

Personal planning for start-up founders



Advanced Planning Group | Family Office Solutions



Centers of excellence

The **Advanced Planning Group** consists of former practicing estate planning and tax attorneys with extensive private practice experience and diverse areas of specialization, including estate planning strategies, income and transfer tax planning, family office structuring, business succession planning, charitable planning and family governance.

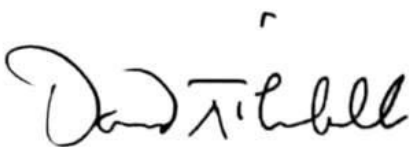
The Advanced Planning Group provides comprehensive planning and sophisticated advice and education to ultra high net worth (UHNW) clients of the firm. The Advanced Planning Group also serves as a think tank for the firm, providing thought leadership and creating a robust intellectual capital library on estate planning, tax and related topics of interest to UHNW families.

Family Office Solutions is a team of specialists that exclusively works with USD 100 million+ net worth families and family offices. The team helps clients navigate the challenges and opportunities across their family enterprises, including their businesses, family offices, philanthropic structures, and passions and interests. Having this expertise under one roof allows for integration and layering of services across the UBS ecosystem, delivering a personalized, holistic client experience.

Letter to the reader

From Silicon Valley to Boston and virtually everywhere in between, we're in what may be a golden age for start-up businesses. Some of the industries where, in recent years, start-ups have flourished include technology, life sciences and social media, but start-ups are transforming virtually every sector of the economy. Start-up founders are passionate about their businesses and willing to take great risks and fail. Many of these businesses are funded by venture capitalists and angel investors with the ultimate goal of being sold to a larger competitor or going public.

So much time and effort is spent growing the business and preparing for a liquidity event that the founder's personal planning often takes a back seat. This is unfortunate. While fortunes can be made through owning a single business, they can also be lost. By planning for the personal side of a liquidity event, both before and after the transaction, a start-up founder can help mitigate risks associated with a founder's equity (particularly income tax, estate and gift tax and concentrated equity risk), and set the stage for personal financial success. As they say, "failing to plan is planning to fail." Just remember how many rich start-up founders of the dot-com boom in the late 1990s lost everything in the dot-com bust of the early 2000s. With the right team of specialists to consult on their planning issues, founders can avoid these missteps and position themselves for both business and personal success on the exit.



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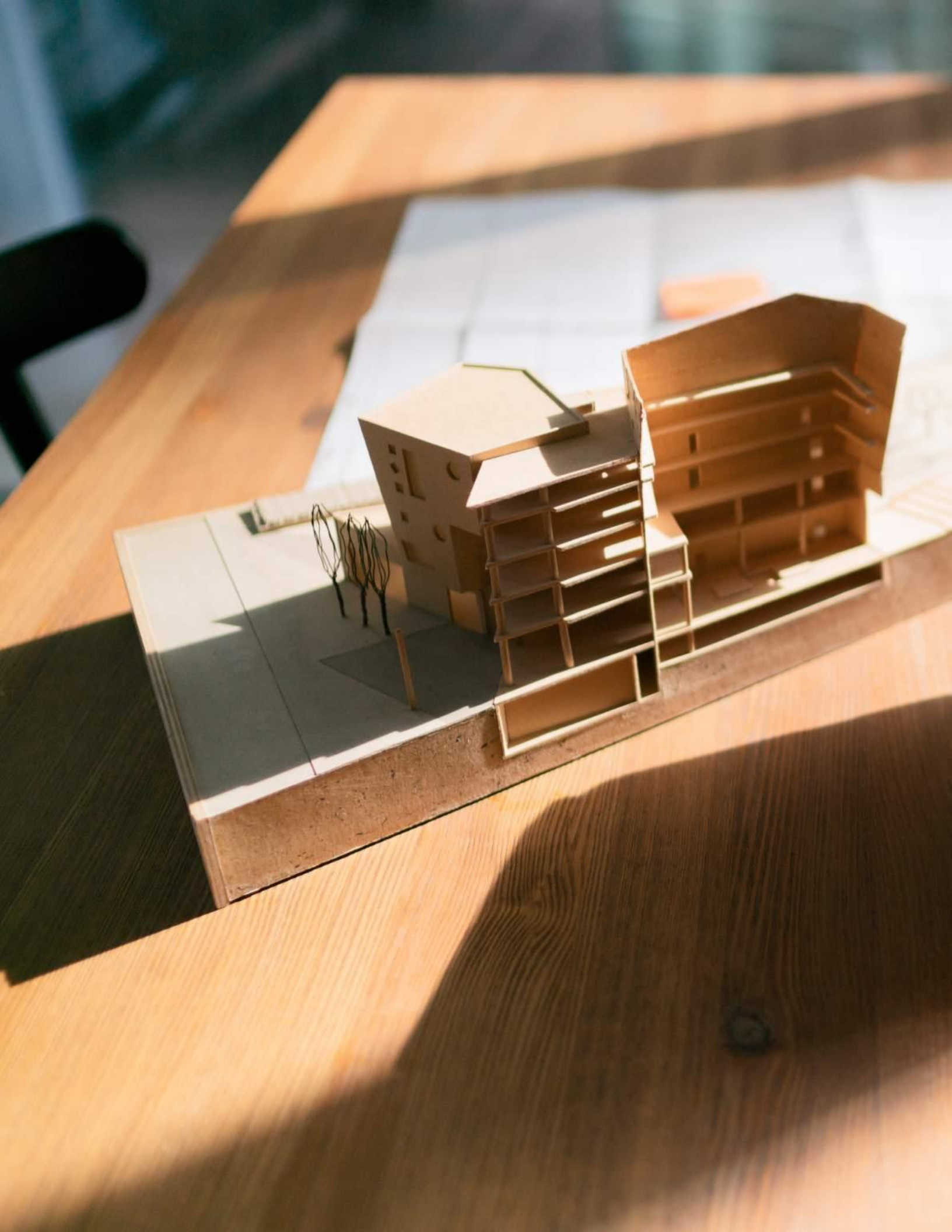
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Anatomy of a start-up

Most start-ups begin life with a few founders, a business idea and a small pool of capital contributed by the founders, their friends and family. Knowing that they may need to seek venture capital funding as they grow, many start-up businesses are either structured as, or convert to, a subchapter C corporation (to be able to take advantage of the tax benefits of qualified small business stock (QSBS), which is discussed below). The founders are issued restricted common stock (sometimes referred to as founders' stock), some or all of which is subject to a vesting schedule. An options pool is also set aside for employees. After the company has some success, it may be able to attract funding from venture capitalists and angel investors (basically wealthy individuals and family offices). These investors receive preferred stock, which has preferential rights to common stock. The preferred stock can be converted to common stock, thereby diluting the percentage ownership of the founders and employees.

If the business continues to grow, additional rounds of venture funding may occur. At a certain point, the venture capitalists expect the business to be sold to a larger company or go public. Generally, an acquisition of the business is far more likely than an initial public offering (IPO). The time frame for the liquidity event typically ranges from five to 10 years following initial venture funding. Assuming everything works out as hoped, the liquidity event will result in a large payday for founders and investors.

Along the way, there are certain traps for founders (particularly dilution of ownership through rounds of financing), as well as opportunities (including income tax mitigation through certain tax elections, estate tax reduction and windows to diversify out of a concentrated equity position).



Planning for start-up equity

Start-ups typically issue equity-based compensation to incentivize employees and give them the opportunity to share in the growth of the business and to align their interests with the interests of other shareholders. This also creates employee “stickiness” as equity-based compensation is frequently forfeited if an employee leaves the company. Equity-based compensation also helps preserve the start-up’s cash position. The types of equity-based compensation frequently used are restricted stock awards, restricted stock units (RSUs), incentive stock options (ISOs) and non-qualified stock options (NSOs).

Vesting and change of control

Virtually all equity-based compensation is subject to vesting. Vesting can occur over time or be based on a mix of time and the achievement of certain performance goals. Typically, vesting takes place over three or four years, with the first vesting date occurring on the first anniversary of the grant (sometimes referred to as a vesting “cliff”). Many equity compensation plans include change of control provisions, allowing for full or partial acceleration of unvested grants on a change of control of the company. This is known as “single trigger” vesting. Other companies use “double trigger” vesting, under which, if there’s a change of control, vesting will accelerate should the employee be terminated without cause within a specific period after the deal closes (typically 6 to 18 months).

Restricted stock awards

Restricted stock is common stock that’s sold or granted to a start-up founder. It’s subject to vesting and is forfeited if vesting requirements aren’t satisfied. If restricted stock is granted, the grant isn’t a taxable

event. At the time of vesting, restricted stock is taxed on its fair market value less any amounts paid for the stock. The vesting event is taxed as wages (i.e., at ordinary income tax rates) and subject to withholding; very commonly, at vesting, shares are net settled, meaning some of the shares are sold to account for income taxes, resulting in a reduction in the number of shares held. Any future sale of the stock will be taxed as capital gains or capital losses, and taxable at either ordinary income rates (for shares held less than one year post-vesting) or long-term capital gains rates (for shares held for more than one year post-vesting).

Restricted stock units (RSUs)

RSUs are similar in most respects to restricted stock awards. The primary differences are twofold. First, although an RSU grant is valued in terms of stock, no company stock is issued at the time of the grant. Second, when vesting requirements are satisfied, the employee typically is given the choice to settle in stock or cash.

Stock options

A stock option is the right given by the company to an employee or consultant (the "option holder") to purchase company stock in the future at a fixed price (typically the fair market value at the date of the grant), which can be exercised for a fixed period of time (typically 10 years). Like restricted stock awards and RSUs, options are subject to vesting. There are two different kinds of options. The first are incentive stock options (also known as statutory stock options). The Internal Revenue Code sets forth the statutory requirements, and, if they're met, ISOs receive favorable income tax treatment. ISOs may only be issued to employees. The second type of stock option is nonqualified stock options. Grants of NSOs may be made not only to employees but also to directors and consultants. Unlike ISOs, NSOs don't provide special tax treatment to the recipients. Typically, there's no taxable event for the recipient on the grant of either ISOs or NSOs.

Income taxation of incentive stock options (ISOs)

On the exercise of ISOs, there's no taxable income recognized by the option holder. However, the spread (difference) between the strike price (price at grant) and the value of the stock at exercise is subject to the alternative minimum tax (AMT) (potentially at the highest rate of 28%). It is important to understand the tax impact of any ISO exercises, so there are no surprises



when taxes are filed. Any gain post-exercise of an ISO is treated as a capital gain upon sale, if the required holding periods are met. The required holding periods are one year from exercise and two years from grant, and the employee must have been employed at least three months before the exercise date. If holding periods aren't met, a disqualifying disposition occurs, resulting in ordinary income taxation on the spread between the strike price and the value of the option on exercise. Only \$100,000 of stock, based on the strike price, may become exercisable in any calendar year, inclusive of all ISO grants that have been made.

Income taxation of non-qualified stock options

NSOs are compensatory stock options that don't meet the statutory requirements for ISOs. Recipients of NSOs are generally taxed at ordinary income tax rates on exercise: they are taxed on the spread between the strike price and the fair market value of the stock. Post-exercise appreciation is taxed as capital gains (long-term capital gains if held more than a year after exercise). Unlike ISOs, there are no limits on the value of NSOs that can be exercised by an employee, director or consultant each year. There are no AMT issues involved with the exercise of NSOs.

Section 83(b) election

An election under Section 83(b) of the Internal Revenue Code may provide significant income tax benefits to the holders of both stock options and restricted stock awards.

(Because there's no actual stock issued until vesting, a Section 83(b) election isn't permitted for RSUs.) Section 83(b) allows a taxpayer to elect to be treated for income tax purposes as if they have received vested, unrestricted property from the employer, which would trigger an immediate income tax liability, even if the stock were subject to a substantial risk of forfeiture. Why would a founder or employee decide to do this? Because they expect the stock to appreciate, which could result in a large income tax benefit. By way of explanation, any future appreciation is taxed at capital gains rates, and if held for more than one year after the Section 83(b) election is made, would receive long-term capital gain treatment rather than ordinary income tax treatment.

A Section 83(b) election must be filed with the Internal Revenue Service (IRS) within 30 days of the receipt of the restricted stock, or exercise of the option, and is generally irrevocable. In addition, it's worth noting that if the property is forfeited in the future because vesting requirements aren't met, the founder or employee may not take a loss for taxes already paid.

