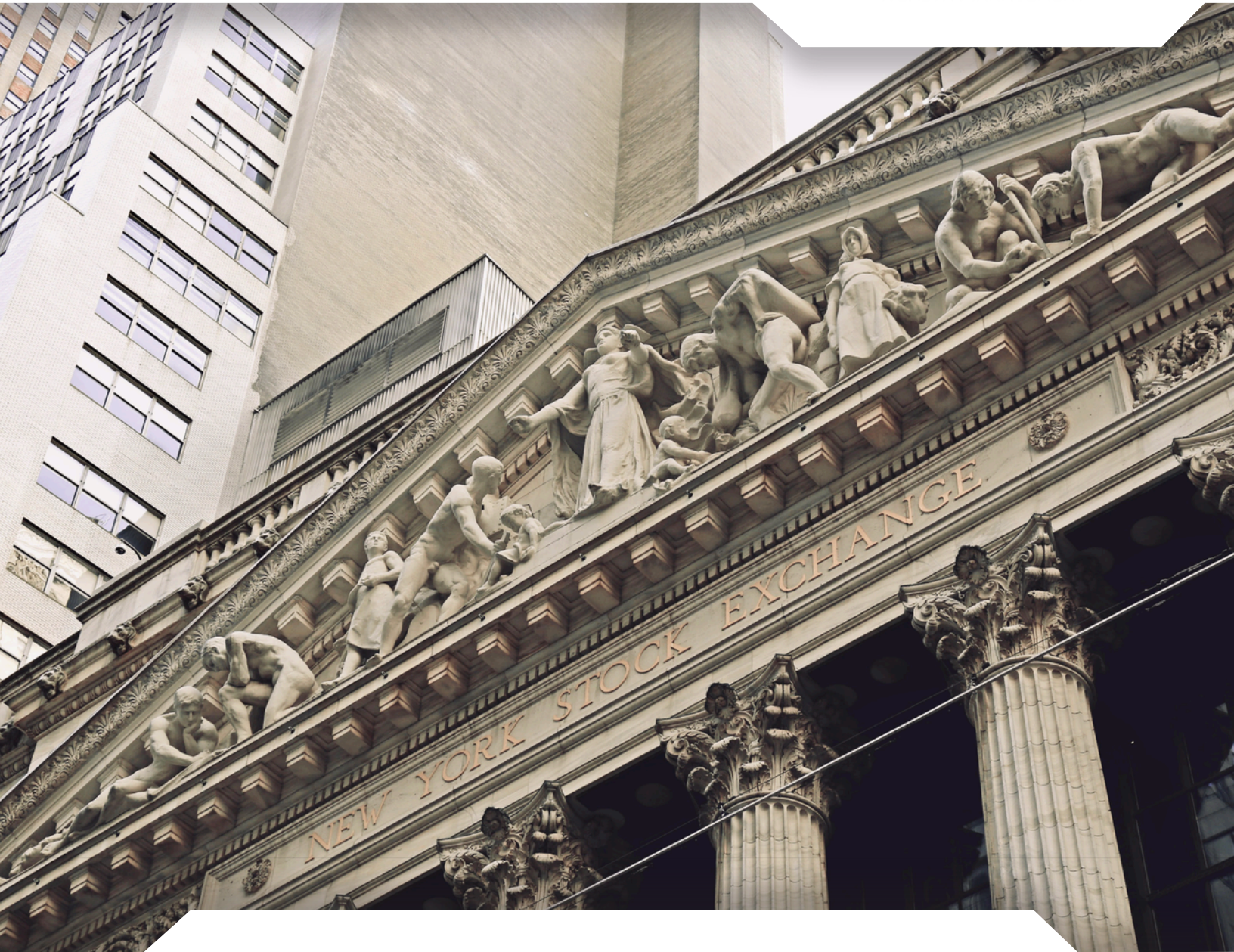




Pre- to Post-IPO Planning to Optimize Your Stock Options

And How to Avoid the Most Commonly Made Mistakes

by King Lip, CFA, CMT, Chief Strategist & Partner, and
Doug Couden, CFA, Chief Investment Officer & Partner

For early-stage employees and executives with stock positions, an IPO can potentially cause significant personal and professional life transitions. If the company you work for is about to go public, you probably have many questions about how to prepare, what to do with your shares, and what happens after the IPO.

