

117TH CONGRESS
2D SESSION

H. R. 6763

To amend the Internal Revenue Code of 1986 to lower the corporate tax rate for small businesses and close the carried interest loophole, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 18, 2022

Ms. CRAIG 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 lower the corporate tax rate for small businesses and close the carried interest loophole, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Small Business Tax
5 Relief Act”.

6 **SEC. 2. GRADUATED CORPORATE TAX RATE TO SUPPORT**
7 **SMALL BUSINESSES.**

8 (a) IN GENERAL.—Section 11(b) of the Internal Rev-
9 enue Code of 1986 is amended to read as follows:

1 “(b) AMOUNT OF TAX.—

2 “(1) IN GENERAL.—Except as provided by
3 paragraph (2), the amount of the tax imposed by
4 subsection (a) shall be 21 percent of taxable income.

5 “(2) SMALL BUSINESSES.—In the case of a cor-
6 poration with taxable income that does not exceed
7 \$5,000,000 in the taxable year, the amount of the
8 tax imposed by subsection (a) shall be the sum of—

9 “(A) 18 percent of so much of the taxable
10 income as does not exceed \$400,000, and

11 “(B) 21 percent of so much of the taxable
12 income as equals or exceeds \$400,000.”.

13 (b) EFFECTIVE DATE.—The amendment made by
14 this section shall apply to taxable years ending after the
15 date of the enactment of this section.

16 **SEC. 3. PARTNERSHIP INTERESTS TRANSFERRED IN CON-**
17 **NECTION WITH PERFORMANCE OF SERVICES.**

18 (a) MODIFICATION TO ELECTION TO INCLUDE PART-
19 NERSHIP INTEREST IN GROSS INCOME IN YEAR OF
20 TRANSFER.—Subsection (e) of section 83 of the Internal
21 Revenue Code of 1986 is amended by redesignating para-
22 graph (4) as paragraph (5) and by inserting after para-
23 graph (3) the following new paragraph:

24 “(4) PARTNERSHIP INTERESTS.—Except as
25 provided by the Secretary—

1 “(A) IN GENERAL.—In the case of any
2 transfer of an interest in a partnership in con-
3 nection with the provision of services to (or for
4 the benefit of) such partnership—

5 “(i) the fair market value of such in-
6 terest shall be treated for purposes of this
7 section as being equal to the amount of the
8 distribution which the partner would re-
9 ceive if the partnership sold (at the time of
10 the transfer) all of its assets at fair market
11 value and distributed the proceeds of such
12 sale (reduced by the liabilities of the part-
13 nership) to its partners in liquidation of
14 the partnership, and

15 “(ii) the person receiving such interest
16 shall be treated as having made the elec-
17 tion under subsection (b)(1) unless such
18 person makes an election under this para-
19 graph to have such subsection not apply.

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

23 (b) EFFECTIVE DATE.—The amendments made by
24 this section shall apply to interests in partnerships trans-

1 ferred in taxable years ending after the date of the enact-
2 ment of this Act.

3 **SEC. 4. SPECIAL RULES FOR PARTNERS PROVIDING IN-**
4 **VESTMENT MANAGEMENT SERVICES TO**
5 **PARTNERSHIPS.**

6 (a) IN GENERAL.—Part I of subchapter K of chapter
7 1 of the Internal Revenue Code of 1986 is amended by
8 adding at the end the following new section:

9 **“SEC. 710. SPECIAL RULES FOR PARTNERS PROVIDING IN-**
10 **VESTMENT MANAGEMENT SERVICES TO**
11 **PARTNERSHIPS.**

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

15 “(1) IN GENERAL.—Notwithstanding section
16 702(b)—

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

21 “(B) subject to the limitation of paragraph
22 (2), an amount equal to the net capital loss
23 with respect to such interest for any partner-
24 ship taxable year shall be treated as an ordi-
25 nary loss.

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

6 “(A) the aggregate amount treated as ordi-
7 nary income under paragraph (1)(A) with re-
8 spect to the investment services partnership in-
9 terest for all preceding partnership taxable
10 years to which this section applies, over

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

15 “(3) ALLOCATION TO ITEMS OF GAIN AND
16 LOSS.—

17 “(A) NET CAPITAL GAIN.—The amount
18 treated as ordinary income under paragraph
19 (1)(A) shall be allocated ratably among the
20 items of long-term capital gain taken into ac-
21 count in determining such net capital gain.

22 “(B) NET CAPITAL LOSS.—The amount
23 treated as ordinary loss under paragraph (1)(B)
24 shall be allocated ratably among the items of
25 long-term capital loss and short-term capital

1 loss taken into account in determining such net
2 capital loss.

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

5 “(A) IN GENERAL.—Net capital gain, long-
6 term capital gain, and long-term capital loss,
7 with respect to any investment services partner-
8 ship interest for any taxable year, shall be de-
9 termined under section 1222, except that such
10 section shall be applied—

11 “(i) without regard to the recharacter-
12 ization of any item as ordinary income or
13 ordinary loss under this section,

14 “(ii) by only taking into account items
15 of gain and loss taken into account by the
16 holder of such interest under section 702
17 (other than subsection (a)(9) thereof) with
18 respect to such interest for such taxable
19 year, and

20 “(iii) by treating property which is
21 taken into account in determining gains
22 and losses to which section 1231 applies as
23 capital assets held for more than 1 year.

