



A MULTI-JURISDICTIONAL COMPARISON

Carried interest

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Introduction

What is carry?

Carried interest (or “carry”) provides the Fund management team a right to share in the profits of the Fund. Carry is generally structured as allocating to the Fund managers a share in the Fund’s profits (usually, but not always, this is a 20% share of the Fund’s profits) once investors have received back an amount equal to their original investment, plus an additional return on their investment (known as the “preferred return” or “hurdle”). Carry is popular with investors because it incentivises the Fund managers to ensure the Fund is a success, thereby creating greater alignment between the carry holders and investors.

The Fund management team will generally be employees of the Fund’s investment advisory entity and will receive an annual salary for providing investment advisory services to the Fund. Senior Fund manager employees will commonly be granted carried interest rights.

Investors are also likely to require that the Fund management team invests its own money in the Fund on the same terms as investors, so that the Fund management team have “skin in the game”. This is often referred to as “GP commitment”, or “co-invest”.

The analysis herein is limited to taxation of carried interest and salary only (and not GP commitment/co-invest).

Structure of the carry vehicle

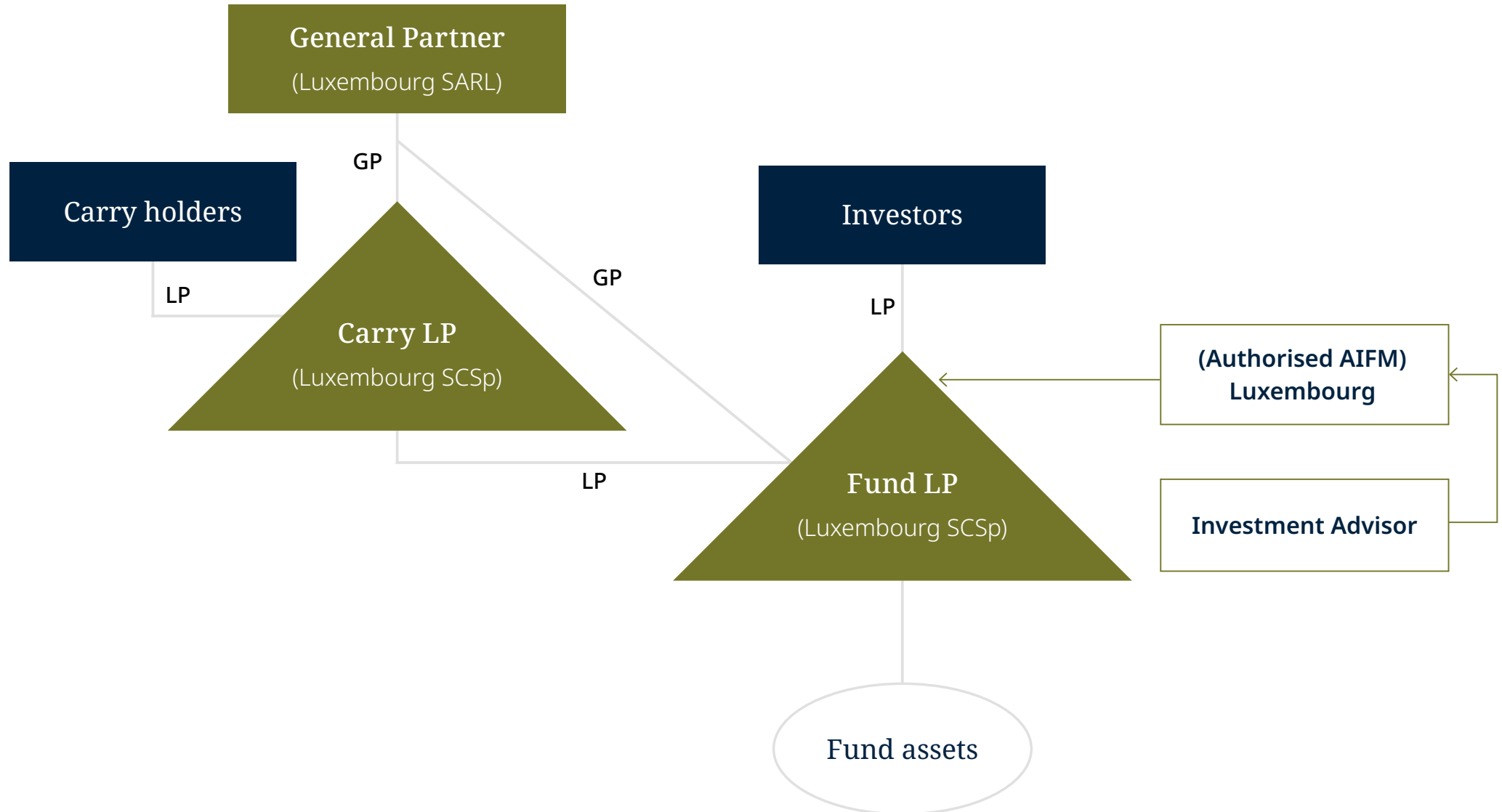
In most jurisdictions carry is held through a separate “carry vehicle”: typically, through a separate limited partnership (eg in European Funds) or through the general partner (eg US Funds), and the carry holders are admitted as limited partners to the carry vehicle (although notably in France for example, Fund managers hold their carry in the Fund direct).

