Options for Managing Your Concentrated Equity Position

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One of the benefits of equity compensation, beyond a chance to share in your company's success and a recognition of your contributions to that success, is the financial flexibility it can give you. Receiving a portion of your compensation in the form of equity can be an accelerant to your goals, helping you to reach them faster — or blow past them. Over time, that additional flexibility can also supplement your cash income, and even afford you the freedom of financial independence.

But it takes careful planning and a long-term perspective to get there. And while you're accumulating it, there may be periods of time when you're holding a lot more equity than you ever anticipated. If that seems likely, or is already the case for you, then you'll want to read on for three ways to manage a concentrated equity position in a way that preserves some of your upside, protects you on the downside, and supports you in realizing the life you want to build.

#1 Sell Your Stake

One way to handle a big equity stake is simply to sell it. Sounds simple, right? It isn't necessarily. Sometimes it's just not practical to sell it all right away, especially a large one. And it might not be desirable. You might see your stake as an important part of your overall portfolio. Selling it in one go would also mean you lose out on any potential upside down the road. One way to balance these considerations would be to set up a schedule and sell a percentage of your stake at regular intervals. That takes your emotions out of the process. Selling on a regular timeframe also allows you to slowly scale into other investments, diversifying your portfolio in a way that lines up with your return objectives, time horizon, and comfort with risk. Regularly selling parts of your holdings and reinvesting your proceeds in other opportunities also enables you to scale into the market at different price points.

#2 Gift Your Stake

Gifting some of your stake could make sense if it helps you achieve a larger goal. For instance, if you're interested in generational wealth transfer, gifting shares of appreciated stock could allow you to achieve two objectives at once. Gifting instead of selling means you can help someone, maybe a younger family member who is in a lower tax bracket and has big future expenses, avoid capital gains tax. Just be aware that you could owe gift taxes if the value of your gifted equity exceeds certain limits. You'll want to work with your financial advisor and a tax expert to make sure you structure your gift in a way that doesn't result in avoidable negative tax consequences.

#3 Donate Your Stake

Donating your shares to a charitable entity, for instance through a donor-advised fund, can be a way to reduce the risk of having too much of your wealth concentrated in a single position while at the same time expressing your values.

It can also have tax benefits. Depending on your tax situation, you could take a deduction for the value of your charitable donation.

There are also more complex strategies for managing a concentrated equity position. These include using options to lock in gains or transferring your shares to a trust. Of course, before deciding to pursue any of these, you'll want to think through the costs versus benefits and weigh the trade-offs.

At the end of the day, what's key is to come up with a plan. Your plan can and often should, change over time, as your circumstances change. But being intentional brings its own benefits. One, it forces you to anticipate, think through, and plan for different scenarios ahead of time. That's valuable because advance preparation can help you avoid pitfalls like sticking with an overly concentrated portfolio for too long, forgetting to manage your downside risk, or flying blind and then finding yourself in a painful tax situation. It also has the benefit of giving you control. While you can't control whether equity prices rise and fall and when, planning early gives you time to deliberate, so that you aren't suddenly having to make a decision under pressure. And that's valuable in itself.

When we work with our clients who have substantial concentrated equity positions, we start with their overall goals, assess their current financial situation, and review future scenarios as part of the process of coming up with a plan that makes sense for them. Along the way, we make sure to collaborate with their tax professionals in coming up with strategies for managing their equity compensation that are in line with their goals, priorities, financial situations, and their values.