For an award of restricted stock, a Section 83(b) election is straightforward. The employee elects to be treated as if they received the stock immediately without vesting restrictions. As such, the employee would have ordinary income equal to the number of shares multiplied by the current fair market value of the stock (usually the 409A valuation obtained by the company in the case of a closely held company).

For a stock option grant, the ability to make a Section 83(b) election will depend on whether the stock option grant agreement allows employees to make an early exercise. If the fair market value is equal to the strike price at the time of exercise, there would be no tax due on the early exercise. The option holder would only need to cover the exercise cost.

Management of awards

Executive compensation is complex, and active management of holdings can produce significant benefits. Prior to going public, the opportunities to access liquidity may be limited—perhaps only through company buybacks or private market offerings. Founders and early employees may not wish to diversify or liquidate any of their holdings because the company is growing far faster than other investments, or maybe because they understand the company's prospects better than anything else. Some examples of proactive management of awards follow.

Early exercise

As a company grows, it will usually need to raise additional capital to support expansion. Increasing sales and demand for the company's products or services generally lead to higher valuations. Employees may seek to exercise options ahead of an impending valuation or capital raise to take advantage of a lower valuation and, therefore, lower the potential tax cost of exercising. Exercising the options and owning the shares outright accelerates the start of the holding period, which may result in receiving preferential tax treatment at long-term capital gains rates upon ultimate sale. Additionally, if the company is established as a subchapter C corporation and its stock otherwise currently qualifies as QSBS, exercising sooner rather than later could have significant tax benefits. For one, exercising the option starts the clock ticking on the holding period for QSBS. Second, the options must be exercised before the gross assets of the company exceed certain thresholds (\$50 million for stock acquired prior to July 5, 2025, or \$75 million for stock acquired on or after July 5, 2025, with the threshold to be adjusted for inflation after 2026). Exercising before these thresholds are exceeded could ensure the shares meet the QSBS requirements. For additional details, see the chapter entitled "Income tax planning prior to the sale."

ISO and NSO exercises

As discussed previously, ISO exercises are potentially subject to AMT while NSO exercises are not. If a founder is not already paying AMT, a good strategy may be to exercise as many ISOs as possible without triggering the AMT. If a founder is already subject to AMT, an alternative could be to look for ways to create additional income, because a higher level of regular income can create "space" to exercise ISOs without incurring additional AMT. One way to do this would be to exercise NSOs; another way would be to convert a traditional IRA into a Roth IRA.



Cashless exercises

The cost of exercising an option and holding it outright is typically the strike price for ISOs (assuming AMT does not apply) and the strike price plus ordinary income taxes on the bargain element (difference between the fair market value and the strike price) for NSOs. For options granted and exercised early in a company's lifecycle, the exercise cost may be rather modest. However, for companies that have grown the bargain element may be substantial, resulting in fairly significant income tax liabilities that must be withheld by the company upon exercise. Many founders and early employees lack the liquidity to fully exercise and hold NSOs that have appreciated significantly. One solution may be to borrow against founders' shares

or other assets to pay exercise costs and taxes. However, there may be limits to how much can be borrowed against founders' shares if a liquidity event is far away, and the interest rate could be prohibitively high. There's also a risk that the stock could go down in value post-exercise, resulting in paying more tax than one would have otherwise paid if the option were exercised later. In a worst-case scenario, the stock might fall to zero and the loan would have to be repaid with other assets.

Another alternative would be to enter into a cashless exercise, where a portion of the proceeds would be used to pay the exercise costs and taxes associated with the exercise. This could be a solution for options that are close to expiration, but

where there's a positive view on the shares' outlook and the holder intends to keep them. Scenario analysis could be helpful for identifying the crossover price point of not exercising and paying ordinary income on a larger number of units, versus doing a cashless exercise and paying long-term capital gains on a smaller number of units.

Exercising and charitable gifting

Exercising NSOs, in particular, can generate significant ordinary income within the tax year. However, this could be offset by pairing the exercise with gifts of highly appreciated publicly traded stock, or gifts of cash to a charitable entity, which would result in a charitable income tax deduction. A gift could be made to a donor advised fund that has no mandatory annual distributions. In effect, an individual could offset some of the taxes with the charitable deduction and invest the assets for growth to create a charitable endowment, which could then be distributed out to various public charities over the person's lifetime. Gifts to a private foundation would accomplish a similar charitable deduction (though there are different rules governing how quickly the charitable deduction may be used), but a private foundation generally must expend 5% of its net asset value for charitable purposes annually. See David T. Leibell and Nicole T. Sebastian, *Charitable giving: the rules of the road* (a publication of the UBS Advanced Planning Group, Family Advisory and Philanthropy, and Family Office Solutions).



Personal planning prior to the liquidity event

Start-up founders and other entrepreneurs typically have a laser focus on their business and tend to overlook some important aspects of their personal and financial lives. As a result, founders are sometimes ill-prepared for an exit event, with the consequences ranging from suboptimal to disastrous. Below are some of the key steps that should be explored well in advance—perhaps at least one to two years—of a liquidity event.

Putting together the team

Start-up founders are typically young and not wealthy. As such, they've rarely appointed outside professionals to review their personal financial affairs. But this needs to change as a business increases in value. Choosing a good certified public accountant (CPA) is the first step. Making sure tax returns are properly filed and tax elections are made on a timely basis is extremely important. Next up is a trusts and estates attorney to make sure an estate plan is in place in case the founder is hit by the proverbial bus. The attorney can also help draft documentation regarding gifts to family members and charity. Finally, a start-up founder should consider retaining a qualified wealth manager. The wealth manager can help with financial planning, including modeling of making early tax elections in connection with equity holdings. For best results, the outside advisors would collaborate with each other regarding important decisions along the way, each bringing to bear specific expertise.

Importance of financial planning

Financial plans, typically prepared by a financial advisor, can help form the foundations of personal planning for start-up founders anticipating a liquidity event. A good financial plan begins by evaluating the founder's financial goals. Once goals are established, the plan will determine the founder's cash flow needs and stress-test the likelihood of reaching certain goals going forward.

As the founder focuses on readying the business for the liquidity event, the financial planning exercise is often overlooked. In our view, this is a mistake. The financial plan allows the founder to preview what their financial life may look like post-sale. It allows the founder to stress-test a host of variables and, ultimately, arms the founder with the information to confidently make decisions. In the business, the founder wouldn't make a strategic decision without estimating the impact on projected profits, so why should the biggest decision of the founder's financial life be made without looking at the numbers?

The financial plan tests the following five key variables among others:

1. How to manage company holdings prior to exit (exercise/hold, exercise/sell, 83(b) elections);
2. Deal terms (exit price, earn-out, rollover, tax considerations);
3. Retirement date and lifestyle spending;
4. Asset allocation (including diversification from company concentration); and
5. Legacy planning (asset transfer pre-/post-sale, charitable planning).

The financial planning process allows the founder to determine the amount of core capital or the assets that will be needed for living expenses, with a high degree of confidence even if the capital markets do not perform well over time. Considerations such as lifestyle spending, time horizon and how assets are allocated will be taken into account. The higher (lower) the spending, the longer (shorter) the time horizon, and the lower (higher) the allocation to return-seeking assets, the higher (lower) their required core capital will be. Any assets above those required for the founder's lifestyle needs would be considered legacy capital and could be set aside using wealth transfer techniques that could, potentially, minimize certain income and transfer taxes.

UBS Wealth Way,¹ our approach to managing wealth, starts with questions and a discussion that helps us focus on what's really important to you. Then, we can help you organize your financial life into three key strategies:

- **Liquidity**—to help provide cash flow for short-term expenses;
- **Longevity**—for longer-term needs; and
- **Legacy**—for needs that go beyond your own.

For more information, see the sidebar entitled "Making the most of the fruits of your labor."

The financial planning process (and it may be iterative as deal terms are further refined) will produce the data needed to aid wise decision-making. What's more, the financial plan will be closely coordinated with the implementation of an estate plan.

¹ UBS Wealth Way is an approach incorporating Liquidity, Longevity, and Legacy strategies that UBS Financial Services Inc. and our Financial Advisors can use to assist clients in exploring and pursuing their wealth management needs and goals over different time frames. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved. All investments involve the risk of loss, including the risk of loss of the entire investment. Timeframes may vary. Strategies are subject to individual client goals, objectives and suitability.



Basic estate planning

Because many start-up founders are young, there's usually no estate plan in place. Start-up founders can have significant paper wealth, which without a will could pass to unintended individuals. In addition, if the start-up founder dies, any amounts over the individual's lifetime gift and estate tax exemption could be subject to a 40% federal estate tax (and, potentially, an additional state estate tax in several states).²

What basic documents should the founder have in place?

Estate planning involves more than simply planning around one's demise. It may also involve the efficient transfer of assets during one's lifetime, the delegation of financial authority during a period of incapacity, or the authorization of a specific medical procedure when death appears imminent. Estate

planning should be comprehensive, yet customized. The core documents typically include:

Will—A will is a legal document in which an individual nominates a personal representative to administer their probate estate, designates a guardian for minor children and outlines how the probate estate should be distributed. To die without a will is to die intestate. If this occurs, the probate court will determine who should care for the individual's minor children, and assets will pass according to state intestacy laws; this may or may not be consistent with the individual's wishes. Additionally, a will can include provisions that create certain types of trusts (e.g., credit shelter trusts and marital trusts) upon the individual's death. Depending on the circumstances, these trusts may provide several benefits such as estate tax reduction, asset protection and additional control over future distributions.

²Under the tax law passed on July 4, 2025, the lifetime gift and estate tax exemption has been adjusted to \$15 million per person (\$30 million for a married couple) beginning in 2026 and it will adjust annually with inflation thereafter.

Revocable Living Trust—A revocable living trust (or, more simply, revocable trust) is a legal document that functions in much the same way as a will. The grantor (person who creates the trust and sometimes is instead called a trustor, settlor or donor) can appoint a person to administer trust assets and outline how assets are to be distributed upon the grantor’s demise. For this reason, a revocable living trust is often referred to as a “will substitute.” However, unlike a will that must be administered by the probate court, a revocable living trust may enable an estate to avoid the probate process altogether, as well as the time and fees often associated with probate. Since the probate court and any documents filed with it are generally open to the public, those individuals who wish to remain private may consider using a revocable living trust.

Durable financial power of attorney—If an individual becomes ill and incapacitated for a period of time, it is important to have someone (referred to as an agent or attorney-in-fact) authorized to make financial decisions on their behalf. A financial durable power of attorney is the legal document that designates an attorney-in-fact to act with respect to non-trust assets.

Medical directive—Advance medical directives provide a plan for medical treatment in advance. Through the use of directives, specific medical procedures may be approved or individuals appointed to make decisions if the principal is incapable. Advance directives may include a living will, health care power of attorney and do not resuscitate orders.

Health Insurance Portability and Accountability Act (HIPAA) Release—This form allows a physician to discuss the details of the individual’s medical condition with someone else (i.e., someone not directly involved in the individual’s medical treatment) without violating the HIPAA privacy rules that were put in place to protect health information.

Insurance considerations

As noted above, a basic estate plan contains the core set of documents that would protect a founder’s interests if something were to happen unexpectedly. In addition to protecting the founder’s current assets, it is important to consider protecting their human capital (i.e., the capacity to earn assets in the future). Insurance is often used to shift this risk from an individual or family to an insurance company.

Disability insurance helps protect against unexpected illness or accident. Individual disability income insurance, also known as income protection, can provide stand-alone or supplemental coverage to what may be provided through employment if an unexpected injury or illness occurs that prevents the insured from working for a period of time.



Life insurance helps protect against an unexpected death. Term life insurance is the least expensive solution and sometimes policies with different lapsing dates are purchased to protect more in the early years and less later on. As an example, a five-year, 10-year and 15-year policy each with a \$5 million death benefit may be purchased, with the assumption being that lower death benefits would be needed the longer the founder lives and continues working. Term insurance is also used to satisfy any buy-sell agreements created among business partners and (depending on the type of agreement) the business itself. It provides a mechanism to buy out the insured's interest and provide

liquidity to the insured's family. For example, multiple partners enter into a cross-purchase agreement by buying insurance on each other's lives. If one partner died, their partner, as a beneficiary of the policy, would receive the death benefit to buy out the deceased partner's interest, thereby providing liquidity to the family and maximizing business continuity. Permanent life insurance is typically used to provide for potential estate taxes. These policies are usually owned in irrevocable life insurance trusts, which are trusts designed to hold life insurance policies and keep the death benefit outside of the insured's taxable estate.

