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# OBBBA: Tax Savings for PE Portcos and Technology Companies

September 4, 2025



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## Session CPE Requirements

You need to attend 50 minutes to receive the full 1 CPE credit.

There will be 4 polling questions throughout the presentation. You must respond to a minimum of 3 to receive the full 1 CPE credit.

**\*\*Both requirements must be met to receive CPE credit\*\***



# Speakers



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Principal



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# Learning Objectives

01

Identify the enhancements to the Section 1202 Qualified Small Business Stock gain exclusions

- The impacts of possible conversion to C corporation

02

Recall the changes to the expensing of R&D rules and how to adopt them

03

Recall the changes to the expensing capital improvements

04

Recall the latest guidance relating to Section 174A R&D expenses under Revenue Procedure 2025-28



# *Agenda*

- OBBBA overview
- Individual provisions
- Business provisions
- Planning opportunities



# Polling Question

- How optimistic are you on the current economic conditions and the impact to your organization?
  - 5 = Very confident
  - 4 = Confident
  - 3 = Neutral
  - 2 = Somewhat confident
  - 1 = Not at all confident





# Changes to Expensing Capital Improvements





# Bonus Depreciation

- Permanently extends 100% expensing – property acquired and placed in service after 1/19/2025
- Qualified Production Property – new 100% expensing for qualified production non-residential real property
- Section 179 expensing increased to \$2.5 million after 12/31/2024





## Section 174A R&E Updates



# R&E Expensing – What Changed?

## Domestic R&E Expenditures

New Section 174A added

Full expensing restored

Retroactive treatment available

## Foreign R&E Expenditures

No change

Continue to capitalize and amortize over 15 years

## Net 280C

Default is to reduce Section 174A by amount of credit

Option to elect reduced credit

## Sec. 59(e) AMT back again

Passive owners

Pass-through entities



# Treatment as of January 1, 2025

## Expense

- Immediate deduction
- Method change

## Continue to capitalize over a period of not less than 60 months

- Method change
- Amortization starts when taxpayer first realizes benefit

## Continue to capitalize but over a 10-year period

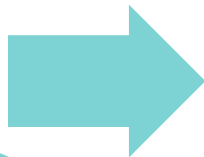
- Election not a method change



# Sec. 174A – OBBBA Retroactive Options

## 1. Small business taxpayer (448(c))

- Elect to move effective date of 174A modifications to 12/31/21
- Amend all applicable returns to remove 174A capitalization
- Apply 280C R&D credit provisions



## 2. All taxpayers

- Election to stop capitalizing 174A beginning for tax years on or after December 31, 2024
- Election to expense unamortized 174A expenses
  - In 2025, or
  - Ratably in 2025 & 2026



# Unamortized Expense Options

## Option 1 – Amending Prior Year Returns

- Must be a small business taxpayer
  - Average annual gross receipts under \$31M
  - Sec. 448(c) rules (aggregation, all revenue items, no tax shelters, etc.)
  - Average annual gross receipts for first taxable year beginning after 12/31/2024
- Election
  - Treasury to provide guidance
  - Must be made no later one year from date of enactment (7/4/2026)
- Adjustments to R&D credit
  - Default is a reduction in Sec. 174A expenditures
  - Have ability to make a late Section 280C election
  - Making an election shall be treated as timely made on amended returns if made within one year of enactment
- Other potential adjustments
  - NOLs
  - Sections 199A, 163(j)
  - State taxable income



# Unamortized Expense Options

## Option 2 – Release in 2025

- Available to all taxpayers
- Unamortized expenses freed up in 2025
- No amended returns required
- No R&D credit adjustments

## Option 3 – Release in 2025 and 2026

- Available to all taxpayers
- Unamortized expenses freed up ratably in 2025 and 2026
- No amended returns required
- No R&D credit adjustments



# Revenue Procedure 2025-2028

- Issued August 28, 2025
- Cover various procedural issues for taxpayers making Sec. 174A changes
- Allows taxpayers to skip capitalization for tax year 2024 if amended returns are filed
- Provides a new option for SBTPs to file an accounting method change (Form 3115) for 2024 rather than amended returns
  - Appears amended returns may still be required to adjust R&D credits
- Deemed election provision included





# Practical Considerations

Recommend  
modeling different  
options

NOL management

Cost of amended  
returns

Wait time for  
refunds

Estimated  
payment impacts

Ancillary impacts  
(fed and state)



# Polling Question

- OBBBA changed the rules for deducting R&E by:
  - Allowing companies to deduct all R&E expenses
  - Allowing companies to deduct only domestic R&E expenses
  - Allowing companies to amortize non-US R&E over 10 years
  - Requiring companies to expense all R&E expenditures





# Understanding Section 1202: Key Facts About Qualified Small Business Stock (QSBS)





# Historical and Legislative Context of Sections 1202 and 1045



# Background and Legislative Intent of Section 1202



## **Section 1045 Tax-Deferred Rollover**

Section 1045 allows tax-deferred rollover of QSBS sales proceeds into replacement stock, deferring gain until sale.

