

**AMENDMENT TO H.R. 3630**

**OFFERED BY MS. JACKSON LEE OF TEXAS**

Page 364, after line 4, insert the following:

1 **Subtitle G—Tax Carried Interest in**  
2 **Investment Partnerships as Or-**  
3 **dinary Income**

4 **SEC. 5601. PARTNERSHIP INTERESTS TRANSFERRED IN**  
5 **CONNECTION WITH PERFORMANCE OF SERV-**  
6 **ICES.**

7 (a) MODIFICATION TO ELECTION TO INCLUDE PART-  
8 NERSHIP INTEREST IN GROSS INCOME IN YEAR OF  
9 TRANSFER.—Subsection (c) of section 83 of the Internal  
10 Revenue Code of 1986 is amended by redesignating para-  
11 graph (4) as paragraph (5) and by inserting after para-  
12 graph (3) the following new paragraph:

13 “(4) PARTNERSHIP INTERESTS.—Except as  
14 provided by the Secretary—

15 “(A) IN GENERAL.—In the case of any  
16 transfer of an interest in a partnership in con-  
17 nection with the provision of services to (or for  
18 the benefit of) such partnership—

19 “(i) the fair market value of such in-  
20 terest shall be treated for purposes of this

1 section as being equal to the amount of the  
2 distribution which the partner would re-  
3 ceive if the partnership sold (at the time of  
4 the transfer) all of its assets at fair market  
5 value and distributed the proceeds of such  
6 sale (reduced by the liabilities of the part-  
7 nership) to its partners in liquidation of  
8 the partnership, and

9 “(ii) the person receiving such interest  
10 shall be treated as having made the elec-  
11 tion under subsection (b)(1) unless such  
12 person makes an election under this para-  
13 graph to have such subsection not apply.

14 “(B) ELECTION.—The election under sub-  
15 paragraph (A)(ii) shall be made under rules  
16 similar to the rules of subsection (b)(2).”.

17 (b) EFFECTIVE DATE.—The amendments made by  
18 this section shall apply to interests in partnerships trans-  
19 ferred after December 31, 2012.

20 **SEC. 5602. SPECIAL RULES FOR PARTNERS PROVIDING IN-**  
21 **VESTMENT MANAGEMENT SERVICES TO**  
22 **PARTNERSHIPS.**

23 (a) IN GENERAL.—Part I of subchapter K of chapter  
24 1 of the Internal Revenue Code of 1986 is amended by  
25 adding at the end the following new section:

1 **“SEC. 710. SPECIAL RULES FOR PARTNERS PROVIDING IN-**  
2 **VESTMENT MANAGEMENT SERVICES TO**  
3 **PARTNERSHIPS.**

4 “(a) TREATMENT OF DISTRIBUTIVE SHARE OF  
5 PARTNERSHIP ITEMS.—For purposes of this title, in the  
6 case of an investment services partnership interest—

7 “(1) IN GENERAL.—Notwithstanding section  
8 702(b)—

9 “(A) an amount equal to the net capital  
10 gain with respect to such interest for any part-  
11 nership taxable year shall be treated as ordi-  
12 nary income, and

13 “(B) subject to the limitation of paragraph  
14 (2), an amount equal to the net capital loss  
15 with respect to such interest for any partner-  
16 ship taxable year shall be treated as an ordi-  
17 nary loss.

18 “(2) RECHARACTERIZATION OF LOSSES LIM-  
19 ITED TO RECHARACTERIZED GAINS.—The amount  
20 treated as ordinary loss under paragraph (1)(B) for  
21 any taxable year shall not exceed the excess (if any)  
22 of—

23 “(A) the aggregate amount treated as ordi-  
24 nary income under paragraph (1)(A) with re-  
25 spect to the investment services partnership in-

1           terest for all preceding partnership taxable  
2           years to which this section applies, over

3           “(B) the aggregate amount treated as or-  
4           dinary loss under paragraph (1)(B) with re-  
5           spect to such interest for all preceding partner-  
6           ship taxable years to which this section applies.

7           “(3) ALLOCATION TO ITEMS OF GAIN AND  
8           LOSS.—

9           “(A) NET CAPITAL GAIN.—The amount  
10          treated as ordinary income under paragraph  
11          (1)(A) shall be allocated ratably among the  
12          items of long-term capital gain taken into ac-  
13          count in determining such net capital gain.

14          “(B) NET CAPITAL LOSS.—The amount  
15          treated as ordinary loss under paragraph (1)(B)  
16          shall be allocated ratably among the items of  
17          long-term capital loss and short-term capital  
18          loss taken into account in determining such net  
19          capital loss.

20          “(4) TERMS RELATING TO CAPITAL GAINS AND  
21          LOSSES.—For purposes of this section—

22          “(A) IN GENERAL.—Net capital gain, long-  
23          term capital gain, and long-term capital loss,  
24          with respect to any investment services partner-  
25          ship interest for any taxable year, shall be de-

1           terminated under section 1222, except that such  
2           section shall be applied—

3                   “(i) without regard to the recharacter-  
4                   ization of any item as ordinary income or  
5                   ordinary loss under this section,

6                   “(ii) by only taking into account items  
7                   of gain and loss taken into account by the  
8                   holder of such interest under section 702  
9                   with respect to such interest for such tax-  
10                  able year,

11                  “(iii) by treating property which is  
12                  taken into account in determining gains  
13                  and losses to which section 1231 applies as  
14                  capital assets held for more than 1 year,  
15                  and

16                  “(iv) without regard to section 1202.

