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Application of Section 1061 to Oil and Gas Joint Ventures

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Legislative Background to Code § 1061

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Carried Interest Basics

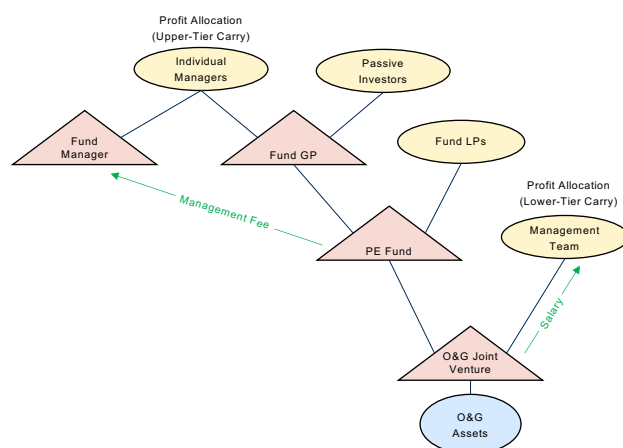
- Investment fund managers often receive economics in the form of a share of the net profits generated by the fund.
 - This share of profits often is referred to as a “carried interest” or “carry.”
- Carried interests typically are structured as partnership profits interests.
 - Fund managers generally receive grants of profits interests on a tax free basis. See Rev. Proc. 93-27; Rev. Proc. 2001-43.
 - The items of income and gain that make up the allocations of carry retain their character including, to the extent applicable, long-term capital gain or qualified dividend income.

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Example: Sponsored O&G Joint Venture



- PE Fund makes capital investment in O&G Joint Venture.
 - PE Fund receives preferred return followed by profit split with Management Team (lower-tier carry).
 - Management Team likely receives salary from O&G Joint Venture (or affiliate).
 - Certain members of Management Team may invest capital.
- Fund LPs make capital investment in PE Fund, which supports PE Fund's investment in O&G Joint Venture.
 - Individual Managers receive share of PE Fund's profits as an allocation from Fund GP (upper-tier carry).
 - Potential for passive capital providers at Fund GP.
- Fund Manager receives fees based on assets under management (e.g., 2%)

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