SELECT U.S. TAX PROPOSALS AFFECTING FUNDS AND INDIVIDUALS

On February 26, 2009, President Obama introduced the 2010 budget proposal (the "Obama Budget"). The Obama Budget contains a number of tax provisions that are far-reaching, including the following, all of which would be effective by 2011:

- Income from "carried interest" would be treated as ordinary income from the performance of services.
- The Bush tax rate cuts would be allowed to expire at the end of 2010, resulting in the 2011 highest marginal individual tax rate increasing from 35% to 39.6% and the top long-term capital gains rate increasing from 15% to 20%. The top tax rates would apply to taxpayers earning more than $250,000 in the case of married filers and $200,000 in the case of individual filers.
- The maximum tax on "qualified dividend income" would increase from 15% to 20%.
- The benefit of itemized deductions would be limited to 28% for married couples earning over $250,000 (and individuals earning above $200,000). This proposal has already been criticized by Congressional leaders from both parties.
- Estate tax, as in effect in 2009, would be permanently extended and indexed to inflation. In 2009, the estate tax exemption is $3.5 million ($7 million for a couple) and the top estate tax rate is 45%.
- The judicially developed "economic substance doctrine" would be codified.

Following the introduction of the Obama Budget, on March 2, 2009, Senator Carl Levin (D-Mich.) introduced proposed legislation (S. 506, the "Stop Tax Haven Abuse Act") in the Senate, and Representative Lloyd Dogget (D-Texas) introduced an identical bill (H.R. 1265) in the House of Representatives (collectively referred to as the "STHAA"). Treasury Secretary Geither on March 3, 2009, confirmed that the administration endorsed the STHAA. The STHAA is essentially an expanded version of a 2007 bill introduced in the Senate by Senator Levin and then Senator Obama, and in the House of Representatives with the support of 47 cosponsors by Lloyd Doggett and then Representative Rahm Emanuel, who is now President Obama's Chief of Staff. In addition, on March 11, 2009, the Senate Finance Committee circulated a discussion draft of legislation for a hearing scheduled for March 17, 2009 regarding issues on offshore tax noncompliance. Considering that the Obama Budget provides for implementation of international tax enforcement by 2011, this area could be one of the top priorities in the near future. The STHAA contains the following provisions:

- Several rebuttable evidentiary presumptions in tax and securities legal proceedings would be established with respect to non-publicly traded entities located in "tax haven" jurisdictions. For example, any funds or assets a taxpayer transfers to or receives from an offshore entity or account would be presumed to have failed to be reported to the IRS if the entity or account is in a tax haven jurisdiction. There are 34 "tax haven" jurisdictions initially listed in the proposal, including Cayman Islands, Hong Kong, Jersey, Lichtenstein, Singapore, Switzerland, and certain members of the European Union (Cyprus, Gibraltar, Luxembourg and Malta). A significant number of the jurisdictions listed have tax treaties with the United States.
- A foreign corporation would be treated as a domestic corporation for U.S. federal income tax purposes and would be fully subject to U.S. corporate income tax if the corporation (i) has at least $50,000,000 in gross assets or is publicly traded and (ii) is "managed and controlled" primarily from the United States. "Managed and controlled" would include control by U.S.-based investment managers. This provision would be effective two years after the date of enactment.

- Effective 90 days after enactment, a 30% U.S. dividend withholding tax would generally be imposed on dividend equivalent and substitute dividend payments (including through the use of swaps, derivatives, and securities lending transactions) made to non-U.S. persons in respect of domestic corporations.
- Hedge funds, private equity funds and "fund formation agents" generally would be subject to anti-money-laundering procedures under rules to be promulgated by the Treasury within 180 days after the date of enactment.
- The STHAA would increase the maximum fine on tax shelter promoters to 150% of their promoter fees, and limit penalty protection of legal opinions on transactions involving tax haven jurisdictions.
- Also included are measures that would (i) extend from three years to six years the amount of time the IRS has to investigate and assess additional tax when involving a tax haven jurisdiction; (ii) increase disclosure requirements relating to offshore accounts, transactions, and entities; (iii) authorize special measures against foreign jurisdictions, financial institutions, and others that impede U.S. tax enforcement; (iv) prevent misuse of foreign trusts for tax evasion; and (v) expand reporting requirements for passive foreign investment companies.
- The judicially developed "economic substance doctrine" would be codified to invalidate transactions that have no meaningful economic substance or business purpose. The Obama Budget also proposed this codification.

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