17                  “(B) NET CAPITAL LOSS.—The term ‘net  
18                  capital loss’ means the excess of the losses from  
19                  sales or exchanges of capital assets over the  
20                  gains from such sales or exchanges. Rules simi-  
21                  lar to the rules of clauses (i) through (iv) of  
22                  subparagraph (A) shall apply for purposes of  
23                  the preceding sentence.

24                  “(5) SPECIAL RULES FOR DIVIDENDS.—

1           “(A) INDIVIDUALS.—Any dividend allo-  
2           cated to any investment services partnership in-  
3           terest shall not be treated as qualified dividend  
4           income for purposes of section 1(h).

5           “(B) CORPORATIONS.—No deduction shall  
6           be allowed under section 243 or 245 with re-  
7           spect to any dividend allocated to any invest-  
8           ment services partnership interest.

9           “(b) DISPOSITIONS OF PARTNERSHIP INTERESTS.—  
10          “(1) GAIN.—

11           “(A) IN GENERAL.—Any gain on the dis-  
12           position of an investment services partnership  
13           interest shall be—

14                   “(i) treated as ordinary income, and

15                   “(ii) recognized notwithstanding any  
16           other provision of this subtitle.

17           “(B) EXCEPTIONS; CERTAIN TRANSFERS  
18           TO CHARITIES AND RELATED PERSONS.—Sub-  
19           paragraph (A) shall not apply to—

20                   “(i) a disposition by gift,

21                   “(ii) a transfer at death, or

22                   “(iii) other disposition identified by  
23           the Secretary as a disposition with respect  
24           to which it would be inconsistent with the  
25           purposes of this section to apply subpara-

1 graph (A), if such gift, transfer, or other  
2 disposition is to an organization described  
3 in section 170(b)(1)(A) (other than any or-  
4 ganization described in section 509(a)(3)  
5 or any fund or account described in section  
6 4966(d)(2)) or a person with respect to  
7 whom the transferred interest is an invest-  
8 ment services partnership interest.

9 “(2) LOSS.—Any loss on the disposition of an  
10 investment services partnership interest shall be  
11 treated as an ordinary loss to the extent of the ex-  
12 cess (if any) of—

13 “(A) the aggregate amount treated as ordi-  
14 nary income under subsection (a) with respect  
15 to such interest for all partnership taxable  
16 years to which this section applies, over

17 “(B) the aggregate amount treated as or-  
18 dinary loss under subsection (a) with respect to  
19 such interest for all partnership taxable years  
20 to which this section applies.

21 “(3) ELECTION WITH RESPECT TO CERTAIN EX-  
22 CHANGES.—Paragraph (1)(A)(ii) shall not apply to  
23 the contribution of an investment services partner-  
24 ship interest to a partnership in exchange for an in-  
25 terest in such partnership if—

1           “(A) the taxpayer makes an irrevocable  
2 election to treat the partnership interest re-  
3 ceived in the exchange as an investment serv-  
4 ices partnership interest, and

5           “(B) the taxpayer agrees to comply with  
6 such reporting and recordkeeping requirements  
7 as the Secretary may prescribe.

8           “(4) DISTRIBUTIONS OF PARTNERSHIP PROP-  
9 ERTY.—

10           “(A) IN GENERAL.—In the case of any dis-  
11 tribution of property by a partnership with re-  
12 spect to any investment services partnership in-  
13 terest held by a partner, the partner receiving  
14 such property shall recognize gain equal to the  
15 excess (if any) of—

16           “(i) the fair market value of such  
17 property at the time of such distribution,  
18 over

19           “(ii) the adjusted basis of such prop-  
20 erty in the hands of such partner (deter-  
21 mined without regard to subparagraph  
22 (C)).

23           “(B) TREATMENT OF GAIN AS ORDINARY  
24 INCOME.—Any gain recognized by such partner  
25 under subparagraph (A) shall be treated as or-



1           dinary income to the same extent and in the  
2           same manner as the increase in such partner's  
3           distributive share of the taxable income of the  
4           partnership would be treated under subsection  
5           (a) if, immediately prior to the distribution, the  
6           partnership had sold the distributed property at  
7           fair market value and all of the gain from such  
8           disposition were allocated to such partner. For  
9           purposes of applying paragraphs (2) and (3) of  
10          subsection (a), any gain treated as ordinary in-  
11          come under this subparagraph shall be treated  
12          as an amount treated as ordinary income under  
13          subsection (a)(1)(A).

14                 “(C) ADJUSTMENT OF BASIS.—In the case  
15          a distribution to which subparagraph (A) ap-  
16          plies, the basis of the distributed property in  
17          the hands of the distributee partner shall be the  
18          fair market value of such property.

19                 “(D) SPECIAL RULES WITH RESPECT TO  
20          MERGERS, DIVISIONS, AND TECHNICAL TERMI-  
21          NATIONS.—In the case of a taxpayer which sat-  
22          isfies requirements similar to the requirements  
23          of subparagraphs (A) and (B) of paragraph (3),  
24          this paragraph and paragraph (1)(A)(ii) shall  
25          not apply to the distribution of a partnership

1 interest if such distribution is in connection  
2 with a contribution (or deemed contribution) of  
3 any property of the partnership to which sec-  
4 tion 721 applies pursuant to a transaction de-  
5 scribed in paragraph (1)(B) or (2) of section  
6 708(b).

