DIGITAL ASSETS

Amending the Good Income and Asset Test for Regulated Investment Companies

Background

Current law significantly limits how regulated investment companies (RICs) can invest in digital assets. Under the Internal Revenue Code, RICs must derive at least 90% of their gross income from specific enumerated sources, including dividends or interest (§851(b)(2)). This is called the "good income" or "qualifying income" test. RICs must also meet an "asset" test that is aimed to limit the concentration of assets in a single issuer or class of assets. Funds that fail to satisfy either test will not qualify as a RIC and will be subject to corporate tax.

Retail investors want access to this asset class, along with the fiduciary and regulatory protections provided by RICs. Legislation is needed to permit RICs to invest directly in these assets, by modifying the "good income" and "asset" tests in Section 851(b) of the Internal Revenue Code. A legislative update to the tax code would allow retail investors greater access to digital assets and promote US leadership in digital assets.

ICI encourages Congress to enact legislative changes that would modernize the taxation of digital assets and expand investor access to digital assets in regulated funds.

Proposal

Amend the good income and asset tests to define income and gains from digital assets (such as virtual currencies, including stablecoins, and tokenized securities) as good income and as a qualifying asset, including:

- income and gain (including staking rewards) from digital assets held directly by the funds; and
- indirect investments in digital assets including derivatives on/referencing digital assets, and interests in grantor trusts and partnerships holding digital assets.

By modernizing the tax code to enable RICs to invest in digital assets, Congress can empower more investors to participate in digital assets with the safeguards and oversight that regulated funds are designed to offer.

Other Digital Tax Issues

ICI also welcomes legislation establishing clear tax guidelines for digital asset staking:

- Determining if staking qualifies as a "power to vary" investment in a grantor trust, or a "trade or business" activity that gives rise to unrelated business taxable income (UBTI) or effectively connected income (ECI).
- Establishing the tax character, timing, and source rules for income from staking rewards.