LEXSTAT LEXIS EXPLANATION IRC SEC. 1202(A)

LexisNexis Explanation

IRC § 1202(a)
Partial Exclusion for Gain from Certain Small Business Stock
Exclusion

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Lexis Explanation IRC Sec. 1202(a)

Individuals and non-corporate stockholders (e.g. trusts) who sell qualifying small business stock acquired at original issue and held for more than 5 years may exclude 50 percent (60 percent for stock of certain empowerment zone businesses) of the gain from the sale, if certain statutory requirements are met. The American Recovery and Reinvestment Act of 2009, P.L. 111-5, 02/17/2009, has increased this exclusion to 75 percent for qualified small business stock acquired after February 17, 2009 and before January 1, 2011. For details, see below.

For stock of a small business corporation acquired after August 10, 1993, as original issue by an individual or other non-corporate stockholder, 50 percent (60 percent for stock of certain empowerment zone businesses acquired after December 21, 2000) of the gain is excluded if the stock is held for more than five years.1 The amount of the overall gain eligible for this computation is limited to 10 times the taxpayer's basis in the stock, or, if it is greater, $10 million (half for a married individual filing separately).2 For example, if the taxpayer's stock contribution is $100,000, the maximum exclusion is $500,000.

For small business stock acquired after December 21, 2000, which qualifies as an empowerment zone business,3 the exclusion is increased from 50 percent to 60 percent, as to gain attributable to periods before 2015.4 Also, the tax-free rollover within 60 days applies if the original zone asset is held for more than one year and replaced by one in the same zone.5

As a result of the exclusion and effective capital gains rates, gain from the sale of qualified small business stock is taxed at effective rates of 14 percent under the regular tax and (i) 14.98 percent under the alternative minimum tax for dispositions before 2011; (ii) 19.98 percent under the alternative minimum tax for dispositions after 2010, in the case of stock acquired before 2001; and (iii) 17.92 percent under the alternative minimum tax for dispositions after 2010, in the case of stock acquired after 2000.6

Exclusion percentage increased to 75 percent. The American Recovery and Reinvestment Act of 2009, P.L. 111-5, 02/17/2009, has increased the percentage exclusion for qualified small business stock sold by an individual or non-corporate stockholder from 50 percent (60 percent for certain empowerment zone businesses) to 75 percent for qualified small business stock acquired after February 17, 2009 and before January 1, 2011. IRC § 1202(a)(2) that provides 60 percent exclusion for certain empowerment businesses does not apply. 7As a result of the increased exclusion, gain from the sale of qualified small business stock to which the provision applies is taxed at effective rates of 7 percent under the regular tax and 12.88 percent under the AMT.

FOOTNOTES

(1) IRC § 1202(a).
(2) IRC § 1202(b).
(3) IRC § 1397C.
(4) IRC § 1202(a)(2).
(5) IRC § 1397B.
(6) IRC § 1(h) and § 55(b)(1).
(7) IRC § 1202(a)(3).