

Tax Newsletter

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How is carried interest precisely taxed?

- The notion carried interest ("CI") dates from the 16th century: the captain of a vessel transporting merchandise was entitled to a part of the after-sale profit.
- In the private equity business industry, investment companies ("InvestCo") are often used, e.g. a Pricaf Privée. In order to align the interests of fund managers with those of passive investors, fund managers are mostly asked to also (in)directly invest in InvestCo. Following a waterfall distribution system, the fund managers are thus entitled to a subordinated return on equity. Indeed, the passive investors will be the first to derive InvestCo income, be it that the return on equity earned by the fund managers is disproportional and therefore higher than the proportional (i.e. in function of their InvestCo stake) income earned by the passive investors. Such disproportional income is called CI. Generally, it is paid one-off when InvestCo is wholly or partially (e.g. upon redemption of its own shares) liquidated.
- As of 2025, the Belgian legislator has come up with a specific personal tax regime for CI.
- Before, there was often discussion upon tax audit or in court as to the classification for tax purposes of CI in the hands of the beneficiary. The tax authorities (but mostly in vain) tried to treat it as 'business income', e.g. in an ESOP context.
- Going forward, CI is treated as 'investment income' taxable at 25% personal tax and without application of local taxes. Taxation as 'business income' is even explicitly excluded.
- As CI qualifies as 'investment income' withholding tax may be due.
- Double good news: when a natural person receives CI through qualifying stock options or warrants, this transaction is out of the scope of CI tax legislation. Moreover, as disproportional return on equity is taxed as CI income, the general 10% capital gains taxation should not be due.
- Conversely, proportional income derived from shares is targeted by the 10% general capital gains taxation. Be careful: if it appears that this is 'abnormal income' derived from shares, 33% personal tax + communal taxes can be due.
- For completeness' sake, if a company has a CI investment on B/S, it cannot record a liquidation reserve.