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## Exploring Flexibility in 83(b) Elections: A Tax Policy Proposal

Brayden Call

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## Exploring Flexibility in 83(b) Elections: A Tax Policy Proposal

Brayden Call\*

*Property awards, such as equity, are taxable to the recipient and have tax implications for employers, too. Without a recipient making an 83(b) election, property awards are taxable when they are granted. For awards that have vesting requirements or are considered “restricted,” they are generally taxable upon vesting. However, making an 83(b) election allows recipients of restricted property awards to be taxed as if the property were vested, meaning more income will shift from ordinary tax rate treatment to preferential tax rate treatment.*

*The preferential tax system is foundational to the 83(b) election. Advocates believe that preferential tax rates in an 83(b) context promote economic growth and encourage efficient capital allocation. However, critics contend that 83(b) elections disproportionately benefit the wealthy because they require electors to pay taxes earlier, which may disadvantage lower-income individuals. Two similarly situated employees may receive significantly different tax treatment based on the type of compensation and whether they make the 83(b) election. Furthermore, the complexities and rigidity of this provision of the tax code create their own inequities. Although the 83(b) election grants flexibility and control for taxpayers, it needs more flexibility by extending the deadline to file. Perhaps providing downside protection for 83(b) electors can encourage more employers to grant property to their employees and service providers. Ultimately, these solutions will allow more people to enjoy the benefits of preferential tax treatment, thereby making preferential tax rates more equitable for everyone.*

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## INTRODUCTION

As an employee of a large, private technology company, you are subject to the highest income tax rates, with ordinary income taxed at 37% and preferential income taxed at 20%. Despite knowing next to nothing about restricted stock, you gratefully accept 10,000 restricted stock awards valued at \$.10 each, granted to you for your exceptional work on the software team. Your manager informs you that the stock has immense potential due to the company's growth trajectory, and the awards will vest provided you remain with the company for at least three years.

After approximately three years, the shares vest and are now valued at \$10 per share. In the year of vesting, you will be taxed at the ordinary tax rate, which amounts to \$37,000 (10,000 shares \* \$10 per share \* 37%). Two years after the shares vest, you decide to sell them for \$15 each, which is the current market value. You will be taxed at preferential tax rates in the year of sale, which amounts to \$10,000 (10,000 shares \* \$5 per share \* 20%). This tax is based on the difference between the sale price of the shares and the price at the date of vesting. Although you sell the stock for \$150,000 (10,000

shares \* \$15 per share), the total taxes paid upon vesting and sale of the stock would amount to \$47,000 (\$37,000 + \$10,000), leaving you with a profit of \$103,000 from the restricted stock awards (\$150,000 - \$47,000).

Now, assume that your competent tax attorney recommended that you file an 83(b) election prior to the issuance of the restricted stock awards. Assuming the same facts as above, but now accounting for your decision to make an 83(b) election, you would have paid taxes at ordinary tax rates amounting to \$370 (10,000 shares \* \$.10 per share \* 37%) in the same year that you are granted the restricted stock awards. Upon vesting, three years later, you would not owe any taxes because you already paid taxes upon receipt. In the year of sale, you would pay taxes at preferential tax rates amounting to \$29,800 (10,000 shares \* \$14.90 per share \* 20%), which is based on the difference in value of the shares at the date of sale and the grant date. With an 83(b) election, the total taxes paid upon the grant and sale of the stock would total \$30,170 (\$370 + \$29,800), leaving you with a profit of \$119,830 from the restricted stock awards (\$150,000 - \$30,170).

Thus, making an 83(b) election can shift more income from ordinary tax rate treatment to preferential tax rate treatment. As seen from the two scenarios above, instead of paying \$37,000 and \$10,000 in ordinary and preferential taxes respectively, with an 83(b) election, the amounts taxed at ordinary and preferential tax rates would be \$370 and \$29,800 respectively. This is how the 83(b) election allows property recipients to increase their post-tax profits.

Table 1

	No 83(b) Election	83(b) Election
<b>Taxes Owed at Grant Date</b>	None	10,000 shares * \$.10/share * 37% = \$370
<b>Taxes Owed at Vesting Date</b>	10,000 shares * \$10/share * 37% = \$37,000	None
<b>Taxes Owed at Sale Date</b>	10,000 shares * \$5/share * 20% = \$10,000	10,000 shares * \$14.90/share * 20% = 29,800

<b>Total Taxes Paid</b>	\$47,000	\$30,170
<b>Total Economic Profit</b>	\$150,000 - \$47,000 = <b>\$103,000</b>	\$150,000 - \$30,170 = <b>\$119,830</b>

This Note raises concerns about 83(b) election accessibility under the Internal Revenue Code (IRC) for less informed and less affluent individuals. To address this issue, this Note suggests three improvements to the IRC. First, lawmakers should consider expanding the rigid thirty-day timeline required to file an 83(b) election. By extending the deadline, property recipients would have more time to consider and make the election, resulting in greater fairness and better incentives. Additionally, providing some downside protection to property recipients would help those with fewer financial resources to benefit from the 83(b) election. Finally, better incentivizing companies to compensate their employees with property could alleviate the problem of the wealthy primarily benefiting from the preferential tax system. To make the election fairer and less convoluted, adding these flexibilities to section 83 of the IRC will make all the difference.

## I. BACKGROUND

Section 83 of the Internal Revenue Code is one of the most influential tax provisions in the entrepreneurship world.<sup>1</sup> It not only impacts the timing and character of property awards, including equity, but also affects the tax consequences for many entrepreneurs, employees, and service providers who receive property as compensation for services.<sup>2</sup> In today's world, equity awards often make up a significant portion of employees' compensation, especially executive compensation. In the past few years, stock awards have become an increasing proportion of an employee's total compensation. For example, from 2018 to 2020, the percentage of named executive officer compensation for stock awards in Russell 3000 companies increased from 44% to 50% of

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1. Clifford A. Degroot & Amy Hwang, *What Is an 83(b) Election and Why Should Startup Founders Care?*, DAVIS WRIGHT TREMAINE LLP (Oct. 6, 2020), <https://www.dwt.com/blogs/startup-law-blog/2020/10/section-83b-election-for-startup-founders>.

2. I.R.C. § 83(b)(1).

total compensation, a 13.6% increase over just two years.<sup>3</sup> The taxation of these awards relies heavily on the preferential tax system and can be significantly affected by section 83 of the tax code.

This Note's following sections discuss how property awards, such as equity, are taxed to the recipient, along with the tax implications for employers. Without an 83(b) election, such awards are taxable when they are granted to the recipient. If held for more than one year, property awards become subject to preferential tax rates. For awards that have vesting requirements or are considered "restricted," they are generally taxable upon vesting. However, making an 83(b) election allows recipients of such restricted property awards to be taxed as if the property were vested, meaning they will be taxed when the restricted property is granted rather than when vested. Thus, 83(b) electors accelerate their tax bills in an effort to allow the property's appreciation during the time of vesting to be taxed at preferential tax rates rather than ordinary tax rates. Employers must take a deduction for property grants in the same year the property recipient pays taxes on that property, whether at the grant date or vesting date. It is also important to note that not all forms of compensation are eligible for an 83(b) election. However, recent legislation has expanded the choices for property recipients to receive more favorable tax treatment in connection with property received for services.<sup>4</sup> This Part will explore the tax code, specifically sections 83(a) and 83(b) and their impacts on employers, along with the forms of compensation that have preferential tax treatment benefits.