In this guide, we discuss some of the things you need to consider when your company enters the public market, such as common mistakes to avoid in the IPO process, a comparison between the different stock options, steps to take after your company goes public, and diversifying your concentrated stock position.

Common Mistakes Made in the IPO Process (and How to Avoid Them)

- **Not seeking professional advice** – The planning phase during the pre-IPO may be one of the most important milestones of your long-term financial well-being. If you are uncertain about how certain provisions affect your tax situation, talk to BakerAvenue – we have licensed tax professionals, experienced financial advisors, and estate planning attorneys on staff.
- **Not starting the planning process early enough** – Your company's plan may include the opportunity to exercise before your shares vest (you would still be subject to the original vesting schedule in order to sell shares). Starting early often means you can start the clock ticking on long-term capital gains treatment on IPO shares. The difference in tax rates between short-term and long-term capital gains can be substantial — potentially 15% or more at the federal level, plus the impact of state taxes. Start the planning process early by exercising your options and consider making an 83(b) election to change tax treatment on any option gains from ordinary income to long-term capital gains.
- **Having funds available** – It takes money to make money. Pre-IPO shares may not have a market by which you can exercise and sell to pay for the exercise and taxes. If you exercise your options early, make sure you will have the funds ready to pay for the options and any potential taxes. We can advise you on unlocking liquidity to exercise options and fund tax liabilities.
- **Not diversifying** – There's an old adage on Wall Street that you concentrate to get rich but diversify to stay rich. Everybody purchases a lottery ticket expecting to win, but not every ticket will win. Diversify to make sure that your financial windfall is protected against potential significant losses.

How to Prepare

PRE-IPO

Early Planning Process
(Pre S-1 filing)



Pre-IPO Strategies that Can Help Build Your Wealth

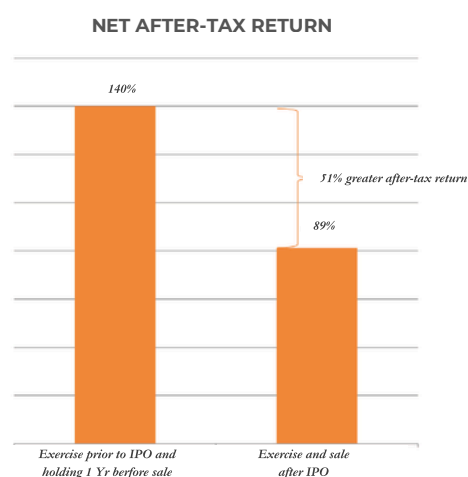
1. Understand What Type of Stock Options You Have

- **Non-Qualified Stock Options (NSOs)** – a company gives an employee the opportunity to purchase stock at a predetermined price at a given time
- **Incentive Stock Options (ISOs)** – stock options that are taxed at a long-term capital gains rate when exercised (also known as qualified stock options)
- **Restricted Stock Units (RSUs)** – grants of stock that a company gives to an employee without any purchase (received as shares or a cash equivalent)

Comparison of NSOs vs. ISOs

OPTION TYPE	RECIPIENT	TRANSFERABLE	OPTION EXPIRATION	EXPIRATION AFTER CO. DEPARTURE	TAXES ON GRANT	TAXES ON EXERCISE	TAX COST BASIS	TAXES ON SALE
Non-Qualified Stock Options (NSOs)	Employee or other service provider	Depends on stock option plan	Depends on stock option plan	Depends on stock option plan	None – assuming there is no market value	Yes – W2 income on the spread between fair market value and strike price	Strike price + spread	Long-term or short-term capital gains depending on holding period after exercise
Incentive Stock Options (ISOs)	Employees only	Non-transferable	No greater than 10 years after grant	ISOs convert to NSOs if not exercised within 90 days after departure	None	No – but may trigger Alternative Minimum Tax (AMT) on the spread	Strike price for calculating capital gains. For AMT calculation, fair market value at exercise	Long-term capital gains if held more than 2 years from grant, and 1 year from exercise