## **Legislative History of Section 1202**

Section 1202 was enacted in 1993 to encourage investment in small businesses through gain exclusion incentives.

## **Proposals for Modernization**

VC groups propose reforms including threshold increases and expanded rollover periods to spur startup investments.

# Debate and Legislative Developments Surrounding Section 1202

## Proponents' Arguments

Supporters believe low taxes on startups encourage job creation and increased angel investment over index funds.

## Critics' Concerns

Critics argue the tax exclusion mainly benefits wealthy taxpayers and lacks strong economic justification for continuation.

## Legislative History

Section 1202 has faced proposals for repeal and extensions, including the Stop Wall Street Looting Act restricting gain exclusions.

## Complexity and Awareness

Despite benefits, Section 1202 remains obscure due to past partial exclusions, alternative minimum tax, and investor unfamiliarity.





# Introduction to Section 1202 of the Internal Revenue Code



# What is Section 1202 QSBS

Qualified small business stock (QSBS) is stock in a domestic C corporation that meets specific requirements under Section 1202 of the Internal Revenue Code. To qualify:

- The stock must be originally issued after August 10, 1993, and acquired by the taxpayer at its original issue (directly or through an underwriter) in exchange for money, property (not including stock), or as compensation for services (other than as an underwriter).
- The corporation must be a qualified small business at the time of issuance, meaning its aggregate gross assets do not exceed \$50 million before and immediately after the stock is issued (\$75 million for stock issued after July 4, 2025, adjusted for inflation after 2026).
- During substantially all of the taxpayer's holding period, at least 80% of the value of the corporation's assets must be used in the active conduct of one or more qualified trades or businesses. Certain service businesses and industries (e.g., health, law, engineering, hospitality, finance, farming, mineral extraction) are excluded.
- The stock must not be subject to certain redemption transactions.







# Tax Advantages Provided by Section 1202



# Tax Benefits

- Non-corporate taxpayers may exclude a percentage of gain from the sale or exchange of QSBS held for the required period:
  - 100% exclusion for stock acquired after September 27, 2010, and held for more than five years.
  - 75% exclusion for stock acquired after February 17, 2009, and before September 28, 2010.
  - 50% exclusion for stock acquired before February 18, 2009.
  - For QSBS acquired after July 4, 2025: 50% exclusion for stock held three years, 75% for four years, and 100% for five or more years.
- The amount of gain eligible for exclusion is limited to the greater of \$10 million (\$15 million for stock acquired after July 4, 2025, adjusted for inflation after 2026) or 10 times the taxpayer's basis in the stock.
- Excluded gain may be a preference item for alternative minimum tax (AMT) for stock acquired before September 28, 2010.



# Tax Benefits

## Example Discussion



# Polling Question

- OBBBA changed the exclusion of capital gain on sale of QSBS stock after five years to :
  - 10 times basis or 10 million, whichever greater
  - 15 times basis or 15 million, whichever is greater
  - 10 times basis or 15 million, whichever is greater
  - 15 million





# Eligibility Criteria for Section 1202 Benefits



# Original Issuance Requirement

- The stock must be originally issued after August 10, 1993, and acquired by the taxpayer at its original issue
- The taxpayer acquires the stock directly or through an underwriter for money or other property (not including stock)
- Stock acquired as compensation for services to provided to the issuing corporation (other than services as an underwrite) count
- If the stock is acquired through the exercise of options and warrants or through a conversion of convertible debt is also treated as acquired at original issuance.
  - Stock options are not treated as stock until the options have been exercised at which time the holding period begins
- If taxpayer acquires the stock by gift or inheritance is considered treated as having received original issued stock with the holding period beginning on the transferor's date received.
- Partnership may distribute qualifying QSBS to its partners which may still qualify
  - Partner must have held an interest in the partnership at the time the stock was acquired by the partnership
  - Partner qualifying amount is limited to the partners interest at the time the stock was originally issued



# Pitfalls on QSBS Original Issuance Requirements

- Redemption transactions by taxpayer or related person can taint issuance
  - Disqualifying Redemptions
    - If a corporation redeems more than a de minimis amount of stock from a taxpayer or related person within a 4-year window (2 years before and after issuance), the stock may lose QSBS status.
      - A redemption is considered de minimis only if:
        - The amount paid exceeds \$10,000, and
        - More than 2% of the taxpayer's or related persons' holdings are repurchased
  - Following are not treated as redemption transactions
    - the transfer of stock by a shareholder to an employee in connection with the performance of services;
    - redemptions upon termination of a shareholder's employment;
    - redemptions due to death, if the stock is redeemed within 3 years and 9 months of the death);
    - redemptions due to the disability or mental incompetency of a shareholder; and
    - redemptions due to divorce.
- Contribution TO a partnership of the stock is considered a transfer and no longer issued at original issuance
- Revocation of S election does not result in original issuance of C Corp stock
  - Alternative drop down structures





# C Corporation vs. Pass-Thru Entities: Tax Considerations for QSBS





# Tax Implications and Historical Preferences for Entity Choice

## Challenges of C Corporations

C corporations faced issues like double taxation, nondeductible dividends, and no personal loss deductions for shareholders.