7 “(c) INVESTMENT SERVICES PARTNERSHIP INTER-  
8 EST.—For purposes of this section—

9 “(1) IN GENERAL.—The term ‘investment serv-  
10 ices partnership interest’ means any interest in an  
11 investment partnership acquired or held by any per-  
12 son in connection with the conduct of a trade or  
13 business described in paragraph (2) by such person  
14 (or any person related to such person). An interest  
15 in an investment partnership held by any person—

16 “(A) shall not be treated as an investment  
17 services partnership interest for any period be-  
18 fore the first date on which it is so held in con-  
19 nection with such a trade or business,

20 “(B) shall not cease to be an investment  
21 services partnership interest merely because  
22 such person holds such interest other than in  
23 connection with such a trade or business, and

24 “(C) shall be treated as an investment  
25 services partnership interest if acquired from a

1 related person in whose hands such interest was  
2 an investment services partnership interest.

3 “(2) BUSINESSES TO WHICH THIS SECTION AP-  
4 PLIES.—A trade or business is described in this  
5 paragraph if such trade or business primarily in-  
6 volves the performance of any of the following serv-  
7 ices with respect to assets held (directly or indi-  
8 rectly) by the investment partnership referred to in  
9 paragraph (1):

10 “(A) Advising as to the advisability of in-  
11 vesting in, purchasing, or selling any specified  
12 asset.

13 “(B) Managing, acquiring, or disposing of  
14 any specified asset.

15 “(C) Arranging financing with respect to  
16 acquiring specified assets.

17 “(D) Any activity in support of any service  
18 described in subparagraphs (A) through (C).

19 “(3) INVESTMENT PARTNERSHIP.—

20 “(A) IN GENERAL.—The term ‘investment  
21 partnership’ means any partnership if, at the  
22 end of any calendar quarter ending after De-  
23 cember 31, 2012—

24 “(i) substantially all of the assets of  
25 the partnership are specified assets (deter-

1           mined without regard to any section 197  
2           intangible within the meaning of section  
3           197(d)), and

4                   “(ii) more than half of the contributed  
5           capital of the partnership is attributable to  
6           contributions of property by one or more  
7           persons in exchange for interests in the  
8           partnership which (in the hands of such  
9           persons) constitute property held for the  
10          production of income.

11                   “(B) SPECIAL RULES FOR DETERMINING  
12          IF PROPERTY HELD FOR THE PRODUCTION OF  
13          INCOME.—Except as otherwise provided by the  
14          Secretary, for purposes of determining whether  
15          any interest in a partnership constitutes prop-  
16          erty held for the production of income under  
17          subparagraph (A)(ii)—

18                           “(i) any election under subsection (e)  
19                           or (f) of section 475 shall be disregarded,  
20                           and

21                           “(ii) paragraph (5)(B) shall not apply.

22                   “(C) ANTIABUSE RULES.—The Secretary  
23          may issue regulations or other guidance which  
24          prevent the avoidance of the purposes of sub-  
25          paragraph (A), including regulations or other

1 guidance which treat convertible and contingent  
2 debt (and other debt having the attributes of  
3 equity) as a capital interest in the partnership.

4 “(D) CONTROLLED GROUPS OF ENTI-  
5 TIES.—

6 “(i) IN GENERAL.—In the case of a  
7 controlled group of entities, if an interest  
8 in the partnership received in exchange for  
9 a contribution to the capital of the part-  
10 nership by any member of such controlled  
11 group would (in the hands of such mem-  
12 ber) constitute property not held for the  
13 production of income, then any interest in  
14 such partnership held by any member of  
15 such group shall be treated for purposes of  
16 subparagraph (A) as constituting (in the  
17 hands of such member) property not held  
18 for the production of income.

19 “(ii) CONTROLLED GROUP OF ENTI-  
20 TIES.—For purposes of clause (i), the term  
21 ‘controlled group of entities’ means a con-  
22 trolled group of corporations as defined in  
23 section 1563(a)(1), applied without regard  
24 to subsections (a)(4) and (b)(2) of section  
25 1563. A partnership or any other entity

1 (other than a corporation) shall be treated  
2 as a member of a controlled group of enti-  
3 ties if such entity is controlled (within the  
4 meaning of section 954(d)(3)) by members  
5 of such group (including any entity treated  
6 as a member of such group by reason of  
7 this sentence).

8 “(4) SPECIFIED ASSET.—The term ‘specified  
9 asset’ means securities (as defined in section  
10 475(c)(2) without regard to the last sentence there-  
11 of), real estate held for rental or investment, inter-  
12 ests in partnerships, commodities (as defined in sec-  
13 tion 475(e)(2)), cash or cash equivalents, or options  
14 or derivative contracts with respect to any of the  
15 foregoing.

16 “(5) RELATED PERSONS.—

17 “(A) IN GENERAL.—A person shall be  
18 treated as related to another person if the rela-  
19 tionship between such persons is described in  
20 section 267(b) or 707(b).

