

What People are Saying about Carried Interest and Tax Equity

IN THEIR OWN WORDS...

“To be clear, I hold no brief against the kings of private equity. Their clients are consenting adults who sign up with full knowledge of the lush fees that private equity managers receive. Some of these managers may even earn their rich rewards. My question is simply this: Why shouldn't they pay taxes like the rest of us? It's true that carry is mostly derived from gains on capital — but it's mostly *someone else's* capital. Which is presumably why former Treasury Secretary Robert E. Rubin said at a conference last month, “I think what they're doing is getting paid a fee for running other people's money.” Sounds right to me. This judgment does not dispute the fact that fund managers' compensation is risky. But so are the incomes of movie actors, the royalties of authors and the prize winnings of golfers — none of which is treated as capital gains.” – **Alan Blinder, Princeton Economics Professor**

“Whether it makes sense to tax the output of expertise and hard work at more than twice the rate of investment returns is debatable. But, for better or worse, that's the way it is. Except, that is, when it isn't. Owners of companies, ranging from small real estate partnerships to multibillion dollar hedge funds and private equity firms, have devised a way to erase this distinction. Their managers pay 15% on their income by dressing it up as investment returns — even though they bear no investment risk or put none of their own money in play. Nice work if you can get it. But in this case it constitutes a frontal assault on fairness. Why should such people pay only 15% when senior corporate executives pay 35% for making many of the same types of business decisions? More to the point, it's hard to see the logic (or the justice) in a school teacher or bus driver with taxable annual family income as low as \$63,700 paying 25% when someone like Blackstone Group CEO Stephen Schwarzman can make nearly \$700 million on the day his firm went public and pay at most 15%.” – **USA Today**

“Deferred compensation, even risky compensation, is still compensation, and it should be taxed as such... The Administration is on the wrong side of the issue [if it opposes the congressional legislation, which] does not seem excessive... When I wrote my book, that was sweat equity... [I oppose] different levels of taxation on different types of compensation.” – **Gregory Mankiw, Harvard Economics Professor and Former Chairman of President Bush's Council of Economic Advisors**

“[T]he underlying question is whether the funds' managers are receiving income from an investment they have made, or a payment that is, in all but name, a performance-related fee... Much the larger part of what they typically receive is exactly akin to a performance-related bonus, not a reward for capital put at risk. To treat it otherwise for tax purposes is a gross distortion. Efforts are doubtless under way in other industries to disguise management fees as carried interest. Correcting this anomaly might be done in different ways... The simplest approach, and most likely the best, would be to set the question of deferral aside, and tax carried interest as ordinary income on realisation. To emphasise, this would not be to single out private equity or hedge fund managers as deserving of a new or specially punitive regime. It is a matter of even-handedly applying the logic of the present code.” - **The Financial Times**

“[The share of investment profits are] basically fees for managing other people's money.” - **William Niskanen, Chairman of the Cato Institute & Former Member of President Reagan's Council of Economic Advisors**

“We believe that we are engaged primarily in the business of providing asset management and financial advisory services and not in the business of investing, reinvesting or trading in securities... We also believe that the primary source of income from each of our businesses is properly characterized as income earned in exchange for the provision of services.” - **Blackstone Group, in an SEC Filing Associated with its IPO**

“If you're in the luckiest 1% of humanity, you owe it to the rest of humanity to think about the other 99%.... If you run a partnership and you have capital gains, you have a 15% tax rate; and if you run a corporation and have capital gains, you have a 35% tax rate. When both entities are operating in a similar manner with many thousands of shareholders, freely tradable shares, people managing them who are attempting to evaluate investments, it seems a bit illogical to have that sort of a spread in the tax rate just depending on form.” – **Investor Warren Buffett**

“...[I]t seems to me that what is happening is that people who run a large fund are basically performing a service and the service is running the capital and as a consequence they get paid a fee in the form of a performance fee. You can characterize it as a performance fee, you can characterize it as a carried interest, you can characterize it any way you want, but basically I think what they're doing is getting paid a fee for running other people's money and if that is essentially what's happening, while you can certainly create all kinds of analogies that are complicated and if I were arguing against this I think I would try to develop a lot of complicated analogies and use that as my way of trying to prevent something from happening, I think at the core there is a very good argument to be made for treating this as ordinary income.” - **Former Treasury Secretary Robert Rubin**

“I think it's its odd that people making that much money off of essentially labor income should be paying lower rates than, than the average... than their secretaries are, to put it baldly. I think it's good that you are considering doing it. I think you have to be careful not to trap others in doing it. I think you are also on the right track when you're thinking about whether publicly traded partnerships ought to be taxed as corporations, since the corporations they are competing with are certainly paying tax at the corporate level, and there's some actual money in some of those areas.” - **Michael Graetz, Former Deputy Under Secretary for Tax Policy under President George H.W. Bush, Yale Law Professor**

