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SITG No. 207

Taxability of ESOP on Proportionate basis



Employee Stock Ownership Plans

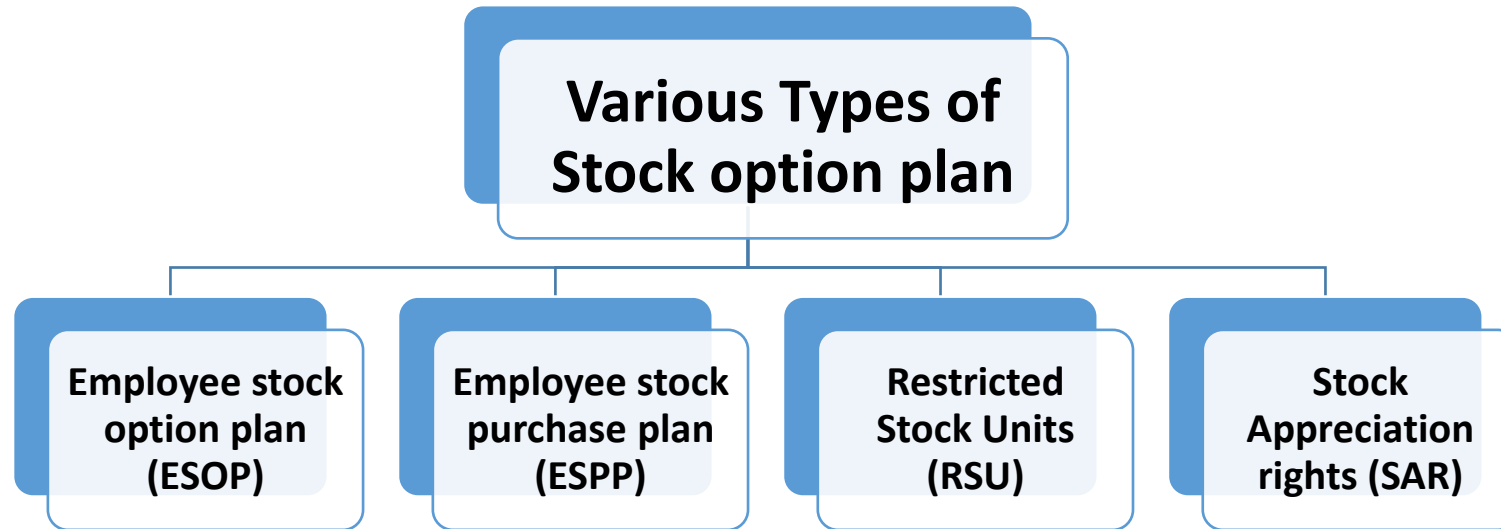
ESOP/ RSU granted to an employee who has worked in different countries during vesting period shall be taxed in different countries on proportionate basis.

25.05.2024



Introduction of Employee Stock Option Plan (ESOP)

ESOP is an employee benefit plan offers securities to an employee at free of cost or at a concessional rate. ESOPs are offered by employers as an award to employees and it acts as a motivational tool for employee. It is taxable as a perquisite under Income tax Act by considering difference between fair market value on exercise date and exercise price paid, if any, by employee in the year in which the securities have been allotted to the employee i.e. when stock option plan are exercised by the employee.



Issues in Cross Border ESOP

For granting ESOP It is not necessary to have direct employer – employee relationship that means foreign companies can grant ESOP to employees of their subsidiaries companies. Further, while working in MNCs employees may migrate in different countries for deputation or secondment basis for work in that case employee becomes resident in more than one country. So, the residential status at the time of grant of ESOP and the time of exercise of ESOP may differ and the ultimate residential status need to be examined by applying Tie-breaker rule as per tax treaty. Therefore, in such cases ESOP are taxable as perquisites (difference between fair market value on exercise date and exercise price paid by employee) in the country on the basis of number of days of services rendered in the country at the time of exercise of option i.e. on proportionate basis [as prescribed in circular of Income tax].

As per the OECD model tax convention relating to taxation of stock option income derived by employee from employment exercised in more than one country which provides employment benefit attributable to the stock option should be considered to be derived from a particular country in proportion of the number of days during which employment has been exercised in that country to the total number of days during which the employment services from which the stock option is derived is exercised.

