H. R. 2834

To amend the Internal Revenue Code of 1986 to treat income received by partners for performing investment management services as ordinary income received for the performance of services.

IN THE HOUSE OF REPRESENTATIVES

JUNE 22, 2007

Mr. Levin (for himself, Mr. Rangel, Mr. Stark, Mr. McDermott, Mr. Lewis of Georgia, Mr. Neal of Massachusetts, Mr. Pomeroy, Mrs. Jones of Ohio, Mr. Larson of Connecticut, Mr. Blumenauer, Mr. Kind, Mr. Pascrell, and Mr. Frank of Massachusetts) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to treat income received by partners for performing investment management services as ordinary income received for the performance of services.

1 Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,
SECTION 1. INCOME OF PARTNERS FOR PERFORMING INVESTMENT MANAGEMENT SERVICES TREATED AS ORDINARY INCOME RECEIVED FOR PERFORMANCE OF SERVICES.

(a) In General.—Part I of subchapter K of chapter 1 of the Internal Revenue Code of 1986 (relating to determination of tax liability) is amended by adding at the end the following new section:

“SEC. 710. SPECIAL RULES FOR PARTNERS PROVIDING INVESTMENT MANAGEMENT SERVICES TO PARTNERSHIP.

“(a) Treatment of Distributive Share of Partnership Items.—For purposes of this title, in the case of an investment services partnership interest—

“(1) In General.—Notwithstanding section 702(b)—

“(A) any net income with respect to such interest for any partnership taxable year shall be treated as ordinary income for the performance of services, and

“(B) any net loss with respect to such interest for such year, to the extent not disallowed under paragraph (2) for such year, shall be treated as an ordinary loss.

“(2) Treatment of Losses.—
“(A) LIMITATION.—Any net loss with respect to such interest shall be allowed for any partnership taxable year only to the extent that such loss does not exceed the excess (if any) of—

“(i) the aggregate net income with respect to such interest for all prior partnership taxable years, over

“(ii) the aggregate net loss with respect to such interest not disallowed under this subparagraph for all prior partnership taxable years.

“(B) CARRYFORWARD.—Any net loss for any partnership taxable year which is not allowed by reason of subparagraph (A) shall be treated as an item of loss with respect to such partnership interest for the succeeding partnership taxable year.

“(C) BASIS ADJUSTMENT.—No adjustment to the basis of a partnership interest shall be made on account of any net loss which is not allowed by reason of subparagraph (A).

“(D) PRIOR PARTNERSHIP YEARS.—Any reference in this paragraph to prior partnership
taxable years shall only include prior partnership taxable years to which this section applies.

“(3) NET INCOME AND LOSS.—For purposes of this section—

“(A) NET INCOME.—The term ‘net income’ means, with respect to any investment services partnership interest, for any partnership taxable year, the excess (if any) of—

“(i) all items of income and gain taken into account by the holder of such interest under section 702 with respect to such interest for such year, over

“(ii) all items of deduction and loss so taken into account.

“(B) NET LOSS.—The term ‘net loss’ means with respect to such interest for such year, the excess (if any) of the amount described in subparagraph (A)(ii) over the amount described in subparagraph (A)(i).

“(b) DISPOSITIONS OF PARTNERSHIP INTERESTS.—

“(1) GAIN.—Any gain on the disposition of an investment services partnership interest shall be treated as ordinary income for the performance of services.
“(2) Loss.—Any loss on the disposition of an investment services partnership interest shall be treated as an ordinary loss to the extent of the excess (if any) of—

“(A) the aggregate net income with respect to such interest for all partnership taxable years, over

“(B) the aggregate net loss with respect to such interest allowed under subsection (a)(2) for all partnership taxable years.

“(3) Disposition of portion of interest.—In the case of any disposition of an investment services partnership interest, the amount of net loss which otherwise would have (but for subsection (a)(2)(C)) applied to reduce the basis of such interest shall be disregarded for purposes of this section for all succeeding partnership taxable years.

“(4) Distributions of partnership property.—In the case of any distribution of appreciated property by a partnership with respect to any investment services partnership interest, gain shall be recognized by the partnership in the same manner as if the partnership sold such property at fair market value at the time of the distribution. For purposes of this paragraph, the term ‘appreciated
property’ means any property with respect to which
gain would be determined if sold as described in the
preceding sentence.