#### A. IRC Section 83(a)

Property granted to founders, employees, or service providers in exchange for services is taxable so long as the property is transferable by the recipient or is not subject to a substantial risk of forfeiture.<sup>5</sup> The property is taxed in the year of grant at ordinary tax

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3. Matteo Tonello & Olivia Tay, *CEO and Executive Compensation Practices in the Russell 3000 and S&P 500*, HARV. L. F. ON CORP. GOVERNANCE (Oct 7, 2021), <https://corpgov.law.harvard.edu/2021/10/07/ceo-and-executive-compensation-practices-in-the-russell-3000-and-sp-500>.

4. Patrick L. Young, *Making the Sec. 83(i) Election*, THE TAX ADVISER (Nov. 1, 2021), <https://www.thetaxadviser.com/issues/2021/nov/making-sec-83i-election.html>.

5. I.R.C. § 83(a).

rates based on the difference between the property's fair value and the amount paid by the recipient (if any).<sup>6</sup>

Any gains or losses realized in the property are considered capital and treated as such through preferential tax treatment upon a realization event, such as a sale of the property.<sup>7</sup> For example, if equity is granted to an employee in January of this year and sold after one year, any gains or losses realized upon the sale would be taxed at preferential tax rates. The holding period "clock," which is the time the IRS uses to determine what is considered short-term versus long-term capital gains and losses, starts when the taxpayer is initially granted the unrestricted equity awards.<sup>8</sup>

### B. IRC Section 83(b)

The 83(b) election is named after section 83(b) of the Internal Revenue Code.<sup>9</sup> If property awards are restricted and subject to a substantial risk of forfeiture (meaning ownership rights are conditioned upon an employee's future performance), then the property is eligible for an 83(b) election.<sup>10</sup> By default, 83(b)-eligible property awards become taxable upon their vesting date, not their grant date.<sup>11</sup> This is because the recipient has not yet earned restricted awards with a substantial risk of forfeiture. Therefore, no taxes are due on such property in the year of the grant. Restricted property typically vests over time or upon the completion of milestones to incentivize recipients to earn the awards and encourage longevity with a company.<sup>12</sup> Due to the uncertainties regarding whether the awards will ever vest, the tax code does not require recipients to include the difference of the fair value and the amount paid for the property in the year it is granted.<sup>13</sup> Instead,

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6. *Id.*

7. INTERNAL REVENUE SERV., CAT. NO. 15074K, PUBLICATION 544: SALES AND OTHER DISPOSITION OF ASSETS (2023), <https://www.irs.gov/publications/p544>.

8. *Id.*

9. I.R.C. § 83(b).

10. *Id.*

11. *Id.*

12. Evan Tarver, *Restricted Shares vs. Stock Options: What's the Difference?*, INVESTOPEDIA (Sept. 29, 2022), <https://www.investopedia.com/ask/answers/061515/what-are-restricted-shares.asp>.

13. I.R.C. § 83(a).

recipients pay taxes after earning the property, which happens in the year the property vests.<sup>14</sup>

In essence, the 83(b) election has an impact on the timing and tax treatment of the eligible property.<sup>15</sup> Specifically, the timing of the tax liability accelerates to the grant date instead of the vesting date, which means the holding period starts earlier. This timing shift can also affect how the property appreciates or depreciates, potentially leading to preferential tax treatment for a larger portion of the gains or losses. For instance, if an 83(b) election is made, ordinary taxes are due on the grant date, and any subsequent appreciation will be taxed at preferential tax rates when the property is sold. In contrast, if no 83(b) election is made, no taxes are owed on the grant date, and the property is taxed at ordinary rates when it vests, while any subsequent appreciation is taxed at preferential rates upon a sale.<sup>16</sup> Section 83(b) requires that the election be made within 30 days of the grant date of the eligible property, which is typically the date when the board of directors approves the grant for the restricted property.<sup>17</sup>

IRC section 83(b) is a valuable carveout in the tax code as it allows property recipients to be taxed based on ordinary income tax rates while the value of the property is presumably much lower than when the award vests.<sup>18</sup> Similarly, the holding period for preferential tax treatment begins at the earlier grant date, allowing the recipient to sell the appreciated property sooner while still receiving preferential tax treatment because the one-year holding requirement began at the earlier grant date.<sup>19</sup>

However, making an 83(b) election on eligible property may not always be the right choice. The decision hinges on three critical assumptions: (1) the recipient has the cash available to pay the taxes at an earlier date, (2) the value of the 83(b)-eligible property awards

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14. *Id.*

15. LAURA E. CUNNINGHAM & NOËL B. CUNNINGHAM, *THE LOGIC OF SUBCHAPTER K: A CONCEPTUAL GUIDE TO THE TAXATION OF PARTNERSHIPS* 196 (6th ed. 2020).

16. Matthew Bartus, *What Is a Section 83(b) Election and Why Should You File One?*, COOLEY GO, <https://www.cooleygo.com/what-is-a-section-83b-election> (last updated Jan. 23, 2022).

17. Daniel Zajac, *Exploring the Life Cycle of Restricted Stock Units*, ZAJAC GROUP, <https://zajacgrp.com/insights/understanding-the-life-cycle-of-restricted-stock/> (Jan. 23, 2023).

18. See DeGroot & Hwang, *supra* note 1.

19. *Id.*



will increase, and (3) the 83(b)-eligible property will, in fact, vest and not be forfeited.

To illustrate these points, consider the scenario where a fast-growing corporation grants 20,000 shares of restricted stock to a valued employee with a five-year vesting period. If the employee makes an 83(b) election within 30 days of the grant, she must pay taxes at ordinary tax rates on the grant date, five years before the vesting date, instead of on the vesting date if no 83(b) election were made. This means the recipient must have the cash to pay the tax bill sooner than the law requires, and the employee would be paying taxes on something she has not yet earned. However, since the value of property awards is typically low when granted, accelerating the tax payment is often not an issue. Assuming the value of the property increases from the grant date, the employee would likely be pleased with her decision to make the 83(b) election. But if the value of the stock awards is not very low, the employee must also consider the opportunity costs of accelerating her tax bill.

Regarding the second critical assumption, making an 83(b) election when the value does not increase is unwise. By making an 83(b) election, the clock for calculating when preferential tax rates apply upon a sale of the restricted stock begins on the grant date.<sup>20</sup> This means that every increase in the property's value results in greater after-tax gains for the employee, whereas every decrease in value would be more detrimental.<sup>21</sup>

The third critical assumption requires the recipient to weigh the odds of staying at the company for five years for the stock to become vested. If the employee does stay for the full five years, she will likely be pleased with her 83(b) election. However, if the employee leaves before the five years, she will not be entitled to any shares, and the taxes paid on the grant date would have been for nothing. For these reasons, an 83(b) election should only be made when the individual has the cash to pay the taxes at the grant date, the value of the property is likely to increase in value, and the awards are very likely to vest and not be forfeited. Not only does

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20. Bartus, *supra* note 16.

