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Taxation Alert

Congress Extends the 100% Tax Exemption for Gain on Certain Qualified Small Business Stock

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Retroactive Effect Through 2013

On January 2, 2013, President Obama signed into law the American Taxpayer Relief Act of 2012 (the "Act").

Among its provisions, the Act extends a tax benefit whereby capital gains from the sale or exchange of certain qualified small business stock ("QSBS") held by non-corporate taxpayers can qualify for a 100% exclusion from federal income taxation, including from the alternative minimum tax. This tax exemption had expired on December 31, 2011.

The new law retroactively restores and extends the exemption. As a result, provided certain holding period and other requirements are satisfied, capital gains from the sale of QSBS acquired after September 27, 2010 and on or before December 31, 2013 can qualify for the 100% tax exemption.

Capital gains that are exempt from taxation under the QSBS rules also should not be subject to the new 3.8% tax on net investment income that, beginning in 2013, generally applies to capital gains realized if certain income thresholds are exceeded.

Looking beyond 2013, if Congress does not enact additional legislation, the capital gain exclusion amount will revert to 50% (60% for certain "empowerment zone corporations") for qualifying sales of QSBS acquired on or after January 1, 2014. Consequently, a portion of the gain from the sale or exchange of such QSBS will be subject to federal income taxation, the alternative minimum tax and the 3.8% tax on net investment income.

For more information on the requirements for qualifying for the QSBS tax exemption, including the greater than 5 year holding period requirement, click here to view an earlier communication on this topic.

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