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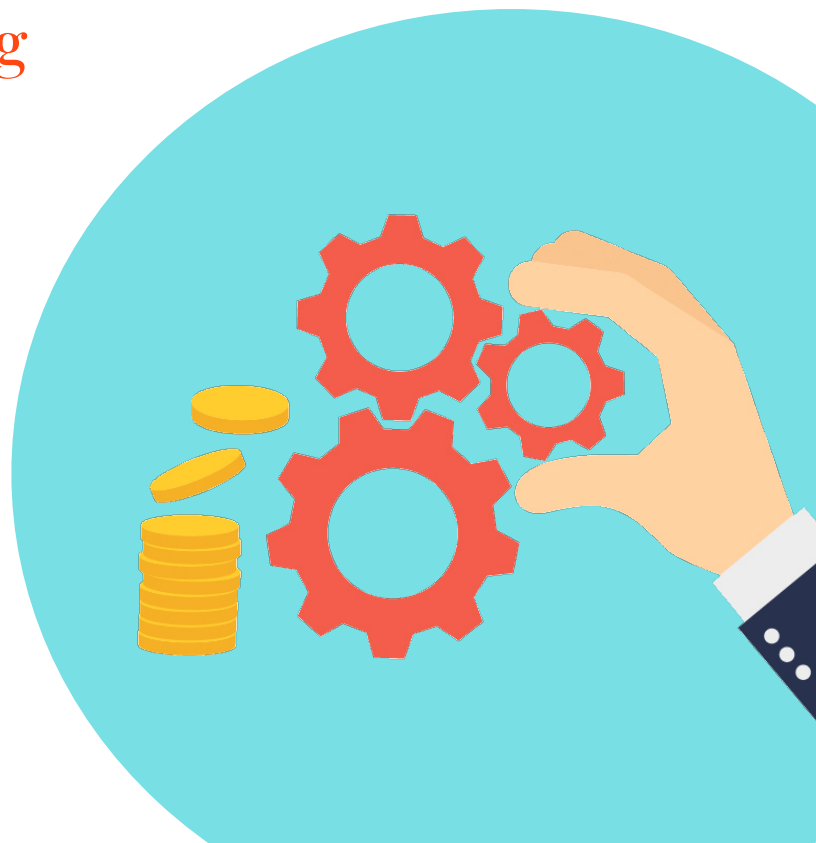
6 Missed Tax & Financial Planning Opportunities

by Founders
& Early-Stage Executives



The company Founder, or early-stage Executive, is understandably so laser-focused on the business that the Founder typically misses opportunities to position and secure her financial future on the personal side. These missed opportunities can ultimately cost the Founder hundreds-of-thousands, if not millions, in taxes and savings.

Learn the six missed tax and financial planning opportunities our firm sees when working with Founders and early-stage Executives.



Missed Opportunity #1: Failing to Exercise on a Timely Basis

Although the conventional wisdom is to exercise Incentive Stock Options (ISOs) as late as possible, sometimes it is more advantageous to exercise ISOs early – when the spread is smaller, and the executive is in a lower tax rate. However, waiting later to exercise – when the spread is possibly higher, and the executive is at a higher tax rate – may mean more in taxes. Similarly, exercising ISOs mid-year or later in the year, rather than at the beginning of the year, may limit the executive's flexibility to consider reversing the exercise if the stock price goes down at the end of the year. ISOs are exposed to the alternative minimum tax (AMT) when exercising ISOs, so the AMT can be highly punitive if the stock price goes down after the exercise.

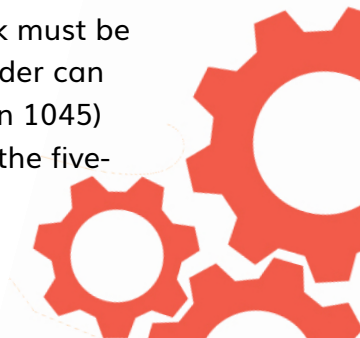


Missed Opportunity #2: 83(b) early election

Early-stage companies often offer an 83(b) early election provision on their stock grants. However, these 83(b) election opportunities have very strict, time-sensitive deadlines to them, or the executive loses this opportunity. In fact, the 83(b) election requires the executive to make this decision within 30 days of the grant date. In essence, the executive is electing to pay the tax upon the grant of the stock, even if the stock has not yet vested. The 83(b) election enables the executive to elect to tax the current value of the grant now as ordinary compensation income (at the executive's current Federal & State tax), so that subsequent growth would be taxed at capital gains at its eventual sale. Also note that the executive's accountant must file the election with the IRS within the 30 days, and the executive will have to pay the tax on the grant this year.

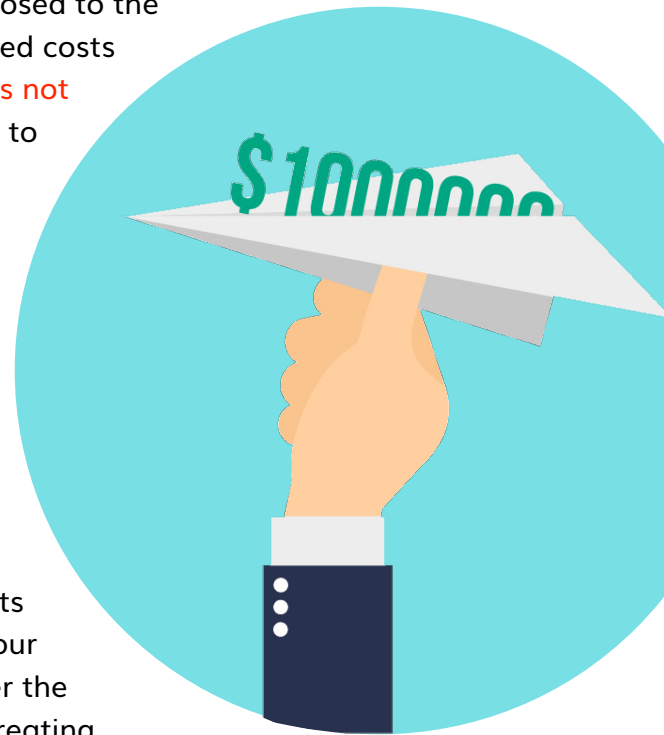
Missed Opportunity #3: QSBS 1045 rollover

