AMERICAN FINANCIAL NETWORK

AN INDEPENDENT FINANCIAL SOLUTIONS FIRM

STOCK OPTION'S & RESTRICTED STOCK

Understanding The Differences

Stock Options – An Incentive for Key Employees

INCENTIVE STOCK OPTIONS (ISO):

Definition: *An Incentive Stock Option is a special stock option granted to employees of a company as part of their compensation that has certain tax advantages.*

Tax Consequences: *In general, there is no tax under the regular tax system upon receipt of an Incentive Stock Option or upon exercise of the option. The Employee does not pay regular income tax until the stock is sold or transferred. If the stock is sold more than two years after the Incentive Stock Option is granted and one year after the Incentive Stock Option is exercised (the employee has held the actual stock for one year or longer), the employee receives the preferential long-term capital gains rate on the sale of the stock.*

Vesting: *Most companies require that employees work for a requisite period or meet certain performance goals before they are eligible for Incentive Stock Options. Once those requirements are satisfied, the options become "vested," regardless of whether or not he or she chooses to exercise any options.*

NON-QUALIFIED STOCK OPTIONS (NSO):

Definition: *A Non-Qualified Stock Option, also known as a non-statutory stock option, is another type of employee stock option granted by an employer. NSOs are simpler and more common than incentive stock options (ISOs).*

Tax Consequences: *With a Non-Qualified Stock Option (NSO) the employee pays ordinary income tax on the difference between the grant price and the price at which the option is exercised.*

Vesting: *Most NSOs are structured such that employees receive the right to purchase a certain number of shares of stock at a predetermined price. That option may be exercisable immediately, after the passage of a certain amount of time or upon the occurrence of a certain event.*

RESTRICTED STOCK:

Definition: *Restricted stock is acquired through an employee stock option plan or other private means and may not be transferred. Restricted stock may be forfeited if any of the SEC rules related to it are broken. The restriction usually lifts in 3 to 5 years when the stock vests. Some plans allow for restrictions to lapse gradually; while others provide that the restrictions will lapse all at once.*

Tax Consequences: *Employees can choose whether to be taxed when the restrictions lapse, in which case they will then pay ordinary income tax on the difference between the current price and anything they may have paid for the shares, or they can pay when the right is first granted by filing an 83(b) election. In that case, they pay tax on the difference (if any) between the current price and the purchase price at ordinary income tax rates, then pay capital gains tax when they actually sell the shares.*

Vesting: *The restricted period is referred to as the Vesting Period. Once the vesting requirements are met, an employee owns the shares of stock without restriction. Vesting periods may be time-based (a stated period from the grant date), or performance-based (often tied to achievement of corporate goals). Some plans allow for restrictions to lapse gradually; while others provide that the restrictions will lapse all at once.*

Any tax or legal information provided here is merely a summary of our understanding and interpretation of some of the current income tax regulations and is not exhaustive. Investors must consult their tax advisor or legal counsel for advice and information concerning their particular situation.

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