“(c) Investment Services Partnership Interest.—For purposes of this section—

“(1) In general.—The term ‘investment services partnership interest’ means any interest in a partnership which is held by any person if such person provides (directly or indirectly), in the active conduct of a trade or business, a substantial quantity of any of the following services to the partnership:

“(A) Advising the partnership as to the value of any specified asset.

“(B) Advising the partnership as to the advisability of investing in, purchasing, or selling any specified asset.

“(C) Managing, acquiring, or disposing of any specified asset.

“(D) Arranging financing with respect to acquiring specified assets.

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

For purposes of this paragraph, the term ‘specified asset’ means securities (as defined in section
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475(c)(2) without regard to the last sentence there-
of), real estate, commodities (as defined in section
475(c)(2))), or options or derivative contracts with
respect to securities (as so defined), real estate, or
commodities (as so defined).

“(2) Exception for certain capital inter-
esths.—

“(A) In general.—If—

“(i) a portion of an investment serv-
ices partnership interest is acquired on ac-
count of a contribution of invested capital,
and

“(ii) the partnership makes a reason-
able allocation of partnership items be-
tween the portion of the distributive share
that is with respect to invested capital and
the portion of such distributive share that
is not with respect to invested capital,
then subsection (a) shall not apply to the por-
tion of the distributive share that is with re-
spect to invested capital. An allocation will not
be treated as reasonable for purposes of this
subparagraph if such allocation would result in
the partnership allocating a greater portion of
income to invested capital than any other part-
\(\text{ner not providing services would have been allo-}\)
\(\text{cated with respect to the same amount of in-}\)
\(\text{vested capital.}\)

\(\text{“(B) Special rule for dispositions.—}\)
\(\text{In any case to which subparagraph (A) applies,}\)
\(\text{subsection (b) shall not apply to any gain or}\)
\(\text{loss allocable to invested capital. The portion of}\)
\(\text{any gain or loss attributable to invested capital}\)
\(\text{is the proportion of such gain or loss which is}\)
\(\text{based on the distributive share of gain or loss}\)
\(\text{that would have been allocable to invested cap-}\)
\(\text{ital under subparagraph (A) if the partnership}\)
\(\text{sold all of its assets immediately before the dis-}\)
\(\text{position.}\)

\(\text{“(C) Invested capital.—For purposes}\)
\(\text{of this paragraph, the term ‘invested capital’}\)
\(\text{means, the fair market value at the time of con-}\)
\(\text{tribution of, any money or other property con-}\)
\(\text{tributed to the partnership.”.}\)

\(\text{(b) Application to Real Estate Investment}\)
\(\text{Trusts.—Subsection (c) of section 856 of such Code is}\)
\(\text{amended by adding at the end the following new para-}\)
\(\text{graph:}\)

\(\text{“(8) Exception from recharacterization}\)
\(\text{of income from investment services partner-}\)
SHIP INTERESTS.—Paragraphs (2), (3), and (4) shall be applied without regard to section 710 (relating to special rules for partners providing investment management services to partnership).”.

(c) CONFORMING AMENDMENTS.—

(1) Subsection (d) of section 731 of such Code is amended by inserting “section 710(b)(4) (relating to distributions of partnership property),” before “section 736”.

(2) Section 741 of such Code is amended by inserting “or section 710 (relating to special rules for partners providing investment management services to partnership)” before the period at the end.

(3) Paragraph (13) of section 1402(a) of such Code is amended—

(A) by striking “other than guaranteed” and inserting “other than—

“(A) guaranteed”,

(B) by striking the semi-colon at the end and inserting “, and”, and

(C) by adding at the end the following new subparagraph:

“(B) any income treated as ordinary income under section 710 received by an indi-
individual who provides a substantial quantity of
the services described in section 710(e)(1);’.

(4) Paragraph (12) of section 211(a) of the So-
cial Security Act is amended—

(A) by striking “other than guaranteed”
and inserting “other than—

“(A) guaranteed”,

(B) by striking the semi-colon at the end
and inserting “, and”, and

(C) by adding at the end the following new
paragraph:

“(B) any income treated as ordinary in-
come under section 710 of the Internal Revenue
Code of 1986 received by an individual who
provides a substantial quantity of the services
described in section 710(e)(1) of such Code;”.

(5) The table of sections for part I of sub-
chapter K of chapter 1 of such Code is amended by
adding at the end the following new item:

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