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KIRKLANDPEN

Private Equity Newsletter

September 14, 2011

Proposed Jobs Act Taxes 100% of Carried Interest as Ordinary Income

PENpoints

The proposed American Jobs Act of 2011, would, if enacted, tax 100% of carried interest income earned by an investment professional as ordinary income.

President Obama's proposed American Jobs Act of 2011, if enacted, would treat 100% of carried interest income earned by an investment professional providing investment services to an investment partnership as ordinary income, effective January 1, 2013.

In contrast, carried interest proposals considered by the House and Senate in 2010 would have treated between 50% and 75% of carried interest income as ordinary income, with the percentage recharacterized depending on various factors, including whether the income was earned in an initial two-year transition period, whether the income related to gain from the disposition of an asset held for more than 5 or 7 years, and whether the income related to the disposition of goodwill of an investment services partnership/LLC. For discussion of the 2010 House and Senate bills, see our previous *KirklandPENs* from 6/17/2010, 6/9/2010, 6/1/2010, and 5/21/2010.

Similar to the 2010 House and Senate bills, the proposed Jobs Act would also:

- apply to gains from the sale of a carried interest;
- apply to appreciation in property distributed in-kind to a carried interest;
- treat carried interest losses as ordinary losses, up to the amount of carried interest income previously taxed as ordinary income under the proposal;
- not apply to income and gain allocations to a "qualified capital interest" held by an investment professional, so long as the capital interest generally receives the same proportionate allocations as significant capital held by unrelated non-service partners (with certain limited exceptions), but such a "qualified capital interest" does not include a partnership/LLC interest purchased with the proceeds of a loan or other advance made or guaranteed, directly or indirectly, by the partnership/LLC or a partner/member (or a related person);
- subject carried interest income to Social Security and Medicare taxes; and
- treat as a corporation any publicly traded partnership earning significant income from carried interest (with the effective date deferred an additional 10 years from the general effective date).

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The proposed Jobs Act contains a number of highly technical changes to the wording of the 2010 House and Senate bills, although these changes do not appear to alter the basic thrust of the proposal to tax as ordinary income carried interest earned by an investment professional in a private equity fund, venture capital fund, hedge fund, mezzanine fund, or real estate partnership/LLC (apart from effective date and percentage of carried interest recharacterized).

If you have any questions about the matters addressed in this *KirklandPEN,* please contact the following Kirkland authors or your regular Kirkland contact.

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PENbriefs

Behind the Headlines—A Closer Look at Antitrust Reverse Termination Fees

In private equity sponsor-led transactions, antitrust risks generally are not material or complex. However, when a private equity firm sells a portfolio company to a competitor or a portfolio company makes a significant add-on acquisition, the deal's antitrust approval risks increase dramatically, making regulatory approval covenants—along with related closing conditions and termination provisions, including break-up fee triggers—the subject of painstaking negotiations. In addition, when a private equity firm sponsors a going-private transaction, it should consider how antitrust risks will impact potential strategic buyers and whether it can offer pro-target terms when formulating its bid and negotiating deal protection provisions.

The recent increase in strategic combinations, together with the more robust regulatory environment expected under the current administration, have focused dealmakers' attention on the antitrust terms of merger agreements, in particular the "efforts" covenant, the "divestiture" covenant, regulatory closing conditions, deal termination and fee triggers, and the features of the termination fee. These market developments affect not only strategic combinations, but also antitrust-sensitive sponsor-led deals. In their recent *Kirkland M&A Update*, Kirkland partners Timothy Muris, Christine Wilson and Daniel Wolf discuss several recent high-profile transactions with substantial antitrust implications, focusing on the interplay among the antitrust provisions of the respective merger agreements and their practical impact on the parties to those transactions.

PENnotes

Practising Law Institute's "Mergers & Acquisitions 2011: What You Need to Know Now"
Chicago - September 22-23, 2011

At this two-day program, top deal lawyers, general counsel, regulators and investment bankers will discuss trends and techniques in tender offers and private equity transactions, dramatic developments in Delaware law and shareholder litigation, continuing vitality of the poison pill and insight into the antitrust regulatory landscape. Kirkland partner R. Scott Falk, P.C., is a co-chair of this event. For more information, or to register for this event, please visit: http://www.pli.edu.