21 “(B) CONTRIBUTION OF PARTNER SERV-  
22 ICES.—Any service described in paragraph (2)  
23 which is provided by a partner of a partnership  
24 shall be treated as also provided by such part-  
25 nership.

1       “(d) EXCEPTION FOR CERTAIN CAPITAL INTER-  
2 ESTS.—

3           “(1) IN GENERAL.—In the case of any portion  
4 of an investment services partnership interest which  
5 is a qualified capital interest, all items of gain and  
6 loss (and any dividends) which are allocated to such  
7 qualified capital interest shall not be taken into ac-  
8 count under subsection (a) if—

9           “(A) allocations of items are made by the  
10 partnership to such qualified capital interest in  
11 the same manner as such allocations are made  
12 to other qualified capital interests held by part-  
13 ners who do not provide any services described  
14 in subsection (c)(2) and who are not related to  
15 the partner holding the qualified capital inter-  
16 est, and

17           “(B) the allocations made to such other in-  
18 terests are significant compared to the alloca-  
19 tions made to such qualified capital interest.

20           “(2) AUTHORITY TO PROVIDE EXCEPTIONS TO  
21 ALLOCATION REQUIREMENTS.—To the extent pro-  
22 vided by the Secretary in regulations or other guid-  
23 ance—

24           “(A) ALLOCATIONS TO PORTION OF QUALI-  
25 FIED CAPITAL INTEREST.—Paragraph (1) may

1 be applied separately with respect to a portion  
2 of a qualified capital interest.

3 “(B) NO OR INSIGNIFICANT ALLOCATIONS  
4 TO NONSERVICE PROVIDERS.—In any case in  
5 which the requirements of paragraph (1)(B) are  
6 not satisfied, items of gain and loss (and any  
7 dividends) shall not be taken into account under  
8 subsection (a) to the extent that such items are  
9 properly allocable under such regulations or  
10 other guidance to qualified capital interests.

11 “(C) ALLOCATIONS TO SERVICE PRO-  
12 VIDERS’ QUALIFIED CAPITAL INTERESTS WHICH  
13 ARE LESS THAN OTHER ALLOCATIONS.—Alloca-  
14 tions shall not be treated as failing to meet the  
15 requirement of paragraph (1)(A) merely be-  
16 cause the allocations to the qualified capital in-  
17 terest represent a lower return than the alloca-  
18 tions made to the other qualified capital inter-  
19 ests referred to in such paragraph.

20 “(3) SPECIAL RULE FOR CHANGES IN SERVICES  
21 AND CAPITAL CONTRIBUTIONS.—In the case of an  
22 interest in a partnership which was not an invest-  
23 ment services partnership interest and which, by  
24 reason of a change in the services with respect to as-  
25 sets held (directly or indirectly) by the partnership



1 or by reason of a change in the capital contributions  
2 to such partnership, becomes an investment services  
3 partnership interest, the qualified capital interest of  
4 the holder of such partnership interest immediately  
5 after such change shall not, for purposes of this sub-  
6 section, be less than the fair market value of such  
7 interest (determined immediately before such  
8 change).

9 “(4) SPECIAL RULE FOR TIERED PARTNER-  
10 SHIPS.—Except as otherwise provided by the Sec-  
11 retary, in the case of tiered partnerships, all items  
12 which are allocated in a manner which meets the re-  
13 quirements of paragraph (1) to qualified capital in-  
14 terests in a lower-tier partnership shall retain such  
15 character to the extent allocated on the basis of  
16 qualified capital interests in any upper-tier partner-  
17 ship.

18 “(5) EXCEPTION FOR NO-SELF-CHARGED  
19 CARRY AND MANAGEMENT FEE PROVISIONS.—Ex-  
20 cept as otherwise provided by the Secretary, an in-  
21 terest shall not fail to be treated as satisfying the  
22 requirement of paragraph (1)(A) merely because the  
23 allocations made by the partnership to such interest  
24 do not reflect the cost of services described in sub-  
25 section (c)(2) which are provided (directly or indi-

1       rectly) to the partnership by the holder of such in-  
2       terest (or a related person).

3           “(6) SPECIAL RULE FOR DISPOSITIONS.—In the  
4       case of any investment services partnership interest  
5       any portion of which is a qualified capital interest,  
6       subsection (b) shall not apply to so much of any  
7       gain or loss as bears the same proportion to the en-  
8       tire amount of such gain or loss as—

9           “(A) the distributive share of gain or loss  
10       that would have been allocated to the qualified  
11       capital interest (consistent with the require-  
12       ments of paragraph (1)) if the partnership had  
13       sold all of its assets at fair market value imme-  
14       diately before the disposition, bears to

15           “(B) the distributive share of gain or loss  
16       that would have been so allocated to the invest-  
17       ment services partnership interest of which such  
18       qualified capital interest is a part.

19           “(7) QUALIFIED CAPITAL INTEREST.—For pur-  
20       poses of this subsection—

21           “(A) IN GENERAL.—The term ‘qualified  
22       capital interest’ means so much of a partner’s  
23       interest in the capital of the partnership as is  
24       attributable to—

1           “(i) the fair market value of any  
2 money or other property contributed to the  
3 partnership in exchange for such interest  
4 (determined without regard to section  
5 752(a)),

6           “(ii) any amounts which have been in-  
7 cluded in gross income under section 83  
8 with respect to the transfer of such inter-  
9 est, and

10           “(iii) the excess (if any) of—

11                   “(I) any items of income and  
12 gain taken into account under section  
13 702 with respect to such interest, over

14                   “(II) any items of deduction and  
15 loss so taken into account.