21. Jennifer Blouin & Mary Ellen Carter, *The Economics of Restricted Stock and the Section 83(B) Election* 9 (Feb. 2010), <https://ssrn.com/abstract=1561923>.

this decision substantially affect the recipient's tax bill, but it also impacts his or her employer's tax situation.

### *C. Impacts on Employers*

Employers are required to pay taxes that correspond with the timing of an employee's tax obligation. For example, an employer is required to pay its portion of payroll taxes, including Federal Insurance Contributions Act (FICA) taxes, in the year it issues property in return for services.<sup>22</sup> If the property is not restricted or subject to a substantial risk of forfeiture, the employer must simultaneously pay its share of payroll taxes and take a deduction for the property equal to the amount includible in the recipient's taxable income on the date the employee is granted the equity awards.<sup>23</sup>

However, if the 83(b)-eligible property's recipient does not make an 83(b) election, the employer must pay taxes and take the corresponding deduction on the vesting date instead of the grant date. When an employee makes an 83(b) election, the employer must pay taxes and take the deduction at the grant date rather than the vesting date.<sup>24</sup> Therefore, an employee's personal tax decision directly impacts when the company pays its portion of taxes and when it may take the deduction for the grant of property.<sup>25</sup>

In addition to the tax implications resulting from issuing property awards for employers, there are financial statement implications for granting property awards as well. The Financial Accounting Standards Board (FASB) requires companies to deduct property awards on their financial statements.<sup>26</sup> Prior to FAS 123R, now known as ASC 718, which governs the accounting rules for these financial statement impacts, no expense was recorded for property issuances. However, because property issuances cause dilution and can be a significant expense for a company's shareholders, the FASB now requires issuances to be expensed over

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22. I.R.C. § 83(h).

23. Michael S. Knoll, *The Section 83(b) Election for Restricted Stock: A Joint Tax Perspective*, 59 SMU L. REV. 721, 723 (2006).

24. *Id.*

25. *Id.*

26. See Financial Accounting Standards Board, 718-20-55-72, ACCT. STANDARDS CODIFICATION, <https://asc.fasb.org/1943274/2147481089/718-20-55-72> (last visited Oct. 16, 2023).

the vesting period of the property, which subsequently lowers a company's profitability.<sup>27</sup>

In addition to tax and financial reporting obligations, companies must also determine, through the help of professionals, the issued property's value.<sup>28</sup> For example, a company without an active market for its securities must determine the securities' value so that both the employer and the recipient pay the correct amount of taxes owed. Valuations can be achieved through a 409A valuation, which is an independent, third-party appraisal of the company.<sup>29</sup> A 409A valuation serves as a safe harbor for the company to rely upon as an accurate valuation of the company, meaning the IRS will consider such valuation method reasonable for tax purposes for both the company and the property recipient.<sup>30</sup>

Table 2<sup>31</sup>: Tax Treatment for Employees and Employers

	Section 83(a)	Section 83(b)
<b>Employee</b>	Employee is taxed when the stock vests at ordinary rates on the excess of fair market value over price paid.	Employee is taxed when the stock is granted at ordinary rates on the excess of fair market value over price paid. That produces a basis equal to fair market value; any subsequent gain or loss is capital.
<b>Employer</b>	Employer receives a tax deduction when the stock vests in an amount that is equal	Employer receives a tax deduction at grant in an amount equal to the employee's inclusion.

27. The Investopedia Team, *FAS 123R: Meaning, Pros and Cons, Example*, INVESTOPEDIA, <https://www.investopedia.com/articles/06/fas123r.asp> (last visited Feb. 20, 2023).

28. Anne Bushman & Karen Field, *General Equity Compensation Valuation Rules for Private Entities*, RSM (Oct. 1, 2018), <https://rsmus.com/insights/services/business-tax/general-equity-compensation-valuation-rules-for-private-entities.html>.

29. *Id.*

30. *Id.*

31. Knoll, *supra* note 23, at 724 tbl.1.

	to the employee's inclusion.	
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Because of the tax, financial reporting, and other burdens placed on employers in connection with issuing property to employees and service providers, employers want to have a say in whether the taxpayer makes an 83(b) election. For instance, employers may require or heavily incentivize employees to either make or refrain from making an 83(b) election as a condition of granting property.<sup>32</sup> A company may, for example, achieve its preferences by either paying the employee a bonus to cover the taxes due upon making an 83(b) election or restricting the employee's ability to make an election through a contractual agreement.<sup>33</sup> The former highly encourages recipients to make the election, while the latter legally prohibits it.

Companies may incentivize or restrict recipients from making an 83(b) election for two reasons: (1) to increase retention and motivation among employees, and (2) to maximize tax deductions.<sup>34</sup> If they want to boost employee retention, companies may require an employee to make an 83(b) election to increase the potential after-tax value of property awards. Conversely, if a company expects significant appreciation of its stock and pays substantial taxes each year, it is more likely to prohibit an 83(b) election through contract. Such prohibitions would maximize the company's tax benefits by allowing it to take a larger deduction at the property's vesting date rather than a smaller deduction at its grant date. Therefore, whether an employee makes an 83(b) election may not be entirely up to him or her when an employer attempts to further motivate an employee or strategically achieve its tax objectives.

#### *D. Forms of Property as Compensation*

Although companies use various forms of property to compensate for services performed by employees or other service providers, not all property types are eligible for an 83(b) election. Of the many properties used for compensation (such as restricted

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32. *Id.*

33. Blouin & Carter, *supra* note 21, at 2, 6.

34. *Id.* at 2.

stock awards (RSAs), incentive stock options (ISOs), non-qualified stock options (NQOs), restricted stock units (RSUs), and stock grants), only RSAs and certain stock options with early exercises may be eligible for 83(b) elections.<sup>35</sup>

Restricted stock awards are typically used in the early stages of a company, and recipients of RSAs are usually founders or very early-stage employees. Since the value of RSAs is relatively small, making an 83(b) election is often beneficial. RSA recipients usually file such elections with the IRS to commence the clock for preferential tax treatment and eliminate any taxes owed upon the vesting of the RSAs.<sup>36</sup>

Incentive stock options are also used to compensate service providers. But in order for ISOs to be eligible for an 83(b) election, the employer's option plan must allow the recipient to exercise the options before they vest.<sup>37</sup> Thus, ISOs rarely qualify as 83(b)-eligible. If a recipient can exercise ISOs before they vest and wants to make an 83(b) election, he or she must do so within 30 days of the exercise date, not the grant date.<sup>38</sup> ISOs that are eligible for the 83(b) election must also be carefully considered because they are sometimes subject to the alternative minimum tax, which makes the decision to make an 83(b) election even more complicated.<sup>39</sup> Non-qualified stock options do not qualify for 83(b) elections because they do not represent a transfer of ownership of the underlying stock, but merely a right to ownership.

