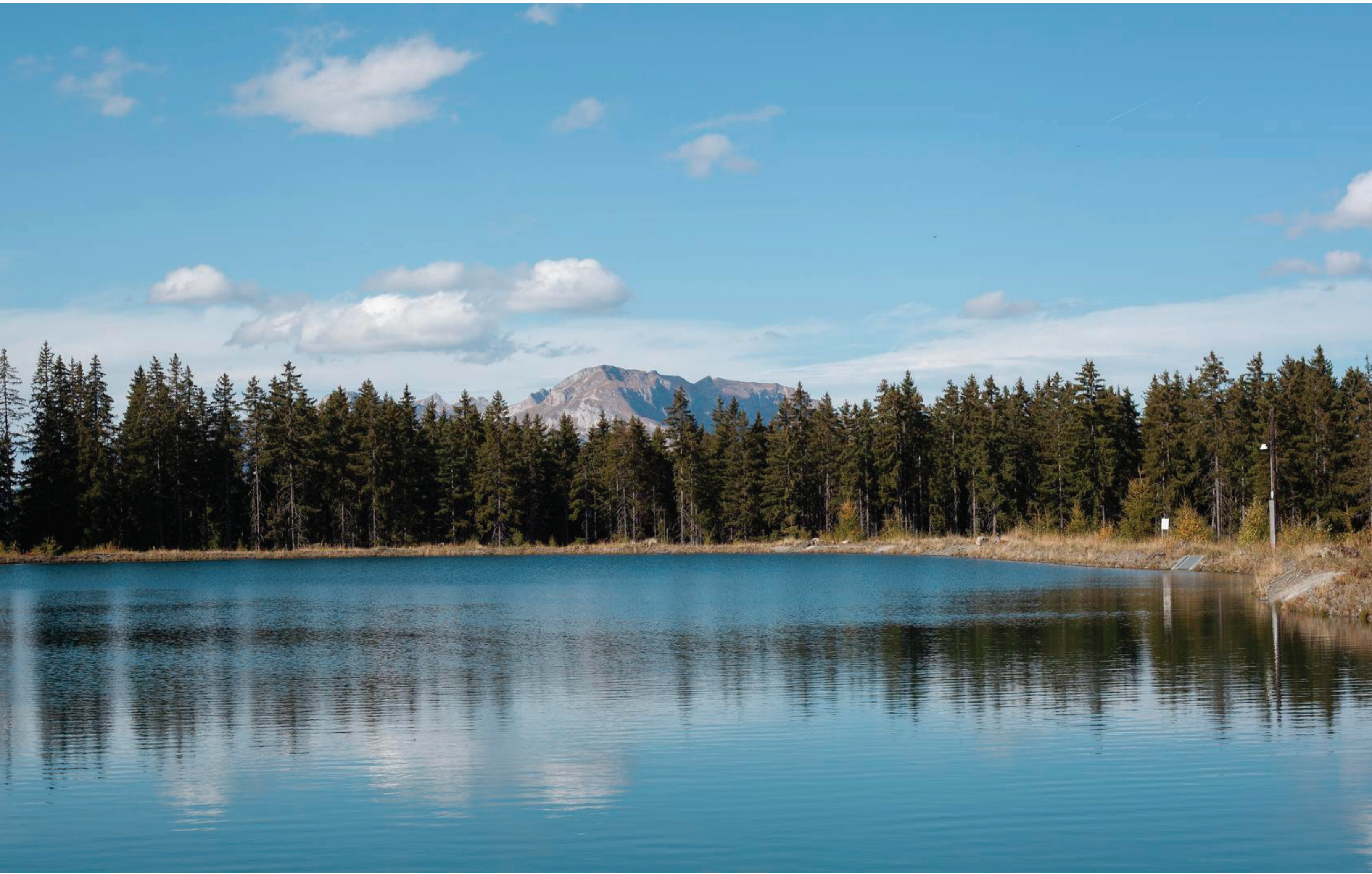
Financial Planning Guide for Microsoft Employees

A Comprehensive Resource from PCM Encore

Introduction

As a Microsoft employee, you have access to one of the most comprehensive compensation and benefits packages in the technology industry. However, navigating the complexities of equity compensation, retirement planning, and tax optimization requires specialized knowledge and strategic planning.

