117TH CONGRESS
1ST SESSION

S. _____

To amend the Internal Revenue Code of 1986 to revise the treatment of partnership interests received in connection with the performance of services, and for other purposes.

IN THE SENATE OF THE UNITED STATES

_____

_____ introduced the following bill; which was read twice and referred to the Committee on _____

A BILL

To amend the Internal Revenue Code of 1986 to revise the treatment of partnership interests received in connection with the performance of services, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the ''Ending the Carried Interest Loophole Act''.

SEC. 2. PARTNERSHIP INTERESTS TRANSFERRED IN CONNECTION WITH PERFORMANCE OF SERVICES.

(a) MODIFICATION OF ELECTION TO INCLUDE PARTNERSHIP INTEREST IN GROSS INCOME IN YEAR OF TRANSFER.—Subsection (c) of section 83 is amended by redesignating paragraph (4) as paragraph (5) and by inserting after paragraph (3) the following new paragraph:

"(4) PARTNERSHIP INTERESTS.—Except as provided by the Secretary—

"(A) IN GENERAL.—In the case of any transfer of an interest in a partnership in connection with the performance of services—

"(i) the fair market value of such interest shall be treated for purposes of this section as being equal to the amount which the partner would receive if the partnership sold (at the time of the transfer) all of its assets for cash at their fair market value in a fully taxable transaction and distributed the proceeds of such sale (reduced by the liabilities of the partnership) to its partners in complete liquidation, and

"(ii) the person receiving such interest shall be treated as having made the election under subsection (b)(1) unless such

person makes an election under this paragraph to have such subsection not apply.

''(B) COORDINATION WITH OTHER PARTNERSHIP RULES.—Except as otherwise provided by the Secretary, if, by reason of subparagraph (A), subsection (b)(1) applies to a partnership interest transferred to a person, then the amount included in the gross income of such person by reason of such subsection shall (at the time of the transfer)—

''(i) be treated as an addition to the capital account of such person with respect to such partnership for purposes of subchapter K, and

''(ii) if such interest is an applicable partnership interest under section 1299 at any time, be treated as invested capital of such person with respect to such interest for purposes of such section.

''(C) ELECTION.—The election under subparagraph (A)(ii) shall be made under rules similar to the rules of subsection (b)(2).

''(D) PARTNERSHIP INTEREST.—

''(i) IN GENERAL.—For purposes of this paragraph, any applicable financial in-

strument or contract (as defined in section 1299(b)(2)(B)) or interest in an entity other than a partnership which is treated as an applicable partnership interest under section 1299(b)(2) shall be treated as an interest in a partnership.

''(ii) REGULATIONS.—The Secretary shall prescribe such regulations or other guidance as the Secretary determines necessary or appropriate to carry out this paragraph, including regulations for the application of this paragraph to applicable financial instruments or contracts (as so defined) or interests in entities other than partnerships which are treated as partnership interests under clause (i).''.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to interests in partnerships transferred after the date of the enactment of this Act.

SEC. 3. TREATMENT OF CERTAIN PARTNERSHIP INTERESTS RECEIVED IN CONNECTION WITH PERFORMANCE OF SERVICES.

(a) IN GENERAL.—Subchapter P of chapter 1 of the Internal Revenue Code of 1986 is amended by adding at the end the following new part:

"PART VII—TREATMENT OF CERTAIN PARTNERSHIP INTERESTS RECEIVED IN CONNECTION WITH PERFORMANCE OF SERVICES

"Sec. 1299. Treatment of certain partnership interests received in connection with performance of services.

"SEC. 1299. TREATMENT OF CERTAIN PARTNERSHIP INTERESTS RECEIVED IN CONNECTION WITH PERFORMANCE OF SERVICES.

"(a) IN GENERAL.—In the case of a taxpayer who holds 1 or more applicable partnership interests in any partnership at any time during any taxable year of the partnership ending with or within the taxable year of the taxpayer—

"(1) there shall be included in the gross income of the taxpayer as ordinary income an amount equal to the aggregate of the deemed compensation amounts determined under subsection (c) with respect to such interests in all partnerships, and

"(2) the taxpayer shall be treated as having for such taxable year of the taxpayer a long-term capital loss equal to the aggregate of such deemed compensation amounts.

"(b) APPLICABLE PARTNERSHIP INTEREST.—For purposes of this section—

''(1) IN GENERAL.—Except as provided in this subsection, the term 'applicable partnership interest' means any interest in a partnership which—

''(A) is directly or indirectly transferred to (or held by) the taxpayer in connection with the performance of services by the taxpayer, or any other person, in any applicable trade or business, or

''(B) is held by a taxpayer who received an applicable loan.

Such term shall not include any interest which is acquired pursuant to a sale or disposition to which subsection (c)(5) applies.