Making the most of the fruits of your labor

UBS Wealth Way can help organize the proceeds of an IPO or a partial to full sale to a strategic partner.

Brian Formento

Head, Client Solutions and Investment Strategy
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For many start-up founders following an IPO or a partial to full sale to strategic partner, initial considerations will include how to best replace their income and determine whether or not they will have enough money to meet all of their spending needs going forward. A good amount of this thinking should be done during the financial planning stage, where hopefully a start-up founder has reflected on their short- and long-term goals. These goals can be incorporated into the asset allocation phase of constructing a portfolio with a stated return objective that provides a high probability of success of reaching those goals. UBS Wealth Way is a comprehensive approach to wealth management, which aids financial advisors and clients in the financial planning process. It is designed to put business, investments, passion and family goals front and center when constructing a plan. Using the UBS Wealth Way approach,¹ your UBS Private Wealth Advisor starts with questions that focus on what's most important to you. Your answers shape three key strategies to help organize your financial life:

Liquidity: To help provide cash flow for short-term expenses

Longevity: For longer-term needs

Legacy: For needs that go beyond your own.

This distinctive approach, which is not a financial plan in and of itself, leverages our framework of Liquidity. Longevity. Legacy. to help focus on what's really important to you. This provides a blueprint for an individual or family that wants to understand how they can appropriately allocate all of their assets and structure liabilities to meet their personal objectives.

Whether using the UBS Wealth Way approach in comprehensive financial planning or separately to invest, UBS Wealth Way focuses on initially grouping assets in such a way as to help accomplish the family's objectives through all market cycles. At its core, this is a framework of interaction between performance-seeking and liability-hedging portfolios that allows for a deeper understanding of the role that each portfolio component plays relative to short- and long-term needs.

With your UBS Private Wealth Advisor, you can map out a comprehensive range of solutions addressing both sides of your balance sheet to help you pursue your goals at every phase of your life.

¹ UBS Wealth Way is an approach incorporating Liquidity. Longevity. Legacy. strategies that UBS Financial Services Inc. and our Financial Advisors can use to assist clients in exploring and pursuing their wealth management needs and goals over different time frames. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved. All investments involve risk of loss, including the risk of loss of the entire investment. Time frames may vary. Strategies are subject to individual client goals, objectives and suitability.



UBS Wealth Way starts with questions and a conversation about what's most important to you. Then, your UBS Private Wealth Advisor can help you organize your financial life into three key strategies, based on the specific time frames of your needs and goals.

It is designed to provide clarity for all financial decisions embedded in the client's specific goals and objectives. It can also help to provide a bulwark against the behavioral mistakes that investors may be prone to making, and reduce inherent investment biases. Evaluating a portfolio on its ability to meet its financial goals can help position investors to set realistic expectations and incorporate rational decision-making. Knowing that near-term expenditures are conservatively segmented may help investors to maintain a long-term view, and may provide some comfort when markets perform poorly.

The three strategies combined will comprise your total portfolio. With your UBS Private Wealth Advisor, you can map out a comprehensive range of solutions addressing both sides of your balance sheet to help you pursue your goals at every phase of your life. However, each strategy should also be viewed

across the entire planning spectrum, including risk management, income tax planning, charitable planning and estate planning. At the end of the day, whether your primary investment objective is to protect or grow your wealth, having an understanding of your objectives, investment time horizon and risk tolerance is crucial. Hence, your UBS Private Wealth Advisor can develop custom asset allocations that exhibit different levels of risk in order to offer portfolios fitting different types of clients. Additionally, depending on your circumstances, your UBS Private Wealth Advisor may consult with the UBS Portfolio Advisory Group to assist in building your portfolio. The Portfolio Advisory Group utilizes the due diligence performed by the UBS Investment Manager Analysis team. They consider client objectives, preferences and investment philosophy when selecting from the UBS open architecture platform.

In building your portfolio, your UBS Private Wealth Advisor will discover your goals and determine your risk profile. Your investment goals and wealth planning objectives are integral to identifying an appropriate risk tolerance, investment time horizon and potential liquidity needs. Next, your current holdings can be analyzed by asset class, style, tax status and risk contribution. In this phase, your wealth can be structured to increase after-tax wealth through various account types like taxable accounts, IRAs, donor-advised funds or trusts. When doing so, the focus will be on each investment and its defined purpose within the portfolio, and how it can help meet your key objectives, which can be accomplished through the use of the UBS Wealth Way approach. Third, your UBS Private Wealth Advisor can employ strategic and tactical allocations to seek to enhance returns and/or manage risk. Based on your primary objectives, the strategic asset allocation should be viewed as a long-term investment plan.

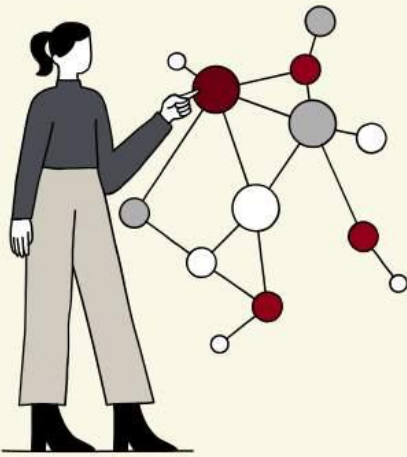
UBS uses strategic asset allocation to help increase potential return, while managing or potentially reducing overall portfolio volatility for long-term investment planning. The UBS Portfolio Advisory Group leverages the UBS Strategic Asset Allocation models, which are optimized baseline portfolios that vary based on risk tolerance. The UBS Portfolio Advisory Group also uses UBS's Tactical Asset Allocation views to seek to take advantage of perceived short-term market opportunities and to improve the risk/return trade-offs. Finally, your UBS Private Wealth Advisor can provide implementation ideas. Based on the analysis, the portfolio will be tailored to meet your goals and objectives. Your UBS Private Wealth Advisor can also review the portfolio with you upon request to help assess if changes are needed. Leveraging the resources of the various UBS research groups, your UBS Private Wealth Advisor can identify non-proprietary and proprietary investments that are appropriately aligned with your investment objectives. Asset allocation does not assure profit or guarantee against loss in declining markets.

Three key strategies

Liquidity: Assets and resources in the Liquidity strategy are allocated to match expenditures in order to provide stable cash flow for short-term expenses, typically the next three years. These assets will typically be used to help maintain your lifestyle and may include entertainment and travel, taxes or purchasing a new home.

Longevity: The Longevity strategy is sized to include all of the assets and resources the family plans to utilize for longer-term expenses, with a time frame generally of four years through the end of life. The Longevity strategy will cover items such as retirement, health care and long-term care expenses, as well as purchasing a second home. A portfolio can be constructed with that goal in mind—a well-diversified portfolio, but with an eye to inflation and managing downside risk.

Legacy: The Legacy strategy is comprised of assets that are to be used for needs beyond your own. The Legacy strategy helps clarify how much a family can do to improve the lives of others—either now or in the future, through making gifts to loved ones or charitable giving. Investment portfolios in the Legacy strategy may be invested fairly aggressively since the time horizon associated with the portfolio can usually be measured in decades.



Full-spectrum wealth management

Our approach to wealth management integrates robust solutions across all aspects of your financial life.

Investment planning	Estate planning	Tax planning	Charitable planning
Cash and short-term high-quality fixed income	Fund revocable trust to help avoid probate	Optimal mix of taxable and tax-free bonds based on marginal income tax rate	Cash and short-term high-quality fixed income
Help provide funding for capital calls	Efficient post-death management structures	Cash contributions to charity	Help provide funding for capital calls
Diversified portfolio tied to risk tolerance and spending goals	Fund revocable trust to help avoid probate	Asset location	Diversified portfolio tied to risk tolerance and spending goals
Illiquid investments	Efficient post-death management structures	Retirement plan contributions	Routine gifts of appreciated property to charity
Long time horizon	Illiquid investments	Tax-efficient investments in taxable accounts	Charitable remainder trusts
May consider risk profile of beneficiaries	Long time horizon	Capital loss harvesting	
	May consider risk profile of beneficiaries	Tax-efficient stock option exercise strategies	
		QSBS	
		ING trusts	
		Charitable remainder trusts	
		Grantor trusts	
		Roth IRA conversions	
		Contributions of qualified appreciated property to charity (pre-liquidity or post-liquidity)	

For illustrative purposes only.

Wealth transfer strategies

Once the basic estate plan has been implemented, the conversation shifts toward opportunities for planning in advance of the liquidity event that will maximize estate tax efficiencies through making gifts to family. These discussions should begin as early in the process as possible to allow sufficient time to stress-test the results in a financial plan, to work with corporate counsel regarding assignability, to re-title assets between spouses (if necessary), and to work with tax and legal advisors to put the proper structures in place.

Gifts to family

Only freely transferrable shares, vested restricted stock and vested NSOs can be gifted to the family. Vested restricted stock, assuming a low qualified appraisal value and appreciation potential, can be an excellent asset to give to family. If the stock is expected to appreciate significantly, none of the appreciation will be included in the founder's estate (only the gift value). Valuation discounts for minority interests when making gifts to family can help reduce the gift's value significantly. Therefore, assuming a 30% discount were applied by a qualified appraiser, a gift of one dollar of restricted stock would only use 70 cents of gift tax value, thereby allowing the founder

to leverage their \$19,000 annual exclusion gifts, their \$15 million lifetime exemption and their \$15 million generation-skipping-transfer (GST) tax exemption.³ (These are the amounts that apply in 2026.) Gifts to family of freely transferrable, vested NSOs can also be attractive, but the founder needs to understand that the income tax liability on the NSOs doesn't transfer to the beneficiary or to the trust for the benefit of the beneficiary. If the founder gifts NSOs, they will still be liable for the income taxes payable on the subsequent exercise of the NSOs. This may actually be an advantage because the tax payment reduces the founder's estate without incurring additional gift taxes.

³ See footnote 2.

Tools for making gifts

Annual exclusion gifts

Federal law allows each individual to transfer up to \$19,000 annually (in 2026 and indexed for inflation) to anyone without eroding that individual's lifetime exemption (discussed below).⁴ A married couple may, potentially, transfer up to \$38,000 to any individual.

Lifetime exemption

Any interests transferred to family members that don't qualify for the annual exclusion (for example, if the gift is over \$19,000 per recipient or, if made by a married couple, potentially \$38,000 per recipient) would use the founder's lifetime exemption. The amount of this exemption is \$15 million.⁵ The gift and estate tax exemption amounts are unified. Simply put, the gift tax exemption is used during life and the estate tax exemption is used at death. That means that the founder can:

1. Give everything away during life, leaving no estate tax exemption;
2. Give away a portion during life, leaving the remaining exemption available to use at death; or
3. Give none away during life, leaving the entire exemption available at death.

Any amounts in excess of the exemption are generally taxed at a flat 40% at the federal level (unless such transfer qualifies for the marital deduction or the charitable deduction). Many states have their own estate taxes that are in addition to the federal estate tax (but are deductible against the federal taxable estate). Connecticut is the only state that levies a state-level gift tax.

Generation-skipping transfer (GST) tax exemption

While the lifetime exemption applies to the founder's assets that are given during lifetime or at death, the GST tax exemption is typically used to avoid tax on the founder's children's or grandchildren's deaths. To understand the GST tax exemption, it's important to provide some context. Soon after the federal estate tax was enacted in 1916, attorneys for wealthy families found that there was a gaping loophole.

The estate tax applies to everything an individual owns at death. What if a wealthy parent paid estate tax at their death and left their child's inheritance in a lifetime trust for the child's benefit, and when the child died, the assets continued in trust for their children? The trust's assets weren't included in the child's estate, because they didn't own them, even though they could benefit from them. The assets were owned by an irrevocable trust that continued at their death for the benefit of their children.

⁴ Treas. Reg. § 25.2503-3(b).

⁵ See footnote 2. See also IRC § 2010.

In 1986, Congress enacted the GST tax to close this and other end-runs around the estate tax. Basically, the GST tax states that the lifetime trust will be subject to a 40% tax (same as the estate tax at the child's death). But, because Congress gives an exemption from the estate tax, it's only fair that it gives an exemption from the GST tax as well. The amount of the GST tax exemption is also currently \$15 million, exactly the same amount as the lifetime exemption.⁶ It's a second exemption that can be layered on top of the lifetime exemption. For example, the founder could transfer shares to an irrevocable lifetime trust for

the benefit of their children in the amount of \$15 million. The taxpayer would file a federal gift tax return (Form 709) and elect to allocate the GST tax exemption to the trust in the same amount. There are also rules that will automatically allocate the GST exemption to trusts if the trust agreement contains certain provisions. The result would be that the trust would be exempt from the GST tax, no matter how significantly the trust assets appreciate, for as long as state law allows the trust to continue (essentially 90 to 100 years in 15 states, several hundred to 1,000 years in 11 states and perpetually in 24 states).

