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MAINTENANCE OF COMMON TRUST FUND BY AFFILIATED BANKS

AUGUST 27, 1976.—Ordered to be printed

Mr. LONG, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 5071]

The Committee on Finance, to which was referred the bill (H.R. 5071) to amend section 584 of the Internal Revenue Code of 1954 with respect to the treatment of affiliated banks for purposes of the common trust fund provisions of such Code, having considered the same, reports favorably thereon without amendment, and recommends that the bill do pass.

I. SUMMARY

H.R. 5071 modifies the rules relating to the maintenance of common trust funds by banks. Under present law a bank may maintain a common trust fund (the income of which is taxed to the participants rather than it being taxed as a corporation) for the collective investment and reinvestment of moneys transferred to the bank in its fiduciary capacity. The Internal Revenue Service has taken the position that a fund which accepts contributions from other banks acting in a fiduciary capacity (even though the banks are affiliated) will not qualify as a common trust fund. This bill provides that where banks which are members of the same affiliated group establish a combined common trust fund, this fund is to be treated as a "common trust fund" for tax purposes during the period of the affiliation.

II. GENERAL STATEMENT

Under existing law a bank may maintain a "common trust fund" which fund itself is neither subject to Federal income taxation nor considered a corporation. A fund qualifies as a common trust fund if it is (1) maintained by a bank exclusively for the collective investment and reinvestment of moneys contributed by the bank in its fiduciary

capacity, and (2) maintained in conformity with rules and regulations of the Comptroller of the Currency pertaining to the collective investment of trusts. The income (including gains and losses from the sale of property) from the fund, representing amounts contributed from various separate trusts, is included in the gross income of each participant in the common fund on the basis of its proportionate share of the income.

The purpose of the common trust fund provision is to permit diversification in the investment of trust funds for which a bank has fiduciary responsibility.

The Internal Revenue Service has taken the position (Rev. Rul. 70–302) that a fund maintained by a member bank of a bank holding company will not qualify as a "common trust fund" if it accepts contributions to the fund by other member banks (or trust companies) acting in a fiduciary capacity. The Internal Revenue Service holds that under present law the common trust fund must be "maintained" by the bank which contributes the moneys to the fund for investment. The committee also understands that the Internal Revenue Service holds that a fund maintained by various members of a bank holding company will not qualify even if each member bank acts as a co-trustee of the common fund.

The committee believes that the tax treatment accorded a common fund by banks which are related through stockholdership with a common parent should be the same as where only one bank is involved because the State where it is located permits branch banking. The committee sees no substantive reason for a difference in tax treatment in these cases and no reason why the pooling of the trust funds for investment purposes should not be permitted. It is the committee's understanding that the Comptroller of the Currency supports this bill and will encounter no additional difficulty in regulating and administering common trust funds maintained by affiliated banks.

Accordingly, the bill amends the provision dealing with common trust funds (sec. 584) to provide that when banks become members of the same affiliated group (within the meaning of sec. 1504) they are, for purposes of this provision, to be treated as one bank for the period of their affiliation. Consequently, if banks are affiliated (as defined in sec. 1504) they may contribute funds held in their capacity as trustee, executor, administrator or guardian to a common trust fund.

It is not necessary under the bill that banks contributing money to the fund act as cotrustees of the common trust fund. The affiliated group of banks may maintain a common trust fund if any member of the group serves as trustee. (Of course, one or more members of the affiliated group may serve as cotrustees, but this is not required.) If a common trust fund in which several affiliated banks participate is later divided because of termination of the affiliation, in those cases where there is not the effect of a sale or exchange or withdrawal, it is intended that the tax consequences of the division be governed by rules similar to those applied under existing rulings relating to the division of common trust funds maintained by a single bank.[1]

The bill applies to taxable years beginning after December 31, 1975.

[1] See Rev. Rul. 68–77, 1968–1 C.B. 289; Rev. Rul. 70–322, 1970–1 C.B. 141.

III. Cost of Carrying Out the Bill and Committee Vote

In compliance with section 252(a) of the Legislative Reorganization Act of 1970, the following statement is made relative to the effect on the revenues of this bill. The enactment of H.R. 5071 will have no effect, or at most a negligible effect, on revenues. The Treasury Department agrees with this statement.