Corporations may issue restricted stock units as a form of compensation, typically in later stages when stock options are too expensive for grantees. However, RSUs are not eligible for section 83(b) treatment. Like NQOs, RSUs are simply promises to grant stock at a future date and do not provide the recipient with stock subject to restrictions as RSAs do.<sup>40</sup> Consequently, RSUs are not

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35. Jeffrey Herman & Adam Frank, *Stock-Based Compensation and the Section 83(b) Election*, J.P. MORGAN WEALTH MGMT., <https://www.jpmorgan.com/insights/investing/investment-strategy/stock-based-compensation> (last visited Oct. 17, 2023).

36. *Id.*

37. *Id.*

38. *Id.*

39. Adam Frank, *Incentive Stock Options and the AMT*, J.P. MORGAN WEALTH MGMT. (Dec. 07, 2022), <https://www.chase.com/personal/investments/learning-and-insights/article/incentive-stock-options-and-the-amt>.

40. Laura Moreno, *RSAs vs. RSUs*, CARTA (Aug. 19, 2022), <https://carta.com/blog/breaking-down-rsas-and-rsus>.

considered property received in connection with the performance of services under section 83 of the IRC.

In 2017, The Tax Cuts and Jobs Act (TCJA) added section 83(i) to the IRC, offering more favorable tax treatment for a broad range of property compensation, including RSUs and stock options.<sup>41</sup> This provision is especially useful for those who may have difficulty affording the taxes associated with such issuances. Taxpayers can defer taxes for up to five years if the issuer is an eligible corporation, including private companies where at least 80% of all employees in the company hold property with rights to receive stock in the company.

Under section 83(i), the amount of federal income tax otherwise due can be deferred until the earliest of the following events:

- The first date the stock becomes transferable, including to the employer;
- The date the qualified employee first becomes an “excluded employee”;
- The first date the employer’s stock becomes readily tradeable on an established securities market;
- The five-year anniversary of the date the employee’s right to the stock became transferable or were not subject to substantial risk of forfeiture; or
- The date the employee revokes his or her section 83(i) deferral election on the stock (at the time and in a manner to be determined in future guidance from the IRS).<sup>42</sup>

A deferral can significantly reduce the upfront tax burden on employees, making it more feasible for them to participate in equity compensation plans.<sup>43</sup> This provision encourages companies to compensate more employees who could perhaps not afford the taxes prior to the adoption of section 83(i) with property, including equity.

To take advantage of the tax deferral benefits provided under section 83(i), employees must make the election within thirty days

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41. I.R.C. § 83(i).

42. I.R.C. § 83(i)(1)(B).

43. Brittany Burke, *Tax Implications of IRC Section 83*, SCARABBA WALKER & CO. LLP (Sep. 1, 2020), <https://swcllp.com/tax-implications-of-irc-section-83>.

of the property's vesting date.<sup>44</sup> By doing so, they can defer the tax owed on the equity until a later date, even if they have not sold it yet. With the addition of section 83(i), recent legislation has expanded the types of property compensation that can receive favorable tax treatment beyond the limited forms eligible for 83(b) elections.

#### *E. Partnerships and 83(b) Elections*

Under Subchapter K of the IRC, section 83(b) can also apply to partnership entities.<sup>45</sup> For capital interests in partnerships, a partner may elect to use section 83(b) to alter the timing of taxation on the interest. However, partners or service providers who receive profits interests in partnerships are not required to make such an election. The IRS does not tax profits interests because they are difficult to value.<sup>46</sup> This is true so long as (a) the profits interest does not relate to a substantially certain or predictable stream of income from the partnership's assets, (b) the partner does not sell or dispose of the profits interest within two years of receipt, or (c) the company is not publicly traded.<sup>47</sup> Similarly, as long as one of the aforementioned conditions are met, profits interests subject to vesting do not require an 83(b) election. In either case, no taxes are owed for the profits interest. Partnerships cannot deduct profits interests awarded because they are difficult to value. Since the partner or service provider is not paying tax on the interests, the partnership should not receive a tax deduction either.<sup>48</sup>

#### *F. Conclusion*

In summary, property awards, such as equity, have tax implications for both the recipient and employer. An 83(b) election accelerates a recipient's tax bill yet converts a greater portion of the property's appreciation or depreciation to preferential tax rate treatment. Employers must take a deduction for property grants in the same year the property recipient pays taxes on that property, whether at the grant date or vesting date. Although not all forms of

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44. Anat Alon-Beck, *Unicorn Stock Options – Golden Goose or Trojan Horse?*, 2019 COLUM. BUS. L. REV. 107, 164 (2019).

45. CUNNINGHAM & CUNNINGHAM, *supra* note 15, at 196.

46. *Id.*

47. *Id.*

48. *Id.* at 197.

compensation given by employers to employees or service providers are eligible for an 83(b) election, recent legislation has expanded the choices for property recipients to receive more favorable tax treatment in connection with property received for services. With that background, the following section of this Note will explore the policy behind 83(b) elections.

## II. TAX POLICY

The preferential tax system is foundational to the 83(b) election, which has both supporters and detractors. Advocates believe that it promotes economic growth and encourages efficient capital allocation. However, critics contend that preferential tax rates disproportionately benefit the wealthy because an 83(b) election requires electors to pay taxes earlier, which may disadvantage lower-income individuals. Section 83 also violates horizontal equity principles, since two similarly situated employees may receive significantly different tax treatment based on the type of compensation and whether they make the 83(b) election. Additionally, section 83 may encourage the very behaviors that the government aims to discourage, like gambling one's earnings to make substantially more earnings. Furthermore, the complexities and rigidity of this provision of the tax code create their own inequities. Although the 83(b) election grants flexibility and control for taxpayers, it needs more flexibility, given that employers can restrict employees from making the election or even pressure them to make it. Therefore, the question arises: Is section 83 a sound tax policy?

### *A. Preferential Tax System*

Preferential tax rates have been a part of the United States tax system since 1921, when the tax rate on capital gains was significantly lowered compared to ordinary income.<sup>49</sup> However, in the 1960s and 1970s, lawmakers increased capital gains tax rates due to perceived tax avoidance and growing social program costs.<sup>50</sup> In response to economic concerns, lawmakers again lowered

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49. CHRISTOPHER H. HANNA, *TAX POLICY IN A NUTSHELL* 95 (2d ed. 2022).