⁶ Like the gift and estate tax exemption, the GST tax exemption is indexed annually for inflation. Under the tax law passed on July 4, 2025, this has been permanently adjusted to \$15 million per person (\$30 million for a married couple) beginning in 2026, and it will adjust annually with inflation thereafter.



Tax goals of gifting to family

The goals for tax-efficient wealth transfer are threefold: removing value, freezing value and locking in the higher exemption values.

Removing value

Removing value from the transfer tax system is difficult to do when transferring the shares of a closely held business. In most cases, if an individual makes a lifetime gift, that gift (valued as of the date of the gift) is technically included in determining the value of the estate at death for estate tax purposes. The lifetime exemption is then used to reduce the size of the taxable estate. However, there are three exceptions to this general rule.

First, if the founder makes a gift using their \$19,000 annual gift tax exclusion, the gift is completely removed from the taxable estate. Second, if the founder transfers shares representing a minority interest in the business, they may be entitled to valuation discounts (ideally) substantiated by a qualified appraisal for lack of control and lack of marketability, among other factors. These discounts may sometimes exceed 30% depending on facts and circumstances, effectively removing that amount from the taxable estate, as long as the transfer or the valuation discount is not challenged by the IRS upon audit. Third, if the shares are transferred to an irrevocable trust that will not be included in the founder's gross estate, the trust can be drafted so that the grantor can pay the trust's income taxes during their lifetime, as opposed to having the trust be its own separate taxpayer. This effectively reduces the founder's taxable estate by the taxes paid on behalf of the trust, without them being considered a gift. This is known as a "grantor trust," and this technique is highly effective in removing value from the founder's taxable estate. While grantor trust status is typically preferred, in the context of establishing irrevocable trusts to leverage additional QSBS exemptions, those trusts would need to be structured as non-grantor trusts, whereby the QSBS trust would be treated as a separate taxpayer for income tax purposes. For more information, see the chapter entitled "Income tax planning prior to the sale."

Freezing value

Freezing value involves the founder making a gift (outright or in trust) using some or all of their gift tax exemption. On the owner's death, the amount of exemption used to make the gift is brought back into the estate for purposes of calculating their estate tax, as described above. Any appreciation on the gift from the date of the gift until the founder's death is excluded from the taxable estate. That is to say that the founder succeeds in "freezing" the value of the gifted property for estate tax purposes at its date-of-gift value, rather than at its date-of-death value.

Wealth transfer techniques

When a founder considers making gifts to family in advance of a liquidity event, there's an alphabet soup of gifting techniques that can be considered, which can easily become overwhelming. Gifts to family in advance of the liquidity event may include outright gifts, gifts to irrevocable trusts and grantor retained annuity trusts (GRATs).

Outright gifts

Outright gifts of shares or interests in a limited liability company or limited partnership are quite easy. A founder generally should obtain a qualified appraisal for purposes of determining the fair market value of those shares or interests. If the founder gifts a minority interest, the fair market value typically reflects valuation discounts. The risks of outright gifts occur after the sale, when the recipient receives cash for the interests. Is the recipient mature enough to handle the money responsibly? Will having the cash outright act as a disincentive to leading a productive life? Will the assets be available to a divorcing spouse? If these and other issues related to an outright gift are a concern and the values are large enough, it may make more sense to hold the assets in an irrevocable

trust for the beneficiary (and the beneficiary's descendants). While large outright gifts to family members are generally frowned upon, there are times when they may be appropriate in order to provide additional QSBS exemptions.

Gifts to irrevocable trusts

These gifts have many advantages. Trusts can be created to protect the trust assets from the beneficiary themselves, from divorcing spouses and from the beneficiary's creditors. If GST tax exemption is allocated to the trust, the trust's assets typically won't be subject to any GST taxes. Finally, if the trust is drafted to be a grantor trust for income tax purposes (as described above), the grantor can continue to pay the income taxes on behalf of the trust (effectively allowing the trust to compound income tax free). If, however, the trusts are set up to take advantage of additional QSBS exemptions, the trusts would need to be established as non-grantor trusts for income tax purposes.

An irrevocable trust can be created for any loved one. For example, a trust can be created by one spouse for the benefit of the other and any joint descendants, known as a spousal lifetime access trust (SLAT). Typically, the spouse is the

primary beneficiary, and the descendants are secondary beneficiaries or even remainder beneficiaries (meaning they may only use trust assets after the death of the beneficiary-spouse). To avoid an argument that the trust should be included in the grantor-spouse's estate for estate tax purposes, the grantor must not have any legal rights to the assets held in the trust, nor can there be any pre-arrangement or understanding between the grantor and the spouse, or the grantor or trustee, that the grantor might use the assets in the trust. Moreover, there are additional considerations for those individuals who live in community property states, and community assets may need to be partitioned prior to transfer to this type of trust.

Nonetheless, if the grantor is in a happy marriage, it can be comforting to know that their spouse will have access to the property in the trust (unless they get divorced or the beneficiary spouse predeceases the grantor). It should be noted that each spouse can establish a SLAT for the benefit of the other spouse, but the terms of the two trusts can't be identical. If they are, the IRS can disregard the trusts and bring the assets back into each grantor's taxable estate under the reciprocal trust doctrine.

A trust may also be created for children, grandchildren and more remote descendants—typically referred to as a “descendant's trust.” Such a trust merely excludes the spouse as a beneficiary. One potential drawback of a descendant's trust versus a SLAT is that the children are the primary beneficiaries and, in most states, have a right to know about the trust at a certain age and, depending on distribution standards in the trust, can make demands on the trustee for distributions. This may fly in the face of the founder's intention to not have young adult beneficiaries know that they have money before they've established themselves as responsible adults.

GRATs and sales to grantor trusts are advanced gifting techniques that do not use up any lifetime exemption. These strategies can be very valuable for moving significant assets without any gift/estate tax. For further information on these techniques, see David T. Leibell, *Planning for the sale of a closely held business* (a publication of the UBS Advanced Planning Group).



Checklist for preparing for an initial public offering (IPO)

Doug Monaster

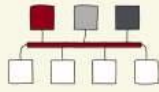
Product Specialist, OneBank Coverage



As you approach the next stage of your business and look toward an IPO, there are a number of considerations that help to ensure that your company is on the right trajectory. Proper planning around strategy, corporate structure and other key elements can help make sure that the IPO process begins smoothly and that your execution timeline stays on track. It's important to think through these items well ahead of an IPO to best position the company for success.

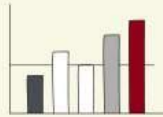


Pre-IPO preparation



Management

- Make sure there is management depth below the chief executive officer and chief financial officer
 - Additions to the finance department
 - Investor relations leadership
-



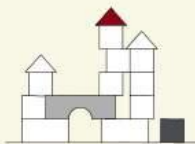
Financial and accounting considerations

- Audited financials
 - Key financial reporting metrics
 - Have appropriate controls in order
 - Sarbanes-Oxley compliance
 - Considerations around audit firm (typically “Big 4”)
-



Financial projections/strategy planning

- Corporate strategy and the business plan should be reviewed, developed and implemented with the IPO in mind
 - Quarterly and five-year annual financial projections are best practice
 - Determining reporting and modeling metrics will be key
 - Highlight key drivers of the business
-



Corporate structure and tax

- Suitability of current organizational structure
 - Tax structure and implications
 - Potential dual class share structure (if desired)
 - Determination of domicile
-



Corporate governance

- Determine composition of board of directors
- Search for independent directors
- Board committees (audit, nomination and compensation)

Income tax planning prior to the sale

Many start-up founders structure the business as a subchapter C corporation in order to obtain certain tax benefits, such as QSBS tax treatment (as described below). The QSBS qualification makes the company an attractive investment for venture capitalists and other investors.

General benefits of qualified small business stock

Upon the sale of QSBS issued prior to July 5, 2025, an eligible QSBS shareholder may exclude from income the greater of \$10 million of gain (\$5 million for married taxpayers filing separately) or the amount of gain equal to 10 times the shareholder's cost basis in the shares.⁷ For QSBS issued after September 27, 2010, but prior to July 5, 2025, the portion of the eligible gain that may be excluded is 100% if held for more than 5 years.⁸ QSBS issued prior to September 28, 2010 may be excluded at a rate of 75% or less, depending on the date of issuance of the shares.⁹

For QSBS issued on or after July 5, 2025, an eligible QSBS shareholder may exclude from income the greater of \$15 million of gain (\$7.5 million for married taxpayers filing separately), to be adjusted for inflation after 2026, or the amount of gain equal to 10 times the shareholder's cost basis in the shares.¹⁰ The portion of the eligible gain that may be excluded is 50% if held for at least 3 years, 75% if held for at least 4 years, or 100% if held for at least 5 years.^{11, 12}

The amount of QSBS gain that a taxpayer may exclude from gross income is determined on a per shareholder and per issuer basis.¹³ This means that with respect to each corporation that issues QSBS, each QSBS shareholder of such corporation is entitled to one exclusion, but if the shareholder owns QSBS issued by a separate corporation, the shareholder should be entitled to a separate exclusion amount with respect to the QSBS issued by such other corporation.¹⁴

The foregoing relates strictly to the exclusion amount for purposes of federal income tax. At the state level, each state determines its own treatment for state income tax purposes of the sale or exchange of QSBS.¹⁵ For example, New York generally follows the federal treatment of QSBS, while California does not.¹⁶ Each relevant state should be considered individually as it relates to planning for QSBS purposes at the state income tax level.

In order to qualify for the QSBS exclusion, there are two sets of requirements that need to be satisfied, one at the shareholder level and one at the corporate level.

⁷ IRC § 1202(b) (1), (3)(A)(i) and (4)(A).

⁸ IRC § 1202(a)(4).

⁹ IRC § 1202(a)(1) and (3).

¹⁰ IRC § 1202(b)(1), (3)(A)(ii) and (5).

¹¹ IRC § 1202(a)(5).

¹² In summary, the gain exclusion percentage is determined as follows:

- 100% for QSB stock acquired after July 4, 2025, and held for at least five years;
- 75% for QSB stock acquired after July 4, 2025, and held for at least four years;
- 50% for QSB stock acquired after July 4, 2025, and held for at least three years;
- 100% for QSB stock acquired after September 27, 2010, and on or before July 4, 2025, and held for more than five years;
- 75% for QSB stock acquired after February 17, 2009, and before September 28, 2010; and
- 50% for QSB stock acquired on or before February 17, 2009.

Polito, 760-4th T.M., *Small Business Corporation Stock: Special Tax Incentives*.

¹³ IRC § 1202(b).

¹⁴ Id.

¹⁵ IRC § 1202(a).

¹⁶ See Cal. Rev & Tax Code § 18152 and NY Tax § 612.

The shareholder level requirements

The shareholder must acquire the stock in a corporation that qualifies for QSBS, at original issuance, in exchange for money or property or as compensation for services rendered.¹⁷ The shareholder may be an individual, a trust, S corporation or a partnership, but not a C corporation. (See below for further rules applicable to QSBS owned through a partnership.) For QSBS issued prior to July 5, 2025, the shareholder must hold it for a minimum of five years.¹⁸ For QSBS issued on or after July 5, 2025, the shareholder must hold it for a minimum of three years to obtain a 50% exclusion; four years to obtain a 75% exclusion; and 5 years to obtain a 100% exclusion.¹⁹ A shareholder who obtains stock that qualifies for QSBS treatment should carefully consider any potential tax implications of making any transfers of the stock, even transfers that would otherwise be tax-free transactions, in order to either take advantage of the QSBS exclusion as part of the transaction or preserve it for future use.

