

Section 1061 Carried Interest Regulations: How does this impact me?

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1

What's New?

- Confirmation § 1231 gains are NOT subject to § 1061.
- Confirmation of entity treatment of partnership interest – Except when it's not.
- Loaning money to your manager taints otherwise qualified capital.
- Related party transfers of carry can accelerate gain on otherwise tax-free gifts.
- We still don't know whether non-fund partnerships are subject to § 1061!

2

What To Look For

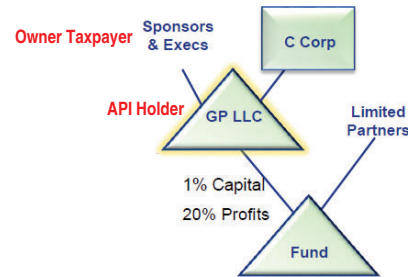
- Carry . . . Promote . . . Profits Interest . . . Performance Fee
- If a partner has a share of profits greater than its share of capital in exchange for services.
- § 1061 is most clearly directed at funds and mandates a 3-year holding period to measure long-term capital gains.
- § 1061 is generally limited to funds or is it???

Background

- §1061 passed as part of the Tax Cut and Jobs Act
- Effective for tax years beginning after Dec. 31, 2017
- §1061 recharacterizes certain long-term capital gain held less than 3 years to short-term capital gain
- Potential Impact:
 - 40.8% tax rate vs. 23.8% tax rate
 - Maybe more next year

Who is Affected?

- Applicable partnership interest **and** applicable trade or business
 - Applies to S-Corporations
 - Applies to Passive Foreign Investment Companies (PFICs) with Qualified Electing Fund (QEF) elections
- Exceptions
 - C-Corporations
 - Capital Interest
 - Non “Applicable Trade or Business” (ATB) Employee
 - Family Office
 - Bona Fide Unrelated Purchaser



What is an Applicable Partnership Interest (API)?

- An API is an interest in a partnership's profits that is transferred or held in connection with the performance of substantial services by the taxpayer, or any other related person, in any applicable trade or business (“**ATB**”).
- The proposed regulations expand the definition of a partnership interest for purposes of § 1061 to also include any financial instrument or contract, the value of which is determined, in whole or in part, by reference to the partnership.
- The proposed regulations surprisingly do not provide certainty of whether a partnership interest associated with a one-off, single property joint venture could be an API.

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