Company Stock in Retirement Plans: Future Benefits

A company may enable employees to acquire its stock as an investment option for a 401(k) or other qualified retirement plan. If it is a good deal, plan participants may jump at the chance, especially if the stock is being offered at a discount. Furthermore, they may be in line for a future tax break.

Basic rule: If a participant receives a payout in the form of company stock at retirement, he or she is taxed only on the original basis of the stock. In other words, any increase in the stock's value from the time it is acquired—called the "net unrealized appreciation" (NUA)—is completely exempt from tax. In contrast, the full amount of other retirement plan distributions is normally taxed at ordinary income rates.

If the stock is subsequently sold, any gain is treated as a capital gain. Under current law, the maximum tax rate for capital gain is scheduled to increase from 15% to 20% in 2011, although more favorable rates may be extended by Congress.

Of course, plan participants should not put all their eggs in one basket. The plan account should be diversified and not invested solely in company stock. Nevertheless, consider the potential benefits of this investment.

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