50. See Mark Luscombe, *Historical Capital Gains Rates*, WOLTERS KLUWER (Jan. 4, 2023), <https://www.wolterskluwer.com/en/expert-insights/whole-ball-of-tax-historical-capital-gains-rates>.



capital gains tax rates in the 1980s and 1990s.<sup>51</sup> Currently, some lawmakers advocate for an increase in preferential tax rates to address income inequality, as the wealthiest 0.5 percent of taxpayers reportedly receive 70.2 percent of all long-term capital gains tax benefits.<sup>52</sup> To combat this, some groups propose eliminating the preference on both dividends and capital interests.<sup>53</sup> Certain studies suggest that there is no correlation between economic growth and preferential tax rates.<sup>54</sup>

Regarding section 83(b), the question remains whether this provision worsens preferential tax treatment inequality or enables more people to benefit from the system, thus reducing some of its inequalities. Proponents of the preferential tax system argue that it encourages individuals to invest in businesses, thereby stimulating the economy and creating jobs.<sup>55</sup> Preferential tax rates, especially under section 83, benefit smaller companies that may not have the cash to offer competitive compensation to attract and retain talented employees.<sup>56</sup> The preferential tax system may also lead to more efficient uses of human capital resources by allowing property recipients to pay preferential rates on appreciated property. Additionally, taxation discourages investors from realizing accumulated capital gains, and it acts as a disincentive for property recipients to accept property over cash as compensation for services.<sup>57</sup>

Proponents of preferential tax rates argue that imposing ordinary tax rates on capital gains is unfair and that preferential

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51. *Id.*

52. Nick Buffie, *5 Little-Known Facts About Taxes and Inequality in America*, CTR. FOR AM. PROGRESS (Aug. 30, 2022), <https://www.americanprogress.org/article/5-little-known-facts-about-taxes-and-inequality-in-america>.

53. *Id.*

54. Sue (Suyoung) Moon, *Revisiting the Preferential Treatment of Capital Gains*, AM. BAR ASSOC. (Jun. 7, 2022), [https://www.americanbar.org/groups/gpsolo/publications/gp\\_solo/2022/may-june/revisiting-preferential-treatment-capital-gains](https://www.americanbar.org/groups/gpsolo/publications/gp_solo/2022/may-june/revisiting-preferential-treatment-capital-gains).

55. *Id.*

56. Eric D. Schoenborn, *Equity Compensation at Private Firms: How to Compete for Executive Talent*, SOC'Y FOR HUM. RES. MGMT. (Jan. 15, 2009), <https://www.shrm.org/resourcesandtools/hr-topics/compensation/pages/equitycompensationatprivatefirms.aspx>.

57. Moon, *supra* note 54.

treatment is necessary to address the bunching dilemma.<sup>58</sup> They claim that if capital gains were taxed at ordinary rates, the proceeds from a sale resulting from years of growth would be lumped into a single year and subject to significantly higher taxation than if the same amount had been earned and taxed over time like a salary.<sup>59</sup> This would unfairly tax the sale of capital interests resulting from years of effort in a single year.<sup>60</sup> However, opponents of this rationale argue that the taxpayer benefits substantially from being able to defer taxes on the growth during that same period.<sup>61</sup> Even if the taxes are higher than they would be if earned over time, the recipient enjoys the benefit of delaying taxes.<sup>62</sup>

### *B. Fairness and Unfairness in 83(b) Elections*

Vertical equity in tax is when people in different income groups pay different amounts of taxes, and horizontal equity is when people in similar income groups pay similar amounts of taxes. Generally, individuals with greater wealth have the resources to start businesses or receive property awards as compensation for services,<sup>63</sup> which inherently violates principles of vertical equity. The question arises whether the government should subsidize the wealthy through 83(b) elections and the associated tax benefits for property awards, which often make up a significant portion of their income, while the less affluent are less likely to utilize this tax strategy.<sup>64</sup> However, restricted property awards can help close the vertical equity gap by allowing companies to provide tax-efficient compensation to rank-and-file employees who tend to be less

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58. See HANNA, *supra* note 49, at 97. The bunching dilemma occurs when one holds a capital asset and sells that capital asset years later, which causes years' worth of growth to be taxed in a single year—the year of the sale. Ordinarily, W-2 income is taxed in the year income is received, so the effective tax rate is lower than the effective tax rate of the same dollar value being taxed in one year (rather than over several years, like W-2 income is). Capital assets often appreciate over time, but some perceive the tax bill to be unfair if it is “bunched” into one year, rather than over time, contingent upon a sale of the asset.

59. Moon, *supra* note 54.

60. HANNA, *supra* note 49, at 97.

61. Moon, *supra* note 54.

62. See Patrick L. Young, *Making the Sec. 83(i) Election*, THE TAX ADVISER (Nov. 1, 2021), <https://www.thetaxadviser.com/issues/2021/nov/making-sec-83i-election.html>.

63. Jeremy Quittner, *Why U.S. Entrepreneurs Are the Most Successful in the World*, INC. (Mar. 8, 2016), <https://www.inc.com/jeremy-quittner/five-traits-that-give-us-entrepreneurs-an-edge.html>.

64. See *id.*

wealthy. Thus, the 83(b) election can be an effective tool for reducing the vertical equity issues that property awards inherently create, because both the wealthy and less wealthy can take advantage of its benefits. Additionally, the adoption of IRC section 83(i) further reduces the vertical equity gap by allowing more tax-advantaged solutions for a wider range of individuals.

However, some policy experts raise concerns about horizontal equity. The 83(b) election creates a system in which individuals who receive property compensation can defer or reduce their tax liability, while those who receive other forms of compensation, such as salaries, are taxed at higher rates, even if the amounts are similar.<sup>65</sup> Wage taxes are already regressive in nature and take a larger portion of income from middle-wage workers compared to higher-wage workers. Appreciated property received for services is subject to preferential tax rates, which exacerbates the inequality of a wage tax on employees who do not receive the same benefits.<sup>66</sup>

Section 83 is also not horizontally equitable since the tax outcomes vary depending on the compensation's form and each recipient's decision.<sup>67</sup> For instance, two individuals receiving the same value of property can have significantly different tax outcomes based on the form of the compensation issued. RSUs are not eligible for 83(b) elections, while RSAs are. Even for two forms of property that are eligible for 83(b) elections, the tax treatment may vary substantially depending on whether the recipient makes an election. However, sometimes a recipient does not make an election because he is prohibited from doing so through contract, or he is unaware of the election. For example, an individual earning \$80,000 through stock options with the ability to exercise early is almost always better off than an individual earning the same amount in salary due to the preferential tax treatment of stock options after an 83(b) election.

Additionally, critics argue that section 83(b) creates an unequal tax system, allowing wealthier individuals to accelerate smaller tax

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65. See Robert Frank, *Biden's Capital Gains Tax Hike Could Spark a Big Sell-Off in Stocks. Here's What That Means for the Market*, CNBC (Sept. 21, 2020, 5:16 PM), <https://www.cnbc.com/2020/09/21/bidens-capital-gains-tax-hike-may-big-sell-off-in-stocks-.html>.