Fringe Benefit Tax (FBT) or Perquisite

CBDT issued circular No. 9/2007 in relation to Fringe tax benefit arising on allotment or transfer of specified security.

An employer is liable to pay Fringe Tax benefit in respect of fringe benefits provided or deemed to have been provided by it to its employees, directly or indirectly during the previous year.

Where an employee was deputed to any other country for work purpose during the vesting period i.e. employee resides in India only part of vesting period then the proportionate amount of value of the fringe benefit will be liable to FBT. The proportionate amount shall be determined by applying to the value of the fringe benefit (fair market value of shares on the vesting date as reduced by the amount actually paid by employee). The proportion is the period of stay in India by employee during the vesting period in relation to total vesting period.

Now let's discuss the same with an example



Example

P Ltd.
Parent Company in INDIA



Mr. A
employee of P Ltd.

Grant 1000 shares in May 2021 at Rs. 30 each
Vesting period- 3 years
Exercise date -April 2024



Migrated to UAE
subsidiary company
on deputation basis in
April 2023 and resides
there till May 2024

S Ltd.
Subsidiary company in UAE



On the exercise date fair market value of share is Rs.150 per share. Further on the exercise date Mr. A resides in Dubai so value of perquisite of Rs.120000 (1000*120) will be taxed in both countries India and UAE in the proportionate basis on the services rendered in country

Taxable value of perquisite in India- 80000
Taxable value of perquisite in UAE- 40000



Case laws related to cross border ESOPs

Anil Bhansali v. Income-tax Officer, Ward -12(2), Hyderabad

- ❖ Assessee is an individual and employee of Microsoft Corporation USA and stocks awards granted to assessee as per stock scheme of Microsoft USA.
- ❖ The stocks award granted to assessee amounting to Rs.1,49,80,713 and vested during the previous year 2006-07.
- ❖ Out of above total value of stocks granted an amount of Rs. 1.05 Crore computed by the assessee on the basis of period of services rendered in India was attributable to services rendered in India and balance amount for services rendered in USA.
- ❖ Further, the residential status of assessee was for the year under consideration was resident but not ordinary resident.
- ❖ Assessee received amount of Rs. 1,80,76,000 in India during the FY 2006-07 which was in the nature of remittance into India through banking channel.

- ❖ The Assessing officer contented that amount of Rs.1,80,76,000 received by the assessee which is more than the value of perquisite declared by the assessee has escaped assessment.
- ❖ Further, the stock option were treated as part of salary in the TDS Certificate issued in the Form 16 by employer for that reason it cant be concluded that entire stock amount is taxable in India.
- ❖ Employee derived income while working in two countries which provides employment benefit attributable to stock option plan considered in proportion of the number of days during which services rendered in that country to the total number of days employment from which stock option is derived.
- ❖ Therefore, without identify how much stock option plan is attributable to services rendered in India, then the entire amount cannot be made taxable only because the money received in India.
- ❖ For the year, assessee have residential status of RNOR only that potion of stock plan attributable to services rendered in India

Unnikrishnan V S v. Income-tax Officer, International Taxation 4(3)(1) Mumbai

Reference Link- [Click Here](#)

Our Comments

Thus, while exercising any option of stock option it is important to note that if you are employed in India at the time of exercise of option but were in different countries during the vesting period, it may happen that the employer might deduct TDS on entire stock options exercised by you and show the same in Form 16. Accordingly it will be important to disclose only the proportionate of the amount to tax if you are not an ordinary resident in India.

Further, one need to carefully think as to how they would offer only the proportionate i.e. for the period when they were in India as the entire perquisite would be offered in Form 16 and if gross salary is shown less than the salary offered in Form 16 then CPC either could claim such Income tax return as defective or ask to offer additional income.

Hence, one could think of reducing such perquisite by way exemption if it is already included in Form 16 by employer as employer also has to deduct TDS at the time of payment of perquisite.

Also, one might have to also file return in all the country where he stayed as the stock option needs to be offered to tax proportionately in the country where employment was exercised during the vesting period.

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