In compliance with section 133 of the Legislative Reorganization Act of 1946, the following statement is made relative to the vote of the Committee on reporting this bill. This bill was ordered favorably reported by the Committee by voice vote.

IV. Changes in Existing Law Made by the Law

In compliance with paragraph 4 of rule XXIX of the Rules of the Senate, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

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SEC. 584. COMMON TRUST FUNDS.

(a) Definitions.—For purposes of this subtitle, the term "common trust fund" means a fund maintained by a bank—

(1) exclusively for the collective investment and reinvestment of moneys contributed thereto by the bank in its capacity as a trustee, executor, administrator, or guardian; and

(2) in conformity with the rules and regulations, prevailing from time to time, of the Board of Governors of the Federal Reserve System or the Comptroller of the Currency pertaining to the collective investment of trust funds by national banks.

For purposes of this subsection, two or more banks which are members of the same affiliated group (within the meaning of section 1504) shall be treated as one bank for the period of affiliation with respect to any fund of which any of the member banks is trustee or two or more of the member banks are co-trustees.

(b) Taxation of Common Trust Funds.—A common trust fund shall not be subject to taxation under this chapter and for purposes of this chapter shall not be considered a corporation.

(c) Income of Participants in Fund.—

(1) Inclusions in taxable income.—Each participant in the common trust fund in computing its taxable income shall include, whether or not distributed and whether or not distributable—

(A) as part of its gains and losses from sales or exchanges of capital assets held for not more than 6 months, its proportionate share of the gains and losses of the common trust fund from sales or exchanges of capital assets held for not more than 6 months;

(B) as part of its gains and losses from sales or exchanges of capital assets held for more than 6 months, its proportionate share of the gains and losses of the common trust fund

from sales or exchanges of capital assets held for more than 6 months;

(C) its proportionate share of the ordinary taxable income or the ordinary net loss of the common trust fund, computed as provided in subsection (d).

(2) DIVIDENDS AND PARTIALLY TAX EXEMPT INTEREST.—The proportionate share of each participant in the amount of dividends to which section 116 applies, and in the amount of partially tax exempt interest on obligations described in section 35 or section 242, received by the common trust fund shall be considered for purposes of such sections as having been received by such participant. If the common trust fund elects under section 171 (relating to amortizable bond premium) to amortize the premium on such obligations, for purposes of the preceding sentence the proportionate share of the participant of such interest received by the common trust fund shall be his proportionate share of such interest (determined without regard to this sentence) reduced by so much of the deduction under section 171 as is attributable to such share.

(d) COMPUTATION OF COMMON TRUST FUND INCOME.—The taxable income of a common trust fund shall be computed in the same manner and on the same basis as in the case of an individual, except that—

(1) there shall be segregated the gains and losses from sales or exchanges of capital assets;

(2) after excluding all items of gain and loss from sales or exchanges of capital assets, there shall be computed—

(A) an ordinary taxable income which shall consist of the excess of the gross income over deductions; or

(B) an ordinary net loss which shall consist of the excess of the deductions over the gross income;

(3) the deduction provided by section 170 (relating to charitable, etc., contributions and gifts) shall not be allowed; and

(4) the standard deduction provided in section 141 shall not be allowed.

(e) ADMISSION AND WITHDRAWAL.—No gain or loss shall be realized by the common trust fund by the admission or withdrawal of a participant. The withdrawal of any participating interest by a participant shall be treated as a sale or exchange of such interest by the participant.

(f) DIFFERENT TAXABLE YEARS OF COMMON TRUST FUND AND PARTICIPANT.—If the taxable year of the common trust fund is different from that of a participant, the inclusions with respect to the taxable income of the common trust fund, in computing the taxable income of the participant for its taxable year, shall be based upon the taxable income of the common trust fund for any taxable year of the common trust fund ending within or with the taxable year of the participant.

(g) NET OPERATING LOSS DEDUCTION.—The benefit of the deduction for net operating losses provided by section 172 shall not be allowed to a common trust fund, but shall be allowed to the participants in the common trust fund, under regulations prescribed by the Secretary or his delegate.

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