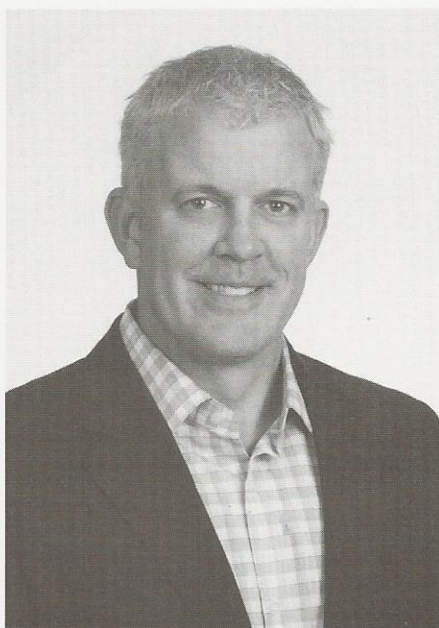
THE WALL STREET JOURNAL.
THURSDAY, JULY 3, 2014 © 2014 Dow Jones & Company, Inc. All Rights Reserved.

Voices: Robert Cheney, on Advising Tech Start-Up Workers


Robert Cheney

Voices is an occasional column that allows wealth managers to address issues of interest to the advisory community. Robert Cheney is the founder of the Portola Valley, Calif.-based Westridge Wealth Strategies.

I've found that advising early-stage tech industry employees and founders involves a unique set of challenges. In both cases, their net worth and future income stream are heavily dependent on the success of the start-up.

These people may be worth a lot on paper, but it's not liquid and it's in a volatile sector. Whether they will be paid in options or restricted stock, typically there's a four-year vesting period.

After that vesting period, advisers need to focus on getting these clients' stock liquid and reinvested in a diversified portfolio as soon as possible. Because these clients are so concentrated in technology, a diversified portfolio of stocks and bonds ensures that their assets will be ready to face any economic scenario.

But convincing such clients to diversify can be difficult. Often times they lack perspective. They're young. All they've experienced is the NASDAQ going straight up. Advisers need to keep such clients focused on the long-term and try to give them a little historical context. The truth of the matter is that over 14 years we've had two significant bear markets.

Such clients will often only want to sell 2% to 5% of their vested stock per quarter. I think that 10% to 20% per quarter is a better number to assure maximum diversification. In some cases, the stock price will continue to go up, even after you've advised your clients to sell.

But advisers can't worry about that; you'll never get the timing correct. Reassure such clients of the value of being diversified versus having a concentrated position in a young, niche-based company.

Advisers should also look for ways to minimize the tax burden for early stage tech employees and founders. They have to pay income tax on their restricted stock, which in California, where many of these companies are based, can be above 50%.

To offset capital gains taxes on tech stocks that have appreciated, advisers can try to harvest losses elsewhere in a client's portfolio. Additionally, investing in certain alternative asset classes like oil and gas funds can offer such clients a tax deduction above the level of the investment itself.

There is one factor that distinguishes the founders of such companies from early stage employees. Even after the "lockup" period expires, founders are expected to retain significant ownership in their company. Although advisers need to diversify founders' assets, they also need to balance their career requirements. Get them liquid to the extent that their future is secure, while not delivering a bad message to the investment community that the founder wants out.

When advisers can reassure such clients that the assets they've diversified into are ready to face any economic scenario, that's peace of mind.

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