At PCM Encore, we work with technology professionals to help navigate their equity compensation, coordinate financial planning, and develop tax-efficient investment strategies. This guide breaks down the key components of your Microsoft benefits and provides actionable insights to help you make informed financial decisions.



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Your Microsoft Retirement Benefits

401(k) Plan Overview

Microsoft offers a robust 401(k) plan administered through Fidelity, featuring:

- **50% company match** on all your contributions up to the IRS annual limit ($23,500 for 2025 = $11,750 match)
- Immediate vesting (100%) of all employer contributions
- High contribution limits: $23,500 for 2025 ($31,000 if age 50+, $34,750 if age 60-63)
- Wide range of investment options including low-cost index funds
- **Note:** Catch-up contributions (if age 50+) are not eligible for the employer match

The Mega Backdoor Roth Strategy:

Microsoft's 401(k) plan allows after-tax contributions beyond the standard $23,500 limit, up to the total contribution limit of $70,000 for 2025 (including employer contributions). These after-tax dollars can be automatically converted to a Roth account by Fidelity, creating tax-free growth opportunities.

Key Consideration: Your retirement plan sits at Fidelity, separate from where your equity compensation may be held. A holistic financial plan coordinates across all your accounts, regardless of custodian.

Maximizing Your Retirement Strategy

Contribution Hierarchy: Consider this approach to maximize your retirement savings:

1. **Contribute the full $23,500** to get the maximum $11,750 match from Microsoft
2. **Consider after-tax contributions** for potential Mega Backdoor Roth conversions (up to $70,000 total for 2025)
3. **Evaluate additional savings vehicles** like taxable brokerage accounts or HSAs

Deferred Compensation Plan (DCP)

Program Overview

Microsoft offers a Deferred Compensation Plan (DCP) exclusively for employees at level 67 and above. This non-qualified supplemental savings plan allows you to defer and invest taxable income until a future year when your income—and therefore your tax rate—may be lower.

The DCP is administered directly by Microsoft Treasury and is designed for highly compensated employees looking to manage their tax liability strategically.

How the DCP Works

The Microsoft DCP allows you to defer two types of compensation:

Salary Deferrals:

- Enrollment period: November 1-30 annually
- Maximum deferral: 75% of base salary
- Takes effect: January of the following year
- Works like a 401(k) deduction from each paycheck

Bonus Deferrals:

- Enrollment period: May 1-31 annually
- Maximum deferral: Up to 100% of annual cash bonus
- Takes effect: 16 months later (e.g., May 2025 election applies to September 2026 bonus)
- Important: You're making a cash flow decision far in advance

Distribution Options

When you enroll, you must elect when and how you'll receive your deferred compensation:

- **At Termination:** Lump sum when you leave Microsoft (default if no election made)
- **Specific Date:** Choose a particular month and year
- **Installment Payments:** Spread over 5, 10, or 15 years

Tax Considerations

Key Tax Benefits:

- Contributions are made pre-tax, reducing your current year's taxable income
- Funds grow tax-deferred while invested
- Distributions taxed as ordinary income when received (ideally in a lower tax bracket year)

State Tax Strategy: If you've elected your deferred compensation at 9 years or less, you're taxed based on the state where you worked, not where you live at distribution. This can be advantageous if you worked in Washington (no state income tax) but retire to a state with income tax. Distributions of 10+ years are taxed based on your residence state at the time of distribution.

Deferred Compensation Plan (DCP)

Critical Restrictions and Risks

Enrollment Windows: Missing your enrollment window means waiting a full year to participate. Mark your calendar for November (salary) and May (bonus) election periods.

Changes Are Difficult: If you need to change a distribution election after it's made:

- You must push the distribution date back by at least 5 years
- The change must be made 12+ months before the scheduled distribution
- You must still be an active employee when making the change
- If you leave Microsoft within 12 months of the change, it reverts to the original election

Credit Risk: Unlike your 401(k), DCP funds are not held in a separate trust. They remain an obligation of Microsoft. While Microsoft is financially strong, these deferrals are subject to the company's credit risk. In the unlikely event of bankruptcy, DCP participants are unsecured creditors.

