Polaris Greystone FINANCIAL GROUP, LLC

Polaris Greystone Educational Series

For more information or to schedule an introductory consultation contact us at: info@polarisgreystone.com I (800) 268-9046 I www.polarisgreystone.com

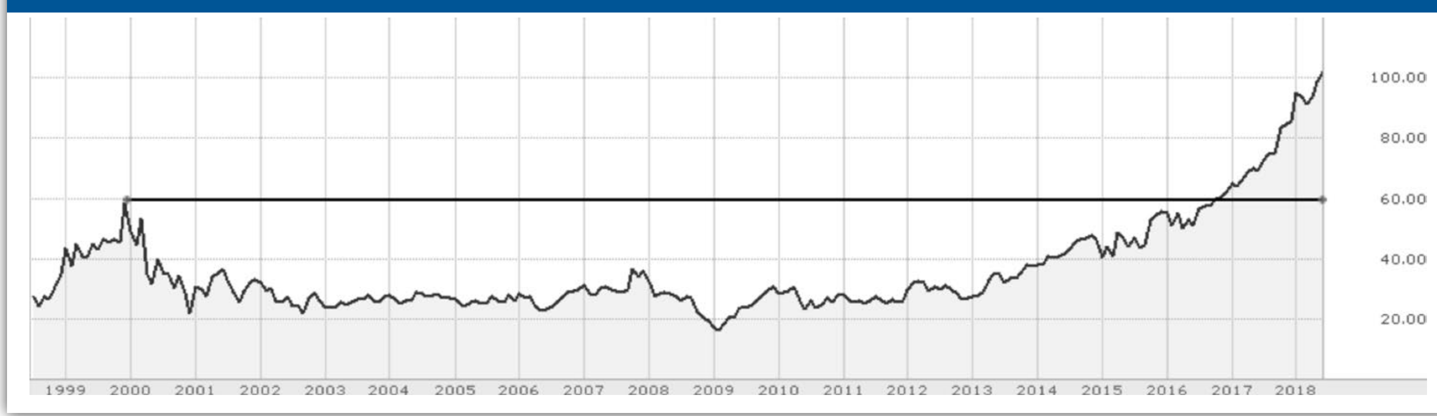
Polaris Greystone Solutions Highly Appreciated Concentrated Stock Positions

Having a highly appreciated concentrated stock position is a blessing and a curse. Often this stock is a client's largest asset, making the decision to keep the position or to diversify out of it that more challenging. What should you consider? Are there better ways of diversifying out of your stock? How do you make the tough decision to sell? These are challenging questions that we hope to help you with in this document.

Decision to Diversify:

I'm sure you've heard the age old saying, "don't keep all of your eggs in one basket." Why? Many of the wealthiest individuals in this country made their wealth by having a significant portion of their net worth in one company. Look at Bill Gates as a perfect example. Had he diversified himself out of Microsoft when the company went public in the 1986, he would most likely not be the billionaire that he is today. As successful and wealthy as Bill Gates is, had he diversified himself at the end of 1999, he would not have had to wait until 2016 before seeing his stock start to show improvement to his total net worth (see the chart below).

Chart of Microsoft from May 1998 to May 2018



Source: TD Ameritrade, Polaris Greystone Financial Group

The decision to diversify is a tough one. You've made a lot of money, but it's not really yours until you lock in that profit. You would hate to see your stock retreat in value but you'd kick yourself if the stock price continues to rise. Then there is the issue of Uncle Sam taking a big chunk of your profits. What should an investor do?

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If You Are Confident Your Stock Will Go Up in Value:

Employees of a firm often know far more about the company than the Wall Street Analysts covering the stock. If you are very confident that your company stock is going to go up in value, keep it! You may want to read below and have other alternative strategies waiting in the wings, just in case you are wrong. Why sell a high performing investment if it's doing well for you and the prospects of it continuing to do well far outweigh the risks of selling it?

Not Sure Which Direction Your Stock's Price Will Go:

If you are unsure which direction the price of your highly appreciated, concentrated stock might go, one strategy comes to mind.

Variable Prepaid Forward Contract (VPF):

If you aren't sure if your concentrated highly appreciated stock is going to go up or may drop then you may want to consider a variable prepaid forward contract (VPF). A VPF is a synthetic "collar" where the investor sells a "call," giving the right to some of the upside of a stock, and uses the proceeds to buy a "put" for downside protection. There has to be at least a 20% variance between the call and the put, otherwise the IRS considers it a constructive sell. The investor then barrows against their "collared" shares to build a diversified portfolio, providing them downside protection without having an immediate tax event. If you'd like to learn more, please reach out to your Polaris Greystone advisor.

Strategies to Sell and Diversify:

There are several strategies to sell your highly appreciated stock, each having different advantages and disadvantages. We have highlighted three of the most popular strategies here for your reading pleasure.

10b5-1 Sale

The Securities Exchange Commission created rule 10b5-1 to allow corporate executives and other corporate insiders of publicly traded companies to systematically sell a predetermined amount of their stock shares over a stated time, regardless if they are subject to blackout periods. For example, the President of XYZ company can set up a 10b5-1 plan to sell 5,000 shares of her stock "at the market" on the first Monday of the month for the next 12 months. 10b5-1 plans should only be adopted or amended when insiders are allowed to trade their company stock. If you'd like to learn more, please reach out to your Polaris Greystone advisor.

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Exchange Fund

An exchange fund is a pool of assets in which investors contribute their highly appreciated stock along with dozens, if not hundreds, of other investors who are contributing their own highly appreciated stock. At least 20% of the fund must be invested in illiquid investments, like real estate. Investors are given a free look at the holdings in the pool. If the investor chooses to move forward, their stock will go into the fund, the value of their investment will appreciate based upon how all of the holdings in the fund do, not their individual stock. After five years, an investor can leave with a collection of individual stocks that once helped make the fund, but will retain the cost basis of their original stock (pro-rated against all of the individual holdings). If you'd like to learn more, please reach out to your Polaris Greystone advisor.

Charitable Remainder Trust

Investors, who are charitably minded, may want to consider placing their highly appreciated, concentrated stock into a charitable remainder trust (CRT). A CRT is a tax-exempt irrevocable trust designed to provide a tax benefit to the donor, an income stream to the donor or the designated beneficiary of the trust, and then at the donor's passing a charitable contribution of the trust's assets. The investor contributes their highly appreciated stock to the trust. They are then able to sell their stock in the CRT with no capital gains tax. The investor will also get a tax credit on their contribution to the CRT. The tax credit varies depending on how much income the donor draws from CRT during their lifetime. At least 10% of the original contribution to the CRT must go to charity when the donors pass away. There are many moving pieces to CRTs. It is very important to coordinate with your accountant, your estate attorney, and your financial advisor when creating and funding a CRT. If you'd like to learn more, please reach out to your Polaris Greystone advisor.

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Conclusion

The decision to diversify yourself from a highly concentrated, highly appreciated stock should not be taken lightly. Tough decisions must be made about potential taxes and opportunity costs. Sell your stock too soon and it could cost you taxes today, plus missed opportunity of the stock growing in value. Hold on to the stock too long, and years of hard work could be lost by a downward spiral in your stock price, all because you were worried about taxes.

No one has tomorrow's newspaper. Making this decision should incorporate many factors. Bringing together your professional team, including your accountant, estate attorney, and your Polaris Greystone advisor is imperative to making the most informed decision possible.

If you have further questions, please feel free to write or call.

Sincerely,

Jeffrey J. Powell
Managing Partner