Net Unrealized Appreciation (NUA)

Net unrealized appreciation (NUA) is the difference between the cost basis of shares of employer stock and their market value at the time they are distributed in kind from a qualified retirement plan as part of a lump-sum distribution. NUA can be a valuable tax planning tool for employees who hold employer stock in a retirement plan.

When an employee receives a distribution from a retirement plan, the distribution is generally taxable to the employee at ordinary income tax rates. However, if the distribution includes employer securities, the employee may be able to defer paying tax on the portion of the distribution that represents NUA. The NUA will remain untaxed until the employee sells the stock. In addition, the NUA will not be taxed at the ordinary income tax rate; it will instead be taxed at the more favorable long-term capital gains tax rate.

Taxation of Net Unrealized Appreciation (NUA) Stock

Post-distribution Gain	Taxed at short or long-term capital gains rates based on holding period from distribution date
NUA Gain	Taxable as long-term capital gains when shares are sold
Cost Basis	Immediately taxable as ordinary income when NUA distribution occurs (may be subject to 10% early withdrawal penalty as well)

There are a few requirements that must be met to qualify for NUA treatment:

- The employee must experience a qualifying event, which includes:
  - Turning age 59 ½
  - Separation from service (not for the self-employed)
  - Disability (only for the self-employed)
  - Death
- The distribution must be a lump sum, fully distributed within one year.
- NUA only applies to the distribution of employer securities, which must be received into a taxable account. Non-employer securities may be rolled over into an IRA.

Here are some additional things to keep in mind about NUA:

- NUA can only be applied to the portion of the distribution that represents the unrealized appreciation in the stock. The portion of the distribution that represents the original cost basis of the stock is taxed as ordinary income.
- Long-term capital gain treatment to the NUA when sold, even if held for less than one year.
- NUA does not get a step up in cost basis at the owner's death.
- A 10% early withdrawal penalty on the cost basis will be applied if the participant is under 59 ½. This may erode much of the potential tax benefit.
- The employee should confirm with their employer that the shares were purchased with pretax contributions or employer matches.
- Because the entire vested balance must be distributed as a lump-sum within one year, distributions should not be taken in years prior to the year the employee wants to utilize the NUA.
- NUA can only be elected once. You cannot change your mind later if you elect NUA treatment for a distribution.

How to Elect NUA Treatment

Complete and submit the NUA election form. The NUA election form is a document that you will need to submit to your retirement plan administrator. The form will ask you to provide information about the employer stock that you are electing NUA treatment for, including the fair market value of the stock on the date of distribution and your cost basis in the stock.

Have the employer stock distributed in-kind to a taxable brokerage account. The employer stock will be distributed to your taxable brokerage account in-kind. This means that you will receive the actual shares of stock, rather than cash.

Pay taxes on the cost basis of the stock. When you elect NUA treatment, you will be taxed on the cost basis of the stock as ordinary income. Taxes on NUA (Net Unrealized Appreciation) are not withheld. When you elect NUA treatment, you will receive a Form 1099-R from your retirement plan administrator. This form will show the amount of NUA that you are required to pay taxes on. You will be responsible for paying these taxes when you file your annual income tax return.

NUA "Depreciation" Strategy

This strategy involves selling the employer stock within the retirement plan at a loss, which will lower your cost basis for the stock. If the stock recovers, this will allow for a larger tax deferral when utilizing the NUA in the future.

"Cherry Picking" Strategy

The strategy of selecting only the company shares with the lowest basis when applying NUA is called cherry-picking. This strategy is allowed under the NUA rules, and it can be a good way to minimize your taxes on the NUA. Because the tax is due immediately on the shares selected for NUA (ordinary income on the cost basis), it may be beneficial to select only the shares with the lowest basis. The other shares, along with the non-employer securities may be rolled over to an IRA tax-free.

The use of NUA can be a powerful tax-saving tool in the right situation. There are risks involved in utilizing the strategy and the rules are complex. We can help you navigate these issues and develop a strategy that is right for you.

Connect with us to learn more.

www.naviterwealth.com

team@naviterwealth.com

501.333.9800

Naviter Wealth, LLC ("Naviter") is a Registered Investment Advisor ("RIA"). Naviter provides investment advisory and related services for clients nationally. Naviter will maintain all applicable registration and licenses as required by the various states in which Naviter conducts business, as applicable. Naviter renders individualized responses to persons in a particular state only after complying with all regulatory requirements, or pursuant to an applicable state exemption or exclusion.

Information provided in this material is for informational and/or educational purposes only and is not, in any way, to be considered investment advice nor a recommendation of any investment product. Information regarding investment services are provided solely to gain an understanding of our investment philosophy, our strategies and to be able to contact us for further information. Advice may only be provided by Naviter's advisory persons after entering into an advisory agreement and provided Naviter with all requested background and account information.

Different types of investments involve varying degrees of risk. Therefore, it should not be assumed that future performance of any specific investment or investment strategy will be profitable. Asset allocation may be used in an effort to manage risk and enhance returns. It does not, however, guarantee a profit or protect against loss. Performance of the asset allocation strategies depends on the underlying investments.

If you have any questions regarding our policies, please Contact Us