

# Compensation Concepts: Understanding 83(b) Elections

Compensation Concepts adds clarity to complex compensation issues, helping advisors guide clients toward smarter decisions.

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## Topic

Tax: Compensation Concepts

## Understanding 83(b) Elections

The Internal Revenue Code states that an 83(b) election allows recipients of restricted stock to pay taxes on the fair market value (FMV) of the stock at the time of grant rather than when it vests. Restricted stock is typically taxed at ordinary income rates at the time it vests. Employees who expect the value of the stock to increase dramatically over time can opt to lock in a lower tax bill early on and convert future appreciation into capital gains (typically taxed at a lower rate than ordinary income) by filing an 83(b) election.

83(b) elections are most beneficial when the FMV of the restricted stock grant is very low but can be used at any point during a company's life cycle. Keep in mind that 83(b) elections are not without risks. Because these elections are being made on stock that has not yet vested, the employee runs the risk that if the stock is later forfeited (e.g., they leave the company before vesting), they will not receive a refund on the taxes paid. Additionally, should the value of the stock take an unexpected turn and decrease between the time of the grant and the time of vesting, the taxes paid pursuant to the 83(b) election will not be refunded. For these reasons, it's important that employees fully understand the risks associated with 83(b) elections before making their decision.

Employees choosing to make an 83(b) election must file within 30 days of the grant date using IRS Form 15620. This is a strict deadline, so consulting a tax advisor early in the process is imperative.

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