Stephanie Kelly
Senior Vice President, Wealth Management
Corporate & Executive Services
45 Rockefeller Center
New York, NY 10111
212-314-0455
skelly@raymondjames.com
www.raymondjames.com/skelly

RAYMOND JAMES®

Concentrated Stock Positions: Considerations and Strategies

Time counts

When dealing with a large stock holding, think about your time frame. Some strategies, such as hedging, might be most suitable in the short term or if you are restricted from selling. Others, such as donating to a trust, may be more cost effective over a longer time period, though your charitable intentions obviously play a role as well.

Whether you inherited a large holding, exercised options to buy your company's stock, sold a private business, hold restricted stock, or have benefitted from repeated stock splits over the years, having a large position in a single stock carries unique challenges. Even if the stock has done well, you may want more diversification, or have new financial goals that require a shift in strategy.

When a single stock dominates your portfolio, however, selling the stock may be complicated by more than just the associated tax consequences. There also may be legal constraints on your ability to sell, contractual obligations such as lock-up agreements, or practical considerations, such as the possibility that a large sale could overwhelm the market for a thinly traded stock. The choices appropriate for you are complex and will depend on your own situation and tax considerations, but here is a brief overview of some of your options.

Sell your shares

Selling obviously frees up funds that can be used to diversify a portfolio. However, if you have a low cost basis, you may be concerned about capital gains taxes. Or you may want to avoid any perception of market manipulation or insider trading. You might consider selling shares over time, which can help you manage the tax bite in any one year, yet allow you to participate in any future growth.

You'll need to consider the tax consequences of any sale. The American Tax Relief Act of 2012 set the maximum tax rate on long-term capital gains at 20% for those in the 39.6% federal income tax bracket; a 15% rate will generally apply for individuals in the 25%, 28%, 33%, or 35% tax brackets, and a 0% rate will generally apply for those in the 10% and 15% brackets. Also, if your adjusted gross income exceeds $200,000 ($250,000 for married couples filing jointly), your net investment income will be subject to an additional 3.8% Medicare contribution tax. In contrast to previous years, these rates are not scheduled to expire at a certain date. That increased certainty should simplify planning.

If you hold restricted shares, you might set up a *10b5-1 plan,* which spells out a predetermined schedule for selling shares over time. Such written plans specify in advance the dates, prices and amounts of each sale, and comply with SEC Rule 144, which governs the sale of restricted stock and was designed to prevent insider trading. A 10b5-1 plan demonstrates that your selling decisions were made prior to your having any insider knowledge that could influence specific transactions. (However, terminating the plan early or selling too much too quickly could raise questions about the plan's legitimacy.)

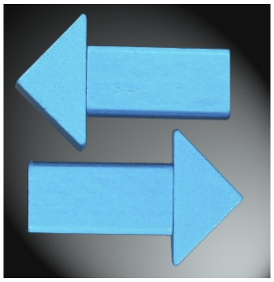
You might also be able to avoid some of the restrictions on how much and when you can sell by selling shares privately rather than on the public market. However, you would likely have to sell at less than the market value, and would still face capital gains taxes.

Hedge your position

You may want to try to protect yourself in the short term against the risk of a substantial drop in price. There are multiple ways to try to manage that risk by using options. However, bear in mind that the use of options is not appropriate for all investors.

Buying a *protective put* essentially puts a floor under the value of your shares by giving you the right to sell your shares at a predetermined price. Buying put options that can be exercised at a price below your stock's current market value can help limit potential losses on the underlying equity while allowing you to continue to participate in any potential appreciation. However, you also would lose money on the option itself if the stock's price remains above the put's strike price.

Selling *covered calls* with a strike price above the market price can provide additional income from your holdings that could help offset potential losses if the stock's price drops. However, the call limits the extent



Make sure your collar's not too tight

Transaction costs in multiple leg options strategies, such as a collar, can be significant and should be considered as these strategies involve multiple commissions, fees, and charges. Also, the prices set for a collar must not violate the rules against a so-called constructive sale. A strategy that eliminates all risk is effectively a sale and thus subject to capital gains taxes. The strike prices of a collar should not be too close to your stock's market price.