Kirkland & Ellis Seminar: "Structuring and Negotiating LBOs"
New York - September 15, 2011
Chicago - September 22, 2011

This biennial Kirkland seminar, chaired by Kirkland partner Jack S. Levin, P.C., will review the legal, tax, structuring and practical negotiating aspects of buyouts and other complex private equity deals. Topics covered will include structuring the buyout of a target company; negotiating acquisitions; negotiating debt and equity financing for acquisitions; compensating target executives through equity-based incentives; tax, SEC, accounting and other legal and practical aspects of acquisitions and financings; special issues in acquiring a public company; special issues in acquiring a distressed company; restructuring a distressed portfolio company; forming private equity funds, including developments in taxation of carried interests; and using partnership, LLC or other tax flow-through entities. Click here for more information about this event.

The NASBIC Venture Capital Institute
Atlanta, Georgia
September 19-22, 2011

The NASBIC Venture Capital Institute will be held from September 19 - 22, 2011, at Emory University in Atlanta. This four-day program will be taught by experienced venture and private equity fund managers and industry professionals. The curriculum will offer innovative techniques for executing effective due diligence; difficult ethical considerations; elements of pricing, structuring and negotiating deals; preparing profitable exit strategies; and understanding current tax and legal issues affecting investments. Kirkland partner Jack S. Levin, P.C., will be speaking on "Critical Legal and Tax Aspects of the Venture and Private Equity Industry." For more information, or to register for this event, please visit: http://www.vcinstitute.org/.

Kirkland & Ellis Seminar: "Sixth Annual Real Estate Private Equity Symposium"
New York, New York
October 24, 2011

Kirkland will host its Sixth Annual Real Estate Private Equity Symposium and cocktail reception in the New York office on October 24, 2011. Barry Sternlicht, chairman and CEO of Starwood Capital Group, will be the keynote speaker. Click here for more information about this event.

Terrapin's "Brazil Investment Summit 2011"
New York, New York
October 25-27, 2011

Kirkland & Ellis is a sponsor of Terrapinn's Brazil Investment Summit 2011, an investment strategy conference for funds, traders and investors focused on Brazilian opportunities. This three-day conference will uncover opportunities across hedge funds, quantitative strategies, private equity, infrastructure, real estate, commodities and more. Kirkland partner Frederick Tanne will participate in a panel discussion on "Private Equity Opportunities." For more information, or to please visit: http://www.terrapinn.com/2011/brazil-investment-summit-usa/index.stm.

IBA's "Private Equity Transactions Conference"
London - December 1, 2011
New York - December 6, 2011

The IBA Private Equity Transactions Conference will be held in London and New York, and will feature discussions on the global private equity market; current market issues and predictions for 2012; emerging markets issues; and current issues in financing. Kirkland & Ellis is a sponsor of this event and partner Kirk A. Radke is a co-chair. Additionally, partner David Patrick Eich will be speaking on "Emerging Markets Issues: Themes from Asia and Latin America" and partner Jay Ptashek will speak on "Financing: Current Market Issues and Themes for Next Year." For more information, or to register for this event, please visit: http://www.int-bar.org/conferences/conf399/.

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Private Equity Practice at Kirkland & Ellis

Kirkland & Ellis LLP's nearly 400 private equity attorneys handle leveraged buyouts, growth equity transactions, recapitalizations, going-private transactions and the formation of private equity, venture capital and hedge funds on behalf of more than 200 private equity firms around the world.

Kirkland has been widely recognized for its preeminent private equity practice. The Firm was named Best M&A Firm in the United States at World Finance's 2011 Legal Awards and was honored as the "Private Equity Team of the Year" at the 2011 IFLR Americas Awards. Kirkland was also recognized as "Law Firm of the Year" in *Buyouts* magazine's "2010 Deal of the Year Yearbook." Kirkland was ranked in the first tier among law firms for both Private Equity Buyouts and Private Equity Funds by *The Legal 500 U.S. 2010*. Additionally, *Pitchbook* named Kirkland as one of the most active law firms representing private equity firms in its 2010 "Private Equity Breakdown."

The Lawyer magazine recognized Kirkland as one of the "The Transatlantic Elite" in 2008, 2009 and 2010, noting that the firm is "leading the transatlantic market for the provision of top-end transactional services ... on the basis of a stellar client base, regular roles on top deals, market-leading finances and the cream of the legal market talent."

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