



## Encourage Investments in Small Business through the Tax Code

One way to encourage investors to make capital commitments to small businesses is to reduce the capital gains rate for holding the investment over the long haul. While the capital gains rate can be as high as 23% for the sale of most long-term assets, Congress has recently allowed taxpayers to exclude capital gains income for investments in qualified small business stock.

Long-term capital investments allow businesses to spend on capital projects and job creation. Many venture and growth companies need extra cash to stay competitive and broaden their products into new markets. As investors seek new opportunities to help small businesses grow, it is imperative that Congress continues promoting long-term investments in qualified small businesses. The 1202 capital gains exclusion is an excellent way to continue to encourage risk taking and patient capital.

The qualified small business investment tax incentive has been tucked into the annual tax extenders' bill for the past few years. Making this provision permanent is very important to provide certainty for investors and to encourage long-term investment and business formation.

Congress should modernize this tax provision to apply to an expanded universe of small business investments. SBIA recommends making these small changes:

1. Modernize the definition of QSB to include all investments consistent with the definition of small business under the Small Business Investment Act of 1958 (as amended). This would simplify eligibility requirements, requiring less paperwork and administrative burdens. Also, it would allow more growth-oriented small businesses to access capital.
2. Clarify that small business stock can include stock acquired upon the exercise of warrants. This would reduce the initial cost of capital for small businesses by adding equity to a debt deal.
3. Allow investors that sell qualified small business stock held over three years to defer recognition of capital gains by reinvesting the sale proceeds in new qualified stock within six months. This would encourage repeat investors to invest in more than one small business.
4. Increase the gross asset test in the Qualified Small Business (QSB) definition from \$50 million to \$75 million and index for inflation. This update of the definition will keep up with the growth of the economy.