Strategic Considerations

The DCP Decision: The DCP can be a powerful tax planning tool, but it's not right for everyone:

Consider the DCP if:

- You're in the highest federal tax brackets (35% or 37%)
- You've already maxed out your 401(k) contributions
- You have sufficient cash flow to maintain your lifestyle with reduced paychecks
- You anticipate being in a lower tax bracket in retirement
- You're comfortable with the credit risk of Microsoft

Proceed with Caution if:

- You haven't maximized your 401(k) match (always capture the company match first)
- Deferring salary would prevent you from maximizing your ESPP (15% or $25,000)
- You need the income for near-term goals or cash reserves
- You're uncertain about your long-term employment with Microsoft

PCM Encore's Approach: We can help level 67+ employees model the tax impact of DCP participation alongside all your other compensation elements. The DCP works best when coordinated with your 401(k), mega backdoor Roth, RSU vesting schedule, and overall cash flow needs. We'll help you determine optimal deferral amounts and distribution strategies that align with your retirement timeline and tax situation.

Employee Stock Purchase Plan (ESPP)

How Microsoft's ESPP Works

Microsoft's Employee Stock Purchase Plan, administered exclusively through Fidelity, allows you to purchase Microsoft stock at a **10% discount** using after-tax payroll deductions.

Key Details:

- Annual purchase limit: Up to 15% of your pay, subject to IRS limits ($25,000 as of 2025)
- No lock-up period—shares are yours immediately
- Purchases occur on a regular schedule

Tax Treatment of ESPP Sales

The tax treatment of your ESPP shares depends on how long you hold them:

Disqualifying Disposition (Selling before holding periods):

- If you sell before holding shares for 2 years from offering date AND 1 year from purchase date
- The discount (10%) is taxed as ordinary income
- Any additional gain is taxed as short-term capital gain

Qualifying Disposition (Meeting both holding periods):

- Hold for at least 2 years from offering date AND 1 year from purchase date
- The lesser of (a) actual gain or (b) 10% discount is taxed as ordinary income
- Any remaining gain is taxed as long-term capital gain

Strategic Considerations

The Immediate Sale Strategy: Many financial advisors recommend selling ESPP shares immediately upon purchase to:

- Lock in the guaranteed 10% return (minus taxes)
- Manage concentration risk in Microsoft stock
- Redeploy capital into a diversified portfolio

The Hold Strategy: Some employees hold ESPP shares to achieve qualifying disposition status, but this introduces:

- Market risk if Microsoft stock declines
- Increased concentration in company stock
- Delayed liquidity

Our Perspective: The "right" strategy depends on your overall financial picture, tax situation, and existing Microsoft equity holdings. PCM Encore can help you evaluate this decision within your holistic wealth plan.

Equity Compensation: Restricted Stock Units (RSUs)

Understanding Your RSU Grant

RSUs are a key element of Microsoft's equity compensation program. Unlike stock options, RSUs have value even if the stock price declines, making them a significant component of your total compensation.

How RSUs Work:

- Granted as part of your offer letter and annual performance reviews
- Vest on a schedule (typically quarterly over 4-5 years)
- Time-based vesting (no performance conditions for most employees)
- Taxed as ordinary income when they vest

Custody Choice: Fidelity or Morgan Stanley

Microsoft gives you a choice of where your vested RSUs are deposited:

- **Fidelity**
- **Morgan Stanley**
- **Default:** If you don't make an election, shares go to Morgan Stanley

PCM Encore works with both Fidelity and Morgan Stanley. Regardless of which custodian you choose, we can manage your equity compensation holdings and integrate them into your comprehensive financial plan. You don't need to change custodians to work with us.

Tax Treatment at Vesting

When your RSUs vest:

1. **Automatic tax withholding occurs** (typically 22% federal supplemental wage withholding, plus state and FICA)
2. **You receive net shares:** For example, if 100 shares vest, you might receive 60-65 shares after withholding
3. **Income is reported on your W-2** at the fair market value on vest date
4. **Your cost basis is established** at the vest-date market value

Critical Tax Consideration: The 22% automatic federal withholding is often insufficient if you're in a higher tax bracket. Many Microsoft employees are in the 32%, 35%, or 37% federal brackets, meaning the withholding doesn't cover the full tax liability. We help you calculate estimated tax payments to avoid surprises and underpayment penalties at tax time.