66. *Id.*

67. See Matthew A. Melone, *The Section 83(b) Election and the Fallacy of "Earned Income,"* 10 BERKELEY BUS. L.J. 53, 96 (2013).

payments in exchange for much more favorable tax treatment on appreciated property, while others are required to pay taxes on their income as it is earned.<sup>68</sup> These critics contend that section 83(b) often leads to significant profits for those who make the election, as they may be taxed on the value of the restricted property when it has an extremely low value, only to sell the property later for a much higher price with preferential tax treatment. But making an 83(b) election carries inherent risks, and sometimes *making* the election can be detrimental also. Overall, however, opponents of section 83(b) argue that the provision is unfair, creates an unequal tax system, and primarily benefits wealthy individuals.<sup>69</sup>

Many tax policy experts are most concerned about tax gamesmanship, and the 83(b) election is at the heart of such abuse.<sup>70</sup> The election allows for the transfer of ordinary income to capital income at minimal costs, which mimics the characteristics of carried interests.<sup>71</sup> Carried interests are also viewed as unfair and are subject to preferential tax treatment under section 1061 of the IRC in connection with private equity or venture capital funds.<sup>72</sup> Other similar tax provisions, such as section 1202 and section 422, are also considered inequitable.<sup>73</sup> Although each of these provisions allows for at least some tax gamesmanship to reduce taxes, they have existed in the tax code for some time.

If the tax code did not include an 83(b) election, recipients of restricted property that is subject to a substantial risk of forfeiture would be potentially exposed to significant tax bills at the time of vesting if the property's value increased between the grant date and the vesting date. In some circumstances, this would require the recipient to sell some of the property to afford the tax bill.<sup>74</sup> On the other hand, the 83(b) election allows a recipient to pay taxes earlier, usually when the value of the property is very low. Therefore, the 83(b) election counters the disincentive for recipients to earn

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68. *Id.* at 83–84.

69. *Id.*

70. See, e.g., Philip F. Postlewaite, *Fifteen and Thirty-Five – Class Warfare in Subchapter K of the Internal Revenue Code: The Taxation of Human Capital Upon the Receipt of a Proprietary Interest in a Business Enterprise*, 28 VA. TAX REV. 817 (2009).

71. Melone, *supra* note 67.

72. I.R.C. § 1061.

73. I.R.C. §§ 1202, 422.

74. Melone, *supra* note 67, at 71.

property awards by preventing ordinary tax rates from wiping out a substantial portion of the value of property awards.

Property received as compensation for services and awarded “wholly or in part upon the attainment of a financial reporting measure” is also subject to clawbacks triggered by statutory rules, common law principles, or contractual requirements.<sup>75</sup> A clawback allows a company to recoup the amount paid to a recipient due to accounting errors or a breach of a non-compete agreement. This means that individuals who make an 83(b) election may be required to return the entire value of the property even after they have paid taxes on property that they never owned and never will own.<sup>76</sup> Thus, making an 83(b) election may have unfair consequences for the recipient, despite the seemingly inequitable benefits of making such an election.

### *C. Inefficiencies of the 83(b) Election*

In addition to the inequalities of the preferential tax system and the 83(b) election, various inefficiencies exist. The first inefficiency requires that taxpayers accelerate tax payments on unearned property. Although this may save property recipients a significant amount of money in the future in taxes, making an 83(b) election is primarily feasible for those with excess cash to pay taxes on awarded property in the grant year. For those who cannot afford to accelerate income tax payments, borrowing money becomes an alternative, making a risky compensation agreement even riskier. Thus, the election not only discriminates against those who cannot afford to accelerate income tax payments, but it may also encourage the poor to make unwise borrowing decisions. Perhaps the goal to incentivize economic and entrepreneurial success goes too far when the tax code incentivizes people to gamble away tax liabilities. Individuals making an 83(b) election are relying on the value of their property awards to increase, which could lead to them becoming overly invested in a venture that is likely to fail.

A second inefficiency arises if a startup fails, and the property awards become worthless. In such instances, making an 83(b)

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75. C. Brophy Christensen, Jeff Walbridge, Robert Plesnarski, Shelly Heyduk, Chris Del Rosso & Warren Fox, *SEC Adopts Final Clawback Rule*, O'MELVENY (Nov. 1, 2022), <https://www.omm.com/resources/alerts-and-publications/alerts/sec-adopts-final-clawback-rule>.

76. Melone, *supra* note 67, at 72.

election would not only have been a waste of the recipient's time and efforts, but those losses on the property would be considered capital losses instead of ordinary losses. This may discourage entrepreneurship if the recipient's ordinary income cannot be offset by the property award losses. The election can shift the timing and character of the property for better or for worse.<sup>77</sup> Thus, the 83(b) election does not provide any benefits when the property does not increase in value.<sup>78</sup>

A third inefficiency occurs when the restricted property subject to a substantial risk of forfeiture does not vest because the employee does not satisfy the vesting requirements.<sup>79</sup> "[T]he decision to make an 83(b) election is considered irrevocable," meaning the taxpayer cannot receive any kind of refund for overpayment of taxes if the award is never ultimately earned.<sup>80</sup> Thus, if the vesting requirements are not met for any one of a variety of reasons, the 83(b) election may prove to be a costly mistake.<sup>81</sup> This may disincentivize employees from accepting property subject to a substantial risk of forfeiture because the 83(b) election only exacerbates the problem if the awards never vest. Perhaps the government should not implement policies like the 83(b) election that dissuade companies from issuing property with vesting requirements to retain talented employees and achieve milestones that are in shareholders' best interests.

It is important to consider the opportunity costs associated with accelerating taxes while making an 83(b) election. A fourth inefficiency arises from the fact that taxpayers forego potential returns by paying taxes at the grant date instead of using that money for other investments that could yield substantially larger payoffs than the ones the property recipients are waiting for.<sup>82</sup> The ability to delay income taxes until property awards vest (i.e., by not making an 83(b) election) is a valuable option that should not be overlooked.

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77. *Id.*

78. *Id.*

79. Bob Harris, *To 83(b), or Not to 83(b)? That is the Election!*, CREATIVE PLAN. (Jun 26, 2019), <https://creativeplanning.com/insights/to-83b-or-not-to-83b-that-is-the-election>.

80. *Id.*

81. *Id.*

82. *Id.*

Despite the inefficiencies of making an 83(b) election, the positive aspects of making the election often outweigh these drawbacks. Making an 83(b) election not only typically lowers an employee's tax obligation in the long term but also signals loyalty to employers. By choosing to accelerate taxes and make the election, employees demonstrate their commitment to stay with the company for the long term and also show they believe that the value of their equity compensation will increase over time. Furthermore, if the restrictions on the equity are tied to performance-based metrics, employees making the election show confidence in their ability to work until the property vests. These signals can align the employees' interests with the company's and serve as a valuable tool for motivating and retaining both employees and founders. Overall, equity compensation has proven to be an effective tool for driving performance and incentivizing loyalty in employees, especially when the 83(b) election creates signals between employers and employees.

#### *D. Draconian Nature of Section 83(b)*

The requirements for filing an 83(b) election are excessively stringent and complex. The process of filing can be convoluted, involving the preparation and submission of a written statement to the IRS within thirty days of the property's grant date. If the taxpayer is even one day late in making the election, the IRS will invalidate it. The risk of such an invalidation places a significant burden on the taxpayer, particularly because tax concerns are usually not a priority for the taxpayer until personal tax returns are due.<sup>83</sup> Furthermore, once the election is made, it cannot be revoked without the Secretary of the Treasury's consent.<sup>84</sup> The administrability costs are increased not only for the taxpayer and the government but also for the taxpayer's employer, because each employer is also responsible for receiving its employees' 83(b) elections and accounting for the costs on its business tax return. For instance, if the employee decides to make the election, the employer must account for its associated expenses on its tax form.