The corporate level requirements

The corporation must meet the QSBS requirements at the time the stock is issued. QSBS is stock in a domestic C corporation that operates an active trade or business. For QSBS issued prior to July 5, 2025, the gross assets of the corporation, and any predecessor entity if applicable, cannot have ever exceeded \$50 million prior to the issuance of the stock or immediately thereafter.²⁰ For QSBS issued on or after July 5, 2025, the gross assets of the corporation, and any predecessor entity if applicable, cannot have ever exceeded \$75 million, (to be adjusted for inflation after 2026) both prior to and immediately after the issuance of the stock.²¹ The corporation must also use at least 80% of its assets (determined by value) in the conduct of a qualifying trade or business, or in start-up activities to establish the qualifying trade or business.²² A qualifying trade or business is defined broadly to include any business other than:

- a business involving the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services or brokerage services;
- any trade or business where the principal asset of such business is the reputation or skill of one or more employees;
- a banking, insurance, leasing, real estate, investing or other similar business;
- farming;
- any mineral extraction business; and
- any hotel, motel, restaurant or similar business.²³

The IRS has issued rulings regarding some businesses that had a tangential relationship to some of the excluded businesses noted above, and found that they were not excluded from QSBS treatment.²⁴ As a result, it is possible that a business will be treated as qualifying for QSBS despite being in a related industry.

¹⁷ IRC § 1202(a)(1).

¹⁸ *Id.*

¹⁹ IRC § 1202(a)(1) and (5).

²⁰ IRC § 1202(d).

²¹ IRC § 1202(b)(4) and (d).

²² IRC § 1202(e).

²³ IRC § 1202(e)(3)(A).

²⁴ See, e.g., PLR 202114002 (relating to a financial technology business), and PLRs 201436001 and 201717010 (relating to medical testing and pharmaceutical development businesses).



The issuing corporation must satisfy the qualification tests at the time the stock in question is issued, and must meet the requirement to conduct a qualifying trade or business during substantially all of the shareholder's holding period.²⁵ There are also anti-abuse rules relating to certain redemptions of stock within certain time periods from when such stock was issued that may disqualify certain stock from qualifying as QSBS.²⁶

If the corporation satisfies these requirements, and the shareholder meets the shareholder level requirements, then the stock should qualify for the QSBS exclusion when the shareholder sells it.

Ownership of QSBS through a pass-through entity

Ownership of QSBS through a pass-through entity such as a subchapter S corporation or an entity treated as a partnership for tax purposes (a "pass-through") in a manner that will provide exclusion of gain to the pass-through owner is narrowly

circumscribed by the statute.²⁷

A pass-through owner that is an eligible QSBS shareholder (i.e., an individual, a trust or an estate) should be allowed an exclusion with respect to their allocable share of the pass-through's gain from its sale of QSBS, provided the stock that meets all the requirements of QSBS in the hands of the pass-through, and that the pass-through has held such QSBS for more than five years (or at least three years with respect to QSBS acquired by the partnership on or after July 5, 2025).²⁸

In addition, in order for the gain to be excluded from the pass-through owner's income, the pass-through owner must have continuously held an interest in the pass-through for the entire holding period during which the pass-through held the QSBS, and the excludible portion allocated to the pass-through owner is limited to the interest in the pass-through the owner held on the date the pass-through acquired the QSBS.²⁹ The statute also provides that an entity taxed as a partnership

²⁵ IRC § 1202(c)(1)-(2).

²⁶ IRC § 1202(c)(3)(A)-(C).

²⁷ IRC § 1202(g).

²⁸ *Id.*

²⁹ IRC § 1202(g)(2)(B) and (3).

may distribute QSBS to the partners, which would allow the QSBS to retain its eligibility in the hands of the partners individually, provided that at the time of the distribution all of the foregoing requirements relative to the partner being able to exclude gain on the sale of QSBS by the partnership were satisfied, without regard to the five-year holding period (or the three-year holding period in the case of QSBS acquired by the partnership on or after July 5, 2025).³⁰ The statute does not provide for the same distribution rule for subchapter S corporations.³¹ Given that the statute explicitly provides for transfers that retain QSBS eligibility in the hands of the transferee, it seems that other transfers—notwithstanding that they may not be recognition events for income tax purposes (such as, for example, a contribution of QSBS to a partnership)—may forfeit the QSBS eligibility in the hands of the transferee.

When a corporation converts from an LLC or merges with another corporation

The benefits of treatment as QSBS may be preserved in certain tax-free reorganizations and tax-deferred exchanges.³² For example, QSBS may be preserved in certain tax-deferred reorganizations under Section 368(a) of the Internal Revenue Code in which a QSBS shareholder exchanges shares in a corporation in exchange for shares in a new corporation. If at the time of the transaction the new corporation qualifies for QSBS, the stock issued should entirely qualify for such treatment. If at the time of the transaction the new corporation is not eligible to issue QSBS, then QSBS treatment, if available at all, may be limited to the amount of gain that exists in the QSBS at the time of the exchange. If the transaction does qualify, the holding period for stock in the new corporation should be measured from the date of issuance of the stock in the old corporation.

If a business is initially formed as a limited liability company (LLC) and is then converted to a corporation, it may qualify for QSBS treatment provided that the corporation satisfies the corporate-level requirements at the time of conversion.³³

Preserving QSBS status through transfers of stock

The statute provides certain exceptions to the original issuance requirement noted above, and certain transferees of QSBS that receive QSBS in transactions noted in the statute are deemed to have satisfied the original issuance requirement and are deemed to have held the QSBS during the holding period of the transferor.³⁴ The exceptions are: for (1) transfers by gift; (2) transfers at death; and (3) distributions from a partnership to a partner.³⁵ The specific requirements for the partnership distribution exception are discussed above.

³⁰ IRC § 1202 (g)(2)(A) and (h)(2)(C).

³¹ IRC § 1202(h).

³² IRC § 1202(h)(4)(A), referring to tax free transactions under IRC §§ 368 and 351.

³³ IRC § 1202(h)(4).

³⁴ IRC § 1202(h)(1).

³⁵ IRC § 1202(h)(2).



Stacking to obtain multiple QSBS exclusions

If a shareholder owns QSBS with gain that exceeds the maximum gain that one shareholder can exclude, there are some strategies that may allow for persons or entities related to the shareholder to obtain additional exclusions, sometimes called “stacking.” The key to each strategy is to transfer shares in a way that maintains the QSBS qualification to a person or entity that is treated as a separate taxpayer. If properly structured, that separate taxpayer may qualify for its own exemption. Use of one or more non-grantor trusts can, if properly formed, allow the shareholder to obtain additional exemptions.

For example, a married founder who has substantial QSBS holdings may consider establishing a trust or trusts for the benefit of the founder’s spouse and children.³⁶ The spouse can be a beneficiary, but for the trust to be treated as a non-grantor trust (i.e., a separate taxpayer from the grantor for income tax purposes), distributions to the spouse would

need to be subject to the approval of another beneficiary.³⁷ If properly drafted, these trusts can be used to achieve both an additional QSBS exclusion and also help with estate planning goals.

Another trust structure that may facilitate stacking is the incomplete non-grantor (ING) trust. An ING trust is structured so that transfers to the trust are not considered completed gifts for gift tax purposes, and the trust is treated as a non-grantor trust. In order to be treated as a non-grantor trust, the trust typically is designed so that a distribution committee made up of trust beneficiaries must approve distributions from the trust to the grantor or the grantor’s spouse. In general, this means that an ING trust is more complicated to establish and administer. However, ING trusts can be useful tools to maximize the income tax efficiency of a liquidity event involving QSBS.

There is, potentially, a significant additional benefit to an ING trust in that a properly drafted ING trust may (depending on the law in the taxpayer’s state of residence) avoid

³⁶ This structure is often called a spousal lifetime access non-grantor trust (SLANT).

³⁷ IRC § 677(a)(2).

income tax at the state level, through using a trust in a state other than the state of the taxpayer's residence. This can be particularly powerful if the taxpayer lives in a state that does not follow the federal income tax treatment of QSBS (i.e., they don't allow an exclusion from state income tax).³⁸ Two states have changed their tax law to ensure the ING trust is taxable at the state level and some states tax any non-grantor trust of which a resident is a grantor, meaning that the state level benefit will not be available to all taxpayers.³⁹ A properly drafted ING trust should, however, qualify for an additional QSBS exclusion at the federal level.

Special considerations for sales to private equity, special purpose acquisition companies and other buyers

In any liquidity event, one important consideration is how to obtain the maximum benefit from QSBS holdings. If the founder plans to retain significant equity and that equity will continue to be eligible for QSBS treatment, then planning for things such as stacking can sometimes be deferred. In recent years, a growing number of companies have been sold to special purpose acquisition companies (SPACs). In a SPAC sale, it is not unusual for founders to retain equity and QSBS qualification by virtue of a tax-deferred exchange, whereby the equity retained by the seller continues to qualify for QSBS treatment (subject, as discussed above, to the extent of the value of the QSBS gain at the time of the exchange). If retaining QSBS status is important, however, it should be planned from the outset, as the structure used in the acquisition would need to be specifically designed to accommodate future QSBS qualification of the equity received in the deal. For instance, in acquisitions by private equity buyers, founders are often left with substantial equity that does not qualify for QSBS. This happens because many private equity deals involve the founder receiving equity in a new entity, often a partnership, that does not qualify for QSBS itself. As a result, when any liquidity event is anticipated, it is highly beneficial to plan well in advance so as to maximize the benefit of QSBS (including stacking) that can be obtained in the initial liquidity event or retain QSBS qualification, if possible, for future use.

Hedging transactions can spoil QSBS eligibility

Having experienced sometimes dramatic increases in the value of their QSBS, some shareholders ask about trading strategies for protecting the stock's gains against a decline in value. For QSBS, however, hedging transactions—such as buying a put, writing a call or establishing a collar—can be fatal to the tax benefits that the stock offers.

³⁸ E.g., California.

³⁹ E.g., California and New York. See Cal. Rev. & Tax Code § 17082 and NY Tax Law § 612(b)(41).



For some directors and officers, hedging isn't feasible. Public companies generally prohibit their directors and officers from hedging the company's stock.⁴⁰ These anti-hedging policies likely save some people from stumbling into transactions that jeopardize the shareholders' ability to exclude the gain on the stock's sale. Other people who own QSBS, however, should beware of using hedging transactions.

A shareholder generally loses the exclusion if the shareholder has an offsetting short position with respect to the QSBS.⁴¹ An offsetting short position is a short sale of substantially identical property or an acquisition of an option to sell substantially identical property at a fixed price.⁴² A short sale includes selling the stock for future delivery and writing a call option that the holder is more likely than not to exercise.⁴³ With

the possible exception of writing a call, the degree to which a hedging transaction provides downside protection is irrelevant. The IRS hasn't published any guidance on what qualifies as substantially identical property, but it may have the same meaning as the term has for purposes of the short sale rule and as the term "substantially identical stock or securities" has for purposes of the wash-sale rule.⁴⁴

A shareholder can preserve the exclusion for the gain from the QSBS only by electing to recognize the gain in the QSBS as if the shareholder sold the stock on the day that the shareholder established the offsetting short position.⁴⁵ The shareholder must have owned the QSBS for more than five years (or at least three years with respect to QSBS acquired on or after July 5, 2025) before establishing the offsetting short position.⁴⁶ If, on the day that the shareholder establishes

⁴⁰ See *The ClearBridge 100 Report for Large-Cap Companies: Executive Compensation Policies*, ClearBridge Compensation Group, November 2020.

⁴¹ IRC § 1202(j)(1).

⁴² IRC §§ 1202(j)(2)(A) and (B). An offsetting short position also includes any other transaction that, in its regulation, the IRS identifies as substantially reducing the risk of loss from holding QSBS stock. IRC §§ 1202(j)(2)(C). So far, the IRS has not adopted any regulations identifying additional types of offsetting short positions.

⁴³ H. Rept. 103-213 (1993), Title XIII, I.B.2.

⁴⁴ The statute governing short sales uses the term "substantially identical property." IRC § 1233. For purposes of the short sale rule, the regulations state that "substantially identical property" is synonymous with "substantially identical stock or securities" as that term is used for purposes of the wash-sale rule. Treas. Reg. § 1.1233-1(d)(1). The statutes governing conversion transactions and constructive sales also use the term "substantially identical property." IRC §§ 1258 and 1259.

⁴⁵ IRC § 1202(j)(1).

⁴⁶ IRC § 1202(j)(1)(A).

the offsetting short position, the shareholder hasn't met the applicable holding period, then the shareholder can't make the election, and the shareholder loses the exclusion.⁴⁷ If the shareholder makes the election, the shareholder will recognize the gain in the QSBS as if the shareholder sold the stock for its fair market value on the day that the shareholder established the offsetting short position.⁴⁸ Subject to the limitations on the excludable amount, the gain from this deemed sale would qualify for the exclusion.⁴⁹ Any gain in the stock after the deemed sale would not.