NSOs - Why Acting Early May Maximize After-Tax Returns



EXERCISING EARLY AND HOLDING 1-YEAR VS. EXERCISE POST-IPO		
	Exercising early and holding 1 yr before selling	Exercise and sell at time of IPO
Option Strike Price	\$10	\$10
Market value at time of exercise	\$10	\$40
Taxable spread income	\$0	\$30
Tax rate on spread income	N/A since no spread	37% (Fed) + State
Market value at time of sale	\$40	\$40
Capital gains	\$30	\$0 – since exercising and selling
Tax rate on capital gains	20% (long-term capital gains)	N/A – since exercising and selling
Total taxable amount	\$30	\$30
Net after-tax gain	\$24	\$18.90
Net after-tax return	140%	89%

2. The 83(b) Election and How to Use It

What is it?

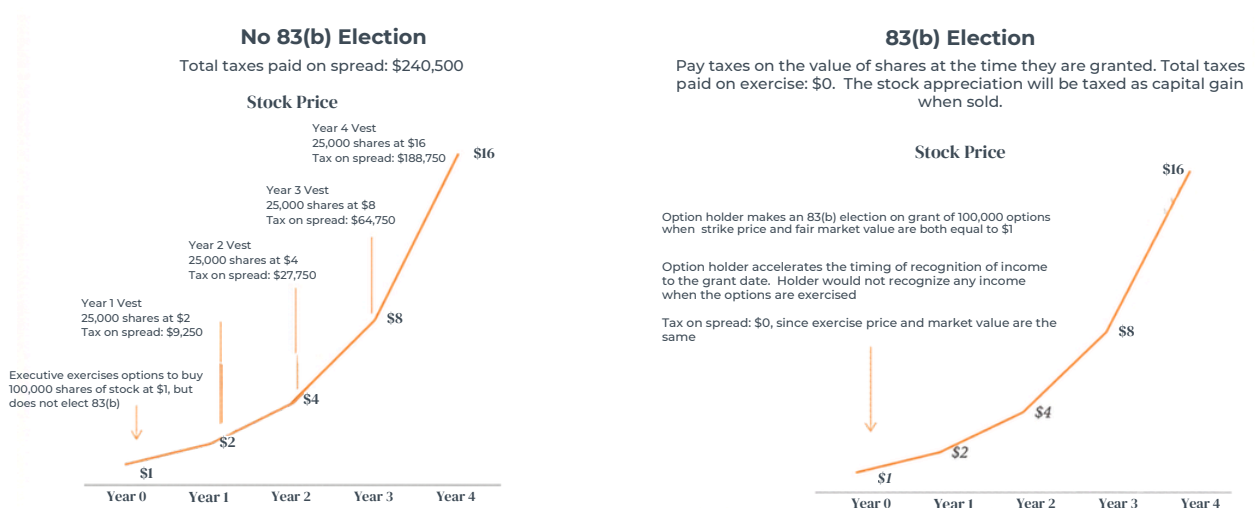
- Under the Internal Revenue Code, there is no taxable income at the time options are granted. A stock option holder does not recognize income until the stock is exercised, and the difference between the strike price (the holder's purchase price) and the stock price when exercised is taxed as ordinary income. Capital gains tax is paid on any increase between the price when stock is exercised and when it is sold. The capital gains holding period is one year.

- If a stock option holder makes a voluntary Section 83(b) election, the holder recognizes “income” at the time the options are granted but not at the time the options are exercised. (Elections are applicable only for stock that is subject to vesting.)

How can you use the 83(b) election to your advantage?

- Typically, at the time options are granted, the holder’s strike price for the stock and the fair market value of the stock are the same. An 83(b) election notifies the IRS that you prefer to be taxed on your restricted stock options on the date they were granted to you rather than the date they vest. Any future gains between your grant date and the stock sale will be considered capital gains, and taxed at a lower rate than ordinary income. In addition, an 83(b) election starts the one-year capital gains holding period.
- Note that 83(b) elections have risks. If you have a large amount of restricted stock, you will have a large tax bill without the ability to sell shares to help pay the taxes. If the stock value falls or you leave the company before your options vest, you will have already paid taxes on the options. It is very important to get professional advice on your situation.
- If the option holder does not make the 83(b) election, then they will have income each time stock is exercised. The income inclusion may be substantial if the value of the shares increases substantially between the time the options are granted and the time the options are exercised.

