Have Appreciated Company Stock In Your 401(k)?

There may be ways to save on the income taxes you'll pay on the gain.

If you've elected to purchase company stock as part of your 401(k) allocation, you may have a significant gain due to its stock price appreciation. If you do, you may be able to save a considerable amount of income tax by taking it as a distribution instead of rolling it over as part of your entire 401(k). Here's why.

Anything you roll into an IRA will be taxed at your ordinary income tax rate when you withdraw it. This tax rate is currently as high as 43.4%. If you rollover that appreciated company stock into your IRA and subsequently sell it, it will be taxed as ordinary income like everything else in your IRA when you take a distribution. By requesting that your company shares be distributed to you, significant savings on the appreciated portion of your company stocks can be realized on their subsequent sale. Here's how it works.

You'll have to pay ordinary income tax on the amount you originally paid for the stock in the company plan. That purchase price will then become your *cost basis*. The difference between the stock's current market value and your cost basis is the *net unrealized appreciation* (NUA.) This amount is subject to lower long-term capital gains rates, currently no higher than 23.8%.

As an example, suppose you purchased $50,000 worth of company stock over your working years in your 401(k) plan and it grows to be worth $500,000 by the time you decide to retire. If that stock is rolled over to an IRA and subsequently sold and withdrawn, a tax as high as $219,000 will be due.

If you decide to take a distribution of that stock from the plan, you would be taxed at ordinary income tax rates on your original purchase of $50,000 in the year of distribution. This would be a maximum of $21,900. But there's no tax on the $450,000 of stock appreciation (i.e. gain or NUA) until you actually sell any of it. And when you do, the tax on that gain will be no more than the current long-term capital-gains rate (23.8%), a maximum of $107,100. **This is a savings of up to $90,000.**

The above refers to federal taxes only. State taxes, if applicable, are not considered here. To discuss the potential tax savings to you, please feel free to call me at (610) 999-3599. There is no cost and no obligation.

Elliot Goldberg is an independent Registered Investment Advisor specializing in helping clients generate dependable lifetime income for their retirement. Please contact him for more information at (610) 999-3599 or eg@goldata.com.

Click here for other articles like this.