PRE-MEETING OVERVIEW

REDUCING TAXES THROUGH EMPLOYER STOCK AND NET UNREALIZED APPRECIATION STRATEGIES

What to know before your meeting

If you hold appreciated employer stock in your workplace retirement plan, there are some important tax rules you should know. You may benefit from favorable tax treatment of any net unrealized appreciation (NUA) in the employer's stock held in the plan, depending on its current value. There are different ways an employer can calculate cost basis for your shares, which you can get directly from your employer. NUA is the difference between the cost basis of employer stock in your plan and its value on the day the shares are distributed as part of a lump-sum distribution. Depending on the amount of NUA and your current circumstances and goals, other approaches (like leaving the stock in your employer's plan, selling it inside the plan, or rolling it over to another employer's plan or IRA) may be more appropriate. Your tax advisor can help you evaluate your options.

Depending on your situation, you may be able to realize significant tax savings as a result of using an NUA tax strategy with a lump-sum distribution that includes employer stock. What's more, if you hold on to the stock, your heirs may receive favorable tax treatment on the NUA and post-distribution appreciation in the stock as well. Ask your tax advisor how much you could benefit from an NUA tax strategy.

Questions to review before your meeting

Q: How does an NUA tax strategy work?

A: Your tax advisor can explain the specific rules and how they will apply to your situation, but generally, when you receive a lump-sum distribution from your plan that includes employer stock or securities, and you take some or all of the employer stock in kind, you have ordinary income in an amount equal to the plan's cost basis in the stock. The NUA on the stock is not taxed until you sell the stock — and any NUA on the stock will then be taxed at the long-term capital gains tax rate. Any subsequent appreciation in stock will be taxed at long-term or short-term capital gains rates depending on the holding period after distribution. Long-term capital gains rates generally are lower than ordinary income rates. If you do not sell the stock and it passes to your heirs, they also may receive similar tax treatment on the stock, noting that any NUA is taxable to the heirs as long-term capital gains and does not qualify for the step-up in basis on death.

Q: How do I qualify for NUA tax treatment?

A: First, you must receive the stock as part of a lump-sum distribution* — that means the balance to the credit of the assets in your employer plan must be paid out within one taxable year. Also, there must be a triggering event, that is, paid because you separated from service (for employees), suffered a disability if you are self-employed, reached age 59½ or passed away. Distributions taken from a plan in a prior year may prevent a subsequent distribution from qualifying as a lump-sum distribution to the participant. All similar plans of the employer are aggregated when determining a participant's balance to the credit for lump-sum purposes. If a distribution does not meet the lump-sum distribution requirements, only the NUA that is attributable to the participant's nondeductible employee contributions may be excluded from gross income for tax purposes. You must receive the stock in kind and move actual shares of stock into a retail brokerage account. You cannot sell your stock within the plan, receive cash and then buy company stock outside of your plan if you want to take advantage of NUA. You cannot move the stock into a rollover IRA if you want NUA tax relief, although you can roll over other assets — including employer stock if you don't intend to use the NUA — from the lump sum distribution to an IRA. If you roll over the stock into your IRA, you will defer taxation on it, and you can sell the stock in the IRA to decrease your portfolio's investment in the employer's securities without tax consequences, but it will be disqualified for NUA treatment and you will be taxed at ordinary income tax rates when you receive distributions from your IRA. Whether a rollover to an IRA is right

* Other special rules apply in order for a distribution to qualify as a lump-sum distribution, for example, in situations where there is more than one employer plan. All decisions must be reviewed by a tax advisor before action is taken.

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for you is a decision that should only be made after considering such things as availability of investment options, fees and expenses, services, portfolio diversification, taxes and penalties, creditor protection, required minimum distributions and the tax treatment of employer stock.

Q: Are there other factors I should consider?

A: If you move ahead with an NUA tax strategy, you will need cash to pay the income taxes on the cost basis of your employer stock. If you are under age 59½, an additional 10% early distribution tax may apply. However, if you are at least age 55 and terminating employment, you can avoid the additional early distribution tax. The decision to take advantage of NUA is not an all-or-none decision. You could transfer some of your shares in-kind and roll over some of the shares to your IRA.

Holding a significant portion of your retirement assets in a single stock may not be an appropriate investment strategy. It exposes you to the risk that your employer's stock will not keep up with the market, decline in value or become worthless. Your financial advisor can help you weigh this risk against the potential tax benefits of following an NUA strategy.

Checklist to complete before your meeting

Your financial advisor can help you review your plan documentation to establish whether an NUA tax strategy may be an option for you. Before you meet with your financial advisor, you may want to gather some important information and documents:

- [ ] The most recent statements from your 401(k), profit sharing or other retirement accounts at work and any legacy plan accounts from prior employers
- [ ] The plan documents that describe your plan, along with your fee disclosure statement
- [ ] Documentation from your employer of the cost basis of your stock
- [ ] Information on your current tax bracket and how it is likely to change in the years ahead
- [ ] The telephone number of your company's benefits administrator so you and your financial advisor can confirm information and clarify any points that may be unclear
- [ ] Information on other IRA or retirement accounts you may have in order to evaluate the impact an NUA strategy may have on your retirement savings strategy and to ensure that your overall retirement assets are appropriately diversified

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