24 “(B) NET CAPITAL LOSS.—The term ‘net
25 capital loss’ means the excess of the losses from

1 sales or exchanges of capital assets over the
2 gains from such sales or exchanges. Rules simi-
3 lar to the rules of clauses (i) through (iii) of
4 subparagraph (A) shall apply for purposes of
5 the preceding sentence.

6 “(5) SPECIAL RULE FOR DIVIDENDS.—Any div-
7 idend allocated with respect to any investment serv-
8 ices partnership interest shall not be treated as
9 qualified dividend income for purposes of section
10 1(h).

11 “(6) SPECIAL RULE FOR QUALIFIED SMALL
12 BUSINESS STOCK.—Section 1202 shall not apply to
13 any gain from the sale or exchange of qualified small
14 business stock (as defined in section 1202(c)) allo-
15 cated with respect to any investment services part-
16 nership interest.

17 “(b) DISPOSITIONS OF PARTNERSHIP INTERESTS.—

18 “(1) GAIN.—

19 “(A) IN GENERAL.—Any gain on the dis-
20 position of an investment services partnership
21 interest shall be—

22 “(i) treated as ordinary income, and

23 “(ii) recognized notwithstanding any
24 other provision of this subtitle.

1 “(B) GIFT AND TRANSFERS AT DEATH.—

2 In the case of a disposition of an investment
3 services partnership interest by gift or by rea-
4 son of death of the taxpayer—

5 “(i) subparagraph (A) shall not apply,

6 “(ii) such interest shall be treated as
7 an investment services partnership interest
8 in the hands of the person acquiring such
9 interest, and

10 “(iii) any amount that would have
11 been treated as ordinary income under this
12 subsection had the decedent sold such in-
13 terest immediately before death shall be
14 treated as an item of income in respect of
15 a decedent under section 691.

16 “(2) LOSS.—Any loss on the disposition of an
17 investment services partnership interest shall be
18 treated as an ordinary loss to the extent of the ex-
19 cess (if any) of—

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

24 “(B) the aggregate amount treated as or-
25 dinary loss under subsection (a) with respect to

1 such interest for all partnership taxable years
2 to which this section applies.

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

8 “(A) the taxpayer makes an irrevocable
9 election to treat the partnership interest re-
10 ceived in the exchange as an investment serv-
11 ices partnership interest, and

12 “(B) the taxpayer agrees to comply with
13 such reporting and recordkeeping requirements
14 as the Secretary may prescribe.

15 “(4) DISTRIBUTIONS OF PARTNERSHIP PROP-
16 PERTY.—

17 “(A) IN GENERAL.—In the case of any dis-
18 tribution of property by a partnership with re-
19 spect to any investment services partnership in-
20 terest held by a partner, the partner receiving
21 such property shall recognize gain equal to the
22 excess (if any) of—

23 “(i) the fair market value of such
24 property at the time of such distribution,
25 over

1 “(ii) the adjusted basis of such prop-
2 erty in the hands of such partner (deter-
3 mined without regard to subparagraph
4 (C)).

5 “(B) TREATMENT OF GAIN AS ORDINARY
6 INCOME.—Any gain recognized by such partner
7 under subparagraph (A) shall be treated as or-
8 dinary income to the same extent and in the
9 same manner as the increase in such partner’s
10 distributive share of the taxable income of the
11 partnership would be treated under subsection
12 (a) if, immediately prior to the distribution, the
13 partnership had sold the distributed property at
14 fair market value and all of the gain from such
15 disposition were allocated to such partner. For
16 purposes of applying subsection (a)(2), any gain
17 treated as ordinary income under this subpara-
18 graph shall be treated as an amount treated as
19 ordinary income under subsection (a)(1)(A).

20 “(C) ADJUSTMENT OF BASIS.—In the case
21 a distribution to which subparagraph (A) ap-
22 plies, the basis of the distributed property in
23 the hands of the distributee partner shall be the
24 fair market value of such property.

1 “(D) SPECIAL RULES WITH RESPECT TO
2 MERGERS AND DIVISIONS.—In the case of a
3 taxpayer which satisfies requirements similar to
4 the requirements of subparagraphs (A) and (B)
5 of paragraph (3), this paragraph and paragraph
6 (1)(A)(ii) shall not apply to the distribution of
7 a partnership interest if such distribution is in
8 connection with a contribution (or deemed con-
9 tribution) of any property of the partnership to
10 which section 721 applies pursuant to a trans-
11 action described in paragraph (2) of section
12 708(b).

