Money Matters

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Skloff Financial Group Question of the Month:
Comparing Employee Incentive Stock Options versus Nonqualified Stock Options versus Restricted Stock Units
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Q: We read the article 'Employee Incentive Stock Options – Use Them or Lose Them' and 'Employee Nonqualified Stock Options – Use Them or Lose Them' and 'Employee Restricted Stock Units'. Our employer has awarded us a combination of incentive stock options (ISOs), nonqualified stock options (NSOs) and restricted stock units (RSUs). Can you compare them?

A: The Problem. Many employers award ISOs and/or NSOs and/or RSUs to attract and retain employees and/or stakeholders. Unfortunately, many employees and stakeholders do not truly understand the mechanics of these instruments, their tax ramifications and how their terms can change.

The Solution – Compare the Instruments Side by Side. If utilized correctly, these financial instruments can benefit both the employers, employees, and stakeholders. Key to utilizing them in the right manner is understanding their similarities and differences, described below.

	Incentive Stock Options (ISOs)	Nonqualified Stock Options (NSOs)	Restricted Stock Units (RSUs)
Eligible Recipients	Employees	Employees and non-employees, like contractors and outside directors	Employees and non-employees, like contractors and outside directors
Taxation on Grant	None	None	None
Taxation on Vest	None	None	Taxed as income
Taxation on Exercise	None	Taxed as income on difference between exercise price and stock price	None
Taxation on Sale	Long term capital gain if sold more than two years after grant date and more than one year after exercising to buy stock	Long term capital gain if sold more than one year after exercising to buy stock	Long term capital gain if sold more than one year after vesting stock
Taxation on Sale	Short term capital gain if sold less than two years after grant date or less than one year after exercising to buy stock	Short term capital gain if sold less than one year after exercising to buy stock	Short term capital gain if sold less than one year after vesting stock
Expiration	Must be exercised within 90 days of termination	Can be exercised up to expiration date	Forfeit upon termination, with exceptions for special situations, like retirement or acquisition

Taxes. Taxation between ISOs, NSOs and RSUs varies widely. Unlike ISOs and NSOs, RSUs are taxed as income upon vesting. Unlike ISOs and RSUs, NSOs are taxed as income on the difference between the exercise price and stock price. ISOs receive long term capital gains rates if sold more than two years after the grant date and more than one year after exercising the option to buy the stock. With NSOs, in addition to income taxes, you are subject to long term capital gains if the stock is sold more than one year after exercising NSOs. Or, in addition to income taxes, you are subject to short term capital gains if the stock is sold in one year or less after exercising the NSOs. With RSUs, shares sod more than one year after vesting are subject to long term capital gains, while shares sold one year or less are subject to short term capital gains.

Short term capital gains rates are equal to your income tax rate. Long term capital gains rates are based on your income, subject to the 0%, 15% or 20% capital gains tax rate and (if applicable) an additional 3.8% Net Investment Income Tax.

Often Overlooked. Many restricted stock unit plans have clear language defining your rights upon termination from the company. A job transitions can be emotional time when you may overlook a material part of your wealth – your ISOs, NSOs and RSUs.

Action Step – Understand Your Incentive Stock Options (ISOs), Nonqualified Stock Options (NSOs)and Restricted Stock Units (RSUs)
Work closely with a Registered Investment Adviser (RIA) to make the best financial decisions.

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