An advantage of the carry vehicle is that it provides privacy, as the main Fund limited partnership agreement (“LPA”) will stipulate that carry is paid to the carry vehicle without disclosing the identity of the carry holders. Furthermore, the carry vehicle provides flexibility with respect to carry, such as allowing new joiners, bad leavers forfeiting carry and rewarding high performers with additional carry.

Carry is a share of the Fund’s profits, and can consist of capital gain (including a share buyback), interest income and dividends. In many jurisdictions the tax rate will vary depending on the nature of the return.



Example of a Luxembourg fund



Multijurisdictional comparison table

As Funds have grown in size and complexity, there has been a corresponding increase in the size of the Fund management team. It is not uncommon for large Fund managers to have teams in five or more jurisdictions. Fund managers tend to be highly educated and internationally mobile, often having lived in more than one jurisdiction and in many instances have the ability and motivation to migrate to live in different jurisdictions for a variety of reasons. This trend has accelerated post-Covid, and is especially the case when relocating to an office in another jurisdiction.

One important factor that Fund managers will need to consider when relocating to another jurisdiction is how they will be taxed on salary and carry.

We have identified 14 jurisdictions which are popular for Fund managers to live in. All jurisdictions share a number of important features: they are developed countries, have well-established and transparent rules of law and they (mostly) have stable political systems. Crucially, they all allow for the free flow of capital.

With respect to each jurisdiction, the table looks at the tax rate as it applies to:

1. Salary
2. Grant of carry
3. Vesting
4. Receipt of carry: gains, dividends and interest

We have also included a high-level tax snapshot with respect to each of the 14 jurisdictions outlining, in broad terms, how each jurisdiction taxes carried interest and salary. Given the complexity of carry structuring and employment rights, the information contained herein should be treated as illustrative in nature, to provide a flavour of how each jurisdiction taxes salary and carried interest.

For further information, please reach out to the relevant DLA Piper contact. Contact details are shown in the snapshot of each jurisdiction.



Key assumptions

The analysis in the table and each snapshot is illustrative only, and no reliance should be given to any information set out therein.

- The tax rates below are for the 2023/2024 tax years (precise periods in accordance with each jurisdiction's tax rules).
- Tax rates set out below are at their highest, combined marginal rate (eg in the US, the rates include federal self-employment and net investment income taxes).
- Unless stated otherwise, city and state tax rates are not included in the table (but reference may be made to this in the snapshot).
- The carry holders are assumed to be employees of the Fund manager or affiliate.
- Unless stated otherwise, in the table, employment/salary tax rates include employee social security (eg in the UK, this is national insurance contributions), but not employer social security contributions.
- Unless stated otherwise, the carried interest is anticipated to be held by Fund manager in their personal capacity and not through a personal holding company.
- Unless stated otherwise, where the table states that there are "employment tax liabilities" on the grant of carry, this is (broadly) the market/fair value of the carried interest right, less consideration paid by the carry holder.

	SALARY (EMPLOYMENT TAX – MAX. % RATE)	GRANT OF CARRY (EMPLOYMENT TAX)	VESTING	SPECIFIC CARRY REGIME (RECEIPT OF CARRY)	ALLOCATION OF CARRY: CAPITAL GAINS	ALLOCATION OF CARRY: DIVIDENDS	ALLOCATION OF CARRY: INTEREST	OTHER
AMERICAS								
Canada	53.53% (Ontario resident)	Employment tax liabilities	Not taxable	No	26.76%	53.53% (Foreign companies); 39.34% (Canadian companies)	53.53%	Fund vehicles should be tax transparent
USA	40.8% (including self-employment tax)	No, unless carry has value on hypothetical liquidation of Fund	Not taxable	Yes	23.8%: for long term capital gains; 40.8%: short term capital gains	23.8% (qualified dividends)	40.8% (unless portfolio interest exemption applies)	Section 83(b) election recommended
EUROPE								
France	49% (plus social contributions up to 25%)	Not taxable if statutory regime ("SR") applies	Not taxable if SR applies	Yes (the SR)	34% under SR	34% under SR	34% under SR	If SR does not apply, receipts of carry instead taxed at: 79% rate
Germany	48%	Employment tax liabilities	Not taxable	Yes ("CIR")	28.5% under CIR	28.5% under CIR	28.5% under CIR	Ruling application can be made if there is uncertainty. There is a pending court case on carry

