Hedge Fund Managers Hedged In By Taxes

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The clock is ticking for hedge fund managers and each tick resonates with the distinctive *ca-ching* of money leaving the manager's pockets.

For years, a tax code loophole enabled hedge fund managers to accumulate offshore gains without the requirement to pay federal or state taxes. Managers of offshore funds could simply defer receipt of compensation (which could be management fees, performance fees, or both) and avoid the immediate tax while also benefiting as the savings grew, tax-free.

It Wasn't Fake News

In 2007, writers at the *New York Times* and other publications helped draw attention to the tax loophole. With the US economy teetering on the edge of financial crisis, aka the Great Recession, Congress had little choice but to vote to close the loop.

Section § 457A of the Internal Revenue Code, which deals with nonqualified deferred compensation, was effectively changed as part of the Emergency Economic Stabilization Act of October 2008, when Congress sought to raise revenue and enhance economic stability. The legislation, however, allowed hedge fund managers a generous ten years, a full decade, to pay the taxes on the accumulated money.

The Hour Draws Near

As Jon Shazar noted in his article, Tax Loophole Closure Forcing Steve Cohen Back To Work (published online by Dealbreaker.com, July 20, 2017), in 2008, the Joint Committee on Taxation estimated that the collective back taxes due could be as much as $25 billion. Other tax specialists have projected the amount to be as great as $100 billion.

Either way, the individual tax bill for some managers will be staggering. The founder of SAC Capital Advisors, Steven Cohen, for example, has a billion dollars of deferred offshore income that is likely to be subject to taxation. And CNBC identified that David Einhorn of Greenlight Capital and Daniel Loeb of Third Point each face tax bills of over $100 million.

Loop Holes Around the Loop Hole?

Despite ten years to strategize, tax advisors have come up with little to offer hedge fund advisors as a workaround to avoid the impending tax payment. Charitable donations or charitable lead annuity trusts may provide tax relief, but these tactics will still separate hedge fund managers from their money.

Meanwhile, at 4.87 percent, the first half of 2017 has been the best year for hedge fund growth since 2009, when hedge funds saw returns of nearly 17 percent.

More:

- Hedge funders scramble for ways to pay tax bill now that a big loophole is closed
- Loophole Closed: Hedge-Fund Managers Prepare Huge Tax Checks
- America is about to get billions in tax dollars from hedge-fund managers