Example of 83(b) Election vs. Non-Election Four-Year Vesting Schedule with a One-Year Cliff



- For the sake of simplicity, this example assumes stock option grant vests annually. More commonly, stock options vest 25% after one year, then subsequent vesting is monthly, quarterly, or semi-annually depending on the plan. This illustration assumes a 37% federal tax rate. In both cases, the option holder would need the funds to pay for the initial option exercise.

How to File an 83(b) Election

Step 1 - In order for an 83(b) election to be effective, the individual must file the election with the IRS within 30 days of the stock grant. (This may be the date the board approves the grant even if the individual doesn’t receive the paperwork right away.) There are no exceptions to this timely filing rule. The last possible day for filing is calculated by counting every day (including Saturdays, Sundays, and holidays) starting with the next day after the date on which the stock is purchased.

Step 2 - A copy of the election should be provided to the company, and another copy should be attached to the taxpayer's federal income tax return for the year in which the grant is acquired.

For example, if the stock options are granted on May 16, the last possible day for filing is June 15. The official postmark date of mailing is deemed to be the date of filing. The election should be filed by mailing a signed election form by certified mail, return receipt requested, to the IRS Service Center where the individual files their tax returns. If the election is mailed after the 27th day, the individual should hand deliver the letter to the post office to obtain an official date-stamp on the certified mail receipt.

2 NOTIFICATION

First Name, Last Name
Street Address
City, State ZIP

Department of Treasury
Internal Revenue Service Center

Re: Election Under Code Section 83(b)

Dear Sir or Madam:

I hereby make an election pursuant to Section 83(b) of the Internal Revenue Code of 1986, as amended, with respect to certain restricted stock received by me. The following information is submitted as required by Treas. Reg. § 1.83-2(c):

1. Taxpayer Information
Name: _____
Street: _____
City: _____ State: _____ ZIP: _____
Taxpayer Identification Number: _____
2. Property for which election is made: _____
3. Date of Transfer: _____
Taxable Year for which Election is made: _____
4. Restrictions to which property is subject: _____
5. Fair Market Value: _____
6. Amount paid for property: _____
7. A copy of this election has been furnished to the Corporation.

Very truly yours,

Signature _____ Date _____

CC:

Post-IPO Strategies that Can Help Maximize & Preserve Your Wealth

How to Prepare **POST-IPO**

Short-Term Planning
(0 - 6 months)

Establish
financial goals
and wealth plan



- "Concentrate to Build Wealth. Diversify to Preserve It."
- Plan for "locking in" a required standard of living
- Establishing appropriate asset allocation
- Development of investment policy

If applicable,
establish reserve
funds for tax
liabilities



Create a diversification
strategy of shares and
future grants



- 10b5-1 plans
- Tax-loss harvesting to offset capital gains

How to Prepare **POST-IPO**

Long-Term Planning

Implement and
manage your
investment
portfolio and asset
allocation plan



Hedge and
monetize



- Protective Put buying
- Collaring
- Lending secured by stock

Determine
optimal time to
exercise and sell



- Company-specific events
- Economic and market conditions

Plan for
scenarios and
risk tolerance



Determine
capital
requirements



- Exercising options
- Tax obligations

1. Strategies for a Concentrated Stock Position

How much stock to sell?

Determining how much stock to sell of your concentrated stock position is not as difficult as it may seem. Our recommendation is generally to sell and diversify enough stock to reinvest in a portfolio that has a good probability of achieving a required standard of living that you would be happy with should your stock suffer a significant decline.