Equity Compensation: Restricted Stock Units (RSUs)

After Vesting: Sell or Hold?

Once your RSUs vest and shares hit your account, you face a key decision: sell immediately or hold?

Sell Immediately:

- Mitigates concentration risk
- Provides liquidity for diversification
- Treats equity comp as cash compensation
- Minimizes additional tax complexity

Hold for Long-Term Capital Gains:

- Potential for additional growth if Microsoft stock appreciates
- If held more than 1 year post-vest, gains taxed as long-term capital gains (15-20%)
- Increases concentration risk in Microsoft stock

Trading Windows

All active Microsoft employees are subject to trading windows that restrict when you can buy or sell Microsoft stock. Generally:

- **Trading windows open** after quarterly earnings announcements
- **Blackout periods** occur before earnings and during material non-public information events
- **Your shares may be deposited** during a blackout period, requiring you to wait for the next window

Understanding and planning around these windows is essential for tax-loss harvesting, rebalancing, and liquidation strategies.

The 55/15 Rule

One of Microsoft's highly valuable benefits is the 55/15 retirement rule: employees who are at least 55 years old with 15+ years of service[1] can retire and retain their unvested RSUs. This creates distinct early retirement planning opportunities that require careful coordination of:

- Healthcare coverage until Medicare eligibility at 65
- Income bridging strategies until Social Security
- Tax-efficient withdrawal sequencing
- RSU vesting schedules post-retirement

Employees who reach 65 years of age may retire and retain their unvested RSUs without the 15 year service requirement.

[1] For employees hired by Microsoft prior to August 1, 2023 as part of an acquisition, the years spent at the acquired company count towards the stock awards vesting at retirement.

Advanced Topics for Microsoft Employees

Rule 10b5-1 Trading Plans

What is a 10b5-1 Plan?

A Rule 10b5-1 trading plan is a pre-established written plan that allows company insiders to sell stock during blackout periods. While most Microsoft employees are not "insiders" subject to Form 4 filings, 10b5-1 plans can benefit anyone subject to trading restrictions.

Key Features:

- Must be established during an open trading window
- Requires a cooling-off period (typically 90 days) before first trade
- Sets predetermined prices, dates, or formulas for sales
- Provides an affirmative defense against insider trading allegations

Who Should Consider a 10b5-1 Plan?

- Form 4 filers (executives and board members)
- Employees with large, concentrated positions
- Those wanting systematic, disciplined diversification
- Anyone seeking to sell during otherwise blackout periods

PCM Encore's Approach: We have the ability to work with Morgan Stanley's trading desk to draft and implement 10b5-1 plans for our clients. Even if your equity is held at Fidelity, we can assist in setting up a 10b5-1 trading account at Morgan Stanley. We will then transfer proceeds back to your primary account.

Form 144: Restricted Stock Sales for Affiliates

What is Form 144?

Form 144 is an SEC filing required when company "affiliates" (officers, directors, and certain large shareholders) sell restricted or control securities.

Who Must File Form 144? At Microsoft, this typically includes:

- All board members
- C-suite executives (CEO, CFO, General Counsel, etc.)
- Other executives designated as reporting persons
- Any shareholder who owns 10% or more of Microsoft's stock

Regular employees are generally not considered affiliates and don't file Form 144, regardless of how much stock they sell.

Filing Thresholds for Affiliates: If you are an affiliate, you must file Form 144 when selling more than 5,000 shares OR $50,000 in value within any 3-month period.

Key Requirements:

- Must be filed concurrently with or before the sale
- Sales limited to the greater of 1% of outstanding shares or average weekly volume
- Public disclosure of all sales
- Available on the SEC's EDGAR database

Why This Matters: If you're subject to Form 144 requirements, your stock sales become public information. Strategic planning around timing, volume, and public perception becomes critical. We help you navigate these considerations with discretion and compliance.

