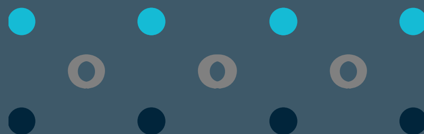
ALCHEMIST
WEALTH

5 THINGS TO KNOW IF YOU HAVE STOCK OPTIONS



Introduction

Whether you're at a pre-IPO start-up, a growing public company, or a blue chip that just developed a life-saving vaccine, stock options can provide a boost to your current and long-term wealth.

The concept is relatively straightforward, but like everything else, the devil is in the details. Maximizing your profit is just one side of the equation – taxes are also a consideration, and the rules are complex. This short read will arm you with enough info to get you started on sorting out your situation.

01

What Are Stock Options?

Stock options aren't the same as owning stock. They are the right to purchase shares of company stock at a certain price, which is usually below market value. The idea is that the price of the shares will rise over time, and you'll be able to sell them at a higher price when you exercise the options.

THE THREE TYPES OF OPTIONS

1

Non-qualified Stock Options (NSOs):

These options provide the right to buy a pre-set number of company shares at a pre-set price.

- Taxes must be paid when the options are exercised (the shares are purchased) and when the shares are sold, assuming the stock has appreciated.
- NSOs are usually taxed as ordinary income.

2 Incentive Stock Options (ISOs)

Provide the right to buy shares at a discounted price and to delay taxes on the shares until they are sold.

- ISOs are usually taxed at the capital gains rate – so exercising the option and holding the stock at least a year will potentially create a tax advantage.

3 Restricted Stock Units

Are a transfer of stock from your employer to you that vest later. Once they vest, you own the stock and can do with it what you would like. It's essential to keep in mind, though, that the fair market value of the stock is included in your taxable wages.

RSUs

Transfer of stock to employee

NSOs

Option to buy shares at a pre-set price

ISOs

Option to buy shares at a discounted price

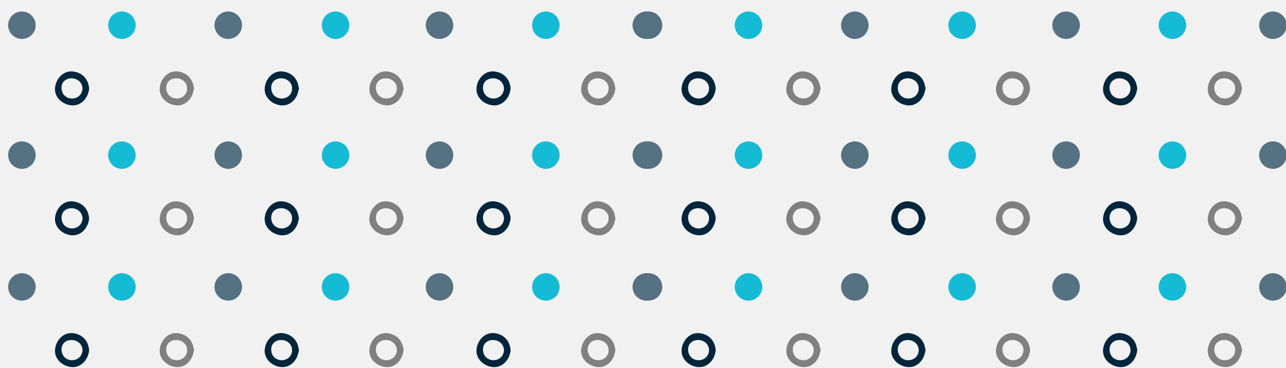
02

Understanding the Terminology

Exercising stock options means buying shares of your employer's common stock at the price specified in your option grant.

The "spread" is the difference in value between the strike price and the shares' value when you exercise your options.

Before you can exercise the options or purchase the shares, the stock must first vest, meaning you have to work for the company for a certain amount of time to obtain those shares. Stock options typically have a vesting schedule. Once they vest, they don't have to be purchased immediately, but there is usually a last date to exercise the options, or they expire.



03

How Do I Decide If I Should Exercise Options?

