

A "carried interest" (also known as a carry, a "promote" or a "promoted interest") is a financial interest in the appreciation of a property, given to the real estate developer by the investors in the project. Carried interest compensation is in excess of the share of capital contributed by the developer, and is given by investors to ensure the developer has a stake in the ultimate success of the project and to compensate the real estate entrepreneur for the risks taken during development and prior to sale of the property.

Carried interest has traditionally been treated as capital gains, but several attempts have been made in Congress to tax carried interests at much higher, ordinary income rates. These attempts have been described by proponents as only affecting Wall Street hedge fund managers, but such a change would in fact have a major adverse impact upon the real estate partnerships and the development industry.

Real Estate Partnership Carried Interests Are:

- **Not Guaranteed Income or Salary:** Carried interests oftentimes cannot be valued at the time they are granted since payment is dependent on success of the project. Unlike salary for services or fee income which are already taxed at ordinary income rates, a carried interest is *not* guaranteed, but more like a *long-term risk investment* to be treated as capital gains.
- **Given In Return for Risks Taken:** A carried interest is given by the investors in a real estate partnership to the developer in return for the risks undertaken by that developer. The developer, who is usually the general partner, will often personally guarantee construction completion of the project, payment of partnership debts, and is at risk for added liabilities such as environmental contamination and other lawsuits.
- **Used To Align Interests of Investors and Developer:** Carried interests are given by investors to incentivize the developer to maximize the ultimate value of the property. By giving the real estate developer a financial interest in the share of the appreciation of the property, the economic interests of the investors and the developer are aligned.

NAIOP Opposes Changing The Capital Gains Tax Treatment of Carried Interests:

- **A Harmful Tax Increase:** Taxing carried interest at ordinary income rates would more than double the tax rate on many real estate partners, increasing taxes from a current capital gains rate of 15 percent to nearly 35 percent, at a time when the commercial real estate industry is struggling.
- **Undermines Economic Activity and Job Creation:** A carried interest tax hike would undermine economic activity in the real estate development industry. If the willingness to take on development risk is reduced by much higher taxes, many job-creating development projects will simply not be undertaken.
- **Ignores Nature of Capital Assets:** Real estate development results in the creation of capital assets - shopping malls, office buildings, housing projects, and industrial developments. This gives rise to jobs and an increased tax base for communities. Increasing taxes on carried interest for all partnerships, without regard to the nature of the investment or impact upon a community, would be shortsighted.
- **A Retroactive Tax Increase:** Efforts to change how carried interest is treated represent an unfair retroactive tax increase on partnerships that already have a carried interest or promoted interest component.