Why Work with PCM Encore

ENCORE

We Understand Tech Company Benefits

We work with employees from technology companies and understand the nuances of equity compensation packages. We're familiar with:

- How trading windows affect your liquidity planning
- The interplay between ESPP, RSUs, and retirement contributions
- Tax considerations across different jurisdictions
- The complexity of coordinating multiple custodial relationships

Holistic Wealth Management

Your Microsoft compensation is just one component of your financial life. We help you with:

- **Tax planning:** Explore tax-smart strategies like strategic RSU sales, tax-loss harvesting, and retirement account optimization
- **Estate planning:** Ensure your wealth transfers efficiently to heirs
- **Risk management:** Appropriate insurance coverage for your income level
- **Education planning:**529 plans and other strategies for children's education
- **Real estate:** Purchase planning and mortgage strategies
- **Charitable giving:** Tax-efficient strategies including donor-advised funds

Custody-Agnostic Approach

We work with both Fidelity and Morgan Stanley.
You don't need to consolidate accounts or change custodians to work with us. We'll meet you where you are and integrate all your accounts into a unified financial plan.

This is particularly important at Microsoft where:

- Retirement plans are at Fidelity
- ESPP shares are at Fidelity
- RSU shares can be at either Fidelity or Morgan Stanley

We coordinate across all these platforms effectively

Experience with Technology Professionals

We work with employees from various technology companies including public and pre-IPO organizations. This experience provides insights into:

- Industry compensation trends and structures
- How different companies structure equity benefits
- Strategies that work for tech professionals at various career stages
- Pre-IPO and liquidity event planning

Common Questions from Technology Professionals

I have $10-15 million in Microsoft stock. How do I diversify without triggering huge taxes?

This is one of the most common situations we encounter. Strategic diversification often involves:

- Systematic selling programs spread over multiple years
- Tax-loss harvesting in other accounts to offset gains
- Charitable giving strategies using appreciated stock
- Exchange funds: Pooling your concentrated Microsoft position with other investors' concentrated positions to achieve diversification while deferring capital gains
- Using Qualified Opportunity Zone investments to defer capital gains, while considering direct indexing strategies to manage tax implications effectively
- Timing sales relative to other income events
- Potentially using options strategies (covered calls, collars) to reduce volatility

Should I max out my 401(k) or pay down my mortgage?

The answer depends on:

- Your mortgage interest rate vs. expected investment returns
- Your tax bracket and the value of 401(k) deductions
- Your employer match (we recommend that you always capture this first)
- Your overall debt-to-asset ratio
- Your psychological comfort with debt

When should I start selling my RSUs after they vest?

There's no one-size-fits-all answer.
We typically recommend:

- Evaluating your total Microsoft holdings relative to net worth
- Establishing target allocation percentages
- Creating a systematic rebalancing program
- Considering tax implications of your overall financial picture
- Factoring in your career stage and income stability

I'm considering early retirement under the 55/15 rule. Am I ready?

Key factors to evaluate:

- Do you have sufficient liquid assets to cover 10+ years of expenses?
- How will you bridge healthcare until Medicare at 65?
- What's your strategy for unvested RSUs post-retirement?
- Have you modeled various market scenarios?
- Will you pursue consulting or other income?

Getting Started with PCM Encore

Maximizing the value of your compensation and benefits requires specialized expertise and proactive planning. At PCM Encore, we aim to serve as your partner in navigating these complexities.

Our Process:

1. **Initial Consultation:** We learn about your financial situation, goals, and concerns
2. **Comprehensive Analysis:** We review your Microsoft benefits, existing holdings, and overall financial picture
3. **Strategy Development:** We create a customized plan addressing equity compensation, taxes, retirement, and wealth building
4. **Implementation:** We help execute your plan, coordinating with your existing custodians (Fidelity, Morgan Stanley, or both)
5. **Ongoing Management:** We meet regularly to adjust your plan as your life and Microsoft's offerings evolve

We work with:

- Recent hires navigating their first equity grants
- Mid-career professionals accumulating substantial equity positions
- Senior employees planning for retirement or early retirement
- Individuals managing concentrated stock positions

Next Steps:

If you're ready to have a conversation about your equity compensation and financial future, we'd welcome the opportunity to speak with you

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