## Tax Reform Impact

The 2017 tax reform reduced corporate tax rates from 35% to 21%, increasing attractiveness of C corporations.

## Entity Choice Trends

Main street businesses preferred pass-through entities, while venture-funded startups favored C corporations.

## Section 1202 Benefits

Section 1202 requires QSBS to be C corporation stock, offering gain exclusion benefits to investors.





# Tech and Private Equity Transactions and Section 1202 Planning



# Structuring QSBS Issuance in Venture-Financed Startups



## **QSBS Issuance Flexibility**

Section 1202 allows QSBS issuance beyond startups, including acquisitions and asset rollups by PEGs.

## **Leveraged Buy-Out Structure**

Typical PEG LBO involves forming Newco, capital investments, equity rollover, and acquisition debt borrowing.

## **C Corporation Requirement**

Only C corporations can issue QSBS, requiring careful structuring in acquisition and investment deals.



# Structuring Leveraged Buy-Outs (LBOs) to Issue QSBS



## Section 1202 Requirements

PEGs must ensure future buyers prefer Newco's QSBS for Section 1202 benefits and consider the five-year holding period for 100% exclusion, and impact for partial year exclusion.

## Gross Asset Tests

Newco must meet \$50 million (\$75 million after July 4<sup>th</sup>) gross asset tests.

## Capital Infusion Strategy

Initial capital infusion into Newco can include Fund equity and target rollover assets to meet asset tests.

## IRS Anti-Abuse Considerations

There is a risk of IRS challenging QSBS exclusions under anti-abuse rules.



# Gross Asset Tests and Anti-Abuse Considerations



## Challenges with C Corporations

Material stock redemptions near stock issuance can disqualify QSBS benefits under Section 1202.

## Use of Blocker Corporations

Forming blocker corporations to acquire majority stock can enable QSBS issuance and compliance.

## Structures for S Corporations and LLCs

Blocker corporations can acquire interests in Newco LLCs holding target assets to facilitate transactions.





# What if not Currently a C Corporation?



## **S Corporation**

F Reorg or Asset Drop Down

## **LLC taxed as a partnership**

Check the box or incorporation of the LLC  
“F Reorg” for partnership.

If the partners have negative basis in their partnership interests, may result in income.

Debt in excess of basis on “contribution” to new corporation can also result in current income inclusion.

# Polling Question

- I would like someone from CLA to contact me to discuss the following services:
  - Research and development tax credit
  - Entity selection (QSBS Consulting)
  - General tax consulting
  - Nothing at this time





# Fund Structures and Eligibility for Section 1202 Gain Exclusion





# Eligibility of Fund Owners and Investor Types for Section 1202

## Section 1202 Gain Exclusion Eligibility

Only owners holding QSBS at acquisition time can claim Section 1202 gain exclusion on sale of distributed QSBS.

## Fund Interest Sales and Exclusion Rights

Selling fund equity interest does not trigger Section 1202 gain exclusion rights for the seller.

## Impact of Transfers on Exclusion

Transfers of fund interests typically void Section 1202 exclusion eligibility, except gifts or inheritance.



# Transfer and Distribution Rules Affecting Section 1202 Exclusion

## Owner's Interest Limitation

Section 1202 gain exclusion is limited by the Owner's interest in the Fund when QSBS was purchased.

## Differing Income and Exclusion Amounts

Taxable income and sales proceeds allocation differ from the Section 1202 gain exclusion available to Owners.

## Eligible Partner Definition

Eligible partners include Owners at acquisition date or those who receive interests by gift or inheritance.

## Section 1045 Expansion

Section 1045 regulations expand Section 1202 to include gifted or inherited Fund equity interests.



# Determining Owner's Interest and Allocation of Gain Exclusion

## Definition of Owner's Interest

Section 1045 defines Owner's interest as the smallest percentage of partnership capital at QSBS acquisition, adjusted for capital changes.

## Limits on Gain Exclusion

Owner's share of Section 1202 gain exclusion is limited by capital interest at purchase and adjusted for reductions before sale.

## Impact on Profits Interest Owners

Profits interest holders with low capital accounts may be excluded from gain exclusion despite profit allocations on sale.



*Thank you!*

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