

MEMORANDUM

To: Reporters and Editors
From: Carol Guthrie for Finance Committee Chairman Max Baucus (D-Mont.)
Jill Gerber for Finance Committee Ranking Republican Chuck Grassley (R-Iowa)
Re: purpose of legislation regarding publicly traded partnerships

Finance Committee Chairman Baucus and Ranking Republican Grassley commented late today on White House and Treasury Department reaction to their legislation regarding the taxation of some publicly traded partnerships. On June 14, the Finance leaders introduced legislation to clarify the 1987 law that requires corporate taxation of all publicly traded partnerships, affirming that publicly traded partnerships that directly or indirectly derive income from investment adviser or asset management services are not entitled to an exemption from the corporate tax that is available to firms whose income is at least 90 percent or passive – derived from dividends or royalties, for instance.

“Our legislation is meant to make sure that tax laws are applied fairly across the board. With few exceptions, all publicly traded partnerships have been taxed as corporations for the past 20 years. Far from singling out one industry for punishment, we’re simply clarifying that private equity firms and similar businesses should not receive special treatment in the tax code. No one group of businesses should gain an edge over its competitors by claiming a tax status for which they do not qualify. Applying our tax laws fairly and according to precedent will make sure that American business continues to thrive and grow across all sectors.”

The Baucus-Grassley bill does not address the separate issue of carried interest. Below please find the June 14 press release outlining the proposed legislation. Additionally, these links will be useful in your reporting:

<http://www.finance.senate.gov/sitepages/leg/LEG%202007/Leg%20110%20061407.pdf> – technical explanation of issues

<http://www.finance.senate.gov/press/Bpress/2007press/prb061407c.pdf> - Baucus statement

<http://www.finance.senate.gov/press/Gpress/2007/prg061407b.pdf> - Grassley statement of introduction

For Immediate Release
June 14, 2007

Contact: Carol Guthrie (Baucus)
Jill Gerber (Grassley)

BAUCUS-GRASSLEY BILL ADDRESSES PUBLICLY TRADED PARTNERSHIPS
Senators seek to clarify tax treatment for partnerships acting as corporations

Washington, DC – U.S. Senators Max Baucus (D-Mont.) and Chuck Grassley (R-Iowa), Chairman and Ranking Republican Member of the Senate Finance Committee, introduced legislation today that would tax as corporations all publicly traded partnerships that directly or indirectly derive income from investment adviser or asset management services. Private equity firms, for instance, derive most of their income directly or indirectly from investment adviser or asset management services.

“The nature of investment vehicles is changing right before our eyes, and the tax code must keep up with the times,” said Baucus. “Creative new structures for investment vehicles may blur the lines for the tax treatment of income. We must make the law clear and apply the law fairly, or risk

the erosion of our corporate tax base. If a publicly traded partnership makes its money by providing financial services, that active business should be taxed as a corporation. ”

“Right now, some businesses are crossing the line between reasonably lowering their tax burden and pretending to be something they’re not to avoid most, if not all, corporate taxes,” said Grassley. “A hallmark of corporate status is access to the capital markets. It’s unfair to allow a publicly traded company to act like a corporation but not pay corporate tax, contrary to the intent of the tax code. We don’t have a workable tax code if we don’t have structural integrity. If left unaddressed, the tax concerns presented by the public offerings of investment managers, like private equity and hedge fund management firms, could fundamentally erode the corporate tax base. That would leave other individuals and business taxpayers with a greater share of the nation’s tax burden.”

Corporations and their shareholders are subject to two levels of tax. Corporations pay taxes, and shareholders pay taxes on distributions received from the corporations. In contrast, partnerships and their partners are subject to only one level of tax. Partners are taxed on their distributive shares of income.

In 1987, Congress became concerned that some partnerships with interests traded on public exchanges were essentially operating as corporations, but avoiding corporate tax. Congress feared that such publicly traded partnerships would erode the corporate tax base and gain an unfair advantage over companies operating as corporations. In response to these concerns, Congress updated the law to generally tax publicly traded partnerships as corporations.

An exception to that general rule exempts publicly traded partnerships from corporate taxation if they can demonstrate that at least 90 percent of their income is passive – for instance, from dividends, interest, or royalties rather than the provision of services. But today, new structuring of investment vehicles may make it possible for partnerships to argue that their income is passive, when it is actually produced by actively providing financial services. In filing this legislation, Baucus and Grassley are seeking to further clarify the law, both to appropriately preserve the corporate tax base and to assure that such publicly traded partnerships do not gain an unfair advantage over established financial services corporations.

Upon passage, the bill will be effective as of the date of introduction.

Baucus and Grassley do not believe that recent and proposed public offerings of private equity and hedge fund management firms are consistent with the intent of the existing rules regarding publicly traded partnerships. In addition to filing this legislation, Baucus and Grassley have written to Secretary Paulson, asking for Treasury’s views on this issue and what plans Treasury and the IRS have to issue guidance and enforce Congressional intent. A copy of that letter and an additional letter were also sent to SEC Commissioner Cox.