Illustration of a Hypothetical Sell and Diversification Plan

Situation:

- \$10 million of a concentrated stock position
- Average of \$200,000 of living expenses inclusive of taxes paid over the past several years $\$200,000 \div 4\% = \5 million
- $\$5 \text{ million} \times 1.28 = \$6.2 \text{ million stock to sell}$
- $\$10 \text{ million} - \$6.2 \text{ million} = \$3.8 \text{ million remaining position in concentrated stock}$

Post-Liquidation Strategy:

- Reinvest proceeds of \$5 million into a broadly diversified portfolio that will generate \$200,000 in total return (dividend and capital appreciation) after taxes.
- Reserve \$1.2 million for taxes payable in a conservative cash reserves account.
- \$3.8 million remaining in concentrated stock position can be used in a several ways:
 - Position may continue to appreciate in value; but if it declines in value, it will not likely affect your lifestyle since you have already sold enough to establish a required minimum standard of living
 - Position can be hedged with protective put purchases or a costless collar
 - Position can be used as collateral to generate income in a secondary account

Follow these guidelines to help determine what may be an appropriate amount to sell and reinvest in a diversified portfolio and the taxes that go along with creating that liquidity:

Step One: Review living expenses over the past several years inclusive of taxes paid. Exclude one-time items and take an average figure.

Step Two: Take the expense figure and divide by 4%.

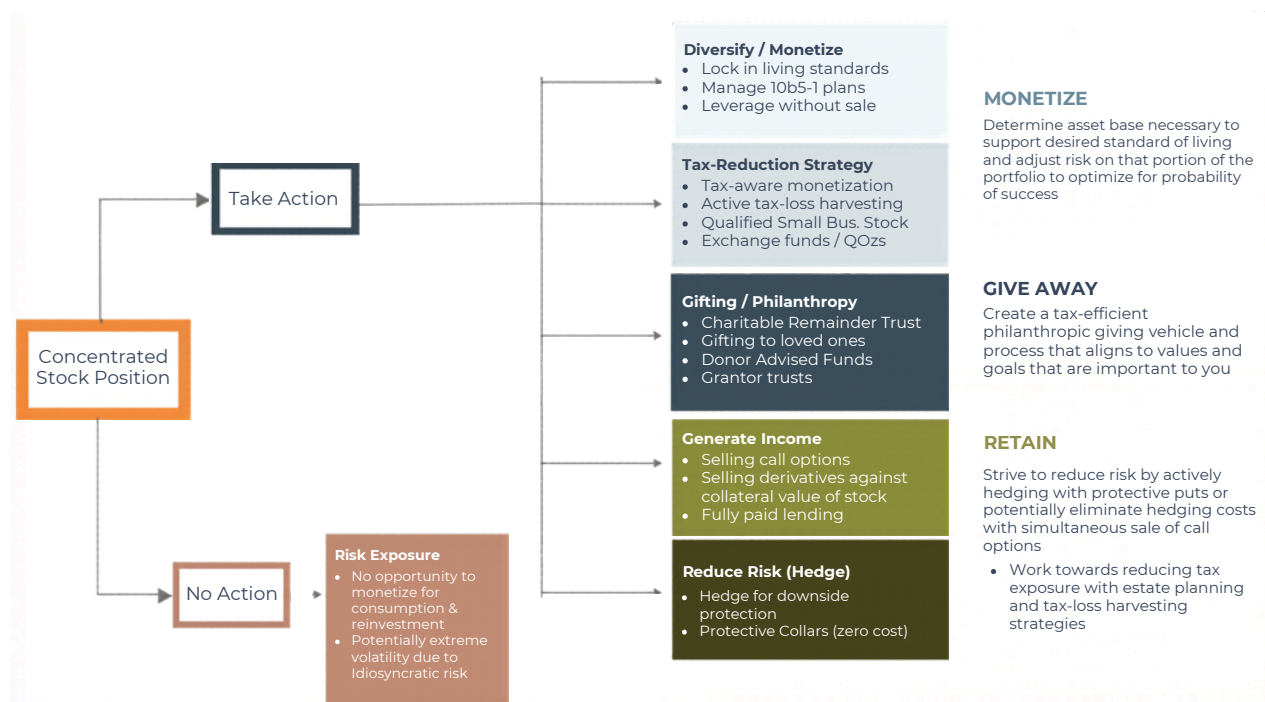
Step Three: Multiply that figure by 1.28, which is how much you will need to sell inclusive of the taxes payable.