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83. *Filing a Section 83(b) Election: Did Your Client Miss the 30-Day Deadline?*, ALAMEDA CNTY. BAR ASS'N: BLOG (Feb. 25, 2016), <https://www.acbanet.org/2016/02/25/did-your-client-miss-the-30-day-deadline-for-filing-a-section-83b-election-heres-a-partial-fix-for-the-tax-problem>.

84. I.R.C. § 83(b)(2).

Additionally, as evidenced by the existence of professional services firms that specialize in assisting with property awards taxes, most individuals are unfamiliar with 83(b) elections and how to implement them. Those who do not know to hire a CPA or lawyer within thirty days of receiving property awards may be at a disadvantage. Perhaps section 83 of the IRC is overly complex and creates unnecessary compliance burdens, particularly because those burdens are on the uneducated taxpayer, not the issuing company, which presumably has greater resources to comply. In 2016, the IRS attempted to reduce the administrative burdens by eliminating the requirement that taxpayers submit a copy of the section 83(b) election with their tax returns.<sup>85</sup> Nonetheless, compliance with section 83 remains problematic because many property recipients are unaware of the election and fail to comply before the thirty-day deadline.

Although taxpayers may challenge the date an equity award was officially granted, thereby shifting the thirty-day window within which to file an 83(b) election, the IRS does not generally favor this position. For instance, if an employee is required to pay a nominal amount for a stock award but fails to pay, the recipient may argue that the stock was not validly granted until the employee paid the required amount. Similarly, if the board of directors is required to approve the grant of property but fails to formally do so, the recipient may argue that the grant date had not actually occurred until the board formally approved the grant.<sup>86</sup> In both cases, it may be argued that the stock was not actually issued, and, therefore, that the thirty-day period had not begun. However, the IRS prefers not to rely on taxpayer's hindsight to pay taxes in a more favorable way, and making an election after the thirty-day window will invalidate the election. Thus, the taxpayer may struggle to convince the IRS that the stock was not validly granted to simply buy more time to make an 83(b) election.

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85. Gabriella Ahdoot and Joshua Miller, *IRS Eliminates Requirement to Submit Copy of Section 83(b) Elections with Tax Return*, PROSKAUER: THE PROSKAUER TAX BLOG (Aug. 9, 2016), <https://www.proskauertaxtalks.com/2016/08/irs-eliminates-requirement-to-submit-copy-of-section-83b-elections-with-tax-return>.

86. T.J. Wilkinson, *What to Do for a Missed Sec. 83(b) Election*, AM. INST. OF CPAS (Jul. 18, 2021), <https://www.aicpa.org/news/article/what-to-do-for-a-missed-sec-83-b-election>.



*E. Flexibility and Control*

One policy rationale behind the 83(b) election is that it provides individuals who receive eligible property awards with more control over the timing and amount of income they report to the IRS. By making the election, an individual can choose to pay taxes on the fair value of the award in the year it was granted rather than waiting until the vesting requirements are met. This allows the individual to lock in his or her tax liability at the lower grant-date value and avoid paying tax on any future appreciation in the value of the property until a realization event occurs. This incentivizes employees to take on some risk by accepting property as compensation for services and gives them control over when and how they pay taxes.

Some provisions in the tax code, such as the 83(b) election, allow individuals to choose when to recognize income related to equity compensation. Other such provisions include section 83(i), section 409(a), and section 541(b). Section 83(i) allows eligible employees of private companies to defer income recognition from the exercise of certain stock options or the settlement of RSUs for up to five years. Section 409(a) governs the taxation of non-qualified deferred compensation plans, including stock options and RSUs, and provides rules for the timing and amount of income recognition for deferred compensation. Section 451(b) governs the taxation of deferred compensation for all types of taxpayers. Like the 83(b) election, each of these provisions aims to provide individuals with more flexibility and control over the timing and amount of income they report related to equity compensation. Though the 83(b) election appears to give property recipients significant flexibility and control, the election is both consistent with other provisions of the tax code and affords taxpayers adequate flexibility.

Admittedly, allowing service providers to choose an alternative date for income recognition might undermine the consistent treatment of individuals in similar circumstances and may diverge from capital gain policy, which holds that income recognition should be tied to a realization event.<sup>87</sup> Providing taxpayers with

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87. See OFF. OF THE SEC'Y OF THE TREASURY, OFF. OF TAX ANALYSIS, REPORT TO CONGRESS ON THE CAPITAL GAINS TAX REDUCTIONS OF 1978 2 (Sept. 1985), <https://home.treasury.gov/system/files/131/Report-Capial-Gains-Reduction-1978.pdf>.

control over the timing of income inclusion conflicts with the traditional notion that income should be taxed upon realization rather than at the taxpayer's discretion, which is precisely what the 83(b) election allows.

Although the benefits of giving taxpayers control over when to include income through the 83(b) election are great, employers sometimes take away that flexibility from the recipient. In some cases, employers may require or incentivize a property recipient to either "make or . . . refrain from making the election . . . as a condition of the [property] grant," giving employers ultimate control over when income is recognized.<sup>88</sup>

Allowing employers to control employees' personal tax decisions may be most beneficial for employers. Unlike salaries and bonuses, where employers can time their tax burdens and deductions for tax planning and cash management purposes, the 83(b) election can make it difficult for employers to compensate with eligible property. However, employers can easily solve this issue by issuing RSUs or stock options, neither of which are eligible for 83(b) elections, and thus preserve their control over tax planning and cash management. When an employer retains control over whether a property recipient can make the 83(b) election, the employer also retains control over when it will have deductions and financial reporting impacts. Thus, depending on the employer, the flexibility the 83(b) election affords can be taken away through contract or financial incentives that effectively prevent the recipient from making, or requiring the recipient to make, an 83(b) election.

#### *F. Conclusion*

The preferential tax system allows taxpayers to pay reduced tax rates for capital income, and the 83(b) election seeks to optimize more opportunities for using preferential tax treatment. This Note explores the fairness, drawbacks, and flexibility of the election from a tax policy perspective.

### III. PROPOSALS

Embracing the 83(b) election can be a valuable tool for both property recipients and employers, and this Part presents three

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88. Knoll, *supra* note 23, at 724.

suggestions to ultimately allow more people to enjoy the benefits of preferential tax treatment. First, making the election more flexible by extending the filing deadline can increase equity and reduce undesirable behaviors. Next, promoting property awards to the less affluent as compensation for services is an important first step toward decreasing income inequality in the United States. Finally, providing downside protection for such individuals in connection with property awards can increase awareness and encourage more people to file 83(b) elections.

