

## Understanding Net Unrealized Appreciation (NUA)

### What is Net Unrealized Appreciation (NUA)?

Net Unrealized Appreciation (NUA) refers to special tax rules that may apply when employer stock is distributed from an employer-sponsored retirement plan, such as a 401(k), into a taxable brokerage account rather than rolled into an IRA. Under certain circumstances, this strategy may allow the appreciation on the employer stock to receive more favorable tax treatment.

The key advantage of NUA is that the appreciation of the company stock (the increase in value while inside the 401(k)) is taxed at more favorable long-term capital gains rates when sold, rather than the higher ordinary income tax rates that apply to traditional retirement account distributions. Potential advantages and disadvantages should be evaluated carefully with qualified tax and financial professionals.

### How to Elect NUA on Company Stock

#### 1. Verify Eligibility

- The distribution must occur due to a triggering event, such as separation from service, death, etc.
- You must take a lump-sum distribution of your entire 401(k) in a single tax year.
- Your plan must allow in-kind distribution of employer stock.

#### 2. Determine Asset Allocation

- Instruct the Plan Administrator to transfer company stock in-kind to your taxable brokerage account.
- Roll over all remaining 401(k) assets (stocks, bonds, cash) into an IRA to maintain tax deferral

*\*Subject to plan provisions and applicable tax rules.*

#### 3. Understand the Tax Implications

- The cost basis of the company stock is taxed at the ordinary income rates in the year of distribution.
- The NUA portion (appreciation in 401k) is taxed at long-term capital gains rates when you sell the stock.
- If you don't sell the shares immediately, any gains after the transfer (post-transfer appreciation) are subject to normal short or long-term capital gains tax treatment, based on your holding period.

#### 4. Report the Distribution Correctly

- Your Plan Administrator will issue a Form 1099-R, detailing the taxable cost basis and NUA amount.
- Your tax professional should ensure proper reporting on your tax return to maximize the tax advantages of NUA.

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## Important Considerations:

The entire 401(k) balance must be distributed in a single tax year to qualify for NUA treatment.

Only the cost basis is taxed as ordinary income at the time of transfer, while the NUA portion is taxed later at long-term capital gains rates.

If you decide not to sell the company stock immediately, any additional appreciation after transfer will be subject to standard capital gains tax rules based on your holding period.

Rolling employer stock into an IRA generally eliminates the ability to use NUA tax treatment. Individuals should evaluate available options with their tax and financial professionals before making rollover decisions.

Factors commonly evaluated when considering NUA treatment include:

- You have significant appreciation in your company stock.
- You want to minimize taxes on withdrawals by paying long-term capital gains rates instead of ordinary income tax.
- You don't need immediate access to the funds and can hold the stock for tax-efficient selling.

However, NUA may not be beneficial if:

- Your company stock has low appreciation (the tax benefit may be minimal)
- You plan to hold the stock indefinitely, as it may qualify for a step-up in basis.
- You need to diversify your investments, as holding too much employer stock can be risky.

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