	SALARY (EMPLOYMENT TAX – MAX. % RATE)	GRANT OF CARRY (EMPLOYMENT TAX)	VESTING	SPECIFIC CARRY REGIME (RECEIPT OF CARRY)	ALLOCATION OF CARRY: CAPITAL GAINS	ALLOCATION OF CARRY: DIVIDENDS	ALLOCATION OF CARRY: INTEREST	OTHER
Ireland	52%	Employment tax liabilities	Not taxable	Yes (VCF)	15% under VCF, otherwise 33%	15% under VCF, otherwise 52%	15% under VCF, otherwise 52%	VCF regimes applies to investment in “start-ups” but not typically eg real estate investment Funds
Italy	52%	Employment tax liabilities	Not taxable	Yes	26%	26%	26%	If carried interest regime not applicable, employment tax rates
Luxembourg	45.78% (excl. social security)	Employment tax liabilities	Not taxable	No favourable regime	0% (subject to conditions)	45.78% (excl. social security); 22.89% reduced rate (subject to conditions)	20% (subject to conditions)	Fund and carry vehicle should be tax transparent
Netherlands	49.5%	Employment tax liabilities	Not taxable	Yes (Box II)	26.9% under Box II	26.9% under Box II	26.9% under Box II	Box II tax rate to increase to 31% in 2024
Spain	54%	Employment tax liabilities, subject to specific carry regime (“SCR”)	Not taxable	Yes	27% under the SCR	27% under the SCR	27% under the SCR	SCR not applicable to real estate or credit Funds, and taxed at 54%

	SALARY (EMPLOYMENT TAX – MAX. % RATE)	GRANT OF CARRY (EMPLOYMENT TAX)	VESTING	SPECIFIC CARRY REGIME (RECEIPT OF CARRY)	ALLOCATION OF CARRY: CAPITAL GAINS	ALLOCATION OF CARRY: DIVIDENDS	ALLOCATION OF CARRY: INTEREST	OTHER
Sweden	55%	No	Not taxable	No, but a “closely held companies” (“CHC”) regime may apply	25% CHC rate on distributions (after five years)	25% CHC rate on distributions (after five years)	30%	Carry is held through a closely held company, and then distributed to carry holders
UK	47%	Employment tax liabilities, subject to possible safe harbour (MoU)	Not taxable	Yes	28% (assuming anti-avoidance rules don't apply)	39.35% (assuming anti-avoidance rules don't apply)	45% (assuming anti-avoidance rules don't apply)	Fund vehicles should be tax transparent. Section 431 elections recommended



	SALARY (EMPLOYMENT TAX – MAX. % RATE)	GRANT OF CARRY (EMPLOYMENT TAX)	VESTING	SPECIFIC CARRY REGIME (RECEIPT OF CARRY)	ALLOCATION OF CARRY: CAPITAL GAINS	ALLOCATION OF CARRY: DIVIDENDS	ALLOCATION OF CARRY: INTEREST	OTHER
APAC								
Australia	47%	Employment tax liabilities	Not taxable	Yes, for specified venture capital vehicles ("VCF regime")	23.5% for VCF regime	26%	26%	If carried interest regime not applicable, employment tax rates
Hong Kong, China	17%	Not taxable	Not taxable	Yes, tax concession regime (CR) available	0% under CR	0% under CR	0% under CR	CR subject to specific conditions, if not satisfied, receipt of carry subject to 17% tax. Tax filing/reporting required for CR
Singapore	24%	Employment tax liabilities	Taxable	No, but carry is generally held through an offshore carry structure	0%	0%	0%, if received from an offshore carry vehicle	

Canada

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of the carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry right less any consideration paid. Any such employment benefit would be subject to applicable employer source deductions for Canadian income tax, Canada pension plan and employment insurance.

Vesting: Vesting does not generally give rise to a Canadian tax liability in the hands of a Canadian carry holder.

Receipt of carry: Canadian carry holders are subject to tax when the carry returns are allocated to the individual carry holders.

The Canadian tax rate depends on the nature of the return and the holder's province of residence. The highest marginal tax rates for an individual resident in the province of Ontario are as follows:

- Capital gains including share buybacks, disposal proceeds or repayment of loan principal: 26.76% tax rate.
- Interest income: 53.53% tax rate.
- Dividends: 53.53% tax rate (non-Canadian companies); 39.34% tax rate (Canadian companies).

In order to benefit from the reduced 26.76% capital gains tax rate and 39.34% tax rate on dividends from Canadian companies, the Fund vehicles and carry partnership must be tax transparent for Canadian tax purposes, otherwise a return of carry (eg from a non-Canadian Fund partnership or carry vehicle) would be treated as a dividend from a non-Canadian company and subject to the higher 53.53% dividend tax rate. It is important to note that United States limited liability companies (LLCs) are not considered to be tax transparent for Canadian tax purposes.

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates for an individual resident in the province of Ontario, is 53.53% (including the Ontario provincial tax rate, there is no city income tax).

