Date Sent: November 6, 2017

Subject Line: Tax Reform Update: Carried Interest Details Emerge

NVCA Members,

Today, the House Ways and Means Committee released a modified tax reform bill, which will be the basis for the committee's markup this week. With this in hand, we have several important updates on some of our tax reform priorities:

Carried Interest Capital Gains: Carried interest arising from assets held shorter than three years will now be taxed as ordinary income due to a provision included in the modified mark. This means that ***capital gains rates will still apply to assets held longer than three years.*** We are pleased that the House Ways and Means Committee has heard our perspective that carried interest based upon holding periods is a much more sensible way to view the issue than blunt changes to the policy that would treat a quick flip of an asset the same as real value created over a number of years. While this is an encouraging sign, please remember: this is still just the beginning of this process; there is a long way and a lot of challenges we will face from now until the end of this process.

Qualified Small Business Stock Rules/R&D Credit Offset: Both QSBS and the ability of early stage startups to offset payroll tax liabilities with R&D credits have

been preserved in the modified mark.

Stock Options: As we understand it, a provision (Section 3801) in the tax reform bill dealing with nonqualified deferred compensation would have some significant impact on nonqualified stock options (NSOs). Basically, this provision would force people to pay taxes on NSOs as they vest, rather than when exercised. There is some relief provided by inclusion of Rep. Erik Paulsen's Empowering Employees through Stock Ownership Act (EESO), which was included in the modified mark and will allow employees at many private companies to defer paying taxes on NSOs for up to 7 years after vesting or until the company goes public. Founder's stock is carved out as well.

We still see several areas where Section 3801 will hurt stock options incentives for growth companies:

- Emerging Growth Companies (EGCs) at IPO.
- EGC executives whose stock options don't qualify for founders stock.
- EGCs who remain private 7 years after vesting.
- EGCs whose stock plans don't qualify for EESO.

This would likely create yet another disincentive for companies to go public, hurt the incentive environment for experienced executives to come in and help build growth companies, and generally increase the risk environment surrounding stock options. We hope to work through the process to get these issues fixed so tax reform can support the concept of employee ownership at startups.

We will continue to provide updates and analysis as the process unfolds, but feel free to reach out to Justin Field, Vice President of Government Affairs, at any time with questions: jfield@nvca.org.

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