1

Are the options in-the-money or underwater? In-the-money means they have increased in value. If they are underwater (trading below your exercise price), it may be prudent to wait for the stock price to rise.

2

Is your company public? If your company is private and does not have plans for filing an IPO in the near term, exercising your options may be risky because you are purchasing shares that may not become liquid. If your company has not yet launched an IPO, you must purchase shares in cash.

3

Will you have to pay taxes? Depending on your situation (what kind of options you have, the number you were granted, and your compensation, etc.), you may have to pay taxes when you exercise.

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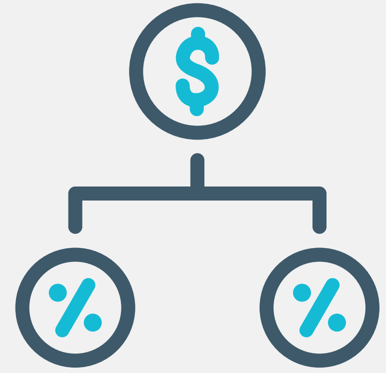

Deciding When to Sell Shares

After exercising your options, you may want to consult with a financial advisor and a tax advisor to discuss the most advantageous and profitable manner to sell the stocks. The type of options you have and your holding period after exercising your options will significantly impact your tax liability.

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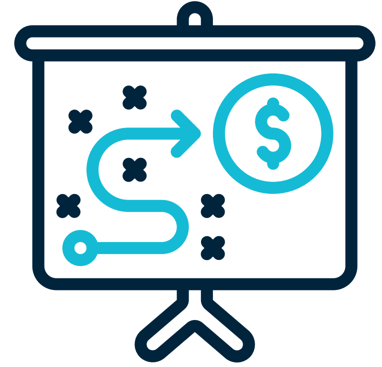
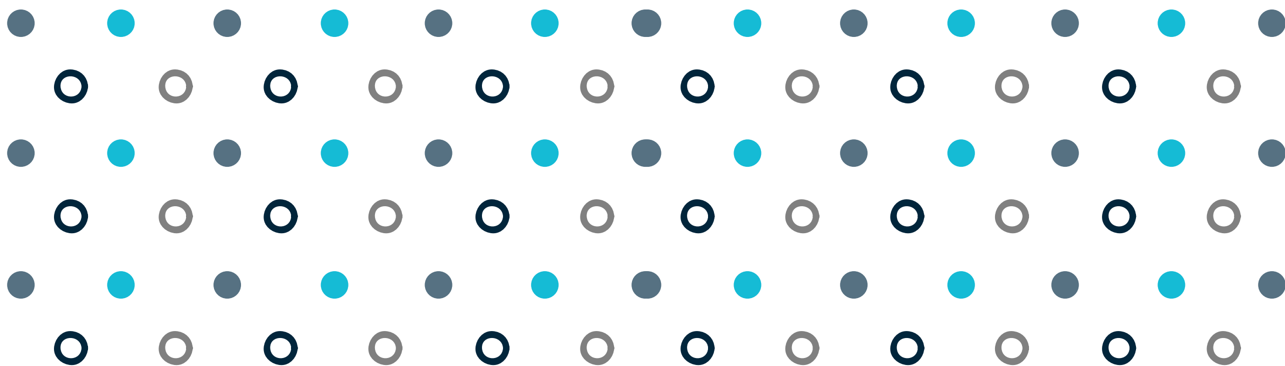


Avoiding Overconcentration

A concentrated stock position is usually defined as 10% or more of a portfolio. Depending on your financial position, continuing to hold a big percentage of your wealth in your company stock can be very risky.

Selling some of your position and redeploying into a more diversified portfolio of assets makes good sense. It can be part of a plan to get you closer to early retirement, and it can also be a way to express your values and beliefs outside of your work if you choose to invest in ESG- focused stocks or funds.

You may also decide to get ahead of some of the big expenses. For example, you could super-fund 529 plans for your children or pay off student loans. The idea is to be thoughtful about your complete financial picture and make a plan for those new funds that will keep you on track.



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