

**NEW YORK GOVERNOR PATERSON PROPOSES TO TAX NONRESIDENT
PARTNERS ON CARRIED INTEREST**

On December 16, 2008, Governor Paterson presented several proposals to close New York State's two-year budget gap of \$15.4 billion. Among these is a proposal to tax non-New York residents on investment income (which is generally not subject to New York tax under current law) attributable to investment management services to a partnership or other entity carried on in New York. This measure is proposed to be effective for taxable years beginning after 2008.

Currently, New York State generally does not tax nonresidents on investment income even if the investment income is earned as a partnership "carried interest" received for providing services in New York. The budget proposal is intended to treat New York and non-New York residents the same on such income if it is attributable to investment management services to a partnership or other entity carried on in New York. It appears that the new tax would apply to non-New York resident partners on income attributable to either (i) a partnership interest received for investment management services that they perform in New York or (ii) a partnership interest, even if not received for services, to the extent such income is attributable to investment income of the partnership earned for investment management services carried on in New York. In addition, the partnership would be required to make estimated tax payments to New York on behalf of nonresident partners who earn such income.

Under the proposal, investment management services would include the following if performed in substantial quantity: advising a partnership as to the value of any specified asset; advising the partnership as to the advisability of investing in, purchasing or selling any specified asset; managing, acquiring or disposing of any specified asset; arranging financing with respect to acquiring specified assets; and any activity in support of any of the foregoing services. Specified asset means securities, real estate, commodities and options, or derivative contracts with respect to securities, real estate or commodities.

The scope of the proposal is unclear. For example, it is unclear how income subject to the new tax but attributable to New York and one or more other states would be allocated among those states. In addition, it is unclear how income from a partnership is attributed to investment management services to the partnership as opposed to invested capital.

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If you have any questions regarding this memorandum, please contact James R. Brown (212-728-8287, jbrown@willkie.com), Richard L. Reinhold (212-728-8292, rreinhold@willkie.com), Joseph A. Riley (212-728-8715, jriley@willkie.com), or the attorney with whom you regularly work.

Willkie Farr & Gallagher LLP is headquartered at 787 Seventh Avenue, New York, NY 10019-6099. Our telephone number is (212) 728-8000 and our facsimile number is (212) 728-8111. Our website is located at www.willkie.com.

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