16           “(B) ADJUSTMENT TO QUALIFIED CAPITAL  
17 INTEREST.—

18           “(i) DISTRIBUTIONS AND LOSSES.—

19           The qualified capital interest shall be re-  
20 duced by distributions from the partner-  
21 ship with respect to such interest and by  
22 the excess (if any) of the amount described  
23 in subparagraph (A)(iii)(II) over the  
24 amount described in subparagraph  
25 (A)(iii)(I).

1                   “(ii) SPECIAL RULE FOR CONTRIBU-  
2                   TIONS OF PROPERTY.—In the case of any  
3                   contribution of property described in sub-  
4                   paragraph (A)(i) with respect to which the  
5                   fair market value of such property is not  
6                   equal to the adjusted basis of such prop-  
7                   erty immediately before such contribution,  
8                   proper adjustments shall be made to the  
9                   qualified capital interest to take into ac-  
10                  count such difference consistent with such  
11                  regulations or other guidance as the Sec-  
12                  retary may provide.

13                  “(C) TECHNICAL TERMINATIONS, ETC.,  
14                  DISREGARDED.—No increase or decrease in the  
15                  qualified capital interest of any partner shall re-  
16                  sult from a termination, merger, consolidation,  
17                  or division described in section 708, or any  
18                  similar transaction.

19                  “(8) TREATMENT OF CERTAIN LOANS.—

20                  “(A) PROCEEDS OF PARTNERSHIP LOANS  
21                  NOT TREATED AS QUALIFIED CAPITAL INTER-  
22                  EST OF SERVICE PROVIDING PARTNERS.—For  
23                  purposes of this subsection, an investment serv-  
24                  ices partnership interest shall not be treated as  
25                  a qualified capital interest to the extent that

1           such interest is acquired in connection with the  
2           proceeds of any loan or other advance made or  
3           guaranteed, directly or indirectly, by any other  
4           partner or the partnership (or any person re-  
5           lated to any such other partner or the partner-  
6           ship). The preceding sentence shall not apply to  
7           the extent the loan or other advance is repaid  
8           before January 1, 2013 unless such repayment  
9           is made with the proceeds of a loan or other ad-  
10          vance described in the preceding sentence.

11                   “(B) REDUCTION IN ALLOCATIONS TO  
12           QUALIFIED CAPITAL INTERESTS FOR LOANS  
13           FROM NONSERVICE-PROVIDING PARTNERS TO  
14           THE PARTNERSHIP.—For purposes of this sub-  
15           section, any loan or other advance to the part-  
16           nership made or guaranteed, directly or indi-  
17           rectly, by a partner not providing services de-  
18           scribed in subsection (c)(2) to the partnership  
19           (or any person related to such partner) shall be  
20           taken into account in determining the qualified  
21           capital interests of the partners in the partner-  
22           ship.

23                   “(e) OTHER INCOME AND GAIN IN CONNECTION  
24           WITH INVESTMENT MANAGEMENT SERVICES.—

25                   “(1) IN GENERAL.—If—

1           “(A) a person performs (directly or indi-  
2           rectly) investment management services for any  
3           investment entity,

4           “(B) such person holds (directly or indi-  
5           rectly) a disqualified interest with respect to  
6           such entity, and

7           “(C) the value of such interest (or pay-  
8           ments thereunder) is substantially related to  
9           the amount of income or gain (whether or not  
10          realized) from the assets with respect to which  
11          the investment management services are per-  
12          formed, any income or gain with respect to such  
13          interest shall be treated as ordinary income.  
14          Rules similar to the rules of subsections (a)(5)  
15          and (d) shall apply for purposes of this sub-  
16          section.

17          “(2) DEFINITIONS.—For purposes of this sub-  
18          section—

19                 “(A) DISQUALIFIED INTEREST.—

20                         “(i) IN GENERAL.—The term ‘dis-  
21                         qualified interest’ means, with respect to  
22                         any investment entity—

23                                 “(I) any interest in such entity  
24                                 other than indebtedness,

1 “(II) convertible or contingent  
2 debt of such entity,

3 “(III) any option or other right  
4 to acquire property described in sub-  
5 clause (I) or (II), and

6 “(IV) any derivative instrument  
7 entered into (directly or indirectly)  
8 with such entity or any investor in  
9 such entity.

10 “(ii) EXCEPTIONS.—Such term shall  
11 not include—

12 “(I) a partnership interest,

13 “(II) except as provided by the  
14 Secretary, any interest in a taxable  
15 corporation, and

16 “(III) except as provided by the  
17 Secretary, stock in an S corporation.

18 “(B) TAXABLE CORPORATION.—The term  
19 ‘taxable corporation’ means—

20 “(i) a domestic C corporation, or

21 “(ii) a foreign corporation substan-  
22 tially all of the income of which is—

23 “(I) effectively connected with  
24 the conduct of a trade or business in  
25 the United States, or

1                   “(II) subject to a comprehensive  
2                   foreign income tax (as defined in sec-  
3                   tion 457A(d)(2)).