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USA

Grant of carry: If a carried interest holder is an employee or service provider to the General Partner, Fund manager or affiliate, the grant of carried interest (ie admitting the carried interest holder to the General Partner or carry limited partnership) should generally not give rise to employment income provided that the hypothetical liquidation value of the carried interest is zero.

The hypothetical liquidation value of the carry right would be zero if the Fund were to hypothetically liquidate immediately after the grant of the carried interest and the carried interest holder would not be entitled to any of the Fund's assets.

A carried interest recipient is often advised to file an election with the IRS under Section 83(b) of the US Internal Revenue Code ("IRC") within 30 days of receiving such interest.

Vesting: Vesting dates do not generally give rise to a US federal or state income tax liability in the hands of a US carried interest holder.

Receipt of carry: US carried interest holders are subject to US federal and state income tax when taxable income from the Fund is allocated to the carried interest holders. Importantly, carried interest holders can be allocated taxable income regardless of whether they have received cash distributions attributable to such income. As a result, Funds typically provide "tax distributions" to allow carried interest holders to receive cash distributions that are at least equal to their tax liabilities in an applicable tax year.

US federal income tax law also has special tax rules applicable to carried interest. The tax rate under the carried interest regime depends on a number of factors, particularly with respect to the length of time that the assets are held by the Fund in order to enjoy favorable long term capital gains rates. The highest marginal tax rate for US individual carry holders is therefore as follows (including the 3.8% US net investment income tax):

- Capital gains tax ("CGT") for US individual taxpayers:
 - Long term CGT rate: more than three years for gains allocable to carried interest, but only more than one year for gains allocable to the carried interest holder's capital invested in the Fund (eg the GP's cash commitment in the Fund): 23.8%.
 - Short term CGT rate: three years or less for gains allocable to carried interest, but only one year or less for gains allocable to the carried interest holder's capital invested in the Fund (eg the GP's cash commitment in the Fund): 40.8%.
- Qualified Dividends: 23.8% (stock held in a US corporation or resident of a tax treaty jurisdiction held for at least 60 days).
- Non-qualified Dividends: 40.8%.
- Interest: 40.8%.

Employment tax on salary: For employment income (eg salary and bonus) earned in 2022, the maximum marginal US federal income tax rate for a US individual is 40.8% (including 3.8% Medicare tax), with state income tax rates ranging from 0-12.3% (plus city taxes as applicable).

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Grant of carry: Provided that the conditions of the French statutory carried interest regime (the “Statutory Regime”) are met, the grant of carried interest rights should not give rise to French tax liability. One important condition of the Statutory Regime is that the carried interest rights must be subscribed to or acquired for a price that is commensurate with their value. In the case of an acquisition, the carried interest rights must be acquired at least for the higher of (i) the latest net asset value (if unavailable, the fair market value) of the carried interest rights; and (ii) their subscription value based on a minimum investment (as a rule: 1% of total investment commitments, if carry holders have a 20% carry entitlement, reduced to 0.5% for the portion of the commitment exceeding EUR1bn).

Vesting: In the context of the Statutory Regime, vesting does not give rise to a French tax liability.

Receipt of carry: French carry holders are subject to tax in France when carry returns are allocated to the French individual carry holders. As mentioned there is a bespoke carry regime, the Statutory Regime.

To the extent that the conditions of the Statutory Regime *are* met, carried interest proceeds received by the French individual carry holders are subject to a 30% flat tax (comprised of income tax at 12.8% and social security taxes at 17.2%). An exceptional tax on high income may also be payable at the rate of (up to) 4% for taxpayers. Therefore, the current maximum effective tax rate is 34%.

To the extent the conditions of the Statutory Regime *are not* met, proceeds received by the French individual carry holders are taxed as employment income, at the rate of (up to) 49%. In addition, the French individual carry holders would be liable to pay an additional specific social contribution of 30%. This would therefore lead to an effective maximum taxation rate of 79%.

Employment tax on salary: As a general rule, employment income is subject to individual income tax at the rate of (up to) 49% and social contributions (at the rate of (up to) approximately 45% for the employer and 25% for the employee).

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Germany

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment tax benefit equal to the fair market value of the carry less any consideration paid. Any such employment benefit would be subject to applicable employer source deductions for German employment tax and social security liabilities at the rate of (up to) 45% (including social security contributions, plus solidarity surcharge of 5.5% on tax rate if applicable).

Vesting: Vesting does not generally give rise to a German tax liability in the hands of a German carry holder.

Receipt of carry: German carry holders are subject to tax when carry returns are allocated to the individual carry holders. For German carry holders, there is a special carried interest tax regime ("CI Regime") which stipulates that 40% of the carried interest payment is tax-exempt, if certain conditions are met (see below).

To the extent that the CI Regime applies, the effective tax rate is c.27% for capital gains, dividends and interest income allocated to carry holders. By contrast, to the extent that the CI Regime does not apply, the effective tax rate is up to 45%, depending on whether the competent tax office deems the carry payment to be a service fee or profit share.

