



Farther

INTELLIGENT WEALTH STRATEGIES: EQUITY COMPENSATION PLANNING

EQUITY COMPENSATION PLANNING

RSU vs. ISO: The Decision Tree.

Two kinds of equity compensation, taxed in almost opposite ways: a practical guide to managing whichever one you have.

01 How each is taxed

02 Concentration risk

03 Vest, assess, diversify

04 The AMT in numbers

05 Tools we use

INTRODUCTION

Same word, “equity comp,” almost opposite tax rules.

Restricted stock units and incentive stock options both show up on an offer letter as “equity.” In practice, the IRS treats them so differently that a strategy built for one can be actively costly applied to the other.

RSUs are taxed the moment they vest, whether you sell or not. There's no election to make and not much to plan around beyond what happens after. ISOs are the opposite: no regular income tax at exercise, but a separate tax system, the Alternative Minimum Tax, can trigger a real cash tax bill on paper gains you haven't actually realized yet.

Get the two confused, and you either sell too early on the asset that rewards patience, or hold too long on the one that doesn't care.

This guide walks through how each is actually taxed, the concentration risk they share, and the framework we use with clients to decide what to do and when.

PART ONE

How each is actually taxed.

RESTRICTED STOCK UNITS

Taxed at vest

- Ordinary income tax applies the moment shares vest, based on the share price that day, regardless of whether you sell
- Your employer typically withholds shares to cover taxes, often at a flat statutory rate that can undershoot your real bracket
- Once vested, any further gain or loss is a normal capital gain: short-term if sold within a year of vesting, long-term after

No election, no exercise decision. The only real choice is when to sell what's already yours

INCENTIVE STOCK OPTIONS

Taxed at exercise (maybe) and sale

- No regular income tax when you exercise, but the “bargain element” (spread between strike and market price) can trigger Alternative Minimum Tax
- Hold the shares more than one year after exercise and two years after grant, and the entire gain qualifies for long-term capital gains rates
- Sell sooner and it becomes a “disqualifying disposition,” taxed partly as ordinary income

The exercise decision is the whole ballgame. Get the timing wrong and AMT can create a cash tax bill before you've sold a single share

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The RSU question is almost always ‘when do I sell.’ The ISO question is almost always ‘do I exercise, and with what cash.’ Confusing the two is where most of the expensive mistakes happen.”

PART TWO

The risk they both create: concentration.

Whichever kind you have, the end state looks the same: a growing pile of stock in the one company you already depend on for a paycheck. If that company has a bad year, your income and a chunk of your net worth take the hit at the same time.

What tax-aware diversification actually means

The instinct to “just sell it all the day it vests” avoids concentration risk but ignores the tax bill you're creating by selling short-term. The instinct to “never sell, I believe in the company” solves nothing and just lets the concentration grow. Tax-aware diversification sits between the two: systematic, planned selling that spreads gains across tax years and holding periods rather than reacting to either extreme.

For employees at public companies with material nonpublic information exposure, a 10b5-1 trading plan (set up in advance, during an open window, with predetermined sale rules) lets selling continue on autopilot even during blackout periods, without the appearance of trading on inside information.



A PRACTICAL RULE OF THUMB

10–15%

of total investable net worth

We generally encourage clients to keep any single employer's stock under roughly 10–15% of total investable net worth once other goals are funded. This is not a hard rule, but as a starting point for a conversation about how much company-specific risk actually makes sense next to everything else you're building.

THE FRAMEWORK

Vest, assess, diversify.

The same three-step sequence applies whether you're holding RSUs, ISOs, or both. Only the specifics inside each step change.

01

Know what you're actually holding

Grant type, vesting schedule, strike price (for ISOs), and current concentration as a percentage of your total net worth. Before any decision, we build the full picture. Most clients are surprised how much of their balance sheet is one ticker.

02

Model the tax consequence before acting

For RSUs, that means checking whether your withholding actually covers your real bracket. For ISOs, that means running an AMT projection before exercising, not after, when the bill has already arrived.

