

# WHAT ABOUT THE IMPACT INCENTIVE

AN EASY (AND LONG-OVERLOOKED) TAX  
POLICY UPDATE THAT COULD HAVE AN  
IMMEDIATE IMPACT ON STARTUPS ACROSS  
THE COUNTRY

DATE

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BY

**JOE MILAM**

CEO, ANGELSPAN, INC.

ABOUT THE

# OPPORTUNITY

Congress has the opportunity to support entrepreneurs, innovators, and job creators across all 50 states by building off of proven and popular private sector incentives.

By modernizing an existing tax incentive, Congress can expand the vision set forth in the Opportunity Zone legislation and harness the productive capabilities of the workforce.

## Impact Incentive

### QSBS Sec. 1244

Passed in 1958 [as part of the Small Business Investment Act](#), the Qualified Small Business Stock (QSBS) under I.R.S Code Sec. 1244 was included in the '1958 Act' to **incentivize investment in** the new asset class called **venture capital**.

QSBS Sec. 1244 allows for **losses** on investment in 'Qualified Small Business Stock' to be **deducted against ordinary income** and applies for the earliest - and most risky - investment rounds startups source to get off the ground.

**Most early venture investors were wealthy families**, and this law was included in the '58 Act to stimulate more investment in SBICs and venture funds.

## Overlooked Since 1978

### [Revenue Act of 1978](#)

As part of the Revenue Act of 1978, the levels/limits of QSBS Sec. 1244 were updated from the original levels/limits to account for inflation.

**However, the levels/limits have not been updated since 1978.**

Simply updating the QSBS Sec. 1244 would not only modernize the law, it would stimulate more investment in new ventures around the country.

**Sec. 1244 is largely overlooked today due to lack awareness.**

# ABOUT THE NEED

Most new job creation comes from innovative new companies - largely funded by angel investors and venture capitalists. However, over 75% of venture activity takes place in 3 regions - Silicon Valley, New York and Boston. There is untapped potential across the country.

## Recognized Need

Numerous organizations have published research framing the need to more equitably distribute the resources required by - and the economic benefits resulting from - vibrant entrepreneurial activity:

- [The Brookings Institute](#)
- [Heartland Forward](#)
- [Kauffman Foundation](#)
- [U.S. Impact Investing Alliance](#)

### Decline in Life Expectancy

[Additional research](#) has drawn links between the decline in life expectancy due to accelerated drug overdoses and suicide rates in the U.S. and the absence of sufficient entrepreneurial/new business job creation in so many communities across the country.

We clearly need a coordinated effort to address this 'opportunity gap' so prevalent across the U.S. today.

### Losing Innovation Race to China

America is losing its competitive edge with China, particularly in critical technologies of the future such as blockchain, artificial intelligence, manufacturing robotics, and alternative/solar energy.

## Supporting Legislation

The NIH, DARPA, DOE, National Science Foundation, et. al., have availed Federal grant funding to support research, scientific innovation, and tech transfer from our National Labs.

There has been numerous legislative efforts to mobilize more capital for startups. Some incorporated Fiscal Policy incentives;

- QSBS Sec. 1244 - '1958 Act'
- QSBS. Sec. 1202 - 1993, updated in 2009 (PATH Act)
- Opportunity Zones - 2017

Other legislation established/regulated formal structures/strategies;

- SBICs - '1958 Act'
- Opportunity Zone Funds - 2017

### Current Legislative Initiatives

There was legislation introduced, with bi-partisan support, to mobilize Federal dollars to support innovation;

- [New Business Preservation Act](#) (May, 2020)
- [Energizing Technology Transfer Act](#) (Sept., 2020)

**Simply updating QSBS Sec. 1244 again would support all these legislative agendas.**

## ABOUT THE

# SPECIFICS

To update/modernize the [Impact Incentive](#) - QSBS Sec. 1244 - simply use the language from the legislation when it was indexed/modernized last, and use the new numbers to account for the change in CPI.

### Specific Levels Needing Updating

When QSBS Sec. 1244 was passed in 1958, it allows for losses from venture investing by taxable individuals to be deducted against ordinary income.

This tax treatment was only available to those taxable investors that were part of the first **\$500,000** invested in the QSBS.

Those investors that took Sec. 1244 deductions were limited to:

- **\$25,000** of losses for single filers
- **\$50,000** of losses for joint tax returns

In 1978, as part of the [Revenue Act of 1978](#), the levels & limits were updated to:

- From \$500,000 investment threshold to **\$1,000,000**
- **\$25,000** of losses for single filers to **\$50,000**
- **\$50,000** of losses for joint tax returns to **\$100,000**

These levels/limits - in 1978 dollar terms - is where the levels/limits remain today - 42 yrs later.

To put the levels/limits in **2020 dollar terms**;

- The **\$1,000,000** investment level would go to **\$3,800,000**
- **\$50,000** for single filers goes to **\$190,000**
- **\$100,000** for joint filers goes to **\$380,000**

### Actual Legislation Language

#### [Updated levels/limits plugged into the Revenue Act legislative language:](#)

#### SEC. 345 SMALL BUSINESS CORPORATION STOCK.

(a) INCREASE TO \$3,800,000 AMOUNT OF STOCK POTENTIALLY SUBJECT TO ORDINARY LOSS TREATMENT; REMOVAL OF EQUITY CAPITAL TEST.- 26 USC 1244. Subsection (c) of section 1244 (relating to losses on small business stock) is amended by striking out paragraph (2) and inserting in lieu thereof the following:

#### "(3) SMALL BUSINESS CORPORATION DEFINED.-

"(A) IN GENERAL.-For purposes of this section, a corporation shall be treated as a small business corporation if the aggregate amount of money and other property received by the corporation for stock, as a contribution to capital, and as paid-in surplus, does not exceed \$3,800,000 (indexed from the current level of \$1,000,000). The determination under the preceding sentence shall be made as of the time of the issuance of the stock in question but shall include amounts received for such stock and for all stock theretofore issued.

"(B) AMOUNT TAKEN INTO ACCOUNT WITH RESPECT TO PROPERTY.-For purposes of subparagraph (A), the amount taken into account with respect to any property other than money 92 STAT. 2844 92 Stat. 2844 1978 PUBLIC LAW 95-600-NOV. 6, 1978 shall be the amount equal to the adjusted basis to the corporation of such property for determining gain, reduced by any liability to which the property was subject or which was assumed by the corporation. The determination under the preceding sentence shall be made as of the time the property was received by the corporation."

(b) INCREASE IN MAXIMUM AMOUNT TREATED AS ORDINARY LOSS FOR ANY TAXABLE YEAR.-Subsection (b) of section 1244 is amended- 26 USC 1244. (1) by striking out "\$50,000" in paragraph (1) and inserting in lieu thereof "\$190,000", and (2) by striking out "\$100,000" in paragraph (2) and inserting in lieu thereof "\$380,000".

ABOUT THE

# URGENCY

Congressional hearings, negotiations, proposed legislation, political campaigns, and media narratives all recognize the urgency to use all tools at our Governments' disposal to support small business and entrepreneurial activity.

It is imperative that leadership  
from both parties simply do what's  
right, what's right in front of them,  
and do it right now.

**JOE MILAM**

CEO, ANGELSPAN, INC.

JOE@ANGELSPAN.COM