Options involve risk and are not suitable for all investors, and investors may lose the entire amount of invested principal in a relatively short period of time. Prior to buying or selling an option, a person must receive a copy of "Characteristics and Risks of Standardized Options." Copies of this document may be obtained from your financial professional and are also available at http://www.theocc.com.

to which you can benefit from any price appreciation. And if the share price reaches the call's strike price, you would have to be prepared to meet that call.

A *collar* involves buying protective puts and selling call options whose premiums offset the cost of buying the puts. However, as with a covered call, the upside appreciation for your holding is then limited to the call's strike price. If that price is reached before the collar's expiration date, you would not only lose the premium you paid for the put, but would also face capital gains on any shares you sold. Be careful about closing one side of the collar while the other side of the trade remains outstanding. For example, if you exercised the put but the shares you sell are later called away prior to the call's expiration date, you could be left with an uncovered call. You could potentially suffer a loss if you had to repurchase the shares at a higher price to fulfill the call.

Monetize the position

If you want immediate liquidity, you might be able to use a *prepaid variable forward (PVF) agreement* . With a PVF, you contract to sell your shares later at a minimum specified price. You receive most of the payment for those shares--typically 80% to 90% of their value--when the agreement is signed. However, you are not obligated to turn over the shares or pay taxes on the sale until the PVF's maturity date, which might be years in the future. When that date is reached, you must either settle the agreement by making a cash payment, or turn over the appropriate number of shares, which will vary depending on the stock's price at that time. In the meantime, your stock is held as collateral, and you can use the upfront payment to buy other securities that can diversify your portfolio. In addition, a PVF still allows you to benefit to some extent from any price appreciation during that time, though there may be a cap on that amount.

Caution: *PVF agreements are complicated, and the IRS warns that care must be taken when using them. Consult a tax professional before using this strategy.*

Borrow to diversify

If you want to keep your stock but need money to build a more diversified portfolio, you could use your stock as collateral to buy other securities on margin. However, trading securities in a margin account involves risks. You can lose more funds than you deposit in the margin account. Consider speaking with a financial professional before considering this strategy.

Exchange your shares

Another possibility is to trade some of your stock for shares in an *exchange fund* (a private placement limited partnership that pools your shares with those contributed by other investors who also may have concentrated stock positions). After a set period, generally seven years, each of the exchange fund's shareholders is entitled to a prorated portion of its portfolio. Taxes are postponed until you sell those shares; you pay taxes on the difference between the value of the stock you contributed and the price received for your exchange fund shares. Though it provides no liquidity, an exchange fund may help minimize taxes while providing greater diversification (though diversification alone does not guarantee a profit or ensure against a loss). Be sure to check on the costs involved with an exchange fund as well as what other securities it holds. At least 20% must be in nonpublicly traded assets or real estate, and the more overlap between your shares and those already in the fund, the less diversification you achieve.

Donate shares to a trust

If you want income rather than growth from your stock, you might transfer shares to a trust. If you have highly appreciated stock, consider donating it to a *charitable remainder trust (CRT).* You receive a tax deduction when you make the contribution. Typically, the trust can sell the stock without paying capital gains taxes, and reinvest the proceeds to provide an income stream for you as the donor. When the trust is terminated, the charity retains the remaining assets. You can set a payout rate that meets both your financial objectives and your philanthropic goals; however, the donation is irrevocable.

Another option is a *charitable lead trust (CLT),* which in many ways is a mirror image of a CRT. With a typical CLT, the charity receives the income stream for a specified time; the rest goes to your beneficiaries. There are costs associated with creating and maintaining trusts. You receive no tax deduction for transferring assets unless you name yourself the trust's owner, in which case you will pay taxes on the annual income. Other philanthropic options include donating directly to a charity or private foundation and taking a tax deduction.

Managing a concentrated stock position is a complex task that may involve investment, tax, and legal issues. Consult professionals who can help you navigate the maze.