4                   “(C) INVESTMENT MANAGEMENT SERV-  
5                   ICES.—The term ‘investment management serv-  
6                   ices’ means a substantial quantity of any of the  
7                   services described in subsection (c)(2).

8                   “(D) INVESTMENT ENTITY.—The term ‘in-  
9                   vestment entity’ means any entity which, if it  
10                  were a partnership, would be an investment  
11                  partnership.

12                 “(f) REGULATIONS.—The Secretary shall prescribe  
13                 such regulations or other guidance as is necessary or ap-  
14                 propriate to carry out the purposes of this section, includ-  
15                 ing regulations or other guidance to—

16                 “(1) provide modifications to the application of  
17                 this section (including treating related persons as  
18                 not related to one another) to the extent such modi-  
19                 fication is consistent with the purposes of this sec-  
20                 tion, and

21                 “(2) coordinate this section with the other pro-  
22                 visions of this title.

23                 “(g) CROSS REFERENCE.—For 40 percent penalty on  
24                 certain underpayments due to the avoidance of this sec-  
25                 tion, see section 6662.”.



1 (b) APPLICATION OF SECTION 751 TO INDIRECT DIS-  
2 POSITIONS OF INVESTMENT SERVICES PARTNERSHIP IN-  
3 TERESTS.—

4 (1) IN GENERAL.—Subsection (a) of section  
5 751 of the Internal Revenue Code of 1986 is amend-  
6 ed by striking “or” at the end of paragraph (1), by  
7 inserting “or” at the end of paragraph (2), and by  
8 inserting after paragraph (2) the following new  
9 paragraph:

10 “(3) investment services partnership interests  
11 held by the partnership,”.

12 (2) CERTAIN DISTRIBUTIONS TREATED AS  
13 SALES OR EXCHANGES.—Subparagraph (A) of sec-  
14 tion 751(b)(1) of the Internal Revenue Code of 1986  
15 is amended by striking “or” at the end of clause (i),  
16 by inserting “or” at the end of clause (ii), and by  
17 inserting after clause (ii) the following new clause:

18 “(iii) investment services partnership  
19 interests held by the partnership,”.

20 (3) APPLICATION OF SPECIAL RULES IN THE  
21 CASE OF TIERED PARTNERSHIPS.—Subsection (f) of  
22 section 751 of the Internal Revenue Code of 1986  
23 is amended by striking “or” at the end of paragraph  
24 (1), by inserting “or” at the end of paragraph (2),

1 and by inserting after paragraph (2) the following  
2 new paragraph:

3 “(3) investment services partnership interests  
4 held by the partnership,”.

5 (4) INVESTMENT SERVICES PARTNERSHIP IN-  
6 TERESTS; QUALIFIED CAPITAL INTERESTS.—Section  
7 751 of the Internal Revenue Code of 1986 is amend-  
8 ed by adding at the end the following new sub-  
9 section:

10 “(g) INVESTMENT SERVICES PARTNERSHIP INTER-  
11 ESTS.—For purposes of this section—

12 “(1) IN GENERAL.—The term ‘investment serv-  
13 ices partnership interest’ has the meaning given  
14 such term by section 710(c).

15 “(2) ADJUSTMENTS FOR QUALIFIED CAPITAL  
16 INTERESTS.—The amount to which subsection (a)  
17 applies by reason of paragraph (3) thereof shall not  
18 include so much of such amount as is attributable  
19 to any portion of the investment services partnership  
20 interest which is a qualified capital interest (deter-  
21 mined under rules similar to the rules of section  
22 710(d)).

23 “(3) RECOGNITION OF GAINS.—Any gain with  
24 respect to which subsection (a) applies by reason of

1 paragraph (3) thereof shall be recognized notwith-  
2 standing any other provision of this title.

3 “(4) COORDINATION WITH INVENTORY  
4 ITEMS.—An investment services partnership interest  
5 held by the partnership shall not be treated as an  
6 inventory item of the partnership.

7 “(5) PREVENTION OF DOUBLE COUNTING.—  
8 Under regulations or other guidance prescribed by  
9 the Secretary, subsection (a)(3) shall not apply with  
10 respect to any amount to which section 710 ap-  
11 plies.”.

12 (c) TREATMENT FOR PURPOSES OF SECTION  
13 7704.—Subsection (d) of section 7704 of the Internal  
14 Revenue Code of 1986 is amended by adding at the end  
15 the following new paragraph:

16 “(6) INCOME FROM CERTAIN CARRIED INTER-  
17 ESTS NOT QUALIFIED.—

18 “(A) IN GENERAL.—Specified carried in-  
19 terest income shall not be treated as qualifying  
20 income.

21 “(B) SPECIFIED CARRIED INTEREST IN-  
22 COME.—For purposes of this paragraph—

23 “(i) IN GENERAL.—The term ‘speci-  
24 fied carried interest income’ means—

1                   “(I) any item of income or gain  
2                   allocated to an investment services  
3                   partnership interest (as defined in  
4                   section 710(c)) held by the partner-  
5                   ship,

6                   “(II) any gain on the disposition  
7                   of an investment services partnership  
8                   interest (as so defined) or a partner-  
9                   ship interest to which (in the hands of  
10                  the partnership) section 751 applies,  
11                  and

12                  “(III) any income or gain taken  
13                  into account by the partnership under  
14                  subsection (b)(4) or (e) of section  
15                  710.