''(2) DETERMINATION OF INTEREST IN A PARTNERSHIP.—

''(A) IN GENERAL.—For purposes of paragraph (1), the term 'interest in a partnership' includes—

''(i) any applicable financial instrument or contract, or

''(ii) to the extent provided by the Secretary, any interest in an entity other than a partnership if such interest would be treated as an applicable partnership interest if such entity were a partnership.

''(B) APPLICABLE FINANCIAL INSTRUMENT OR CONTRACT.—For purposes of this paragraph—

''(i) IN GENERAL.—The term 'applicable financial instrument or contract' means any financial instrument or contract the value of which is determined in whole or in part by reference to any partnership or partnership-related item (including the amount of partnership distributions, the value of partnership assets, or the results of partnership operations).

''(ii) EXCEPTION FOR NON-CONVERTIBLE DEBT.—Such term shall not include a financial instrument or contract if such instrument or contract—

''(I) is treated as debt for Federal tax purposes, and

''(II) is not convertible into or exchangeable for any partnership interest and does not provide for a payment of similar or equivalent value.

''(3) APPLICABLE TRADE OR BUSINESS.—

''(A) IN GENERAL.—For purposes of paragraph (1)(A), the term 'applicable trade or

business' means any activity conducted on a regular, continuous, and substantial basis which, regardless of whether the activity is conducted in one or more entities, consists, in whole or in part, of—

"(i) raising or returning capital, and

"(ii) either—

"(I) investing in (including acquiring or disposing of) specified assets (or identifying specified assets for such investing, acquisition, or disposition), or

"(II) developing specified assets.

"(B) SPECIFIED ASSETS.—

"(i) IN GENERAL.—The term 'specified assets' means securities, commodities, real estate held for rental or investment, cash or cash equivalents, options or derivative contracts with respect to any of the foregoing, and an interest in a partnership if such partnership has a direct or indirect interest in any of the foregoing.

"(ii) SECURITIES.—For purposes of clause (i), the term 'securities' has the

meaning given such term under section 475(c)(2), determined—

''(I) by applying subparagraph (B) thereof without regard to whether the partnership or trust is widely held or publicly traded, and

''(II) without regard to the last sentence thereof.

''(iii) COMMODITIES.—For purposes of clause (i), the term 'commodities' has the meaning given such term under section 475(e)(2), except that such term shall not include commodities held in connection with the active conduct of a commodities business as a producer, processor, merchant, or handler of commodities.

''(4) APPLICABLE LOAN.—

''(A) IN GENERAL.—The term 'applicable loan' means, with respect to any partnership interest, any loan issued directly or indirectly from the partnership, any other partner of the partnership, or any person related to such other partner or such partnership.

''(B) SAFE HARBOR.—The term 'applicable loan' does not include any loan which—

''(i) is fully recourse to the borrower or fully secured by the borrower's assets, and

''(ii) requires payments of interest with a stated rate not less than the specified rate determined under subsection (c)(2).

''(c) DEEMED COMPENSATION AMOUNT.—For purposes of this section—

''(1) DEEMED COMPENSATION AMOUNT.—

''(A) IN GENERAL.—The term 'deemed compensation amount' means, with respect to any applicable partnership interest for any partnership taxable year, an amount equal to the product of—

''(i) the specified rate determined under paragraph (2) for the calendar year in which such taxable year begins, multiplied by

''(ii) the excess (if any) of—

''(I) an amount equal to the applicable percentage of the weighted average of the aggregate of invested capital of all partners of the partner-

ship on each measurement date occurring within such taxable year, over

"(II) the weighted average of invested capital with respect to the applicable partnership interest on each measurement date occurring within such taxable year.

"(B) MEASUREMENT DATE.—For purposes of subparagraph (A), the term 'measurement date' means—

"(i) the last day of the partnership taxable year,

"(ii) any date specified in the regulations under subchapter K as a date on which to revalue property of the partnership for purposes of adjusting capital accounts of the partner (without regard to whether the partnership capital accounts are adjusted on that date), and

"(iii) any other date specified by the Secretary.

"(2) SPECIFIED RATE.—The term 'specified rate' means, with respect to any calendar year, a percentage equal to the sum of—

"(A) the first segment rate (as defined in section 430(h)(2)(C)(i)) for the first month of such calendar year, plus

"(B) 9 percentage points.

"(3) APPLICABLE PERCENTAGE.—

"(A) IN GENERAL.—The term 'applicable percentage' means, with respect to any applicable partnership interest, the highest percentage of profits of the partnership which could be allocated to such interest (consistent with the partnership agreement and determined as if all performance targets with respect to such interest had been met).

"(B) SECRETARIAL AUTHORITY.—The Secretary shall prescribe rules for the determination of the applicable percentage in cases in which the percentage of profits of a partnership which may be allocated to the applicable partnership interest under the partnership agreement may temporarily exceed the highest percentage determined under subparagraph (A).

