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Grab Your Fistful Of Zuckerberg's IPO Dollars

Image via bostinno.com

Facebook's Mark Zuckerberg is about to pay the ***largest individual tax bill ever*** because of his mountainous pile of stock options. This statistic naturally invites chatter over how stock options are taxed. See Top Tax Tips From Zuckerberg's Facebook Bonanza. Plus, many are already looking to scoop up some of the money that will bubble up like lava.

If the IRS "likes" Zuckerberg, California ***loves*** him. According to a report by California's Legislative Analyst's Office, the Golden State hopes for a ***$2.5 billion revenue boost*** when Facebook employees and investors become even wealthier. See California Expects To Collect $2.5B From Facebook IPO. California expects $500 million this fiscal year and $1.5 billion the next, give or take. What's not to like?

Yet this mega-IPO elicits questions from Buffett-like deep thinkers whether wealth buildup itself should be taxed. See The Zuckerberg Tax. Most say no. See A Proposal To Tax Stocks Annually. Besides, that might require throwing out thousands of pages of tax code and regulations. But there ***are*** plenty of tax questions to ask, including about ordinary income versus capital gain.

In 2005, Zuckerberg received options to buy 120 million shares for 6 cents a share. Each share is currently valued at more than $40. The spread between option price and market price is usually taxed upon exercise as compensation income. See Ten Tax Tips For Stock Options.

For Zuckerberg, that means 35%, yielding $1.5 billion in federal tax and $500 million in California tax. Significantly, Facebook gets a corresponding deduction for "paying" it, even if it isn't doing so in cash. That deduction has become controversial and Senator Carl Levin (D-MI) proposed changing it.

Even as compensation income, Zuckerberg's post-tax take is huge. Yet an even bigger bonanza might have been capital gain treatment for some or all of his options. For this to work, he would have had to ***elect*** to pay tax when his options were granted under Section 83 of the Internal Revenue Code. The idea is to include it in income at a ***low*** value, locking in capital gain treatment for future appreciation.

An 83(b) election with the IRS would report the value of what he received as compensation. See Code Section 83(b) Elections: The Good, the Bad, and the Ugly. Yet this could work only with restrictions that will lapse. With restrictions that never lapse the IRS values the property subject to them. See Ten Tax Tips For Stock Options.

According to filings, Zuckerberg plans to exercise all his options but sell only enough shares to cover his taxes. Retaining the rest of the shares should mean continued appreciation. That means Zuckerberg will likely get long term capital gain treatment for the shares once they are held more than a year.

For more, see:

Top Tax Tips From Zuckerberg's Facebook Bonanza

Ten Tax Tips For Stock Options

Restricted Stock SNAFUs

Zuckerberg Remains the Undisputed Boss at Facebook

Personal Data's Value? Facebook Is Set to Find Out

Option and Restricted Stock Basics, Part II

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