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

15 “(1) IN GENERAL.—The term ‘investment serv-
16 ices partnership interest’ means any interest in an
17 investment partnership acquired or held by any per-
18 son in connection with the conduct of a trade or
19 business described in paragraph (2) by such person
20 (or any person related to such person). An interest
21 in an investment partnership held by any person—

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

1 “(B) shall not cease to be an investment
2 services partnership interest merely because
3 such person holds such interest other than in
4 connection with such a trade or business, and

5 “(C) shall be treated as an investment
6 services partnership interest if acquired from a
7 related person in whose hands such interest was
8 an investment services partnership interest.

9 “(2) BUSINESSES TO WHICH THIS SECTION AP-
10 PLIES.—A trade or business is described in this
11 paragraph if such trade or business primarily in-
12 volves the performance of any of the following serv-
13 ices with respect to assets held (directly or indi-
14 rectly) by one or more investment partnerships re-
15 ferred to in paragraph (1):

16 “(A) Advising as to the advisability of in-
17 vesting in, purchasing, or selling any specified
18 asset.

19 “(B) Managing, acquiring, or disposing of
20 any specified asset.

21 “(C) Arranging financing with respect to
22 acquiring specified assets.

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

25 “(3) INVESTMENT PARTNERSHIP.—

1 “(A) IN GENERAL.—The term ‘investment
2 partnership’ means any partnership if, at the
3 end of any two consecutive calendar quarters
4 ending after the date of enactment of this sec-
5 tion—

6 “(i) substantially all of the assets of
7 the partnership are specified assets (deter-
8 mined without regard to any section 197
9 intangible within the meaning of section
10 197(d)), and

11 “(ii) less than 75 percent of the cap-
12 ital of the partnership is attributable to
13 qualified capital interests which constitute
14 property held in connection with a trade or
15 business of the owner of such interest.

16 “(B) LOOK-THROUGH OF CERTAIN WHOL-
17 LY OWNED ENTITIES FOR PURPOSES OF DETER-
18 MINING ASSETS OF THE PARTNERSHIP.—

19 “(i) IN GENERAL.—For purposes of
20 determining the assets of a partnership
21 under subparagraph (A)(i)—

22 “(I) any interest in a specified
23 entity shall not be treated as an asset
24 of such partnership, and

1 “(II) such partnership shall be
2 treated as holding its proportionate
3 share of each of the assets of such
4 specified entity.

5 “(ii) SPECIFIED ENTITY.—For pur-
6 poses of clause (i), the term ‘specified enti-
7 ty’ means, with respect to any partnership
8 (hereafter referred to as the upper-tier
9 partnership), any person which engages in
10 the same trade or business as the upper-
11 tier partnership and is—

12 “(I) a partnership all of the cap-
13 ital and profits interests of which are
14 held directly or indirectly by the
15 upper-tier partnership, or

16 “(II) a foreign corporation which
17 does not engage in a trade or business
18 in the United States and all of the
19 stock of which is held directly or indi-
20 rectly by the upper-tier partnership.

21 “(C) SPECIAL RULES FOR DETERMINING
22 IF PROPERTY HELD IN CONNECTION WITH
23 TRADE OR BUSINESS.—

24 “(i) IN GENERAL.—Except as other-
25 wise provided by the Secretary, solely for

1 purposes of determining whether any inter-
2 est in a partnership constitutes property
3 held in connection with a trade or business
4 under subparagraph (A)(ii)—

5 “(I) a trade or business of any
6 person closely related to the owner of
7 such interest shall be treated as a
8 trade or business of such owner,

9 “(II) such interest shall be treat-
10 ed as held by a person in connection
11 with a trade or business during any
12 taxable year if such interest was so
13 held by such person during any 3 tax-
14 able years preceding such taxable
15 year, and

16 “(III) paragraph (5)(B) shall not
17 apply.

18 “(ii) CLOSELY RELATED PERSONS.—
19 For purposes of clause (i)(I), a person
20 shall be treated as closely related to an-
21 other person if, taking into account the
22 rules of section 267(c), the relationship be-
23 tween such persons is described in—

24 “(I) paragraph (1) or (9) of sec-
25 tion 267(b), or

1 “(II) section 267(b)(4), but solely
2 in the case of a trust with respect to
3 which each current beneficiary is the
4 grantor or a person whose relationship
5 to the grantor is described in para-
6 graph (1) or (9) of section 267(b).

7 “(D) ANTIABUSE RULES.—The Secretary
8 may issue regulations or other guidance which
9 prevent the avoidance of the purposes of sub-
10 paragraph (A), including regulations or other
11 guidance which treat convertible and contingent
12 debt (and other debt having the attributes of
13 equity) as a capital interest in the partnership.

14 “(E) CONTROLLED GROUPS OF ENTI-
15 TIES.—

16 “(i) IN GENERAL.—In the case of a
17 controlled group of entities, if an interest
18 in the partnership received in exchange for
19 a contribution to the capital of the part-
20 nership by any member of such controlled
21 group would (in the hands of such mem-
22 ber) constitute property held in connection
23 with a trade or business, then any interest
24 in such partnership held by any member of
25 such group shall be treated for purposes of

1 subparagraph (A) as constituting (in the
2 hands of such member) property held in
3 connection with a trade or business.