“...[T]he bills' supporters rightly conclude that it is untenable for the most highly paid Americans to enjoy tax rates that are lower than those of all but the lowest-income workers. Fairness is not the only reason to change the rules. The private equity industry is on shaky ground when it claims that current practice is a correct application of the law. Many of the firms' partners are not investing their own money in the various funds and ventures, and so have no direct risk of loss, the general test for claiming capital-gains treatment on one's earnings....They're actively managing assets, and should be taxed accordingly as managers earning compensation... Congress will achieve a significant victory, for fairness and for fiscal responsibility, if it ends the breaks that are skewing the tax code in favor of the most advantaged Americans.” - **The New York Times**

“We can't allow the carried interest tail to wag the capital gains dog... Contrary to the claims of some press reports, lobbyists, and politicians, our inquiry, and any proposal that it may produce, is not about raising taxes on capital income. It is not an attack on the investor class. It is about the definition of capital income versus labor income... I make this point to some Republicans and some Democrats who may have come down on this issue on opposite sides before they even know the facts.” - **Senator Charles Grassley**

“The bill would not affect the other investors in these funds, nor would it affect the tax rate for profits that fund managers make on investments with their own money... Critics of the two bills argue that investment fund managers should be rewarded for taking high risks. But these fund managers, for the most part, are not risking their own money... Besides, plenty of risky industries don't enjoy comparable tax benefits. Income earned from managing an investment partnership fund should be treated just like the income earned for providing any other service.” - **The Washington Post**

“It really isn't all that hard to decide how to properly tax carried interest. Is [it] income which a money manager earns on his or her personal investments, or, instead, is it the performance fee earned for managing other people's investments? If carried interest is personal investment income, then it is properly entitled to capital gains treatment – however, if it is a performance fee, as my 20 years of first-hand experience clearly tells me it is, then it should be taxed as ordinary income...Congress is not considering changing the tax rates on the investments made by investors. Congress is only considering restoring fairness in how the men and women who manage these investments are individually taxed compared to other managers and to regular workers. And it is beyond disingenuous to predict dire unintended consequences when no consequences at all will occur. A tax loophole the size of a Mack truck is right now generating unwarranted and unfair windfalls to a privileged group of money managers, and, to no one's surprise, these individuals are driving right through this \$12 billion-a-year hole.” – **Leo Hindery, Private Equity Fund Manager**

“[The current treatment of carried interest is] a policy mistake: It was earned by the work of promoters [in the private equity industry] and it should be taxed as compensation.”- **John Chapoton, Former Assistant Treasury Secretary for Tax Policy Under President Reagan**

“Both the management fee and the carried interest represent compensation for the work that we do... Our management fee is taxed as ordinary income. However, the carried interest, even though it is compensation, is primarily taxed at capital gains rates. I can understand why many in my industry want to preserve this special tax advantage. Clearly, it has served US and ME well. The tax subsidy each year to private equity fund, hedge fund, and venture capital fund managers is in the *billions* of dollars. But I think this special tax break is neither fair nor equitable. Many Americans invest sweat equity in their jobs and their businesses, take risks, contribute to the economy, and may have to wait a long time before their hard works pays off. But they still pay ordinary income tax rates on their compensation. To the extent we take risk, we take it with other people’s money.” – **William Stanfill, Venture Capital Fund Manager**

“I think sitting here is very hard to predict whether private equity or hedge funds managers, general partners, if they were faced with higher taxation, would believe that the response should be increasing the 2 & 20... It is simply too hard for me to predict that. I think that at some point there is a level of resistance on the part of investors and I think that tax-exempt institutions in particular who have a lot of leverage, to use the often cited word today, would probably not be happy paying significantly higher fees, so the result might well be, even though the managers would say ‘well look we’re paying much higher taxes we need to generate more fees,’ that that cost would really be picked up by the managers and by the general partners of private equity funds.” – **Attorney Daniel Shapiro, on behalf of the Managed Funds Association**

“I don’t think there’s an argument on the equality side for the current tax treatment.” - **Irwin M. Stelzer, Hudson Institute Director of Economic Policy**

“Most economists, however, would view at least part and perhaps all of the carried interest as performance-based compensation for management services provided by the general partner rather than a return on financial capital invested by that partner. That perspective would suggest taxing at least some component of the carried interest as ordinary income, as most other performance-based compensation is currently treated, regardless of the nature of the underlying investments generating the profits of the fund.” – **Peter Orzag, Director, Congressional Budget Office**

“It's not exactly straight salary, but none of this income comes from [a hedge fund manager] putting his own wealth at risk. Except for the fact that he might make a billion dollars a year, he resembles a waitress whose income depends on a mix of wages and tips, or a salesman who lives on a mix of salary and commissions, more than he resembles an entrepreneur who sinks his life savings into a new business. So why does he get the same tax breaks as that entrepreneur? Not to put too fine a point on it, why does Henry Kravis pay a lower tax rate on his management fees than I pay on my book royalties?” - **Paul Krugman, Princeton University Economics Professor**

“The argument that this is about the interests of retired public employees is ludicrous.” - **Orin Kramer, Hedge-Fund Manager and Chairman of the New Jersey State Investment Council**

“Suggesting that changing the tax status on carried interest would lead to public-sector pensions being jeopardized is taking a pretty extreme view of their importance.” – **Michael Musuraca, Trustee, New York City Employees Retirement System**