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Planning Strategies for the $1 Million Plus 401(k) Plan

It is not unusual for executives to acquire large positions in their company's stock through long-term participation in their 401(k) plan. In fact, for someone who has worked at a company for thirty or forty years, their account balances can be in the millions. When large concentrations of stock are inside a qualified plan, it usually means that these shares were bought at a low price and have appreciated significantly over the years. In technical terms, this is called Net Unrealized Appreciated ("NUA"), and in the right situation NUA can lead to some creative planning opportunities. The example below illustrates how an executive might take advantage of NUA that has accumulated inside their 401(k).

Joe Smith retires from the XXX Corporation in 2014. He has a 401(k) plan worth $2 million, as well as significant other investment assets. He and his wife, both age 60, are very involved in several charities in their community and want to volunteer their time and make some gifs to help these causes financially. They implement a technique called the "NUA/CRT rollover." Here's how it works. Let's assume that Joe's 401(k) consists exclusively of shares of company stock. Also assume that Joe paid only $100,000 for these shares over the years — in other words, the shares have net unrealized appreciation of $1,900,000. Joe requests an in-kind distribution of his 401(k) account, i.e. he receives a stock certificate for his shares that are inside the plan. When Joe receives his certificate, he will also receive a statement describing the tax implications of his distribution. In this case, his taxable amount will only be $100,000 due to a special benefit allowed by the tax code. Once Joe receives his shares, he then transfers them to a special trust called a Charitable Remainder Trust. He and his wife receive a charitable income tax deduction of approximately $570,000 for transferring these shares to the trust. The shares are then sold and reinvested for diversification purposes without incurring any income taxes (the trust is a tax-exempt trust).

For the rest of their lives, Joe and his wife receive a check equal to 5% of the value of their trust. Then, after their death, selected charities receive the balance of the trust. Joe's 401(k) plan has been distributed virtually income tax free, he's created a lifetime income stream of approximately $100,000 per year for he and his wife, and they've benefited several charities in the process — a win, win, win situation.

Is this strategy right for you? If you have lots of NUA inside your 401(k) plan and a desire to benefit one or more charities in the future, then this technique might be something for you and your spouse to consider. We are happy to discuss this technique further with you.

The information contained in this article is intended to be educational and informational in nature. It should not be construed as specific investment, legal or tax advice for your particular situation. Please consult a Brightworth Wealth Advisor with any questions. Also remember that with investing, past performance is not a guarantee of future results.

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