4 “(ii) CONTROLLED GROUP OF ENTI-
5 TIES.—For purposes of clause (i), the term
6 ‘controlled group of entities’ means a con-
7 trolled group of corporations as defined in
8 section 1563(a)(1), applied without regard
9 to subsections (a)(4) and (b)(2) of section
10 1563. A partnership or any other entity
11 (other than a corporation) shall be treated
12 as a member of a controlled group of enti-
13 ties if such entity is controlled (within the
14 meaning of section 954(d)(3)) by members
15 of such group (including any entity treated
16 as a member of such group by reason of
17 this sentence).

18 “(F) SPECIAL RULE FOR CORPORA-
19 TIONS.—For purposes of this paragraph, in the
20 case of a corporation, the determination of
21 whether property is held in connection with a
22 trade or business shall be determined as if the
23 taxpayer were an individual.

24 “(4) SPECIFIED ASSET.—The term ‘specified
25 asset’ means securities (as defined in section

1 475(c)(2) without regard to the last sentence there-
2 of), real estate held for rental or investment, inter-
3 ests in partnerships, commodities (as defined in sec-
4 tion 475(e)(2)), cash or cash equivalents, or options
5 or derivative contracts with respect to any of the
6 foregoing.

7 “(5) RELATED PERSONS.—

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

12 “(B) ATTRIBUTION OF PARTNER SERV-
13 ICES.—Any service described in paragraph (2)
14 which is provided by a partner of a partnership
15 shall be treated as also provided by such part-
16 nership.

17 “(d) EXCEPTION FOR CERTAIN CAPITAL INTER-
18 ESTS.—

19 “(1) IN GENERAL.—In the case of any portion
20 of an investment services partnership interest which
21 is a qualified capital interest, all items of gain and
22 loss (and any dividends) which are allocated to such
23 qualified capital interest shall not be taken into ac-
24 count under subsection (a) if—

1 “(A) allocations of items are made by the
2 partnership to such qualified capital interest in
3 the same manner as such allocations are made
4 to other qualified capital interests held by part-
5 ners who do not provide any services described
6 in subsection (c)(2) and who are not related to
7 the partner holding the qualified capital inter-
8 est, and

9 “(B) the allocations made to such other in-
10 terests are significant compared to the alloca-
11 tions made to such qualified capital interest.

12 “(2) AUTHORITY TO PROVIDE EXCEPTIONS TO
13 ALLOCATION REQUIREMENTS.—To the extent pro-
14 vided by the Secretary in regulations or other guid-
15 ance—

16 “(A) ALLOCATIONS TO PORTION OF QUALI-
17 FIED CAPITAL INTEREST.—Paragraph (1) may
18 be applied separately with respect to a portion
19 of a qualified capital interest.

20 “(B) NO OR INSIGNIFICANT ALLOCATIONS
21 TO NONSERVICE PROVIDERS.—In any case in
22 which the requirements of paragraph (1)(B) are
23 not satisfied, items of gain and loss (and any
24 dividends) shall not be taken into account under
25 subsection (a) to the extent that such items are

1 properly allocable under such regulations or
2 other guidance to qualified capital interests.

3 “(C) ALLOCATIONS TO SERVICE PRO-
4 VIDERS’ QUALIFIED CAPITAL INTERESTS WHICH
5 ARE LESS THAN OTHER ALLOCATIONS.—Alloca-
6 tions shall not be treated as failing to meet the
7 requirement of paragraph (1)(A) merely be-
8 cause the allocations to the qualified capital in-
9 terest represent a lower return than the alloca-
10 tions made to the other qualified capital inter-
11 ests referred to in such paragraph.

12 “(3) SPECIAL RULE FOR CHANGES IN SERVICES
13 AND CAPITAL CONTRIBUTIONS.—In the case of an
14 interest in a partnership which was not an invest-
15 ment services partnership interest and which, by
16 reason of a change in the services with respect to as-
17 sets held (directly or indirectly) by the partnership
18 or by reason of a change in the capital contributions
19 to such partnership, becomes an investment services
20 partnership interest, the qualified capital interest of
21 the holder of such partnership interest immediately
22 after such change shall not, for purposes of this sub-
23 section, be less than the fair market value of such
24 interest (determined immediately before such
25 change).

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

10 “(5) EXCEPTION FOR NO-SELF-CHARGED
11 CARRY AND MANAGEMENT FEE PROVISIONS.—Ex-
12 cept as otherwise provided by the Secretary, an in-
13 terest shall not fail to be treated as satisfying the
14 requirement of paragraph (1)(A) merely because the
15 allocations made by the partnership to such interest
16 do not reflect the cost of services described in sub-
17 section (c)(2) which are provided (directly or indi-
18 rectly) to the partnership by the holder of such in-
19 terest (or a related person).

