



## Stock option strategies

If you've got stock options, you're in more mixed company than you might think. Once a reward reserved for the highest-flying executives, options have become much more common in recent years, thanks in part to the growth of the high-tech sector and its bid to attract and retain highly educated and skilled employees. Companies are also offering options to more employees in an effort to align the interests of employees with those of shareholders.

According to Thane Stenner, first vice-president with CIBC Wood Gundy in Vancouver, and author of *True Wealth: An Expert Guide for High-Net-Worth Individuals (and Their Advisors)*, the entry point for employees receiving stock options has been dropping.

"The National Center for Employee Ownership figures that U.S. employees own, or have the option to own, over \$800 billion in stock," reports Stenner, adding that a 2000 study of 1,300 companies by global consulting firm Watson Wyatt found the "average lowest salary" at which employees receive options is \$58,100.

"All in all, that's quite a trend," he observes.

### **HOW MUCH ARE YOUR OPTIONS WORTH, AND WHEN SHOULD YOU CASH THEM IN?**

Your stock option benefit is calculated as the difference between the exercise price (i.e. the share purchase price) of the options and the fair market value of the share on the day you exercise the options (i.e. the day you purchase the shares).

This amount, if any, is taxed as an employment benefit – regular income and not capital gains, even though you don't receive any proceeds until you sell the shares. However, if you meet certain requirements, you can





claim a deduction equal to half of the benefit so that only 50 per cent of its value is taxed, much like a capital gain.

While it might be tempting to exercise your options almost as soon as you get them, often you are better advised to bide your time.

“Most options have a considerable shelf-life – five to 10 years is common – and statistically speaking, the longer you hold them, the more your potential for gain,” according to Stenner.

On the other hand, don't be greedy. When company stock takes flight, you may be tempted to hang on longer than you should, hoping the upward trend will continue – only to find yourself still hanging on when the stock takes a dive.

Beware of situations where you exercise your options (i.e. acquire the shares) but don't immediately sell the shares, as the consequences can be quite severe if their value declines after acquisition. Not only will you be taxed on the difference between the exercise price and the share price at acquisition, but also the capital loss triggered on the sale can only be used to offset other capital gains – it cannot be used to offset the employment benefit included in income. This could potentially leave you with a significant tax liability that you will have to pay using other funds.

If you have a significant number of options, your best bet is to consult your financial advisor about exercising them in the most profitable, tax-effective manner.

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