03

Diversify on a schedule, not a feeling

A pre-set selling plan (by calendar, by concentration threshold, or by 10b5-1 plan) takes the emotion out of “is this the right time to sell” and replaces it with a rule you decided on when you were thinking clearly. Once trading restrictions lift, the plan can lean on more than a straight sale: a collar to protect the position while it sells down gradually, an exchange fund for a position too large to unwind quickly, or shares routed to a donor-advised fund instead of cash for giving you were already planning.

SEEING IT IN NUMBERS

Why the AMT catches people by surprise.

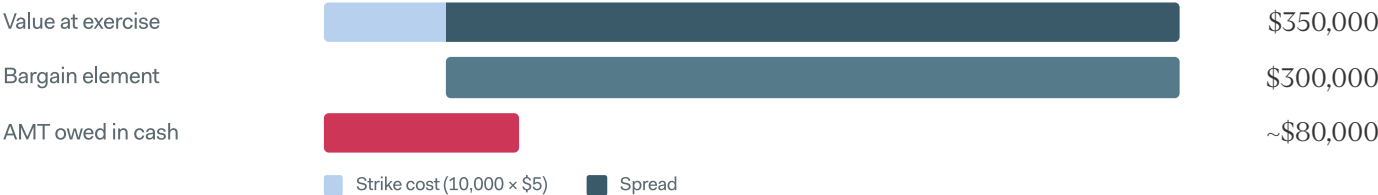
This is the single most common ISO planning mistake we see: exercising a large block early in the year without checking the AMT impact first.

ILLUSTRATION: HYPOTHETICAL, FOR EDUCATION ONLY

A hypothetical employee exercises 10,000 ISOs with a \$5 strike price when the stock is trading at \$35, and holds the shares rather than selling.

MEASURE	VALUE
Shares exercised	10,000
Strike price	\$5.00
Fair market value at exercise	\$35.00
AMT “bargain element” (the spread, taxed for AMT purposes)	\$300,000
Illustrative AMT owed, no shares sold to cover it	~\$80,000

From paper gain to cash bill



That AMT bill is often payable in cash the following April, on stock the employee still owns and hasn't sold. It isn't a reason to avoid ISOs. It's a reason to run the projection before exercising, and to plan for the cash (or a partial “exercise-and-sell-to-cover”) rather than being surprised by it.

TOOLS WE USE

The mechanics worth knowing.

10b5-1 trading plans

Pre-scheduled sales set up during an open window, executed automatically. This removes timing risk and blackout-period restrictions from the diversification plan.

Qualifying disposition timing

Holding ISO shares past the one-year (from exercise) and two-year (from grant) marks converts the whole gain to long-term capital gains treatment.

Collar strategies

An options overlay that limits how far a concentrated position can fall in exchange for capping some of the upside. It's a way to stay invested and protected while a sale plan runs its course.

AMT credit tracking

AMT paid on an ISO exercise often generates a credit usable in future years when regular tax exceeds AMT. Tracking it prevents leaving money on the table.

Exercise-and-sell-to-cover

Selling just enough shares at exercise to cover the tax bill: a middle path between exercising with outside cash and selling the entire position immediately.

Exchange funds

For a position too large to sell down quickly without moving the stock or the tax bill, pooling shares into an exchange fund can diversify exposure without a taxable sale, typically with a multi-year lockup of its own.

How Farther helps

Equity compensation planning is one of our four core focus areas, and it's rarely a one-time conversation. Vesting continues, strike prices and 409A valuations change, and tax law shifts. We build your equity position into the same plan as everything else, model the AMT and diversification impact before you act, and coordinate directly with your CPA when a decision has tax-return consequences.

“Ready to talk through your situation? No obligation, no commitment, just a conversation about where you are and whether Farther is a fit.”

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Important information

FIGURES CURRENT AS OF EARLY 2026

AMT exemption amounts and phase-out thresholds are set by statute and indexed for inflation. Confirm current figures with your CPA before acting. This guide does not update automatically as limits change.

HYPOTHETICAL ILLUSTRATION

The example on page 6 of this guide is hypothetical and for educational purposes only. It is not a projection or recommendation for any individual, and actual results depend on your specific tax situation.

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