#### *A. Embrace 83(b) Elections*

Despite the provision's vast inequalities and complexities, there is currently no serious discussion about curtailing the 83(b) election. This is largely because the provision incentivizes employers to grant restricted property awards, benefitting companies' retention efforts and increasing their ability to issue tax-advantaged compensation to recipients. The preferential tax system should remain in effect to encourage economic growth and efficient use of capital and services subject to economists' approval. A company's use of restricted property subject to a substantial risk of forfeiture is the very employee-focused incentive that helps a business grow from a garage startup into a several-trillion-dollar enterprise. Such awards would mean much less for recipients without the ability to shift the timing and character through an 83(b) election. Ultimately, the economic benefits resulting from the use of restricted property awards will supply more revenue to the government than the tax relief that section 83(b) affords.

Additionally, section 83(b) shares similarities with other provisions in the tax code, such as carried interests and qualified small business stock, that provide preferential treatment. These provisions offer flexibility and positive economic effects by shifting ordinary income to preferential tax treatment. Removing section 83(b) would require the reconsideration of various interrelated tax provisions that aim to achieve similar outcomes. Although horizontal and vertical equity principles may be violated in some instances, the broad application of Section 83(b) helps to counteract some of the main equity concerns. Giving taxpayers control over how they earn income and pay corresponding taxes is fairer than if such decisions were entirely in the hands of the government. Instead of repealing section 83(b) altogether, any inequities and

complexities can be addressed through simple amendments to the code, which are discussed below.

### *B. Less Severe Consequences*

Extending the 83(b)-election deadline from thirty to ninety days would be fairer for less affluent recipients of restricted property. The success of the election depends on three critical assumptions: that the individual has the funds to pay taxes at an earlier date, that the restricted property's value will increase, and that the restricted equity will vest. However, the inflexible thirty-day deadline for filing the election with the IRS serves as yet another constraint to filing the election. To encourage more individuals, especially those who are less affluent, to make the election, the IRS should extend the filing requirement timeline. Extending the deadline would lead to more individuals being able to make the election, allow for better decision-making and tax planning, and give additional time for more individuals to become aware of the election and file it.

Allowing taxpayers to make the 83(b) election within ninety days, instead of thirty days, would give less-affluent individuals the chance to make the election because they could seek tax and legal counsel as well as save the necessary funds to make the election possible. Many individuals already think about taxes in quarters due to quarterly tax payments. The ninety-day deadline would thus make it easier for more individuals to seek the help they need to decide whether to file the election, especially when the election would accelerate their tax bill.

Extending the filing deadline could lead to better decision-making and help property recipients assess whether the election is a wise choice without providing them with so much hindsight that the additional time might be considered unfair. This solution could also discourage taxpayers from gambling away tax liabilities since they would have greater visibility on the wisdom of making the election. Although the ninety-day window could create additional administrative burdens and opportunities for tax gamesmanship, particularly if the income spans two tax years, these gamesmanship risks also exist under the current thirty-day window and do not seem to pose significant problems.

Additionally, allowing more time to gather information about whether the property's value will increase would prevent an unwise 83(b) election if the value was unlikely to increase.

Allowing more time to make this decision could assist taxpayers in better tax planning. Such an extension would enable property recipients to evaluate their long-term career goals without having to make a crucial decision within the current thirty-day window. And since property values are typically low on the grant date, the government would not lose significant revenue by providing recipients with an extended period to make the election. The government should promote the rational and efficient use of time and labor rather than increasing the pressure created by the existing short filing deadline.

Extending the deadline for making an 83(b) election would also allow property recipients more time to decide if they believe the property will ultimately vest. If the property never vests, taxpayers are paying taxes on something they never owned and will never own. If taxpayers are given more time to decide, the consequences of filing an 83(b) when the recipients should not have done so will be reduced.

A significant issue many individuals face concerning the 83(b) election is the lack of awareness about its existence. This problem particularly affects less educated or less affluent individuals. For example, most taxpayers, upon receiving the property, fail to consult with CPAs or attorneys in time to know about the election and make it. Even if the taxpayer does consult with a tax professional about the tax implications of receiving such awards, many professionals may be unaware of the election or understand its ramifications. An extended filing period of the 83(b) election would minimize the negative effects of this issue, which disproportionately impact less-educated and less-wealthy individuals.

Another proposal regarding the 83(b) election is to allow property recipients to claim an ordinary loss if the stock is ultimately forfeited and their income is below a certain threshold. This would provide some downside protection for the taxpayer already taking a risk by accepting property in exchange for services. Currently, if the property is forfeited after an 83(b) election, there is no way to recover from the poor decision. An amendment to section 83 that allows for such losses would promote greater equity and encourage more middle-to-lower-class taxpayers to take risks and benefit from making an 83(b) election. The wealthy typically have no issue paying taxes on forfeited property, but it is much more challenging for less affluent taxpayers to do so.

This proposal would also increase awareness of the 83(b) election, encouraging more individuals to make the election and generating additional revenue for the Treasury, particularly during times of economic downturn. For instance, during recessions or times when there is a higher risk of devaluation, taxpayers are less inclined to make an 83(b) election. Offering property recipients downside protection if the property awards fail to appreciate can boost governmental revenues during such downturns.

### *C. Income Equality*

Another proposal is to create more incentives for companies to offer property awards in exchange for services rendered. This could be accomplished by allowing companies to always deduct restricted property awards at the vesting date, regardless of whether a recipient makes an 83(b) election. Incentivizing companies to offer property awards in exchange for services would give employees more control over their finances, and employers would be more inclined to offer restricted property to a larger number of employees, further reducing income inequality concerns in the United States. While such awards can reduce a company's profitability because they must be expensed over the life of the awards, the tax benefits often outweigh the negative financial reporting impacts.

Implementing section 83(i) in 2017 was a significant step toward incentivizing companies to issue more property awards to employees: it encourages more property awards for a greater number of taxpayers, leveling the playing field for both the ultra-wealthy and rank-and-file employees. This provision allows RSU and option recipients to delay taxes, just as the wealthy use section 83(b) to receive preferential tax treatment on RSAs, thus incentivizing employers to issue more property to their employees. This is a positive step toward reducing income inequality in the United States as more companies grant property in return for services. Allowing companies to receive additional tax benefits for issuing property to rank-and-file employees could make stock compensation benefit more than just the uber-wealthy.

## CONCLUSION

Section 83 plays a crucial role in the tax code, particularly for property awards with a substantial risk of forfeiture. However, the preferential tax system that makes the election worthwhile can create inequalities as the rich are more likely to benefit from it than similarly situated taxpayers who receive different forms of compensation. The 83(b)-election deadline is also very strict, and many people either miss the thirty-day window or are unaware of it. To create a more flexible and fair system, an extended deadline could provide downside protection for less affluent property recipients.

Some argue that the election gives taxpayers too much flexibility and control, and that the poor are less likely to receive property awards and make the election. To reduce income inequality, companies incentivized through the tax code can compensate more employees with property, as in section 83(i), thereby allowing more people to benefit from the preferential tax system. The goal is to make the 83(b) election more accessible and beneficial to a larger group of individuals, and increasing flexibility in the code will help achieve this.