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

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

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

11 “(7) QUALIFIED CAPITAL INTEREST.—For pur-
12 poses of this section—

13 “(A) IN GENERAL.—The term ‘qualified
14 capital interest’ means so much of a partner’s
15 interest in the capital of the partnership as is
16 attributable to—

17 “(i) the fair market value of any
18 money or other property contributed to the
19 partnership in exchange for such interest
20 (determined without regard to section
21 752(a)),

22 “(ii) any amounts which have been in-
23 cluded in gross income under section 83
24 with respect to the transfer of such inter-
25 est, and

1 “(iii) the excess (if any) of—

2 “(I) any items of income and
3 gain taken into account under section
4 702 with respect to such interest, over

5 “(II) any items of deduction and
6 loss so taken into account.

7 “(B) ADJUSTMENT TO QUALIFIED CAPITAL
8 INTEREST.—

9 “(i) DISTRIBUTIONS AND LOSSES.—

10 The qualified capital interest shall be re-
11 duced by distributions from the partner-
12 ship with respect to such interest and by
13 the excess (if any) of the amount described
14 in subparagraph (A)(iii)(II) over the
15 amount described in subparagraph
16 (A)(iii)(I).

17 “(ii) SPECIAL RULE FOR CONTRIBU-
18 TIONS OF PROPERTY.—In the case of any
19 contribution of property described in sub-
20 paragraph (A)(i) with respect to which the
21 fair market value of such property is not
22 equal to the adjusted basis of such prop-
23 erty immediately before such contribution,
24 proper adjustments shall be made to the
25 qualified capital interest to take into ac-

1 count such difference consistent with such
2 regulations or other guidance as the Sec-
3 retary may provide.

4 “(C) MERGER, CONSOLIDATION, DIVISION,
5 ETC., DISREGARDED.—No increase or decrease
6 in the qualified capital interest of any partner
7 shall result from a merger, consolidation, or di-
8 vision described in section 708, or any similar
9 transaction.

10 “(8) TREATMENT OF CERTAIN LOANS.—

11 “(A) PROCEEDS OF PARTNERSHIP LOANS
12 NOT TREATED AS QUALIFIED CAPITAL INTER-
13 EST OF SERVICE PROVIDING PARTNERS.—For
14 purposes of this subsection, an investment serv-
15 ices partnership interest shall not be treated as
16 a qualified capital interest to the extent that
17 such interest is acquired in connection with the
18 proceeds of any loan or other advance made or
19 guaranteed, directly or indirectly, by any other
20 partner or the partnership (or any person re-
21 lated to any such other partner or the partner-
22 ship). The preceding sentence shall not apply to
23 the extent the loan or other advance is repaid
24 before the date of the enactment of this section
25 unless such repayment is made with the pro-

1 ceeds of a loan or other advance described in
2 the preceding sentence.

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

15 “(9) SPECIAL RULE FOR QUALIFIED FAMILY
16 PARTNERSHIPS.—

17 “(A) IN GENERAL.—In the case of any
18 specified family partnership interest, paragraph
19 (1)(A) shall be applied without regard to the
20 phrase ‘and who are not related to the partner
21 holding the qualified capital interest’.

22 “(B) SPECIFIED FAMILY PARTNERSHIP IN-
23 TEREST.—For purposes of this paragraph, the
24 term ‘specified family partnership interest’

1 means any investment services partnership in-
2 terest if—

3 “(i) such interest is an interest in a
4 qualified family partnership,

5 “(ii) such interest is held by a natural
6 person or by a trust with respect to which
7 each beneficiary is a grantor or a person
8 whose relationship to the grantor is de-
9 scribed in section 267(b)(1), and

10 “(iii) all other interests in such quali-
11 fied family partnership with respect to
12 which significant allocations are made
13 (within the meaning of paragraph (1)(B)
14 and in comparison to the allocations made
15 to the interest described in clause (ii)) are
16 held by persons who—

17 “(I) are related to the natural
18 person or trust referred to in clause
19 (ii), or

20 “(II) provide services described
21 in subsection (c)(2).

22 “(C) QUALIFIED FAMILY PARTNERSHIP.—

23 For purposes of this paragraph, the term
24 ‘qualified family partnership’ means any part-
25 nership if—

1 “(i) all of the capital and profits in-
2 terests of such partnership are held by—

3 “(I) specified family members,

4 “(II) any person closely related
5 (within the meaning of subsection
6 (c)(3)(C)(ii)) to a specified family
7 member, or

8 “(III) any other person (not de-
9 scribed in subclause (I) or (II)) if
10 such interest is an investment services
11 partnership interest with respect to
12 such person, and

13 “(ii) such partnership does not hold
14 itself out to the public as an investment
15 advisor.

16 “(D) SPECIFIED FAMILY MEMBERS.—For
17 purposes of subparagraph (C), individuals shall
18 be treated as specified family members if such
19 individuals would be treated as one person
20 under the rules of section 1361(c)(1) if the ap-
21 plicable date (within the meaning of subpara-
22 graph (B)(iii) thereof) were the latest of—

23 “(i) the date of the establishment of
24 the partnership,

1 “(ii) the earliest date that the com-
2 mon ancestor holds a capital or profits in-
3 terest in the partnership, or

4 “(iii) the date of the enactment of this
5 section.