The application of the CI Regime is subject to the following conditions:

- The Fund qualifies as an "asset-managing entity" (*vermögensverwaltende Gesellschaft*) see below further.
- The purpose of the Fund is to acquire, hold and dispose of shares in corporations (applicable to most asset classes).

- The carry income is paid as remuneration for services rendered by the carry holder to the entity as contribution to its purpose (the Fund LPA should ideally contain provisions with respect to this).
- The Fund must be a limited partnership and.
- The carry income is only paid after full return of capital commitment to the other investors.

The definition of "asset managing entity" referred to above, in turn contains a number of further conditions set out in Guidance published by the Ministry of Finance, including no reinvestment of sales proceeds and no entering into short term holdings (less than a 3-5 year hold period).

Please note that there are pending court proceedings at the German Federal Fiscal Court regarding the interpretation of the carried interest regime (BFH – VIII R 3/21). The outcome may impact certain carry structures.

Finally, if there is uncertainty on the carry and Fund structure, a ruling application can be made to the German Tax Authorities. In particular with respect to real estate Funds, credit Funds and Funds in corporate form.

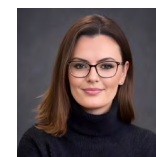
Employment tax on salary: The employment tax rate on earning, at the highest marginal tax rate, is 45% (including social security contributions, plus solidarity surcharge of 5.5% on tax rate if applicable).

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Ireland

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry less any consideration paid. Employment income is subject to the tax rates of up to 52% (including Universal Social Charge and Pay Related Social Insurance).

Vesting: Vesting does not generally give rise to an Irish tax liability in the hands of an Irish carry holder.

Receipt of carry: Irish carry holders are subject to tax when the carry returns are allocated to the individual carry holders. There is a specific carried interest regime in Ireland that must be considered, the Venture Capital (“VC”) regime.

The Irish tax rate depends on the nature of the return, and the highest tax rates are as follows (for individuals):

- Capital gains: 15% if the VC regime applies, otherwise a 33% tax rate applies.
- Dividends: 15% if the VC regime applies, otherwise a 52% tax rate applies.
- Interest income: 15% if the VC regime applies, otherwise a 52% tax rate applies.

There are a number of qualifying conditions in order to qualify for the VC regime, including the following:

- The qualifying VC Fund (“VCF”) must be an entity structured as a partnership.
- The main purpose of the qualifying VCF must be to make long term investments (3+ years) in “relevant investments”, which means unquoted shares or securities of private trading companies that carry on a business of research and development activities or the development of new technological, telecommunication, scientific or business processes, and does not carry on certain excepted trades. Accordingly, a venture capital Fund would likely carry on relevant investments, but a real estate investment Fund would ordinarily not.
- The investors in the qualifying VCF must be obliged under a legally binding agreement to provide capital sums for investment purposes over a period of time.
- The regime only applies to the proportion of carried interest that derives from relevant investments in EEA states (including Ireland) and the United Kingdom. The carried interest also must not exceed 20% of the total profits of the qualifying VCF.

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates, is 52% (including Universal Social Charge and Pay Related Social Insurance).

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Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the fair market value of the carry less any consideration paid. Employment income is subject to the ordinary marginal rates up to 52% (including surcharges and social security contributions).

Vesting: Vesting does not generally give rise to an Italian tax liability in the hands of an Italian carry holder.

Receipt of carry: Absent any special rule, carried interest receipts are subject to employment tax rates. There is however a bespoke carried interest tax regime which provides a reduced rate, and this applies to all asset classes.

Under the bespoke carried interest regime, subject to certain conditions, carried interest is treated as receipts as “financial income”, in the case of interest, dividends and capital gains, and subject to tax at the rate of 26%.

In summary the conditions under the regime are that:

- The total coinvest (ie GP commitment) invested by the Managers is equal to at least 1% of the Fund investment.
- The carried interest is only paid to the Managers after all investors in the Fund (including Managers on the coinvest) have received an amount equal to their equity invested plus the hurdle rate.
- The managers maintain their co-investment in the Fund for at least five years.

If the above conditions are not satisfied, the carried interest proceeds are not automatically treated as employment income. It is possible to file a ruling request to the Italian Tax Authorities to demonstrate the financial nature of the carried interest (instead of being treated as employment income).

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates, is 52% (including surcharges and social security contributions).

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Luxembourg

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of the carried interest (eg admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry right less any consideration paid. Any such employment benefit would be subject to applicable employer source deductions for Luxembourg tax purposes.

Vesting: Vesting does not generally give rise to a Luxembourg tax liability in the hands of a Luxembourg carry holder.

Receipt of carry: Luxembourg carry holders are subject to tax when the carry returns are allocated to the individual carry holders.

