



Tax Aware

Taxes, Charity, and Hedge Funds: Tax Implications of Charitable Contributions of Leveraged Partnership Interests

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As a result of recent Treasury regulations, investment partnerships, such as hedge funds, might be required to allocate nonrecourse liabilities to their limited partners (LPs). This allocation of nonrecourse liabilities could result in recognition of capital gains by LPs when they contribute their partnership interests to a charity. We explain how such taxable gains upon charitable contributions arise and quantify how punitive they might be. Although investors in tax-efficient leveraged funds organized as investment partnerships are likely to recognize capital gains upon charitable contributions, when these capital gains are evaluated in the context of tax benefit and pre-tax return opportunities, they do not present a hurdle for tax efficient investing. For charitably inclined leveraged fund investors, the benefits of a fund's tax efficiency greatly outweigh the capital gain tax liability they might incur upon contribution of their fund holdings to a charity.

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