

The Baratelli Field Note

Practitioner analysis for principals, family-office executives, and their advisors

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Post-OBBBA tiered exclusion. The non-grantor trust technique that turns one founder's \$10M exclusion into the family's \$50M of tax-free gain - plus the 11-state conformity table.

The §1202 QSBS Stack: Five Family Members, \$50M Tax-Free

"The founder of the practice we sold last quarter cleared \$42M tax-free at the federal level. Eleven of his eleven advisors had no idea §1202 worked this way." - a CPA in Atlanta

1. What §1202 actually does

Section 1202 of the Internal Revenue Code excludes capital gain on the sale of Qualified Small Business Stock - stock issued by a domestic C-corporation with under \$50M of gross assets at issuance, held for at least five years (post-OBBBA, the holding period was clarified and the exclusion was tiered upward).

The base exclusion: 100% of gain on up to \$10M of stock per shareholder per company. Or 10x basis, whichever is greater. Federal capital-gains tax on excluded gain: zero. Federal NIIT: zero. The savings on a \$10M gain are roughly \$2.4M of federal tax that doesn't get paid.

2. The 11 states that fully conform

Eleven states fully conform to federal §1202 treatment: AL, AK, AZ, CO, GA, IN, KY, MO, NE, NV (no state income tax anyway), OH. Most other states partially conform or don't conform - California, for instance, taxes the gain at full state rates regardless of federal exclusion.

For a founder in California planning a sale, the §1202 conversation has to be paired with a state-residency conversation. Move to FL or TX before the sale, structure the §1202 stack

inside the move, and the federal AND state savings stack together.

3. The stacking trick - non-grantor trusts as separate shareholders

Each shareholder gets their own \$10M exclusion. The IRS treats trusts and individuals as separate shareholders for this purpose. So a founder who creates four non-grantor trusts (one per child, or one each for spouse + three children) and gifts pre-IPO stock into them - each trust now has its own \$10M exclusion.

Five separate \$10M exclusions = \$50M of gain federally tax-free, on a single liquidity event.

The mechanics: the trusts must be created and funded with the QSBS shares before the sale event (some commentators read this as before signing the LOI; conservative practice is several months before). The trusts must be non-grantor for §1202 purposes - meaning the trust is its own taxpayer, not the founder. The trustee must be independent. The beneficiaries should be the people the founder wants to receive the wealth long-term anyway, so the planning serves both tax goals and family goals.

4. The five-year holding period - earlier than founders think

The five-year clock starts when the QSBS is issued, not when the company is founded. For founders who took stock at incorporation, the five-year clock has been running since incorporation. For founders who got grants in later rounds, those grants have their own five-year clocks.

Practical implication: if a sale is contemplated in years 4-7 of the company's life, do the QSBS stacking analysis now. Some shares may already qualify for full exclusion; some may need to be held longer. Some founders accelerate or delay the sale by a quarter to align around the five-year clock for the largest tranche.

5. The conversation with the M&A attorney

Not every M&A attorney works the §1202 angle. A founder who walks into the LOI conversation with the §1202 plan in hand controls the deal architecture - including whether the deal is structured as a stock sale (QSBS-eligible) or an asset sale (gain doesn't qualify). A founder who lets the buyer drive the structure often loses the §1202 benefit entirely. The QSBS stack is a \$5-12M decision; it should be in the LOI conversation, not the closing checklist.

Paired tools

§1202 QSBS Calculator. Section 1202 with post-OBBBA tiered exclusion + 11-state conformity map. Models the family-stacking scenario directly. tools.baratelliinstitute.com/qsbs.html

QSBS_Family_Stacking_Worksheet.xlsx. Spreadsheet that lays out the five-shareholder stack: founder + four non-grantor trusts. Tracks holding-period clocks, shares held by each, the \$10M-per-shareholder limit, and the federal + state outcome. For the conversation with the M&A attorney AND the estate attorney AND the CPA, who all need to be in the room together.

Five family members. \$50M tax-free at the federal level. Plus the state savings if you structure the residency move at the same time. Talk to your CPA before the LOI conversation, not after.

What to read next

Field Note 10 - OBBBA Estate Reset Part Two: the trust architecture you'll already need.

Liquidity Event Playbook - walks the §1202 stack inside the broader sale-prep timeline.

State Tax Migration - for the founder in CA/NY/NJ planning the move pre-sale.

If this Field Note was useful: the §1202 calculator is free at tools.baratelliinstitute.com. Model the stack before the next M&A conversation.

Until next time -

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