Each of those sections has an exception for an MMF (or shares in an MMF) that "computes its current price per share for purposes of distributions,

redemptions, and purchases so as to stabilize the price per share at a constant amount that approximates its issue price or the price at which it was originally sold to the public.” §§1.6045-1(c)(3)(vi), 1.6045A-1(a)(1)(v), and 1.6045B-1(a)(5) of the Income Tax Regulations. The Treasury Department and the Service have proposed regulations to clarify that these exceptions apply to all MMFs, including floating-NAV MMFs. See §1.6045-1(c)(3)(vi) of the proposed Income Tax Regulations.

.02 Wash Sale Rules

(1) Section 1091(a) disallows a loss realized by a taxpayer on a sale or other disposition of shares of stock or securities if, within a period beginning 30 days before and ending 30 days after the date of such sale or disposition, the taxpayer acquires (by purchase or by an exchange on which the entire amount of gain or loss is recognized by law), or enters into a contract or option to so acquire, substantially identical stock or securities (unless the taxpayer is a dealer in stock or securities and the loss is sustained in a transaction made in the ordinary course of such business).

(2) If a taxpayer acquired property and that acquisition resulted in the nondeductibility of a loss under section 1091(a), then under section 1091(d), the taxpayer's basis in the property so acquired equals the basis of the stock or securities disposed of at a loss, increased or decreased to take into account any difference between the price at which the replacement property was acquired and the price at which the original stock or securities were disposed of.

(3) A shareholder that redeems shares in a floating-NAV MMF may realize a loss on the redemption. Moreover, because many MMF shareholders engage in frequent

purchases of MMF shares (including purchases made as a result of sweep arrangements and reinvestments of monthly distributions), a shareholder that realizes a loss on a redemption of MMF shares will often acquire shares in that MMF within 30 days before or after the redemption.

(4) Redemptions of shares of MMFs, which are expected to have relatively stable values even when share prices float, do not give rise to the concern that section 1091 is meant to address. Moreover, given the expected volume of transactions in floating-NAV MMF shares, tracking wash sales of MMF shares will present shareholders of floating-NAV MMFs with significant practical challenges.

.03 Notice 2013-48

(1) The Service published Notice 2013-48 on July 29, 2013, in response to the SEC MMF Reform Proposal. The notice proposed a revenue procedure providing that the Service would not treat a loss realized upon a redemption of a floating-NAV MMF share as subject to the wash sale rules if the amount of the loss was not more than one half of one percent of the taxpayer's basis in that share.

(2) The Service received comments indicating that the proposed revenue procedure would not significantly reduce the tax compliance burdens associated with applying the wash sale rules to floating-NAV MMFs, because shareholders would still have to track wash sales to determine whether the amount of the wash sale exceeds the 0.5% *de minimis* test. The commenters suggested that MMFs are not the type of investment with which the wash sale rules are concerned because investors do not

have any expectation of capital appreciation. As a result, the commenters requested that floating-NAV MMFs be exempted entirely from the wash sale rules in section 1091.

(3) Because of the expectation that values of floating-NAV MMFs will be relatively stable and because of the administrative burdens associated with applying section 1091 to shares in floating-NAV MMFs, it is in the interest of sound tax administration for the Service not to treat a redemption of a floating-NAV MMF share as part of a wash sale under section 1091.

SECTION 3. SCOPE

This revenue procedure applies to a redemption of one or more shares in an investment company registered under the 1940 Act if—

.01 The investment company is regulated as an MMF under Rule 2a–7 and holds itself out to investors as an MMF; and

.02 At the time of the redemption, the investment company is a floating-NAV MMF.

SECTION 4. APPLICATION

If a redemption is within the scope of section 3 of this revenue procedure and results in a loss, the Service will not treat the redemption as part of a wash sale. Therefore, section 1091(a) will not disallow the deduction for the resulting loss in the year realized and section 1091(d) will not cause the basis of any property to be determined by reference to the basis of the redeemed shares.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for redemptions on or after the effective date of the SEC MMF Reform Rules (which is expected to be 60 days after the date that they are published in the Federal Register).

SECTION 6. DRAFTING INFORMATION

The principal author of this revenue procedure is Jason Kurth of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue procedure contact Mr. Kurth at (202) 317-6842 (not a toll free call).