"(4) INVESTED CAPITAL.—

"(A) IN GENERAL.—The term 'invested capital' means, with respect to any partner as of any day, the excess of—

''(i) the sum of—

''(I) the total cumulative value, determined at the time of contribution, of all money or other property contributed by the partner to the partnership on or before such day (net of any liabilities the partnership is considered to assume or take subject to), plus

''(II) the aggregate amounts of the partner's distributive share of income and gain as of such day, over

''(ii) the sum of—

''(I) the aggregate value, determined at the time of distribution, of all money or other property distributed to the partner from the partnership on or before such day (net of any liabilities the partner is considered to assume or take subject to), plus

''(II) the aggregate amount of the partner's distributive share of loss and deductions of the partnership as of such day.

''(B) SPECIAL RULES.—

"(i) IN GENERAL.—For purposes of subparagraph (A), invested capital shall be determined—

"(I) without regard to amounts considered as a contribution of money or as a distribution of money by reason of subsection (a) or (B) of section 752, and

"(II) without regard to income required to be recognized by a contributing partner under section 704(c) with respect to property described in subparagraph (A)(i)(I).

"(ii) ADJUSTMENTS.—The Secretary may provide for rules making such adjustments as the Secretary determines necessary to the determination of invested capital under subparagraph (A) in order to carry out the purposes of this section.

"(C) TREATMENT OF BORROWINGS FROM PARTNERSHIPS OR OTHER PARTNERS.—For purposes of paragraph (1)(A), the amount of invested capital with respect to any applicable partnership interest shall be reduced by the

amount of any applicable loan to a partner who is described in subsection (b)(1)(B).

''(5) ACCELERATED INCLUSION IN CASE OF DISPOSITION OF APPLICABLE PARTNERSHIP INTEREST.—

''(A) IN GENERAL.—If a taxpayer who holds an applicable partnership interest sells or disposes of any portion of such interest during a taxable year in the applicable period, the amount determined under this subsection for such taxable year shall be the sum of—

''(i) the amount determined under paragraph (1) for the taxable year (determined as if no such sale or disposition had occurred), plus

''(ii) an amount equal to the product of—

''(I) the excess of the amount determined under clause (i) over the amount determined under paragraph (1) for the taxable year, and

''(II) the number of taxable years beginning after the date of the sale or disposition and before the last day of the applicable period.

"(B) APPLICABLE PERIOD.—For purposes of this paragraph, the applicable period is the 10-year period beginning on the later of—

"(i) the date the taxpayer acquired the applicable partnership interest, or

"(ii) the last date described in paragraph (1)(B)(ii) on which there was an increase in the amount of the taxpayers applicable percentage of the aggregate invested capital of all partners of the partnership.

"(6) MULTIPLE INTERESTS.—If at any time during a taxable year a taxpayer holds directly or indirectly more than 1 applicable partnership interest in a single partnership, such interests shall be treated as 1 applicable partnership interest for purposes of applying this subsection.

"(d) RELATED PERSON.—For purposes of this section, a person shall be treated as related to another person if the relationship between such persons would be described in section 267(b) or 707(b).

"(e) REPORTING.—A partnership shall report to the Secretary, and include with the information required to be furnished under section 6031(b) to each partner, the amount of the partner's deemed compensation amount for

the taxable year, if any. A similar rule applies to any entity that receives a report of a deemed compensation amount for the taxable year.

''(f) REGULATIONS.—The Secretary shall issue such regulations or other guidance as necessary to carry out this section, including regulations—

''(1) to prevent the abuse of the purposes of this section, including through—

''(A) the allocation of income to tax indifferent parties, or

''(B) a reduction or increase in the invested capital of any partner (including attempts to undervalue or overvalue property),

''(2) which provide for the application of the rules of subsection (c) to applicable financial instruments and contracts and to entities other than partnerships,

''(3) which provide in appropriate circumstances for purposes of this section the aggregation of assets held by related partnerships or for the disaggregation of assets within 1 partnership,

''(4) which provide for the application of this section in cases of tiered structures or entities,

''(5) which provide guidance with respect to forgiveness of any loan described in subsection (b)(4)(B), and

''(6) which provide rules for transfers or liquidations of applicable partnership interests by gift, inheritance, substituted basis transactions, and other transactions in which income is not recognized at the time of the transaction.''.

(b) CONFORMING AMENDMENTS.—

(1)(A) Part IV of subchapter O of chapter 1 of the Internal Revenue Code of 1986 is amended by striking section 1061.

(B) The table of sections for part IV of subchapter O of chapter 1 of such Code is amended by striking the item relating to section 1061.

(2) The table of parts for subchapter P of such Code is amended by adding at the end the following new item:

''PART VII—TREATMENT OF CERTAIN PARTNERSHIP INTERESTS RECEIVED IN CONNECTION WITH PERFORMANCE OF SERVICES''.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years of a taxpayer beginning after date of enactment of this Act, with or within which ends the taxable year of a partnership which begins after such date.