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

8 “(1) IN GENERAL.—If—

9 “(A) a person performs (directly or indi-
10 rectly) investment management services for any
11 investment entity,

12 “(B) such person holds (directly or indi-
13 rectly) a disqualified interest with respect to
14 such entity, and

15 “(C) the value of such interest (or pay-
16 ments thereunder) is substantially related to
17 the amount of income or gain (whether or not
18 realized) from the assets with respect to which
19 the investment management services are per-
20 formed,

21 any income or gain with respect to such interest
22 shall be treated as ordinary income. Rules similar to
23 the rules of subsections (a)(5) and (d) shall apply
24 for purposes of this subsection.

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

3 “(A) DISQUALIFIED INTEREST.—

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

7 “(I) any interest in such entity
8 other than indebtedness,

9 “(II) convertible or contingent
10 debt of such entity,

11 “(III) any option or other right
12 to acquire property described in sub-
13 clause (I) or (II), and

14 “(IV) any derivative instrument
15 entered into (directly or indirectly)
16 with such entity or any investor in
17 such entity.

18 “(ii) EXCEPTIONS.—Such term shall
19 not include—

20 “(I) a partnership interest,

21 “(II) except as provided by the
22 Secretary, any interest in a taxable
23 corporation, and

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

1 “(B) TAXABLE CORPORATION.—The term
2 ‘taxable corporation’ means—

3 “(i) a domestic C corporation, or

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

6 “(I) effectively connected with
7 the conduct of a trade or business in
8 the United States, or

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

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

16 “(D) INVESTMENT ENTITY.—The term ‘in-
17 vestment entity’ means any entity which, if it
18 were a partnership, would be an investment
19 partnership.

20 “(f) EXCEPTION FOR DOMESTIC C CORPORATIONS.—
21 Except as otherwise provided by the Secretary, in the case
22 of a domestic C corporation—

23 “(1) subsections (a) and (b) shall not apply to
24 any item allocated to such corporation with respect
25 to any investment services partnership interest (or

1 to any gain or loss with respect to the disposition of
2 such an interest), and

3 “(2) subsection (e) shall not apply.

4 “(g) REGULATIONS.—The Secretary shall prescribe
5 such regulations or other guidance as is necessary or ap-
6 propriate to carry out the purposes of this section, includ-
7 ing regulations or other guidance to—

8 “(1) require such reporting and recordkeeping
9 by any person in such manner and at such time as
10 the Secretary may prescribe for purposes of enabling
11 the partnership to meet the requirements of section
12 6031 with respect to any item described in section
13 702(a)(9),

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

19 “(3) prevent the avoidance of the purposes of
20 this section (including through the use of qualified
21 family partnerships), and

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

1 “(h) CROSS REFERENCE.—For 40-percent penalty
2 on certain underpayments due to the avoidance of this sec-
3 tion, see section 6662.”.

4 (b) APPLICATION OF SECTION 751 TO INDIRECT DIS-
5 POSITIONS OF INVESTMENT SERVICES PARTNERSHIP IN-
6 TERESTS.—

7 (1) IN GENERAL.—Subsection (a) of section
8 751 of such Code is amended by striking “or” at the
9 end of paragraph (1), by inserting “or” at the end
10 of paragraph (2), and by inserting after paragraph
11 (2) the following new paragraph:

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

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

20 “(iii) investment services partnership
21 interests held by the partnership,”.

22 (3) APPLICATION OF SPECIAL RULES IN THE
23 CASE OF TIERED PARTNERSHIPS.—Subsection (f) of
24 section 751 of such Code is amended—

1 (A) by striking “or” at the end of para-
2 graph (1), by inserting “or” at the end of para-
3 graph (2), and by inserting after paragraph (2)
4 the following new paragraph:

5 “(3) an investment services partnership interest
6 held by the partnership,” and

7 (B) by striking “partner.” and inserting
8 “partner (other than a partnership in which it
9 holds an investment services partnership inter-
10 est).”.

11 (4) INVESTMENT SERVICES PARTNERSHIP IN-
12 TERESTS; QUALIFIED CAPITAL INTERESTS.—Section
13 751 of such Code is amended by adding at the end
14 the following new subsection:

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

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

20 “(2) ADJUSTMENTS FOR QUALIFIED CAPITAL
21 INTERESTS.—The amount to which subsection (a)
22 applies by reason of paragraph (3) thereof shall not
23 include so much of such amount as is attributable
24 to any portion of the investment services partnership
25 interest which is a qualified capital interest (deter-

1 mined under rules similar to the rules of section
2 710(d)).

3 “(3) EXCEPTION FOR PUBLICLY TRADED PART-
4 NERSHIPS.—Except as otherwise provided by the
5 Secretary, in the case of an exchange of an interest
6 in a publicly traded partnership (as defined in sec-
7 tion 7704) to which subsection (a) applies—

8 “(A) this section shall be applied without
9 regard to subsections (a)(3), (b)(1)(A)(iii), and
10 (f)(3), and

11 “(B) such partnership shall be treated as
12 owning its proportionate share of the property
13 of any other partnership in which it is a part-
14 ner.