16                  “(ii) EXCEPTION FOR QUALIFIED CAP-  
17                  ITAL INTERESTS.—A rule similar to the  
18                  rule of section 710(d) shall apply for pur-  
19                  poses of clause (i).

20                  “(C) COORDINATION WITH OTHER PROVI-  
21                  SIONS.—Subparagraph (A) shall not apply to  
22                  any item described in paragraph (1)(E) (or so  
23                  much of paragraph (1)(F) as relates to para-  
24                  graph (1)(E)).

1                   “(D) SPECIAL RULES FOR CERTAIN PART-  
2                   NERSHIPS.—

3                   “(i) CERTAIN PARTNERSHIPS OWNED  
4                   BY REAL ESTATE INVESTMENT TRUSTS.—  
5                   Subparagraph (A) shall not apply in the  
6                   case of a partnership which meets each of  
7                   the following requirements:

8                   “(I) Such partnership is treated  
9                   as publicly traded under this section  
10                  solely by reason of interests in such  
11                  partnership being convertible into in-  
12                  terests in a real estate investment  
13                  trust which is publicly traded.

14                  “(II) 50 percent or more of the  
15                  capital and profits interests of such  
16                  partnership are owned, directly or in-  
17                  directly, at all times during the tax-  
18                  able year by such real estate invest-  
19                  ment trust (determined with the ap-  
20                  plication of section 267(c)).

21                  “(III) Such partnership meets  
22                  the requirements of paragraphs (2),  
23                  (3), and (4) of section 856(c).

24                  “(ii) CERTAIN PARTNERSHIPS OWN-  
25                  ING OTHER PUBLICLY TRADED PARTNER-

1 SHIPS.—Subparagraph (A) shall not apply  
2 in the case of a partnership which meets  
3 each of the following requirements:

4 “(I) Substantially all of the as-  
5 sets of such partnership consist of in-  
6 terests in one or more publicly traded  
7 partnerships (determined without re-  
8 gard to subsection (b)(2)).

9 “(II) Substantially all of the in-  
10 come of such partnership is ordinary  
11 income or section 1231 gain (as de-  
12 fined in section 1231(a)(3)).

13 “(E) TRANSITIONAL RULE.—Subpara-  
14 graph (A) shall not apply to any taxable year  
15 of the partnership beginning before the date  
16 which is 10 years after January 1, 2013”.

17 (d) IMPOSITION OF PENALTY ON UNDERPAY-  
18 MENTS.—

19 (1) IN GENERAL.—Subsection (b) of section  
20 6662 of the Internal Revenue Code of 1986 is  
21 amended by inserting after paragraph (7) the fol-  
22 lowing new paragraph:

23 “(8) The application of section 710(e) or the  
24 regulations or other guidance prescribed under sec-

1       tion 710(h) to prevent the avoidance of the purposes  
2       of section 710.”.

3               (2) AMOUNT OF PENALTY.—

4                       (A) IN GENERAL.—Section 6662 of the In-  
5               ternal Revenue Code of 1986 is amended by  
6               adding at the end the following new subsection:

7       “(k) INCREASE IN PENALTY IN CASE OF PROPERTY  
8       TRANSFERRED FOR INVESTMENT MANAGEMENT SERV-  
9       ICES.—In the case of any portion of an underpayment to  
10      which this section applies by reason of subsection (b)(8),  
11      subsection (a) shall be applied with respect to such portion  
12      by substituting ‘40 percent’ for ‘20 percent’.”.

13                      (B) CONFORMING AMENDMENT.—Subpara-  
14              graph (B) of section 6662A(e)(2) is amended  
15              by striking “or (i)” and inserting “, (i), or (k)”.

16               (3) SPECIAL RULES FOR APPLICATION OF REA-  
17      SONABLE CAUSE EXCEPTION.—Subsection (c) of sec-  
18      tion 6664 is amended—

19                      (A) by redesignating paragraphs (3) and  
20              (4) as paragraphs (4) and (5), respectively;

21                      (B) by striking “paragraph (3)” in para-  
22              graph (5)(A), as so redesignated, and inserting  
23              “paragraph (4)”; and

24                      (C) by inserting after paragraph (2) the  
25              following new paragraph:

1           “(3) SPECIAL RULE FOR UNDERPAYMENTS AT-  
2           TRIBUTABLE TO INVESTMENT MANAGEMENT SERV-  
3           ICES.—

4           “(A) IN GENERAL.—Paragraph (1) shall  
5           not apply to any portion of an underpayment to  
6           which section 6662 applies by reason of sub-  
7           section (b)(8) unless—

8                   “(i) the relevant facts affecting the  
9                   tax treatment of the item are adequately  
10                  disclosed,

11                   “(ii) there is or was substantial au-  
12                  thority for such treatment, and

13                   “(iii) the taxpayer reasonably believed  
14                  that such treatment was more likely than  
15                  not the proper treatment.

16           “(B) RULES RELATING TO REASONABLE  
17           BELIEF.—Rules similar to the rules of sub-  
18           section (d)(3) shall apply for purposes of sub-  
19           paragraph (A)(iii).”.

