Expanding The Ownership Economy: Aligning Tax To Time Of Sale

INNOVATOR
Alliance
EMPOWERING INNOVATION THROUGH STRATEGIC TAX POLICY

THE ISSUE:

Equity compensation is a cornerstone of innovation, enabling startups to attract top talent by offering ownership stakes in exchange for contributions to unproven products or markets. However, current tax policy creates significant barriers to equity ownership, particularly for employees.

Under current law, stock options—such as non-qualified stock options, which are the most common form of startup equity compensation—are taxed when employees purchase the options, even if they have not sold the shares or realized any actual profit. In addition, this illiquid equity may be factored into the alternative minimum tax calculation. As a result, employees are often required to pay taxes on theoretical paper gains - not actual gains - even when they lack the financial resources to cover the purchase price and tax liability.

This system creates unnecessary financial burdens, discouraging equity ownership and penalizing the very employees - especially those early in their careers - who contribute to the success of startups and growth-stage companies.

IMPACT ON INNOVATION:

Equity ownership drives performance, innovation, and economic opportunity and enables entrepreneurs to raise capital based on an idea and to turn that concept into a thriving business. Tax policies that penalize equity ownership undermine the U.S. innovation ecosystem in critical ways:

Reduced Employee Incentives: Taxing equity before employees realize actual gains discourages participation in equity compensation programs, particularly for early-career employees and those with limited financial resources. Employee-owners should be able to participate in the profits they are helping to produce, providing them access to the uncapped upside of asset ownership and wealth creation.

Attracting and Retaining Talent: Startups rely on equity compensation to compete for top talent and create an engaged workforce focused on long-term success. This is critical for startups and growth-stage companies building unproven products in unproven markets. Misaligned tax policies diminish the attractiveness of these packages, making it harder for startups to build and retain strong teams.

Economic Opportunity: Income inequality continues to climb. Equity ownership is not a panacea, but provides employees a sustainable growth asset that offers the uncapped upside of asset appreciation to supplement their wage and promote wealth creation, helping to reduce income inequality. Current policies prevent employees from fully realizing these benefits.

REQUESTED ACTION:

We respectfully urge Congress to align tax liability— both directly and through alternative minimum tax—on equity ownership to the year of sale.