TAXATION OF SWEAT EQUITY SHARES

As per Section 17(2)(vi) of Income-tax Act, 1961:

- the ***value*** of
- any ***specified security*** or
- ***sweat equity shares***
- allotted or transferred,
- by the employer, or former employer,
- free of cost or at concessional rate
- to the employee

is taxable as perquisite.

Notes :

(1) ***"specified security"*** means the securities as defined in Section 2(h) of the Securities Contracts (Regulation) Act, 1956 and, where employees' stock option has been granted under any plan or scheme therefor, includes the securities offered under such plan or scheme.

As per Section 2 (h) of the Securities Contracts (Regulation) Act,1956, ***"Securities"*** include :

(i) ***Shares***, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(ii) Government securities;

(iii) Such other instruments as may be declared by the Central Government to be securities; and

(iv) Rights or interest in securities.

(2) ***"sweat equity shares"*** means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

(3) the ***"value"*** of any specified security or sweat equity shares shall be the **fair market value** of the specified security or sweat equity shares, as the case may be, on the date on which the **option** is exercised by the assessee as reduced by the amount actually paid by, or recovered from the assessee in respect of such security or shares.

(4) ***"option"*** means a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price.

(5) ***"fair market value"*** means the value determined in accordance with the method as may be prescribed*.

*CBDT Vide its Notification No. 94/2009/ F.No.142/25/2009-S O (TPL), dated 18-12-2009 has introduced Income-tax (Thirteenth Amendment) Rules, 2009 wherein CBDT has provided Rule 3(8) for determination of FMV for the purposes of Section 17(2)(vi) which is discussed in simple language as under :

❖ <u>Determination of FMV for the purposes of Section 17(2)(vi) : Rule 3(8)</u>

(I) For the purposes of Section 17(2)(vi), the ***FMV*** of any ***<u>equity share</u>*** in a company, on the date on which the option is exercised by the employee, shall be determined as follows :

(a) <u>If share of the company is listed only on one recognized stock exchange</u> :

Average of the ***opening price*** and ***closing price*** of the share on the date on which the option is exercised by the employee.

(b) <u>If share of the company is listed on more than one recognized stock exchange</u> :

Average of opening price and closing price of the share on the recognised stock exchange which records the highest volume of trading in the share on the date on which the option is exercised by the employee.

(c) <u>If share of the company is listed only on one recognized stock exchange and there is no trading in the share</u> :

The closing price of the share on a date closest and immediately preceding to the date of exercising of the option by the employee.

(d) <u>If share of the company is listed on more than one recognized stock exchange and there is no trading in the share</u> :

The closing price of the share on a recognised stock exchange, which records the highest volume of trading in such share, on a date closest and immediately preceding to the date of exercising of the option by the employee.

<u>Notes</u> :

(1) ***Opening price*** of a share on a recognised stock exchange on a date shall be the price of the first settlement on such date on such stock exchange. However, if the stock exchange quotes both buy and sell prices, the opening price shall be the sell price of the first settlement.

(2) ***Closing price*** of a share on a recognised stock exchange on a date shall be the price of the last settlement on such date on such stock exchange. However, if the stock exchange quotes both buy and sell prices, the closing price shall be the sell price of the last settlement.

(e) <u>If share in the company is not listed on a recognised stock exchange</u> :

The FMV shall be such value of the share in the company as determined by a ***merchant banker*** on the ***specified date***.

(II) For the purposes of Section 17(2)(vi), the ***FMV*** of any specified security, ***<u>not being an equity share</u>*** in a company, on the date on which the option is exercised by the employee, shall be such value as determined by a ***merchant banker*** on the ***specified date***.

<u>Notes</u> :

(1) ***Merchant banker*** means Category I merchant banker registered with Security and Exchange Board of India established under Section 3 of the Securities and Exchange Board of India Act, 1992.

(2) ***Specified date*** means :

i) the date of exercising of the option; or

ii) any date earlier than the date of the exercising of the option, not being a date which is more than 180 days earlier than the date of the exercising.