20           (e) INCOME AND LOSS FROM INVESTMENT SERVICES  
21           PARTNERSHIP INTERESTS TAKEN INTO ACCOUNT IN DE-  
22           TERMINING NET EARNINGS FROM SELF-EMPLOYMENT.—

23           (1) INTERNAL REVENUE CODE.—

24                   (A) IN GENERAL.—Section 1402(a) of the  
25           Internal Revenue Code of 1986 is amended by



1 striking “and” at the end of paragraph (16), by  
2 striking the period at the end of paragraph (17)  
3 and inserting “; and”, and by inserting after  
4 paragraph (17) the following new paragraph:

5 “(18) notwithstanding the preceding provisions  
6 of this subsection, in the case of any individual en-  
7 gaged in the trade or business of providing services  
8 described in section 710(c)(2) with respect to any  
9 entity, investment services partnership income or  
10 loss (as defined in subsection (m)) of such individual  
11 with respect to such entity shall be taken into ac-  
12 count in determining the net earnings from self-em-  
13 ployment of such individual.”.

14 (B) INVESTMENT SERVICES PARTNERSHIP  
15 INCOME OR LOSS.—Section 1402 of the Inter-  
16 nal Revenue Code is amended by adding at the  
17 end the following new subsection:

18 “(m) INVESTMENT SERVICES PARTNERSHIP INCOME  
19 OR LOSS.—For purposes of subsection (a)—

20 “(1) IN GENERAL.—The term ‘investment serv-  
21 ices partnership income or loss’ means, with respect  
22 to any investment services partnership interest (as  
23 defined in section 710(c)), the net of—

1           “(A) the amounts treated as ordinary in-  
2           come or ordinary loss under subsections (b) and  
3           (e) of section 710 with respect to such interest,

4           “(B) all items of income, gain, loss, and  
5           deduction allocated to such interest, and

6           “(C) the amounts treated as realized from  
7           the sale or exchange of property other than a  
8           capital asset under section 751 with respect to  
9           such interest.

10          “(2) EXCEPTION FOR QUALIFIED CAPITAL IN-  
11          TERESTS.—A rule similar to the rule of section  
12          710(d) shall apply for purposes of applying para-  
13          graph (1)(B)(ii).”.

14          (2) SOCIAL SECURITY ACT.—Section 211(a) of  
15          the Social Security Act is amended by striking  
16          “and” at the end of paragraph (15), by striking the  
17          period at the end of paragraph (16) and inserting “;  
18          and”, and by inserting after paragraph (16) the fol-  
19          lowing new paragraph:

20          “(17) Notwithstanding the preceding provisions  
21          of this subsection, in the case of any individual en-  
22          gaged in the trade or business of providing services  
23          described in section 710(c)(2) of the Internal Rev-  
24          enue Code of 1986 with respect to any entity, invest-  
25          ment services partnership income or loss (as defined

1 in section 1402(m) of such Code) shall be taken into  
2 account in determining the net earnings from self-  
3 employment of such individual.”.

4 (f) CONFORMING AMENDMENTS.—

5 (1) Subsection (d) of section 731 of the Inter-  
6 nal Revenue Code of 1986 is amended by inserting  
7 “section 710(b)(4) (relating to distributions of part-  
8 nership property),” after “to the extent otherwise  
9 provided by”.

10 (2) Section 741 of the Internal Revenue Code  
11 of 1986 is amended by inserting “or section 710 (re-  
12 lating to special rules for partners providing invest-  
13 ment management services to partnerships)” before  
14 the period at the end.

15 (3) The table of sections for part I of sub-  
16 chapter K of chapter 1 of the Internal Revenue Code  
17 of 1986 is amended by adding at the end the fol-  
18 lowing new item:

“Sec. 710. Special rules for partners providing investment management services  
to partnerships.”.

19 (g) EFFECTIVE DATE.—

20 (1) IN GENERAL.—Except as otherwise pro-  
21 vided in this subsection, the amendments made by  
22 this section shall apply to taxable years ending after  
23 December 31, 2012.

1           (2) PARTNERSHIP TAXABLE YEARS WHICH IN-  
2           CLUDE EFFECTIVE DATE.—In applying section  
3           710(a) of the Internal Revenue Code of 1986 (as  
4           added by this section) in the case of any partnership  
5           taxable year which includes January 1, 2013, the  
6           amount of the net income referred to in such section  
7           shall be treated as being the lesser of the net income  
8           for the entire partnership taxable year or the net in-  
9           come determined by only taking into account items  
10          attributable to the portion of the partnership taxable  
11          year which is after such date.

12          (3) DISPOSITIONS OF PARTNERSHIP INTER-  
13          ESTS.—

14                (A) IN GENERAL.—Section 710(b) of such  
15                Code (as added by this section) shall apply to  
16                dispositions and distributions after December  
17                31, 2012.

18                (B) INDIRECT DISPOSITIONS.—The amend-  
19                ments made by subsection (b) shall apply to  
20                transactions after December 31, 2012.

21          (4) OTHER INCOME AND GAIN IN CONNECTION  
22          WITH INVESTMENT MANAGEMENT SERVICES.—Sec-  
23          tion 710(e) of such Code (as added by this section)  
24          shall take effect on January 1, 2013.