Step Four: Reinvest proceeds into a broadly diversified portfolio that matches your return objectives and risk tolerance.

Step Five: Invest taxes payable in a conservative cash reserves account until taxes are due.

Note: The 4% withdrawal rate and 1.28 tax multiplier used above are illustrative estimates. Actual figures should be customized based on each client's specific federal and state tax rates, return objectives, and risk tolerance. California clients, for example, may face a combined capital gains rate above 33%, materially affecting the calculation.

Strategies for a Concentrated Stock Position



2. Managing Your Alternative Minimum Tax (AMT) Liability on ISOs

Incentive stock options are not subject to ordinary income tax when exercised, but the difference between the strike price and fair market value at exercise is subject to the AMT on exercise.

3. Comparison of Different Tax-Mitigation Strategies for Capital Gains

STRATEGY	OVERVIEW	BENEFITS	CONSIDERATIONS
Active Tax-Loss Harvesting	Funds are used to actively harvest losses while mimicking the returns of a selected market index.	Losses generated from an active tax-loss harvesting strategy can be used to offset gains realized from diversify a concentrated stock position	- Investors needs is have funds available aside from concentrated stock to utilize this strategy - Tax losses may not fully offset gains realized from concentrated stock
Charitable Remainder Trust (CRT)	Investor contributes highly appreciated securities into a CRT and receives an annuity income stream.	- Investor diversifies concentrated stock position with no initial tax - Can name different beneficiaries - Partial tax deduction	- Taxes are paid on annuity income - Irrevocable - Tax return filing on CRT - Tax deduction is one time only
Exchange Fund	Investor contributes concentrated stock with low basis into a partnership to receive a basket of diversified securities after 7 years.	Investor receives a basket of diversified securities after 7 years and benefits from diversification without having to realize capital gains.	- Fund may not accept position - High fees - Illiquidity for 7 years 20% of the fund is invested in real estate - Cost basis remains the same - Investor is required to be a "Qualified Purchaser" (investments > \$5 million, excluding residence)
Opportunity Zones (QOZ 2.0)	Investor contributes capital gain into a QOZ to defer original capital gains tax	- Original capital gain deferred for 5 years - Gains on QOZ investment may be eliminated if held for 10 years	- Generally limited to "Accredited Investors" (net worth > \$1 million, excluding residence) - Illiquidity for 5 -10 years
Variable Prepaid Forward Contract	Investor receives cash upfront on 75-85% of position generated by a loan. The stock is collared with a floor and ceiling price.	- Deferral of taxes for 2-5 years - Investor protected against large losses in the stock	- Costly to implement - Challenged by IRS
Donor Advised Fund (DAF)	Investor contributes highly appreciated stock into aDCF and receives an upfront tax deduction. Investor can take time to make charitable contributions.	- Assets sold tax free - Charity benefits - Investor receives full value of tax deduction	Assets are given to charity for the purposes of receiving a full tax deduction

4. Qualified Small Business Stock (QSBS)

What is it?

- The QSBS regime offers Federal tax incentives for taxpayers to invest in small businesses.
- Under Section 1202 of the Internal Revenue Code, taxpayers are allowed to exclude from gross income up to 100% of the gain recognized on the sale or exchange of QSBS that is held more than 5 years.
- For QSBS acquired **on or before July 4, 2025** (pre-OBBBA): The maximum exclusion is the higher of \$10 million or 10 times the price paid for the shares.
- For QSBS acquired **after July 4, 2025** (post-OBBBA): The per-issuer exclusion cap has been increased to \$15 million (inflation-indexed). Additionally, the OBBBA introduces a tiered exclusion schedule:
 - 50% exclusion after 3-year holding period
 - 75% exclusion after 4-year holding period
 - 100% exclusion after 5-year holding period

How can you use QSBS to your advantage?

- Tax savings from the QSBS gain exclusion can be substantial, but QSBS qualification is subject to a number of key requirements.