If the shareholder establishes the offsetting short position and makes the election, the shareholder also should consider what the character of any expected gains will be upon the actual sale or disposition of the QSBS in the future. While there is no authority directly on point in the QSBS context, it seems likely that the deemed recognition event caused by the election would cause the holding period of the QSBS to reset. If this were the case, then, to the extent the offsetting short position would prevent the holding period from maturing to long term (by virtue, for example, of the rules governing straddles for tax purposes), the subsequent gain on the actual disposition of the QSBS may be short term and subject to higher tax rates than those applicable to long-term capital gains.⁵⁰

⁴⁷ Id.

⁴⁸ IRC § 1202(j)(1)(B).

⁴⁹ IRC § 1202(j)(1).

⁵⁰ SIRC § 1092(c).



A shareholder also loses the exclusion if a related person has an offsetting short position.⁵¹ A broad array of persons are, potentially, related persons. For example, with respect to an individual shareholder, a related person includes:

- Any parent, grandparent or other ancestor
- Any child, grandchild or other descendant
- Any trust of which the shareholder is a grantor or beneficiary
- Any beneficiary of a trust of which the shareholder is a grantor
- Any partnership of which the shareholder owns 50% of the capital interests or 50% of the profits interests⁵²

Thus, if a shareholder creates an irrevocable non-grantor trust of which the shareholder's children are the beneficiaries (perhaps as part of a stacking strategy), contributes QSBS to the trust and the trustee subsequently buys a put on the stock, the shareholder generally would no longer be able to exclude any of the gain from the sale of the QSBS that the shareholder retained. Under this related person rule, one person can, potentially, spoil a good thing for a lot of people.

Gifts to charity

Some founders may be interested in transferring equity compensation to charity prior to a liquidity event. While the intent is noble, it's not always possible. Equity compensation can be difficult to gift. Often, there are restrictions put in place by the company that prohibit transfers. In addition, the IRS takes the position that the transfer of an unvested NSO isn't a completed gift for gift tax purposes. Most tax professionals apply the same methodology to restricted stock and advise that unvested shares of restricted stock may not be gifted. Stock options generally don't qualify as ISOs if you gift or otherwise transfer them. Therefore, only vested restricted stock and vested NSOs may provide opportunities for gifting to charities.

Charitable gifts of vested restricted stock (not subject to company transfer restrictions) that has been held for more than one year after exercise or after a Section 83(b) election should be considered a long-term capital gain asset and should entitle the donor to a fair market value deduction when contributed to a public charity, including a donor-advised fund. The deduction generally will be limited to 30% of the donor's adjusted gross income (AGI) in the year of the gift,⁵³ with

⁵¹ IRC § 1202(j)(2) flush language.

⁵² See IRC §§ 267(c) and 707(b).

⁵³ The One Big Beautiful Bill Act passed on July 4, 2025 created new itemized deduction limitations effective for tax years ending after December 31, 2025 that may apply to reduce the donor's charitable deduction. First, charitable contributions are only deductible to the extent they exceed 0.5% of the donor's contribution base. Second, if the taxable income of the donor, determined before reduction for itemized deductions, exceeds the dollar amount at which the 37% bracket applies to the donor, the charitable deduction will be further reduced by 2/37 of the lesser of: (1) total itemized deductions, or (2) the portion of taxable income, determined before reduction for itemized deductions, that exceeds the dollar amount at which the 37% bracket applies to the donor.

a five-year carryforward for any unused deduction.⁵⁴ Because the business is closely held, a qualified appraisal will determine fair market value, taking into consideration discounts for lack of marketability and lack of control. These discounts generally range from 15% to 30% or more, which, depending on the extent of the discount, can basically wipe out the income tax benefit of contributing prior to a liquidity event.

Gifts of closely held stock to private foundations are treated less favorably. The deduction is typically limited to the donor's basis.

Charitable gifts of freely transferable vested NSOs typically aren't attractive. When the charity exercises the NSOs, the donor will be taxed on the bargain element at ordinary income rates, and the donor's charitable deduction will be limited to basis, which is typically zero.

Ideally, gifts to family members (noted above) would occur in the previous tax year to the gift made to charity. For gifts to family, donors are seeking low asset valuations, whereas for gifts to charity, donors are seeking high asset valuations in order to maximize the charitable deduction. Gifts made to family and charity in the same tax year may lead to substantially similar values for each gift.

Charitable giving before the sale

Charitable planning in advance of the sale of a closely held business sounds like a great way to minimize income taxes. The founder would, seemingly, donate stock to a charitable organization and receive a full fair market value deduction against their income taxes subject to certain AGI-based percentage limitations. Unfortunately, the reality is not that simple. The success or failure of a gift of closely held stock in advance of the sale of the business depends on the following two factors:

1. The nature of the asset (for example, whether it's a C corporation, an S corporation, an LLC or a partnership); and
2. The type of structure you want to use for the gift (for example, private foundation, donor-advised fund or charitable split-interest trust such as a charitable remainder trust).

Types of entities

Closely held businesses are organized as C corporations, S corporations, partnerships or LLCs. The structure of the business can have a major impact on the viability of a particular charitable gift. A C corporation is initially taxed

⁵⁴ More precisely, the percentage limitation on the deductibility of charitable contributions is based on the donor's contribution base, which is the donor's adjusted gross income calculated without regard to any net operating loss carrybacks.



at the corporate level, which means that the corporation itself realizes the benefit or burden of any tax characteristics of its specific income and loss. If the C corporation pays out dividends to the shareholders, the shareholders are taxed on this amount as a dividend, independent of the tax characteristics of the corporate income. The other entities described above are all pass-through entities, meaning that all income, loss, deductions and credits pass through to the S corporation shareholders, partners or LLC members. Because there is no tax at the entity level, the owners, not the entity, realize the specific tax characteristics.⁵⁵ While flow-through entities are popular structures for closely held businesses, they pose distinct problems in the context of charitable giving. The fact that a C corporation is considered a separate taxpayer makes it the easiest of the closely held structures to give to

charity. Flow-through entities, on the other hand, trigger numerous tax traps. There are detailed and highly technical rules regarding a charitable entity's investments and operations under the Internal Revenue Code. Many of these rules make various charitable contribution options involving closely held business interests difficult, undesirable or impossible. It's important to be aware of these rules. See David T. Leibell and Nicole T. Sebastian, *Charitable giving: the rules of the road* (a publication of the UBS Advanced Planning Group, Family Advisory and Philanthropy, and Family Office Solutions).

Charitable recipients

Founders engaging in philanthropic planning have a range of charitable structures to choose from when considering a charitable gift in advance of the sale of the business.

⁵⁵ An S corporation that previously was a C corporation, however, may be subject to tax at the corporate level.

In addition to outright gifts to traditional public charities (like churches, hospitals and universities), alternatives include private foundations, donor-advised funds and charitable split-interest trusts such as charitable remainder trusts. The choice of strategy may be influenced not only by the type of business entity (discussed above), but also by the specific advantages and considerations of the potential charitable recipients.

Private foundations

A private foundation is a charitable organization to which a donor can make contributions that qualify for income, gift and estate tax charitable deductions. It can be structured either as a trust or a corporation. A private foundation commonly receives its funding from, and is controlled by, one or a few private sources (usually an individual, family or corporation). The principal activity of a private foundation tends to be making grants to public charities and awarding scholarships to individuals (although some private foundations also run charitable programs). The general rule is that a private foundation must expend 5% of its net asset value for charitable purposes annually. Private foundations involve a fair amount of administrative complexity and are subject to burdensome rules, but offer the greatest amount of control of all the charitable vehicles.

If a donor funds a private foundation with cash or qualified appreciated stock (i.e., publicly traded stock), the donor's income tax charitable deduction is based on the full fair market value of the amount contributed; otherwise, the deduction is limited to the lesser of the fair market value or basis. As such, and for other reasons discussed below, lifetime gifts of closely held business interests to a private foundation are not particularly attractive. In addition, a donor may deduct cash gifts to a private foundation only up to 30% of their AGI for the year and 20% for gifts of long-term capital gain property.⁵⁶ Deductions in excess of these AGI-based percentage limitations can be carried forward for five years.

Donor-advised funds

A donor-advised fund acts much like a private foundation and is a much simpler philanthropic option in terms of administration when compared to a private foundation. However, when using a donor-advised fund, the donor loses an element of control. Typically speaking, a donor makes a gift to a sponsoring organization (usually a community foundation or a commercially affiliated charitable organization), which sets aside the gift in a separate account in the donor's name, from which the donor suggests grants—typically to other public charities which the donor wishes to support. The donor doesn't have legal control over grantmaking decisions from the account—the sponsoring organization does, although it generally follows legitimate grant recommendations

⁵⁶ See footnote 53.

made by the donor. Donor-advised funds, at least with respect to the deductibility rules, are more attractive than private foundations. Because the organizations sponsoring donor-advised funds are public charities, charitable contributions of closely held business interests held long term qualify for a full fair market value charitable deduction. As a result of this tax advantage over private foundations, donor-advised funds are increasingly willing to accept contributions of closely held business interests, although because of the tax traps, such gifts may not always be tax-

efficient, and the sponsoring charity would typically look for a way to liquidate the assets in the short term (which should not be a problem if the business is being sold). If a donor funds a donor-advised fund with cash, the donor generally may deduct the gift up to 60% of their AGI for the year. If a donor funds a donor-advised fund with long-term capital gain property (like certain closely held business interests), the donor generally may deduct the gift up to 30% of their AGI for the year. Deductions in excess of these AGI-based percentage limitations can be carried forward for five years.⁵⁷

⁵⁷ See footnote 53.



Charitable remainder trusts

A charitable remainder trust is a type of split-interest trust typically used when a donor wants to make a charitable gift in a tax-efficient manner, but wants to continue to have an income stream from the contributed asset. A charitable remainder trust is an irrevocable trust that provides for the payment of:

1. A specified distribution, at least annually;
2. To one or more individuals;
3. For life or for a term of years (not to exceed 20); and
4. With an irrevocable remainder interest to be paid to charity (a public charity or private foundation) at the end of the charitable remainder trust's term.

A charitable remainder trust is generally tax-exempt. There's typically no capital gain incurred by the donor on the transfer of appreciated property to the trust, or its subsequent sale by the trust. It should be noted that if a charitable remainder trust had any unrelated business taxable income (UBTI) (discussed below), it would pay a 100% excise tax on such income. The donor of a charitable remainder trust is entitled to an income tax charitable deduction equal to the present value of the charity's remaining interest at the end of the charitable remainder trust's term, in some cases limited to basis (including transfers of property that are not cash or publicly traded stock),



if a private foundation is, or can be, named as a remainder beneficiary. If the trust instrument provides that only public charities can be named as remainder organizations, the deduction is based on the present value of the full fair market value of the property contributed to the trust.

The minimum annual payout is 5% (but may be higher in certain circumstances). The payment can be a fixed amount annually (a charitable remainder annuity trust or CRAT) or a percentage of the trust assets calculated annually (a charitable remainder unitrust or CRUT). Although a charitable remainder trust is generally a tax-exempt entity, distributions to the individual beneficiaries are subject to income tax. A charitable remainder trust (and in particular a CRAT because the distributions are fixed) established for a fixed term of years (not to exceed 20 years) and funded with QSBS, may allow the donor to avoid some of the capital gain tax on the annuity or unitrust payments during the trust term. See David T. Leibell and Nicole T. Sebastian, *Charitable giving: the rules of the road* (a publication of the UBS Advanced Planning Group, Family Advisory and Philanthropy, and Family Office Solutions).

Additional income considerations

Structuring the transaction

Structuring the sale of a closely held business in an income tax-efficient manner can have a significant impact on the after-tax proceeds available to the family. Depending upon

whether a business is structured as a C corporation or a flow-through entity such as an S corporation, partnership or an LLC that's taxable as a partnership, the family should consider different tax rates as well as whether taxes will be due at the entity level, individual level or both.

Sales of businesses structured as flow-through entities typically have one level of tax. Proceeds from the sale of the company and its assets flow through to the owner's personal income tax return and are added to other items of personal income. Notably, a flow-through entity affords the owner the opportunity to take advantage of preferential long-term capital gains treatment, with a top federal rate of 20% for certain assets held longer than one year. Additionally, active owners of the business may be able to avoid the 3.8% net investment income tax.

On the other hand, sales of businesses structured as C corporations (or S corporations that converted from a C corporation within the prior five years) may result in two levels of tax if the buyer purchases assets rather than stock of the company. In an asset sale, the first tax is at the corporate level with a maximum rate of 21%. The second tax may be eligible for the long-term capital gains rate of 20% mentioned earlier and generally the 3.8% net investment income tax will also apply; however, the potential for double taxation may cause the owner to pursue a stock sale or other alternative form.

