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KIRKLANDPEN
Private Equity Newsletter

December 22, 2017

Final Tax Bill Will Have Significant Impact on Private Equity Sponsors and Their Portfolio Companies

PENpoints

The Act will have wide-ranging effects on private equity sponsors and their portfolio companies.

President Trump signed this morning the final version of the tax reform bill commonly known as the Tax Cuts and Jobs Act (the "Act"), which was passed by Congress on December 20, 2017. The Act will have wide-ranging effects upon private equity sponsors and their portfolio companies.

We highlight what we expect to be the most significant changes below. A more detailed description of the Act and our view as to the likely impact of the Act on raising investment capital, organizing business operations and structuring and financing M&A transactions is available in the accompanying *Kirkland Alert*, which you can access by clicking here.

Legislative Changes

The Act changes a number of key aspects of U.S. federal tax law that will have a meaningful impact on public and private companies. In particular, the Act:

- Reduces the corporate income tax rate from 35% to 21%;
- Creates a preferential tax rate for investors in certain flow-through businesses and REITs through a 20% deduction;
- Retains capital gains rates for carried interest allocations, but imposes a three-year holding period before certain income qualifies for long-term capital gains tax rates;
- Limits the deductibility of interest by a leveraged business to 30% of EBITDA (as defined in the Act) until 2021 and to 30% of EBIT (as defined in the Act) for 2022 and thereafter;
- Allows an immediate write-off of the full cost of certain business property;
- Limits use of net operating losses generated in taxable years beginning in 2018 to 80% of taxable income and prohibits carrybacks of such net operating losses; and
- Fundamentally overhauls the taxation of cross-border investments.

Impact on Market Practices

The Act's impact on raising investment capital, organizing business operations, and structuring and financing M&A transactions remains to be seen. However, based on current market practice and the substantial changes the Act makes to the taxation of U.S.-based businesses, we expect that:

- C corporations may become more attractive as investment vehicles as compared to flow-through entities;
- Public companies pursuing a "dual-track" process in which either a spin-off or a taxable sale is contemplated may find a taxable sale more attractive;
- Immediate expensing may make asset-level M&A transactions more attractive in some cases;
- Distressed businesses may face new challenges as a result of the limitations on interest deductions and the use of net operating losses; and
- Taxpayers involved in the energy industry may benefit from attractive tax rules under the Act, including the retention of the deduction for intangible drilling costs, the elimination of the corporate alternative minimum tax, and the 20% deduction available to certain flow-through entities.

Regardless of one's political views, it is generally fair to say that the Act was designed with an objective to encourage investment inside the U.S. In particular, the Act includes significant provisions that benefit businesses that make substantial investments in U.S.-based

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employees and U.S.-based tangible property. Similarly, the international provisions in the Act provide powerful incentives for the repatriation of cash to the U.S., and provide disincentives for the movement of intangible property to overseas destinations.

While we do not purport to be economists and we certainly have no idea whether the Act will provide the enhanced economic growth that the Republican Congress expects, we are confident that private equity sponsors and their portfolio companies and investors will find that the Act provides both meaningful opportunities for tax minimization and also traps for the unwary.

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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PLI Drafting and Negotiating Corporate Agreements 2018
New York NY, January 18, 2018
Chicago, IL, January 31, 2018

This PLI seminar will teach the basics of drafting and negotiating corporate agreements — from how the provisions of an agreement fit together, to the fundamental drafting and negotiating principles common to all corporate agreements. Kirkland partners Jonathan Davis and Keith Crow will be panelists at the New York and Chicago events, respectively. Click here for more information or to register.

45th Annual Securities Regulation Institute
Coronado, CA, January 22-24, 2018

Hosted by Northwestern Law, the 43rd Annual Securities Regulation Institute will take place in Coronado, California. One of the most visible and highly regarded securities and corporate law conferences in the country, the Securities Regulation Institute reaches prominent attorneys from both firm and in-house practices. Kirkland partner Scott Falk is on the planning committee and will be a panel member for the Mergers & Acquisitions session. Click here for more information or to register.

