



Why AB 2731 is Bad Policy

AB 2731 would impose a 17 percent surtax on carried interest earned by venture capitalists and other partnerships. Despite AB 2731's populist appeal and misrepresentation as closing a loophole, this bill would wreak significant economic damage by singling out venture capital for a punitive tax increase.

AB 2731 Will do Great Harm to the California Economy

AB 2731 would impose one of the largest tax increases in state history on the industry that is responsible for building the next generation of California companies. Damage to the economy would include:

- **VC Exodus:** It's likely that the bill would lose a significant amount of the promised revenue simply by the targets moving before realizing their carried interest capital gains.
- **Depressed startup activity:** Because VCs fund high growth companies that have become so important to the California revenue base, it would only take a few missed opportunities to more than offset all of the potential revenue gained by this bill. Given the unprecedented size of the tax increase, this is highly likely to happen.
- **Declining participation in venture capital by underrepresented groups:** Increasing taxes on carried interest will make it harder for people of diverse backgrounds, who are more likely to start smaller firms and thus be reliant on carried interest to make economics work, to break into the industry.

What is Carried Interest?

Carried interest is the profit share that VCs receive if their overall fund is successful (meaning new companies and technologies we successfully built). When an individual in a successful endeavor decides to sell their share, longstanding tax policy has recognized that as a capital gain. This is as true for somebody who opens a restaurant with outside capital, for a real estate partnership, or for a venture capital partnership.

How Would this Compare to Other States?

If AB 2731 passed, California would tax carried interest earned by venture capitalists at more than **three times** the rate of the next highest state in the country:

Potential Tax Rates by State on Carried Interest if AB 2731 Passes

California	30.30%
Oregon	9.90%
Utah	5.00%
Arizona	4.54%
Nevada	0.00%
Washington	0.00%

Added to the Federal Tax Bill the Impact of AB 2731 Could be Devastating California VCs were hit by higher taxes on carried interest arising from projects of less than three years and the severe curtailment of the deductibility of state and local taxes (SALT). Most economists agree that the loss of SALT deductibility will make taxpayers more sensitive to state tax changes, especially those of the size of AB 2731