In a stock sale, there is only one tax at the shareholder level and no tax at the corporate level. Because the negative impact of double taxation is avoided, many C corporation owners prefer a stock sale. Sales of C corporation stock generally will be subject to the 3.8% net investment income tax.

In some cases, it may be possible to avoid immediate taxation upon a sale of the company. Income tax on a sale won't apply if it's structured as a tax-free reorganization whereby a portion of the sale price paid is stock of the buyer. In order to qualify, the selling company must be structured as a corporation and at least 40% of the total consideration paid must be in the buyer's corporate stock. Rather than owing tax upon sale of the company, shareholders may defer any tax liability for stock received until that stock is eventually sold. It is important to note that tax will be due on that portion of the sales price paid in cash. Reorganization may also be possible for an LLC that has previously (and not part of the same plan) elected to be treated as a corporation for federal income tax purposes.

Tax can also be deferred in the case of an installment sale. When a buyer pays the purchase price over an extended period of time, the seller can defer income recognition until actual payment is received (along with applicable interest). However, installment sale treatment is not allowed for that portion of the sale that results in ordinary income, such as accounts receivable and inventory. In addition, real estate or equipment subject to depreciation recapture will not be eligible for deferral. Finally, if the deferred portion of the sale price exceeds \$5 million, the seller is required to make interest payments that could offset the benefit of tax deferral.

State tax planning

In addition to federal income tax, many states impose a state income tax on sales of businesses. If the founder changes their residence well in advance of the sale (ideally in a different tax year) to a state with no income tax, there should be no state income tax on the sale, unless it's deemed to be state-sourced income. For additional information, see Catherine McDermott, *Changing State of Residence* (a publication of the UBS Advanced Planning Group).

If a change of residence isn't possible or palatable, another possibility for residents of certain states is an ING set up in a state like Delaware (where the trust is called a DING trust) or Nevada (where the trust is called a NING trust). Such trusts allow individual taxpayers who are residents in certain states with high income taxes (for example, New Jersey) to avoid being taxed on non-source income in such states. Unfortunately, ING trusts are complicated and may not work to avoid state income taxes in all states based on state law (for example, New York, California and Connecticut). For a more in-depth discussion of ING trusts, see Ann Bjerke and Tess Mayo, *ING Trusts* (a publication of the UBS Advanced Planning Group).



Strategies for managing concentration risk

Matt Fleming

Structured Solutions, OTC Equity Solutions Sales



Many liquidity events for start-up founders result in the founder owning a significant amount of stock in a publicly traded company. Whether that path to the public markets comes via a traditional IPO, a direct listing or an acquisition by an already publicly traded company (which may include the use of a SPAC), the founder now has to contend with a whole new set of considerations and how they relate to their personal finances. Your financial advisor can help you to think about the impact a concentrated stock position would have on your investment portfolio, what strategies exist to help address the position, and the various legal, contractual and practical considerations that accompany owning the stock. It is important to note that the strategies available and the associated considerations may change as time passes and as your relationship with the company evolves. For example, a founder who ultimately chooses to leave a company may have more flexibility around the type and timing of strategies available, versus a founder who remains with the company in some capacity.



Lockups

For some period of time following an IPO or an acquisition involving a SPAC (and occasionally following a traditional merger), it is customary for there to be a contractual restriction that prohibits the sale or transfer of any shares, a prohibition known as a lockup. A transfer of shares usually includes pledging the stock (e.g., as collateral for a loan) or using options or other derivatives to reduce the risk of the position (see Risk Management Strategies below). There are generally certain exceptions granted to this limitation, allowing for things like charitable gifting or other estate planning transactions, provided that the party receiving the shares agrees to be bound by the same lockup provisions.

The most typical lockup duration is 180 days from the date of the IPO or merger, but recent years have seen an increase in creativity in the structuring of these agreements. It is now not uncommon to see lockup expirations timed to coincide with company earnings announcements or specific price targets (where, for example, the lockup may expire early if the stock price is above a predetermined level for a specific time period). In the case of many direct listings, an alternative to the traditional IPO process, there may be no lockup period at all.

The existence of a lockup, while limiting the ability to execute transactions, does not preclude you from working with your financial advisor to establish a road map for the future, and most will use this time to lay out the next steps of their financial plan, incorporating real-time information about the stock, its current valuation and what they think the value might be in the future.

Company trading policies

Every public company has a written set of policies that describes the type of transactions that its senior executives and directors can enter into with respect to their stock positions. These company trading policies will tell the executive not just what they can do, but when they can do it. These policies can at times be fairly restrictive, and in many instances—outside of charitable gifts or transfers for estate planning purposes—the only permitted path to liquidity is to sell their stock into the market. Companies will generally designate certain periods of time, called “trading windows,” when executives are able to make these sales.

While selling stock seems relatively straightforward, an executive at a now public company has a number of items to contend with, not least that their role will likely expose them at times to information that is considered both material and non-public. This can complicate efforts to sell stock, since trading while in possession of material non-public information is clearly illegal. Trading windows are established with an eye toward mitigating this problem, as they typically open shortly after the company reports quarterly earnings to the market, and close some time before the next quarter’s end. These are usually periods when executives are least likely to have any material non-public information, as the previous quarter’s earnings release should contain most of this accumulated information.

Rule 10b5-1 trading plans

But what of executives whose position constantly exposes them to material non-public information? Or what if the executive would like to be able to sell stock outside of the narrowly defined trading window? Or what about an executive who would just like to be as careful as

possible when they sell stock? For these executives, adopting a Rule 10b5-1 trading plan may be an appropriate course of action.

The SEC adopted Rule 10b5-1 in August of 2000, both as a way of clarifying what it means to trade on the basis of material non-public information but also to provide investors with certain affirmative defenses against allegations of insider trading. One of the most common affirmative defenses is the use of a pre-existing written plan that complies with the requirements of Rule 10b5-1(c), also known as a 10b5-1 plan. While there are a number of provisions under the rule, a 10b5-1 plan will generally specify a number of shares to sell over a prescribed time period, with the sales executed through a broker that agrees to the plan. The plan must be adopted at a time when the executive does not have material non-public information and would otherwise be able to transact in an open trading window. Once it is put in place, the executive should have no influence over the sales made under the plan; they are essentially on autopilot. A company's trading policy may also have other company specific requirements for 10b5-1 plans that can be discussed with your financial advisor and incorporated into a customized plan tailored to your specific objectives.

Risk management strategies

Beyond just selling stock, there are a number of risk management strategies that holders of concentrated stock positions can consider, many of which involve the use of options. These strategies include hedging transactions, which can protect against a fall in the value of the stock while maintaining some or all of the potential upside in the position. Examples of hedging transactions include purchasing a put option or entering into an equity collar, where a purchased put option is combined with a covered call option to reduce the cost of the protection. Monetization transactions allow an investor access to proceeds today by protecting the position or by enhancing the overall yield on the stock, all with the potential to defer recognition of the embedded gains in the stock. Examples of common monetization transactions include pre-paid variable forwards and covered calls.

Hedging or monetization strategies can be very effective at helping to reduce the risk of a public stock position, but their availability may depend on the ongoing relationship the founder has with the public company. To the extent that the founder still works for the company or sits on the board, the company's trading policy will apply to any potential transaction. As previously noted, many company trading policies are restrictive in what they permit, and hedging and monetization transactions are often prohibited outright, or can be executed only with the permission of senior management or the board of directors. Founders who have parted ways with the public company should have no contractual limitations on considering these types of transactions, and should discuss their benefits and considerations with their financial advisors.

Securities law considerations

In addition to contracts, there are certain securities law considerations associated with owning a public stock, and the extent to which these apply will depend on the size of the founder's stock position and the ongoing relationship (if any) with the company. While the following presents an extremely brief overview of the relevant items, care should be taken to understand these issues with the benefit of your own legal counsel and, where appropriate, the company's internal or external counsel.

Restricted or control securities. Securities acquired directly from a company under an exemption from registration (“restricted securities”) or securities held by an affiliate of the company (“control securities,” where an “affiliate” is someone who can influence the management and policies of the company, often an officer, director or significant shareholder). Sales of these types of securities are subject to Rule 144, which can impose certain limitations on the amount of stock that can be sold during specific time periods and certain reporting obligations (such as a Form 144), among other requirements.

Section 16. Under Section 16 of the Securities Exchange Act, officers, directors and 10% or greater shareholders have certain filing requirements to report transactions in their stock, as well as limitations on the type and timing of certain transactions.

Section 13. Under Section 13 of the Securities Exchange Act, any person owning more than 5% of a class of securities is required to file reports on Schedule 13D or Schedule 13G, with periodic updates required for changes to ownership.

Conclusion

A start-up founder who ends up with a concentrated position in a publicly traded stock has reached an exciting milestone in the evolution of their personal and professional life, complete with new opportunities and challenges.

Understanding the implications of having a large position in a public company is an important first step on the next leg of your financial journey. Working closely with your financial advisor, you should apply the same level of thoughtfulness and care to this stage as you used to plan for the liquidity event itself.



Planning after the liquidity event

A common form of exit is an IPO where shares are listed on a public stock exchange. Typically a six-month lockup may apply post-IPO where shares owned by key executives cannot be traded. Executives may be restricted by blackout periods where shares cannot be traded without the presence of a trading plan (commonly called a “10b5-1 plan”) created beforehand, during a period where the executives were not in possession of material non-public information. Actively managing the company exposure—through hedging, selling vested shares, exercising options and selling the newly acquired shares, and making charitable or non-charitable gifts using shares—requires vigilance and coordination among the founder and their key advisors.

Restrictions on transfer, hedging or pledging public securities

Just when the founder thinks they have seen the other end of a successful liquidity event and is ready to diversify their concentrated stock position, corporate lockup agreements and certain securities law requirements say “not so fast.” Public stock received in an IPO or an acquisition is typically subject to a lockup period (imposed by the underwriters in the case of an IPO and the acquiring public company in the case of an acquisition) of up to 180 days before the stock is permitted to be sold. In addition, most companies have restrictions on insider trading, hedging and pledging shares by executives. Founders may want to consider an SEC Rule 10b5-1 plan (a pre-established trading plan) to allow them to avoid violating corporate policies or securities laws. Finally, SEC Rule 144 provides a safe harbor from registration of certain securities so that an employee may sell securities in a public market place. The rules differ depending on whether the employee is considered a control person or a non-control person.

QSBS planning after a liquidity event

If the company went public via an IPO, the founder would be subject to a lockup (discussed previously) but may consider holding onto their stock anyway if the five-year holding period (or the three-year holding period with respect to stock issued on or after July 5, 2025) has not yet been met for QSBS purposes. If the QSBS is held for more than six months at the time of a sale (but hasn't met the applicable holding period), a QSBS shareholder may elect to defer the gain on the sale if such gain is reinvested into replacement stock that also qualifies as QSBS (sometimes called a “Section 1045 rollover”).⁵⁸ The adjusted basis of the replacement QSBS is equal to the basis in the original QSBS, less any gain deferred on the sale.⁵⁹ The holding period of the replacement QSBS generally includes the holding period of the original QSBS.⁶⁰ This allows for preservation of QSBS qualification for stock that has not reached the applicable holding period.

⁵⁸ IRC § 1045(a).

⁵⁹ RC § 1045(b)(3).

⁶⁰ IRC § 1223(13).

In order to elect treatment under a Section 1045 rollover, a QSBS shareholder must make an election by the due date (including extensions) for filing the income tax return for the tax year in which the QSBS is sold.⁶¹ The election is only revocable with the written consent of the IRS.⁶²

QSBS shareholders who have not met the applicable holding period requirement and are, therefore, ineligible to exclude gain on the sale of QSBS, and who are presented with an opportunity to sell their shares, can use a Section 1045 rollover to defer the gain until such time as they have met the holding period requirements.

When holding QSBS through a partnership, there are detailed regulations that provide for situations in which deferral of gain under Section 1045 of the Internal Revenue Code is available. In general, a partnership that holds QSBS for more than six months, then sells the QSBS and purchases replacement QSBS, may elect to defer the gain under Section 1045. In addition, a QSBS shareholder who sells QSBS that has been held for more than six months and purchases replacement QSBS through a purchasing partnership may also elect to defer the gain. For purposes of this rule, a purchasing partnership is defined as a partnership that acquires replacement QSBS and in which the QSBS shareholder is a partner (either directly or indirectly through another partnership) on the date on which the partnership purchases the replacement QSBS.