17th Annual Beecken Petty O'Keefe & Company Private Equity Conference
Chicago, IL, February 23, 2018

Kirkland is a sponsor of this annual event, which brings together financiers, students and entrepreneurs to network and share insights into the dynamics of investing in a constantly changing economy. This year's conference is themed "Remaining Nimble and Achieving Returns While Facing Uncertainty and Volatility." Click here for more information.

13th Annual Stern Private Equity Conference
New York, NY, March 2, 2018

Kirkland will sponsor New York University's Stern School of Business' 13th Annual Stern Private Equity Conference. The conference will provide a forum for industry leaders to discuss the opportunities and risks of today's private equity and venture capital environment, including how tepid global growth, regulatory dynamics, political pressure and financial market conditions are posing challenges to fundraising, deal financing and operations. More information to follow.

25th Annual Columbia Business School Private Equity Conference
New York, NY, February 23, 2018

Kirkland will partner with Columbia Business School to sponsor its annual Columbia Business School Private Equity Conference. The event will focus on the emerging challenges and opportunities facing the private equity and venture capital industries in the coming year. The conference will bring together industry professionals, students, alumni and faculty to share their knowledge and experiences. Click here for more information or to register.

24th Annual Harvard Business School Venture Capital Private Equity Conference
Boston, MA, January 27, 2018

Kirkland is a sponsor of the 24th Annual Harvard Business School Venture Capital and Private Equity Conference, which will address a range of today's most relevant topics. Keynote speakers at this year's event are Kewsong Lee, deputy CIO of private equity and head of global market strategies at The Carlyle Group; Sean Klimczak, global head of infrastructure at Blackstone; and Paul Maeder, co-founder and managing general partner at Highland Capital Partners. Click here for more details or to register.

Wharton Private Equity & Venture Capital Conference
New York, NY, March 16, 2018

The Wharton School's Private Equity and Venture Capital Conference will showcase several keynote speeches and panel discussions on the state of the private equity and venture capital industries. Kirkland partner Robert Blaustein will moderate the Funds panel and partner Stephen Hessler will moderate the Distressed Opportunities panel. Click here for more information or to register.

2018 Kellogg Private Equity and Venture Capital Conference
Chicago, IL, April 25, 2018

Kirkland is a sponsor of this annual student-led conference, which brings industry professionals, alumni, students and Kellogg faculty together for a day of discussion on the current state of the industry and its most pressing issues. More information to follow.

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Kirkland & Ellis' nearly 500 private equity attorneys handle leveraged buyouts, growth equity transactions, recapitalizations, going-private transactions and fund formations on behalf of more than 400 private equity firms and hedge funds around the world.

Kirkland has been widely recognized for its preeminent private equity practice. The Firm was named "Private Equity Group of the Year" in each of the last six years by *Law360* and was commended as being the most active private equity law firm of the last decade in *The PitchBook Decade Report*. U.S. News Media Group and Best Lawyers have ranked Kirkland as a Tier 1 law firm for Leveraged Buyouts and Private Equity Law for seven consecutive years and as a top-tier firm for Private Funds/Hedge Funds Law since 2012. The Firm was recognized as the #1 law firm for private equity in the 2017 Vault 100 rankings, and, in 2016, Private Equity International named the Firm "Law Firm of the Year in North America: Fund Formation" for the third year in a row.

In 2012-2016, Chambers and Partners ranked Kirkland as a Tier 1 law firm for Investment Funds in the United States, United Kingdom, Asia-Pacific and globally. The Firm was ranked as the #1 law firm for both Global and U.S. Buyouts by deal volume in Mergermarket's *League Tables of Legal Advisors to Global M&A for Full Year 2011-2016*, and has consistently received top rankings among law firms in Private Equity by The Legal 500, the Practical Law Company and IFLR, among others.

The Lawyer magazine has recognized Kirkland as one of its "Transatlantic Elite," having noted 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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