Carried interest is defined as meaning that the investors in the Fund are repaid their capital commitment prior to payment of carried interest (which is generally the case in most Funds). There is currently no favourable carried interest taxation regime in Luxembourg. In the most typical fund structures (ie tax transparent funds) the tax treatment depends on the nature of the underlying assets, but may generally be described as follows:

- Capital gains would be taxable at a progressive income tax rate of up to 45.78% (excluding social security), when the disposal takes place within six months of the acquisition. After the six month holding period, the capital gain realised

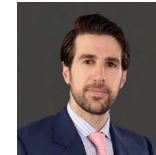
on the disposal of underlying shares is not taxable unless the taxpayer has substantial participation in the company (generally via a direct or indirect participation of more than 10% of the shares), however this is rarely applicable where there are a number of carry holders. For completeness, capital gains realised on a substantial participation more than six months after the acquisition thereof are taxed at a lower rate according to the half-global rate method.

- Dividends would be taxable at a progressive income tax rate of up to 45.78% (excluding social security). A 50% exemption may be available under certain conditions.
- Interest will generally be subject to a 20% tax (subject to conditions).

For completeness, carried interest profit entitlement derived from *tax opaque funds* will be taxed as miscellaneous income at a progressive income tax rate of up to 45.78% (excluding social security, and other than capital gains on the securities, shares or units representing carried interest realised six months after the acquisition thereof).

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates, is 45.78% (excluding social security).

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Netherlands

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of the carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry right less any consideration paid. Any such employment benefit would be subject to Dutch individual income tax at the rate of 49.5% (including employee contributions).

Vesting: Vesting does not generally give rise to a Dutch income tax liabilities.

Receipt of carry: Dutch carry holders are subject to tax when carry returns are allocated to the individual carry holders.

Dutch carry holders can opt to structure their carry investment in a bespoke carry regime, known as the Box II regime (“Box II Regime”) allowing for a more favourable tax treatment.

The Box II Regime requires Dutch carry holders to hold their carry investment through a separate (generally Dutch) pooling entity (eg a personal holding company). Such pooling entity must satisfy the conditions under the (Dutch) participation exemption on income and capital gains received and a Dutch carry holder must hold a so-called substantial interest (eg a minimum

5% interest in a class of shares) in the pooling entity. Furthermore, upon receipt of any income or capital gains from the carried interest rights, the pooling vehicle must distribute at least 95% of such income or capital gains to Dutch carry holders in the same calendar year. The Dutch carry holder must report such distribution in its individual income tax return as Box II Regime income for that year.

To the extent that the conditions of the Box II Regime *are* met, carried interest proceeds received by the Dutch individual carry holders are subject to a 26.9% flat tax (2023 rate) (expected to go up to a maximum 31% flat tax rate in 2024). This applies irrespective of the nature of the return, as consisting of capital gains, interest income or dividends.

To the extent the conditions of the Box II Regime *are not* met, proceeds received by the Dutch individual carry holders are taxed at the rate of (up to) 49.5% (2023 rate).

Employment tax on salary: As a general rule, employment income is subject to individual income tax at the rate of (up to) 49.5% (including employee contributions).

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Spain

Grant of carry: The grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry right less any consideration paid. Any such employment benefit would be subject to Spanish employment tax and social security obligations.

There is however a favourable carried interest tax regime applicable to venture capital and buyout Funds only, under which it is arguable that no tax liabilities arise on the granting of the carry, subject to the carried interest condition being satisfied, see below. Please note however that the carried interest regime came into force in January 2023, and further Guidance from the Spanish Tax Authorities is forthcoming which may impact this analysis herein.

Vesting: Vesting does not generally give rise to a Spanish tax liability in the hands of a Spanish carry holder.

Receipt of carry: Spanish carry holders are subject to tax when the carry returns are allocated to the individual carry holders.

Irrespective of the nature of the return allocated to the carry holder, the carry returns are treated as employment income. The Spanish tax rate on employment income, at the highest marginal tax rates for an individual, is 54%.

Under the bespoke carried interest tax regime, there is a 50% reduction of the employment tax liability, and therefore the effective rate would be 27% on receipt of the carried interest.

The conditions to be satisfied under the bespoke carried interest regime, include as follows:

- The Fund must invest in venture capital and buyout (ie real estate and credit Funds are excluded).
- The carry rights are conditional upon the investors obtaining a minimum guaranteed return (hurdle rate).
- The carried interest rights must be held by the carry vehicle for a minimum of five years (or, in the absence of carry vehicle, by the managers).
- This tax regime only applies to carried interest from Spanish venture capital entities, EU vehicles (eg EuVECA, EUSEF, ELTIFs) and equivalent investment entities in other jurisdictions (this will include for example a Luxembourg SCsp or English limited partnership). However, the favourable tax regime does not apply to carried interest from investment vehicles located in non-cooperative jurisdictions (eg Cayman or Channel Islands partnerships).

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates, is 54%.

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Sweden

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) should not give rise to Swedish employment tax.

Vesting: Vesting does not generally give rise to a Swedish tax liability in the hands of a Swedish carry holder.