15 “(4) RECOGNITION OF GAINS.—Any gain with
16 respect to which subsection (a) applies by reason of
17 paragraph (3) thereof shall be recognized notwith-
18 standing any other provision of this title.

19 “(5) COORDINATION WITH INVENTORY
20 ITEMS.—An investment services partnership interest
21 held by the partnership shall not be treated as an
22 inventory item of the partnership.

23 “(6) PREVENTION OF DOUBLE COUNTING.—
24 Under regulations or other guidance prescribed by

1 the Secretary, subsection (a)(3) shall not apply with
 2 respect to any amount to which section 710 applies.

3 “(7) VALUATION METHODS.—The Secretary
 4 shall prescribe regulations or other guidance which
 5 provide the acceptable methods for valuing invest-
 6 ment services partnership interests for purposes of
 7 this section.”.

8 (c) TREATMENT FOR PURPOSES OF SECTION
 9 7704.—Subsection (d) of section 7704 of such Code is
 10 amended by adding at the end the following new para-
 11 graph:

12 “(6) INCOME FROM CERTAIN CARRIED INTER-
 13 ESTS NOT QUALIFIED.—

14 “(A) IN GENERAL.—Specified carried in-
 15 terest income shall not be treated as qualifying
 16 income.

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

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

21 “(I) any item of income or gain
 22 allocated to an investment services
 23 partnership interest (as defined in
 24 section 710(c)) held by the partner-
 25 ship,

1 “(II) any gain on the disposition
2 of an investment services partnership
3 interest (as so defined) or a partner-
4 ship interest to which (in the hands of
5 the partnership) section 751 applies,
6 and

7 “(III) any income or gain taken
8 into account by the partnership under
9 subsection (b)(4) or (e) of section
10 710.

11 “(ii) EXCEPTION FOR QUALIFIED CAP-
12 ITAL INTERESTS.—A rule similar to the
13 rule of section 710(d) shall apply for pur-
14 poses of clause (i).

15 “(C) COORDINATION WITH OTHER PROVI-
16 SIONS.—Subparagraph (A) shall not apply to
17 any item described in paragraph (1)(E) (or so
18 much of paragraph (1)(F) as relates to para-
19 graph (1)(E)).

20 “(D) SPECIAL RULES FOR CERTAIN PART-
21 NERSHIPS.—

22 “(i) CERTAIN PARTNERSHIPS OWNED
23 BY REAL ESTATE INVESTMENT TRUSTS.—
24 Subparagraph (A) shall not apply in the

1 case of a partnership which meets each of
2 the following requirements:

3 “(I) Such partnership is treated
4 as publicly traded under this section
5 solely by reason of interests in such
6 partnership being convertible into in-
7 terests in a real estate investment
8 trust which is publicly traded.

9 “(II) Fifty percent or more of
10 the capital and profits interests of
11 such partnership are owned, directly
12 or indirectly, at all times during the
13 taxable year by such real estate in-
14 vestment trust (determined with the
15 application of section 267(c)).

16 “(III) Such partnership meets
17 the requirements of paragraphs (2),
18 (3), and (4) of section 856(c).

19 “(ii) CERTAIN PARTNERSHIPS OWN-
20 ING OTHER PUBLICLY TRADED PARTNER-
21 SHIPS.—Subparagraph (A) shall not apply
22 in the case of a partnership which meets
23 each of the following requirements:

24 “(I) Substantially all of the as-
25 sets of such partnership consist of in-

1 terests in one or more publicly traded
2 partnerships (determined without re-
3 gard to subsection (b)(2)).

4 “(II) Substantially all of the in-
5 come of such partnership is ordinary
6 income or section 1231 gain (as de-
7 fined in section 1231(a)(3)).

8 “(E) TRANSITIONAL RULE.—Subpara-
9 graph (A) shall not apply to any taxable year
10 of the partnership beginning before the date
11 which is 10 years after the date of the enact-
12 ment of this paragraph.”.

13 (d) IMPOSITION OF PENALTY ON UNDERPAY-
14 MENTS.—

15 (1) IN GENERAL.—Subsection (b) of section
16 6662 of such Code is amended by inserting after
17 paragraph (7) the following new paragraph:

18 “(8) The application of section 710(e) or the
19 regulations or other guidance prescribed under sec-
20 tion 710(g) to prevent the avoidance of the purposes
21 of section 710.”.

22 (2) AMOUNT OF PENALTY.—

23 (A) IN GENERAL.—Section 6662 of such
24 Code is amended by adding at the end the fol-
25 lowing new subsection:

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

7 (B) CONFORMING AMENDMENT.—Subpara-
8 graph (B) of section 6662A(e)(2) of such Code
9 is amended by striking “or (i)” and inserting “,
10 (i), or (k)”.

