



## **Tax the income of hedge fund managers as ordinary (wage) income: \$21 billion over 10 years**

**The Idea:** The "carried interest" loophole allows hedge fund managers to treat the commissions they earn as investment managers as capital gains. Since most of them are very wealthy, this loophole allows them to reduce what would probably be a tax rate of 35 percent to the capital gains tax rate, which is now just 15 percent. If the income of hedge fund managers was taxed like other commissioned workers or fee-for-service workers, the country would have another \$21 billion<sup>16</sup> in revenue over the next 10 years.

**The Rationale:** Closing this loophole would make the tax system more equitable. Hedge fund managers are typically paid for their services through performance fees, charged as a percentage of the fund's profit. Since the fund's profits are capital gains, the carried interest loophole allows hedge fund managers to call the fees they earn capital gains for tax purposes, even though the fees are essentially salary or commission income.

There is little justification for the carried interest loophole, which treats the income of hedge fund managers differently from the income of other workers. It has allowed a small number of hedge fund managers to reap large windfalls over time. [According](#) to the Center for American Progress, the 25 richest hedge fund managers make as much as the combined income of 441,000 middle-class families.

**Support for Idea:** Public opinion polls show the public favors closing the carried interest loophole. Legislation has recently been introduced to do just that. Rep. John Tierney (D-MA) introduced the "Tax Equity and Middle Class Fairness Act of 2011," which would close the carried interest loophole and force hedge fund managers to pay the same tax rate on their income as regular workers do.

Of the plans reviewed for this revenue project, the following support closing the carried interest loophole: Center for American Progress' *Budgeting for Growth*, and President Obama's *2012 budget* and *Living within Our Means*.

<sup>16</sup>[Reducing the Deficit: Spending and Revenue Options](#), CBO, pg. 157.