Receipt of carry: Swedish carry holders are subject to tax when the carry returns are allocated to the individual carry holders. There is no specific carried interest tax regime in Sweden.

Case law from the Supreme Administrative Court of Sweden in 2018 states that carried interest returns should be taxed under the Closely Held Company rules (Swe. Fåmansföretag).

Depending on the circumstances however, there is a possibility for the carry holders to hold their carried interest rights through a Swedish holding company. This can either be a single company holding the carry rights for all the carry holders (a pooling vehicle) or each carry holder will have their own personal holding company ("PHC") (each, a "Holding Company").

There are three key advantages to holding carried interest through a Swedish Holding Company:

- Timing: receipts of dividends and capital gains by the Holding Company is not subject to Swedish tax on dividend and capital gains received (under the participation exemption rules). Accordingly, carry receipts can be reinvested into new investments (particularly in the case of a PHC). Interest received by the Holding Company is however subject to Swedish corporation tax at the rate of 20.6%.

- Tax rate *after* five years of Manager ceasing to be active: if the Holding Company makes distributions to the Manager shareholder five years after the Manager is no longer active (ie in practice this means five years after the Fund has liquidated and the Manager is not active with respect to another qualifying closely held company) the shareholder is taxed at the 25% tax rate on dividends and capital gains repatriations (eg liquidation or share buybacks) to the Manager shareholder.
- Tax rate *within* five years of Manager ceasing to be active: even if the Holding Company makes distributions or capital repatriations to the Manager shareholder within five years of the Manager ceasing to be active, the individual tax rate is still less than receiving carry direct, and the tax rate is broken down depending on the amount of the dividend and capital gain received (the below thresholds assume that the carry holder is holding carry through a wholly owned PHC):
 - Tier 1 – savings threshold of circa EUR16,000: dividends and capital gains: 20% tax rate.
 - Tier 2 – exceeding Tier 1 savings threshold and below c. EUR590,000 dividends and c. EUR646,000 for capital gains: dividends and capital gains taxed as employment income tax rates of (up to) 55% (although no social security liabilities).
 - Tier 3 – amounts exceeding Tier 2: dividends and capital gains taxed at a 30% tax rate.

Employment tax rate on salary: 55% for an employee (and employer pays social security at the rate of 31.42%).

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UK

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to an employment benefit equal to the market value of the carry right less any consideration paid, at the employment tax rate of up to 47%. Any such employment benefit would be subject to applicable employer source deductions through PAYE (and including national insurance obligations).

There is a safe harbour test (pursuant to a Memorandum of Understanding (the "MoU")) in the UK which can mitigate such employment tax liability, subject to a number of conditions being satisfied. These conditions include: (i) a capital contribution made by all the UK carry holders, in aggregate, for acquisition of carry, at the rate of GBP2,500 per GBP100m of capital contributions by the investors, and (ii) grant of carry should take place prior to the Fund making any investments, or if later, prior to the market value of the Fund investments exceeding their acquisition cost. A number of other conditions must also be satisfied.

A section 431 election should also be signed between employer and employee within 14 days of acquisition, and a notification of the grant of carry to a UK employee should be made to HMRC (ERS return).

Vesting: Vesting does not generally give rise to a UK tax liability in the hands of a UK carry holder, in particular if a section 431 election is signed by the employer and employee.

Receipt of carry: UK carry holders are subject to tax when the carry returns are allocated to the individual carry holders. The UK tax rate depends on the nature of the return, and the highest tax rates are as follows:

- Capital gains including share buybacks, disposal proceeds or repayment of loan principal: 28% tax rate (note that this is higher than the ordinary 20% capital gains tax rate).
- Interest income: 45% tax rate.
- Dividends: 39.35%.

There are a number of complex anti-avoidance rules that look to recharacterize what would otherwise be a capital gain (subject to the 28% tax rate), into income (subject to 45% tax rate, plus social security). These anti-avoidance rules are complex, and although we don't generally expect them to apply in most cases, careful analysis is required, and for certain Funds (in particular Real Estate Funds), structural changes may also be required.

In order to benefit from the reduced 28% capital gains tax rate, the Fund vehicles and carry partnership must be tax transparent for UK tax purposes, otherwise a return of carry would be treated as a dividend.

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates, is 47% (including employee national insurance, plus employer national insurance at the rate of 13.8%).

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Australia

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of carried interest (ie admitting the carry holder to the carry limited partnership) could give rise to Australian fringe benefits tax ("FBT") levied on the employer, on the market value of the carry less consideration paid. FBT is generally levied on the employer at the rate of 47%.

Vesting: Vesting does not generally give rise to Australian tax implications for the Australian carry holder or Fund manager.

Receipt of carry: Australian carry holders are subject to tax when carry returns are allocated to the individual carry holders. The general position is that carried interest returns (capital gains, dividends and interest) are taxed as ordinary income, up to the rate of 47%.