Lastly, an eligible partner of a partnership that sells QSBS may elect to defer the gain if the eligible partner purchases replacement QSBS either individually or through a purchasing partnership. For these purposes, an eligible partner is defined as a taxpayer other than a C corporation that is a partner in the partnership on the date the partnership acquires QSBS and at all times thereafter until the partnership disposes of the QSBS, which period must be more than six months.

These provisions allow for important tax deferral techniques available to partners in private equity and venture fund partnerships that are selling QSBS before the applicable holding period required generally for exclusion of gain under the statute.

Concentrated equity planning

Assuming transfers, hedging and pledging of public stocks is permissible, there are a variety of concentrated stock strategies (in addition to outright sale) that can help with the risk of a concentrated stock position. The most common strategies are equity collars, prepaid variable forward contracts, charitable remainder trusts and exchange funds.

⁶¹ Rev. Proc. 98-48, 1998-38 IRB 7.

⁶² *Id.*



Charitable planning

Charitable planning after a liquidity event can be a tax-efficient way to be philanthropic while offsetting some of the taxes in the year of the liquidity event. Unlike pre-liquidity charitable planning, post-liquidity charitable planning is fairly straightforward. In the liquidity event, the founder receives cash, public stock, or a combination of cash and public stock. Charitable gifts of public stock often are more tax-efficient than charitable gifts of cash, even though the AGI limitations for gifts of public stock (30% for a gift to a public charity) are lower than for gifts of cash (60% for a gift to a public charity).⁶³ This is because, when gifting any stock to a public charity or public stock to a private foundation, any income tax on the built-in capital gains on the stock is tax-exempt for a public charity or subject only to a 1.39% excise tax for a private foundation. All charitable vehicles are available post-sale, including outright gifts to public charities (including donor-advised funds), gifts to private foundations, and gifts to charitable remainder and charitable lead trusts.

Investment and financial planning

Once the liquidity event has occurred, the founder, working with a financial advisor, should update the financial plan with the actual dollar amounts (taking into consideration taxes that may be owed on the liquidity event). Using UBS Wealth Way (see the sidebar entitled “Making the most of the fruits of your labor”), a UBS Private Wealth Advisor can advise on a strategic asset allocation to best achieve the short- and long-term cash flow goals of the founder. The financial plan should be updated regularly to reflect changes in circumstances and to chart progress toward the achievement of goals and milestones.

Forming a family office

Following the liquidity event, there may be substantial liquid wealth held by the founder and various entities or trusts for the benefit of various family members. The family may seek a coordinated enterprise to carry out the administrative needs of numerous stakeholders while maintaining the founder’s vision and philosophy of how the family’s

⁶³ See footnote 53.

wealth should be deployed. To this end, the founder may consider creating a family office to manage the family's wealth while nurturing the family's identity and values across a wide range of areas, such as: wealth management, wealth transfer, philanthropy and family governance. See Ann Bjerke, David T. Leibel and Brian Hans, *Building a family office to steward family wealth and values* (a publication of the UBS Advanced Planning Group and Family Office Solutions) and Mark Tepsich and Nicole T. Sebastian, *Family matters: The family-focused family office* (a publication of UBS Family Office Solutions and Family Advisory and Philanthropy Services).

Let's have a conversation

Planning for the personal side of a liquidity event—both before and after the transaction—can help start-up founders avoid common missteps and set the stage for business and personal financial success.

Please speak with your UBS Private Wealth Advisor to explore how we can put our insights to work for you.



Author biographies

David Leibell

Executive Director, Senior Wealth Strategist
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As a Senior Wealth Strategist, David focuses on comprehensive strategies to assist clients with their complex financial needs such as preservation, transfer and management of wealth. David serves as an internal resource for clients on all issues related to tax, estate planning, philanthropy and wealth planning. David is also a Specialist for the Family Office Solutions (FOS) team, which holistically serves \$100 million+ clients and family offices in partnership with Private Wealth Advisors.

Prior to joining UBS in 2013, David worked at Wiggin and Dana where he was a partner in the Private Client Services Department focused on representing wealthy individuals and families, along with business succession and charitable planning. Prior to Wiggin and Dana, he was a partner in the Private Clients Group at Cummings & Lockwood.

David has authored over one hundred articles on charitable, estate and tax planning and given several hundred lectures and webinars to lawyer and non-lawyer audiences throughout the United States. He serves as the Chairperson of the Family Business Committee for *Trusts & Estates* magazine and is listed in *The Best Lawyers in America* for two practice areas—Trusts and Estates and Charities/Nonprofits. Since 2009, David has been listed in *Connecticut Super Lawyers* magazine.

After receiving a B.A. from Trinity College, David continued to earn a J.D. from Fordham Law School and an LL.M. in taxation from New York University. David is on the Advisory Board of the Central Park Conservancy and is a former member of the Estate & Gift Taxation Committee of the New York City Bar.

Brian Hans

Executive Director, Senior Wealth Strategist
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Brian works with UHNW clients to help coordinate their tax planning with a particular focus on cross-border strategies and income tax planning. He has extensive expertise and experience with developing tax-efficient strategies for US and non-US-based investing, pre-immigration tax planning and structuring family offices. Brian is also a Specialist for the Family Office Solutions (FOS) team, which holistically serves \$100 million+ clients and family offices in partnership with Private Wealth Advisors.

Prior to joining UBS, Brian was Counsel at the international law firm Winston & Strawn. Brian also previously served as a trial attorney for the Office of Chief Counsel to the Internal Revenue Service where he litigated and advised the IRS regarding issues of domestic and international estate planning and income tax issues.

Brian received his Bachelor of Business Administration from Hofstra University in 2004. He received his J.D., cum laude, from Hofstra University in 2008, where he was a member of the National Moot Court Team and the Tax Law Society. Brian received his LL.M. in taxation from the New York University School of Law in 2009.

Brian Schimpf, CFA®

Executive Director, Senior Quantitative Strategist
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As Senior Quantitative Strategist, Brian creates customized analytics to help ultra high net worth clients and family offices make financial, income tax and estate tax planning decisions. He has extensive expertise in cash flow-based planning relating to wealth transfer, charitable giving, and various income tax and estate tax mitigation strategies.

Prior to joining UBS in 2015, Brian worked in Bernstein's Wealth Planning and Analysis Group, and before that, he was an independent financial advisor. Brian has 15+ years' experience in the financial services industry.

Brian received his B.A. from Wake Forest University, double majoring in economics and English. He went on to earn his M.B.A. with an emphasis in finance from the Carlson School of Management at the University of Minnesota.

Brian holds the Chartered Financial Analyst® designation,⁶⁴ as well as the Series 7 and 66 securities licenses.

⁶⁴ For designation disclosures visit ubs.com/us/en/designation-disclosures.html.

Contributor biographies

Tess Mayo

Executive Director, Senior Wealth Strategist
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Tess works with ultra-high net worth families, helping them to design and implement wealth strategies that reflect their goals and values. She helps them create multigenerational structures for managing their wealth, fulfilling their philanthropic visions and optimizing tax effects. In addition, she reviews their trust agreements and other estate planning documents to ensure that the documents align with their planning objectives.

Before joining UBS, Tess was General Counsel of Perspecta Trust. She previously was a Partner in Cleveland, Waters and Bass and earlier served as President of Cambridge Trust Company of New Hampshire and a Senior Vice President of Cambridge Trust Company. Before that, she practiced trust and tax law.

Tess is the consulting editor of *Private Trust Companies: A Handbook for Advisers* (Globe Law and Business, 2020) and a co-author of *Effective Trusts: Minimising Disputes Through Design, Governance and Administration* (Globe Law and Business, 2022). She is a contributing author to *Advising the Wealthy Client: A Handbook for Working with the Ultra Wealthy* (Globe Law and Business, 2020) and *Beneficial Ownership Registers: The STEP Handbook for Advisers* (Globe Law and Business, 2021).

Tess also has written numerous articles. These include articles on trust governance structures and protecting settlor intent, which appeared in the *International Family Office Journal*. Other articles have appeared in *Estate Planning*, the *STEP Journal*, *Trusts & Estates* and *Trusts & Trustees*.

Tess helped write many of New Hampshire's laws governing trusts and trust companies. Notably, she was a principal author of the New Hampshire Family Trust Company Act (which governs private trust companies) and the New Hampshire Foundation Act (which was the first act in the United States recognizing civil law-style foundations).

Tess earned a B.A. in economics and history from Georgetown University, a J.D. from the University of California, Hastings College of the Law, and an LL.M. in taxation from the University of Florida.

Matthew Fleming

Executive Director, Structured Solutions Specialist
Family Office Solutions

Within the Family Office Solutions team, Matt focuses on delivering customized structured products as well as equity and fixed income derivative solutions to help clients implement tactical views and efficiently manage risks within their portfolios.

Before joining UBS in 2019, Matt spent five years at Goldman Sachs as a senior member of the Equity Solutions Group within Private Wealth Management, focusing on providing bespoke investment and risk management solutions to the ultra high net worth space, including concentrated stock hedging solutions and structured investments. Prior to Goldman Sachs, he was one of four founding partners at Varick Asset Management, a derivatives asset management firm, and was responsible for product development and marketing of the firm's investment offerings. Prior to that, he was a Director in the Investor Solutions group at Barclays Capital and served as the Senior Marketer for over-the-counter derivatives and structured investments for family offices, high net worth investors, private banks and registered investment advisors. Matt spent the first 10 years of his career at Lehman Brothers, where he was a Senior Vice President in the Structured Equity Solutions group, running the firm's single stock risk management business.

Matt received his B.A. in applied mathematics from Harvard University and his M.B.A. from New York University's Stern School of Business. He holds the Series 7 and 63 securities licenses.

Brian W. Formento, CAIA®

Executive Director, Head, Client Solutions and Investment Strategy
Family Office Solutions

With an extensive track record of working with UHNW and family office clients, Brian works with Advisors to deliver customized advice to clients of substantial financial wealth. He understands client needs and works with Advisors to coordinate cross-divisional coverage to ensure their UHNW clients and family offices are properly covered by a team comprising relevant FOS specialists.

In addition to the responsibilities above, he remains a member of the Portfolio Advisory Group specializing in asset allocation and portfolio construction advice for the family office segment. Brian works closely with Advisors to define risk-based asset allocation strategies and develop customized investment ideas for the largest clients at UBS. Brian previously was a key member of the Private Wealth Management Alternatives Advisory Board and the Private Wealth Management Family Office Strategy Team.

Before joining UBS in July 2006, Brian was a Managing Director and Senior Investment Strategist for OTC derivatives and alternatives at Deutsche Bank Private Wealth Management. Previously, he held senior positions at several private investment advisory firms and was Head of Proprietary Fixed Income Trading North America and Desk Head of the primary dealer at Paribas Capital Markets, now BNP Paribas.

Brian graduated magna cum laude and with distinction, receiving a B.A. and M.A. in economics from Boston University. He is a past chair and member of the Economic Department's Board of Advisors for the college and graduate school. Brian, a Chartered Alternative Investment AnalystSM (CAIA®),⁶⁵ is also a member of the Structured Products Association (SPA) as well as the Professional Risk Managers' International Association (PRMIA). More recently, Brian has been an industry contributor to curriculum development for the CFA program and has completed Wharton's Private Wealth Executive Education Program and Columbia University's Earth Institute Investment Academy on Sustainability. He is a trustee for historic Morven in Princeton, NJ. He currently holds the Series 7, 24, 3, 63, 66 and 55 securities licenses and the life and health insurance licenses.

⁶⁵ For designation disclosures visit ubs.com/us/en/designation-disclosures.html.

Doug Monaster

Executive Director, Private Markets Group
OneBank

Doug is an Executive Director in the UBS Private Markets Group, a partnership between UBS Private Wealth Management and UBS Investment Bank. He advises founder, entrepreneur and family-led businesses on strategic alternatives and corporate finance transactions.

Doug has significant experience across a wide range of transactions including mergers and acquisitions (M&A), private capital raising and equity capital markets (IPOs).

Doug joined UBS in 2010 and has over 20 years of investment banking and corporate finance experience. Most recently, he was an Executive Director in the UBS Technology, Media and Telecommunications Investment Banking Group, advising clients across the Media and Entertainment ecosystem.

Prior to joining UBS, Doug held various strategy and finance roles at NBC Universal and 21st Century Fox.

Doug received his M.B.A. from New York University's Stern School of Business and his B.B.A. from Emory University.

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