Founders often own Qualified Small Business Stock (QSBS) shares that receive preferential tax treatment under IRS Section 1202. Depending on when the stock was acquired, the Founder can exclude up to 100% of capital gains, up to the greater of \$10,000,000, or "10 times" (10x) the adjusted basis of the stock. QSBS stock must be held for five years to qualify for the preferential tax treatment, but the Founder can choose to re-invest the proceeds into another QSBS ("rollover" under Section 1045) within 60 days, if the Founder wants to sell her original QSBS shares before the five-year holding period.



Missed Opportunity #4: Saving on Future Estate Taxes

Exposure to capital gains taxes and income taxes are not the only tax concerns for the successful Founder, or early-stage Executive. Sometimes known as the "death tax" or "inheritance tax," large estates are exposed to the Federal Estate Tax. In some states, there are also added costs of the State Estate Tax. (Note: **California currently does not have an estate tax.**) Many Founders, or Executives, fail to realize that the estate tax can be optional with proper gift and transfer planning. A formal gifting strategy can take advantage of available tax credits and additional leveraging strategies. For example, prior to sale, you have an opportunity to transfer minority interests in your business and appreciation on these interests to the next generation free of gift tax by utilizing your current exemption amount and taking advantage of valuation discounts. Upon sale, the value of the interests transferred to the next generation through Generation-Skipping Transfer Trusts will be excluded from your estate and the estates of your descendants. Furthermore, Founders can also transfer the QSBS exclusion to multiple other family members by creating separate irrevocable trusts that each qualify for the Section 1202 exclusion, creating a "multiplier effect" on the exclusion. Preferred techniques in the current economic, low-interest environment include GRATs, CLATs, and IDGTs.



Missed Opportunity #5: Liquidity Windows

The inability to have liquidity is typically one of the impediments to making progress in the Founder's personal plan. The Founder may be able to sell shares in a secondary sale ("secondaries") to take some risk off the table. This can be a prudent approach. Alternatively, there are third-party liquidity markets for a private sale (e.g. EquityZen, Forge, etc.) or private financing (e.g. ESO Fund, etc.), but these "brokers" typically come at a high cost, and prefer later-stage companies (e.g. Series D, valuations greater than \$500 million). Likewise, many companies prohibit these transactions, and there could be a negative perception by other investors if the Founder engaged in one of these transactions.





Missed Opportunity #6: Starting the Planning Process Too Late

Perhaps the biggest missed opportunity for the Founder is the inability to see the forest for the trees. That is, the Founder is so focused on the business that she forgets about securing her personal future. Maybe there's an element of a well-intentioned deferral, so as not to "jinx" her current success. However, the most common excuses I hear from a Founder are: "I don't have anything to plan for," or "We just need to get through the next round of financing," or "I'll start once I have the liquidity event." Granted, it does take a forward-looking (and confident) Founder, who sees a pathway to entrepreneurial success, to be able to look into her own personal future.

More so than taking advantage of the tax and planning techniques available to the Founder, planning is really about obtaining the peace-of-mind around rapidly-rising or "overnight" wealth. Most Founders are under-prepared – not strategy or tactic-wise, but psychologically and emotionally – for this possibility. To toil and toil for years without reward or recognition, with a sudden new set of burdens brought on by wealth, brings on stresses and worries not previously there, to not only the Founder, but her family.

Engaging in an intentional planning process can help clarify the Founder's true values (beyond the business), and define what is truly important to her, and what kind of lasting legacy she would like to provide to her family, her children, and her community. Perhaps the next phase for the Founder is to maintain financial independence to pursue new start-up ventures, career changes, and personal interests. Starting the planning process also does not have to be an all-or-none proposition, but rather an incremental engagement, no different than building a business from the start-up to a successful mature one.

When working with Founders and early-stage Executives, our work typically goes beyond the tactics and strategies of sophisticated investment management or financial planning, but rather *life and career planning*. Ultimately, the Founders our firm works with are highly intelligent, successful people, with families (partners, spouses, children, aging parents) and real-life problems.



Our firm does our best work with clients who fit one or more of the following:

- Talented, Highly-Sought-After "Creatives," Executives, and Founders in Technology, who have a desire to "get it right" the first time, and value the flexibility in their career and their family, so that they can move forward with confidence no matter what direction their life takes.
- Have complex Compensation and Benefits Packages, and seek assistance to make sure they are getting the best package they deserve.
- Have concentrated stock holdings (e.g. stock option grants – ISOs/NQSOs, restricted stock units – RSUs, and stock appreciation rights – SARs, etc.)
- Desire a meaningful commitment (e.g. intention, desired goal, or a plan already in place – e.g. Schedule A Itemized Deductions – Gifts to Charity, Donor Advised Funds, Charitable Trusts – CRTs CLTs, etc.) to giving back for Social Good and Social Responsibility.
- Constantly seeking to improve or refine one's own situation, and open to new ideas.
- Understands that time (and the proper usage of this time) is probably their most valuable asset.
- Appreciates and values expertise through counsel, and aims to build a collaborative relationship with their existing advisors (e.g. attorney, accountant, etc.).
- Above all, our clients are intelligent, open-minded, and display the highest character and integrity.

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