There is however a special tax regime available with respect to certain venture capital Funds, which taxes all carried interest receipts (capital gains, dividends and interest) from such Funds at concessional rates of up to 23.5% (a 50% reduction to the highest marginal tax rate of 47%).

The tax regime applies to payments of carried interests received by:

- General partners of Venture Capital Limited Partnership ("VCLPs"), early stage VCLPs and Australian venture capital fund of funds ("AFOFs"); and
- Limited partners in venture capital management partnerships ("VCMPs").

A number of conditions must be satisfied in order to benefit from the reduced 23.5% rate.

Furthermore, where a carry holder in one of these concessional vehicles is non-Australian resident, carried interests will be tax exempt to the extent it is not attributable to taxable Australian property.

Employment tax on salary: the employment tax rate on earnings, at the highest marginal tax rate, is 47% (including the 2% Medicare levy).

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Hong Kong SAR China

Grant of carry: An employee or director of the Fund manager or affiliate should not be subject to tax on the grant of carried interest.

Vesting: Vesting does not generally give rise to a Hong Kong tax liability in the hands of a Hong Kong carry holder.

Receipt of carry: Hong Kong carry holders are subject to salaries tax when the carry returns are allocated to the individual carry holders. Hong Kong's top progressive salaries tax rate is (up to) 17%. There is however a bespoke carry regime, which if applicable, provides a full exemption from tax on eligible carried interest, irrespective of the nature of the carry return (gains, interest income and dividends), to the extent that the relevant conditions are satisfied. These conditions include:

- The carried interest must be an eligible carried interest which is a profit-related return subject to a hurdle rate as stipulated in the agreement governing the operation of the Fund (eg the LPA).
- The carried interest must be distributed by a "qualifying investment Fund", which is a Hong Kong established Fund, certified by the Hong Kong Monetary Authority specifically for this regime.
- The carried interest must be derived from "qualifying transactions", which include transactions in shares, securities and loan stock, provided that the profits distributed to the Fund are exempt from Hong Kong tax at Fund level pursuant to the unified Fund exemption regime.

- The Hong Kong carry holder must be an employee employed by a "qualifying person". Such qualifying person must be:
 - (i) a corporation or authorised financial institution licensed under the Hong Kong Securities and Futures Ordinance,
 - (ii) a person carrying out investment management services in Hong Kong for a qualifying investment Fund, or
 - (iii) a Hong Kong Innovation and Technology Fund Corporation.
- The qualifying persons must satisfy the following "substantial activities" requirements:
 - The average number of full-time employees in Hong Kong carrying out the prescribed investment management services should be two or more; and
 - The operating expenditure incurred in Hong Kong for the provision of the prescribed investment management services should be HKD2m or more.

In order to benefit from the concessionary tax treatment, both the Fund Manager (as the employer) and Hong Kong carry holder (as the employee) must also fulfill certain tax filing and reporting requirements.

Employment tax on salary: The employment tax rate on earnings, at the highest marginal tax rates for an individual resident in Hong Kong, is 17%.

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Singapore

Grant of carry: If a carry holder is an employee or director of the Fund manager or affiliate, the grant of the carried interest (ie admitting the carry holder to the limited partnership) could give rise to an employment tax benefit equal to the fair market value of the carry right, less any consideration paid.

Any such benefit would be subject to Singapore personal income tax, to the extent it is considered Singapore sourced employment emolument. The personal income tax rate employment income ranges from 0% up to 24% (the highest 24% tax rate applies to income in excess of SGD1m).

Vesting: Upon vesting of the carry, the open market price of the shares on the date of vesting less any price paid for the shares (or employment tax on the market value of the shares on grant) will be subject to Singapore personal income tax in the hands of the employee.

Receipt of carry: There are no specific guidelines or bespoke tax regime with respect to the taxation of carried interest in Singapore. As such it follows the ordinary Singapore taxation principles.

If the carry is held through an onshore Singapore resident company the following would apply with respect to returns received from the Singapore resident company:

- Dividend distributions and capital gains: tax exempt.
- Interest income: may be subject to Singapore personal income tax (at the rate of up to 24%).

If the carry is held through an offshore carry vehicle, the following would apply with respect to returns received from the offshore carry vehicle:

- Dividend distributions: considered foreign sourced income for Singapore tax purposes, and as such exempt in the hands of the Singapore resident carry holder, unless dividends are received by a resident individual via a Singapore partnership.
- Capital gains: tax exempt as Singapore does not tax capital gains.
- Interest income paid by the offshore vehicle to the carry holder is exempt from tax unless received via a Singapore partnership.

In practice, Singapore based investment professionals generally acquire their carried interest through an offshore carry structure, although carry held through an onshore Fund manager is also not uncommon.

Technically, there is a risk that the receipt of carried interest (dividends and gains) could be recharacterized as taxable personal service/employment income. Although in practice, this is rare.

Employment tax: The employment tax on earnings, at the highest marginal tax rates for an individual resident in Singapore, is 24% (the highest 24% tax rate applies to income in excess of SGD1m).

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