QSBS Qualification Requirements:

- Stock is issued by a Domestic "C" Corporation.
- The "C" Corporation has gross assets of less than \$50 million at the time the stock is issued.
- For QSBS acquired **on or before July 4, 2025**: The "C" Corporation has gross assets of less than \$50 million at the time the stock is issued.
- For QSBS acquired **after July 4, 2025**: The gross asset ceiling has been raised to \$75 million (inflation-indexed from 2027).
- Corporation uses at least 80% of its assets (by value) in an active trade or business.
- Stock is acquired by the taxpayer on original issuance by the Corporation.
- Shares must be held at least five years (holding period doesn't include time the investment was held via a convertible debt note).

Important Notes

- Once the Corporation exceeds the \$50 million asset threshold, it can never again issue QSBS. Stock issued as QSBS does not lose that character if the Corporation later does not meet the QSBS qualifications.

To learn more about specific steps you can take if the company you work for goes public, please contact a BakerAvenue expert who can discuss the following questions with you:

- When should I exercise my options? What is my tax exposure if I exercise ISOs versus NSOs?
- Should I sell my shares during my open window? If so, how much should I sell?
- How do I hedge the downside on my shares?
- How do I best reduce my tax exposure?
- How do I obtain funds to exercise my options?
- At what price point should I sell my shares?

In addition, we can provide a comprehensive view of your overall wealth management needs.

Why Choose BakerAvenue

 Concentrated Stock Expertise	 Tactical Active Management	 Proactive Risk Mitigation	 Tax Strategy & Estate Planning
Understanding the position and perform in-depth stock analysis through the lens of multiple (macro, technical, fundamental) disciplines	We proactively implement static hedging, which can be particularly expensive, and can save approximately 4% - 10% of the cost annually	We reduce risk by tactically scaling positions (rather than all in hedging) and avoid trading on key company announcements	We provide an integrated approach to tax strategy, as well as filing and estate planning services bundled with investment management (for portfolio sizes \$5MM & up)

Disclosures

The content provided is for illustration purposes only and information is the opinion of Baker Avenue Asset Management LP and does not constitute investment advice. All information is subject to change. Before purchasing any investment, a prospective investor should consult with its own investment, accounting, legal and tax advisers to evaluate independently the risks, consequences and suitability of any investment as each individual's goals and objectives may vary. Baker Avenue Asset Management LP is registered as an investment adviser with the Securities and Exchange Commission (SEC). The firm only transacts business in states where it is properly registered, or is excluded or exempted from registration requirements. Registration does not constitute an endorsement by securities regulators nor does it indicate that the adviser has attained a particular level of skill or ability. Baker Avenue Asset Management LP is not engaged in the practice of law or accounting. Baker Avenue Asset Management LP is engaged in the practice of tax for its tax preparation clients. All investment strategies have the potential for profit or loss. Changes in investment strategies, contributions or withdrawals, and economic conditions may materially alter the performance of your portfolio. Past performance is not a guarantee of future success. Different types of investments involve varying degrees of risk, and there can be no assurance that any specific investment or strategy will be suitable or profitable for a client's portfolio. There are no assurances that a portfolio will match or outperform any particular benchmark. Information presented is believed to be factual and up-to-date, but we do not guarantee its accuracy and it should not be regarded as a complete analysis of the subjects discussed. The information provided does not involve the rendering of personalized investment advice and should not be construed as an offer to buy or sell, or a solicitation of any offer to buy or sell the securities mentioned. Charts and graphs are for educational purposes only and should not be used to predict security prices or market levels. Any suggestion of cause and effect or of the predictability of economic or investment cycles is unintentional. Fact-check review completed June 2026. Tax law references reflect the One Big Beautiful Bill Act (OBBBA) signed July 4, 2025, which made permanent the TCJA individual tax provisions and expanded QSBS and Opportunity Zone program rules.

Plan with Confidence. Live with Clarity.

Since 2004, BakerAvenue has guided clients through personal and professional life transitions. Our firm provides comprehensive wealth management and investment expertise for high-net-worth individuals, families, trusts, foundations, and endowments. We're headquartered in San Francisco with offices nationwide.

For more information, please [contact us](#) or visit us at bakerave.com.

