Compensation Concepts: Employee Stock Purchase Plans

Compensation Concepts adds clarity to complex compensation issues, helping advisors guide clients toward smarter decisions.

Authors	Date	Topic
Holly Swan	12/18/2025	Tax: Compensation Concepts

Employee Stock Purchase Plans

An employee stock purchase plan (ESPP) is a company-run program that allows certain employees to purchase shares of their employer's stock, often at a discounted price. It's a benefit designed to encourage employees to become shareholders and share in the company's success they contributed toward.

Employees choose whether to participate in the plan and how much of their paycheck they want to contribute (subject to certain limitations). That amount is deducted from their paycheck over a set period, called the offering period. At the end of the offering period, the accumulated funds are used to buy company stock at a discount of up to 15% off the market price. Some plans even use a lookback provision, under which the discount is applied to the stock price at the beginning or end of the offering period—whichever is lower. Once purchased, the shares belong to the employee. They can hold, sell, or transfer their shares, depending on the plan rules.

Generally, employees are taxed on any stock purchased through an ESPP in the year in which the stock is sold. Sales are treated as either qualifying or disqualifying dispositions, depending on how long the stock was held, and are taxed as follows:

Qualifying dispositions

If shares are held for at least one year from the date of purchase and two years from the offering/grant date (the date on which the employer allows ESPP payroll contributions to start), the sale is considered a qualifying disposition and taxed as follows:

- **Ordinary income, at the lessor of one of the following:**
  a) the discount offered on the stock's grant date (discount percent multiplied by the grant date fair market value)
  b) the actual gain (sale price – purchase price)
- **Long-term capital gains** for additional gains

Disqualifying dispositions

If shares are sold before the qualifying disposition holding period requirements are met, the sale is considered a disqualifying disposition and taxed as follows:

- The discount based on the stock's value at purchase is taxed as **ordinary income**.

- The difference between the sale price and the stock's value at purchase is treated as **capital gains/losses**.

Given the potential double benefit of discounted shares and preferential tax treatment, ESPPs can be a considerable benefit for eligible employees.

ALL-12112025-tjr83stg

Allspring Global Investments does not provide accounting, legal, or tax advice or investment recommendations. Any tax or legal information on this page is merely a summary of our understanding and interpretations of some of the current income tax regulations and is not exhaustive. Investors should consult their tax advisor or legal counsel for advice and information concerning their particular situation.