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Tax Update July 15, 2025

Focus on QSBS Provisions in the One Big Beautiful Bill Act

This update details key changes the Act makes to section 1202, significantly expanding the tax benefits available for investments in qualified small business stock (QSBS).

The One Big Beautiful Bill Act (the OBBBA or the Act)[1] significantly expanded the tax benefits available for investments in qualified small business stock (QSBS) under section 1202.[2] This alert discusses the key changes the Act makes to section 1202. For a discussion of the broader changes to federal income tax law introduced under the Act, please read our Tax Highlights of the One Big Beautiful Bill Act.

Background

Under pre-OBBBA law, section 1202 allowed taxpayers to exclude from their gross income up to 100 percent of gain from the sale of QSBS held for at least five years, provided that certain other requirements were satisfied.

QSBS is stock issued by a qualified small business (QSB) in exchange for money or other property or as compensation for services provided to the QSB. A business was a QSB if, among other requirements, its aggregate assets did not exceed $50 million at all times before and immediately after the issuance date of the relevant stock.

The amount of gain that a taxpayer may exclude from their gross income with respect to the sale of QSBS is capped at the greater of a lifetime dollar-based limitation ($10 million under pre-OBBBA law) or ten times the taxpayer's tax basis in the QSBS (the per-issuer limitation).

OBBBA Changes

First, the Act shortens the holding period required to qualify for QSBS benefits by introducing a 50-percent exclusion for gain recognized on the sale of QSBS held for at least three years but less than four years, and a 75-percent exclusion for gain recognized on the sale of QSBS held for at least four years but less than five years. The Act retains the 100-percent exclusion under current law if the stock is held for five years or more. If a taxpayer takes advantage of the new 50-percent or 75-percent exclusion, the recognized portion of the resulting gain would be taxed at a 28-percent rate. The new holding period rules apply to QSBS acquired after July 4, 2025.

Second, effective for QSBS issued after July 4, 2025, the Act increases the aggregate gross asset value cap for QSBS issuers from $50 million to $75 million (adjusted for inflation for taxable years beginning after 2026). Therefore, issuers that previously did not qualify for QSBS (because their aggregate gross assets exceeded $50,000,000) may become immediately eligible to issue QSBS.

Lastly, the Act amends the formula for the per-issuer limitation by increasing the lifetime dollar-based limitation from $10 million to $15 million (also adjusted for inflation for taxable years beginning after 2026). As a result, taxpayers will be able to exclude (at least) an additional $5 million of taxable gain with respect to QSBS acquired after July 4, 2025; however, upon a taxpayer exceeding the new $15 million cap once (as adjusted for inflation), the taxpayer is not able to exclude any further gain simply by reason of the per-issuer limit increasing for inflation in subsequent periods. The new $15 million cap applies only with respect to stock acquired by the taxpayer after July 4, 2025.

[1] The actual name for the Act is "an Act to provide for reconciliation pursuant to title II of H. Con. Res. 14."

[2] The text of the Act can be found here. Unless indicated otherwise, all section references are to the Internal Revenue Code of 1986, as amended (the Code), and all Treas. Reg. § references are to the regulations promulgated by the U.S. Department of the Treasury (Treasury) and the Internal Revenue Service (the IRS) under the Code, in each case as in effect as of the date of this alert.

The following Gibson Dunn lawyers prepared this update: Matt Donnelly, Bree Gong, and Kamia Williams.

Gibson Dunn lawyers are available to assist in addressing any questions you may have regarding this proposed legislation. To learn more about these issues or discuss how they might impact your business, please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any member of the firm's Tax and Tax Controversy and Litigation practice groups:

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