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CLIENT ALERT

Proposed New York State Carried Interest Tax Legislation

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On January 18, 2018, Governor Andrew Cuomo submitted a budget bill to the New York State Legislature, known as S7509 in the Senate and A9509 in the Assembly, which would include a 17% tax on the portion of income from a carried interest attributable to investment management services rather than passive investment income. The tax is intended to increase the total sum of federal, state, and local tax on investment professionals who receive income taxed as capital gain from a carried interest, up to approximately the amount paid by New York persons receiving an equivalent amount of ordinary income. The tax would apply to investment managers working in New York State, including those living outside the state.

Governor Cuomo's proposed tax would apply to an investment professional's share of the proceeds from a partnership to the extent the share exceeds "the amount such distributive share would have been if the partner had performed no investment management services for the partnership." The tax would apply similar treatment to shareholders who provide investment management services for an S corporation, to the extent of the share attributable to their investment management services. The tax would not apply to carried interest that is subject to federal income tax at ordinary income rates.

The law defines "investment management services" broadly to include activities such as "rendering investment advice regarding the purchase or sale of securities…," "managing, acquiring, or disposing of any such asset," "arranging financing with respect to the acquisition of any such asset," or "related activities in support of any service described…" Notably, the law provides an exception for managers of real estate companies by exempting partners in partnerships and shareholders of S corporations whose assets derive 80% of their fair market value from real estate held for rental income or investment.

The bill describes this as a “conditional tax” which would not take effect, even after enactment, until Connecticut, New Jersey, Massachusetts and Pennsylvania enact legislation having substantially the same effect. The bill does not elaborate further on criteria that would establish the necessary degree of similarity between legislation enacted in those states and the proposed tax described in Part M of the current budget bill in New York. This conditional language could be a significant barrier to the actual implementation of the tax, even if the bill is passed into law, unless momentum develops in the other states to enact similar legislation.

If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

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