11 (3) SPECIAL RULES FOR APPLICATION OF REA-
12 SONABLE CAUSE EXCEPTION.—Subsection (c) of sec-
13 tion 6664 of such Code is amended—

14 (A) by redesignating paragraphs (3) and
15 (4) as paragraphs (4) and (5), respectively,

16 (B) by striking “paragraph (3)” in para-
17 graph (5)(A), as so redesignated, and inserting
18 “paragraph (4)”, and

19 (C) by inserting after paragraph (2) the
20 following new paragraph:

21 “(3) SPECIAL RULE FOR UNDERPAYMENTS AT-
22 TRIBUTABLE TO INVESTMENT MANAGEMENT SERV-
23 ICES.—

24 “(A) IN GENERAL.—Paragraph (1) shall
25 not apply to any portion of an underpayment to

1 which section 6662 applies by reason of sub-
2 section (b)(8) unless—

3 “(i) the relevant facts affecting the
4 tax treatment of the item are adequately
5 disclosed,

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

8 “(iii) the taxpayer reasonably believed
9 that such treatment was more likely than
10 not the proper treatment.

11 “(B) RULES RELATING TO REASONABLE
12 BELIEF.—Rules similar to the rules of sub-
13 section (d)(3) shall apply for purposes of sub-
14 paragraph (A)(iii).”.

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

18 (1) INTERNAL REVENUE CODE.—

19 (A) IN GENERAL.—Section 1402(a) of
20 such Code is amended by striking “and” at the
21 end of paragraph (16), by striking the period at
22 the end of paragraph (17) and inserting “;
23 and”, and by inserting after paragraph (17) the
24 following new paragraph:

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

10 (B) INVESTMENT SERVICES PARTNERSHIP
11 INCOME OR LOSS.—Section 1402 of such Code
12 is amended by adding at the end the following
13 new subsection:

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

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

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

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

1 “(C) the amounts treated as realized from
2 the sale or exchange of property other than a
3 capital asset under section 751 with respect to
4 such interest.

5 “(2) EXCEPTION FOR QUALIFIED CAPITAL IN-
6 TERESTS.—A rule similar to the rule of section
7 710(d) shall apply for purposes of applying para-
8 graph (1)(B).”.

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

15 “(17) Notwithstanding the preceding provisions
16 of this subsection, in the case of any individual en-
17 gaged in the trade or business of providing services
18 described in section 710(c)(2) of the Internal Rev-
19 enue Code of 1986 with respect to any entity, invest-
20 ment services partnership income or loss (as defined
21 in section 1402(m) of such Code) shall be taken into
22 account in determining the net earnings from self-
23 employment of such individual.”.

24 (f) SEPARATE ACCOUNTING BY PARTNER.—Section
25 702(a) of the Internal Revenue Code of 1986 is amended

1 by striking “and” at the end of paragraph (7), by striking
2 the period at the end of paragraph (8) and inserting “,
3 and”, and by inserting after paragraph (8) the following:

4 “(9) any amount treated as ordinary income or
5 loss under subsection (a), (b), or (e) of section
6 710.”.

7 (g) CONFORMING AMENDMENTS.—

8 (1) Subsection (d) of section 731 of such Code
9 is amended by inserting “section 710(b)(4) (relating
10 to distributions of partnership property),” after “to
11 the extent otherwise provided by”.

12 (2) Section 741 of such Code is amended by in-
13 serting “or section 710 (relating to special rules for
14 partners providing investment management services
15 to partnerships)” before the period at the end.

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

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

19 (4) Part IV of subchapter O of chapter 1 of
20 such Code is amended by striking section 1061, and
21 the table of sections for such part is amended by
22 striking the item relating to section 1061.

23 (h) EFFECTIVE DATE.—

1 (1) IN GENERAL.—Except as otherwise pro-
2 vided in this subsection, the amendments made by
3 this section shall apply to taxable years ending after
4 the date of the enactment of this Act.

5 (2) PARTNERSHIP TAXABLE YEARS WHICH IN-
6 CLUDE EFFECTIVE DATE.—In applying section
7 710(a) of the Internal Revenue Code of 1986 (as
8 added by this section) in the case of any partnership
9 taxable year which includes the date of the enact-
10 ment of this Act, the amount of the net capital gain
11 referred to in such section shall be treated as being
12 the lesser of the net capital gain for the entire part-
13 nership taxable year or the net capital gain deter-
14 mined by only taking into account items attributable
15 to the portion of the partnership taxable year which
16 is after such date.

17 (3) DISPOSITIONS OF PARTNERSHIP INTER-
18 ESTS.—

19 (A) IN GENERAL.—Section 710(b) of such
20 Code (as added by this section) shall apply to
21 dispositions and distributions after the date of
22 the enactment of this Act.

23 (B) INDIRECT DISPOSITIONS.—The amend-
24 ments made by subsection (b) shall apply to

1 transactions after the date of the enactment of
2 this Act.

3 (4) OTHER INCOME AND GAIN IN CONNECTION
4 WITH INVESTMENT MANAGEMENT SERVICES.—Sec-
5 tion 710(e) of such Code (as added by this section)
6 shall take effect on the date of the enactment of this
7 Act.

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