Anchin Alert

**Anchin, Block & Anchin LLP**
**Accountants and Advisors**

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## Proposed Carried Interest Bills Still Alive

Earlier this year, we shared information with you about several proposed bills that would increase taxes due on investment performance allocations, commonly known as carried interest. Carried interest is the share of profits that fund managers receive in exchange for managing investments. The controversy over carried interest arises because the current tax rules allow managers to pay taxes on portions of the carried interest allocation at the (long term) capital gains rate rather than the higher tax rate that normally applies to ordinary income.

Some state lawmakers want to change the current system and impose additional taxes on carried interest. Here's the latest on their progress.

**State Bills**

Six state legislatures are considering bills to increase taxes on carried interest: Connecticut, Illinois, Massachusetts, New Jersey, New York, and Rhode Island.

Illinois

On May 23rd, the Illinois Senate passed a bill that would impose a 20% surcharge on the tax on carried interest for state residents. As of this date, the Illinois House is still considering the measure – nothing has been finalized yet.

While Governor Rauner had indicated that he would have vetoed any new taxes on carried interest, as the Illinois budget crisis deepened, rumors were that he might be wavering in his commitment. As this is the state bill farthest along in the process, it is the one to watch.

The Other States

Connecticut, Massachusetts, New Jersey, New York, and Rhode Island are all working on bills that would impose a 19% surtax on the tax on carried interest income for state residents. However, if the federal government makes a change and starts taxing carried interest as ordinary income, the states would then eliminate their surtaxes.

The state legislatures realize they must work together to pass an effective surtax. If only one state increases taxes on carried interest, it would be relatively easy for fund managers to move to a neighboring state to avoid paying the increased tax. As a result, these state bills each have provisions stating that the new surtax on carried interest won't go into effect until the other four states also make the change.

To date, these state legislatures are still working on bills but have yet to vote. Therefore, as more time goes by, it seems highly unlikely that we will see increased state taxes in 2017.

**Federal Bill**

On May 2nd, Senator Tammy Baldwin and Representative Sander Levin announced "T*he Carried Interest Fairness Act of 2017*." If this federal bill passes, income from carried interest would be taxed as ordinary income. The goal of the bill is to make carried interest taxation a part of the upcoming tax reform debate.

President Trump supported increasing taxes on carried interest during his campaign but his current tax plan does not propose changes to the current capital gains rates. However, the plan does impose a 15% tax on pass through income. The bill seems unlikely to pass the Republican controlled House and Senate, thus continuing the uncertainty around the future taxation of carried interest at the Federal level.

Anchin will continue to monitor these (and other) bills and will keep you informed as legislation evolves in 2017.

For more information, contact your Anchin relationship partner, Jeffrey I. Rosenthal, or E. George Teixeira of Anchin's Financial Services Practice at 212.840.3456.

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