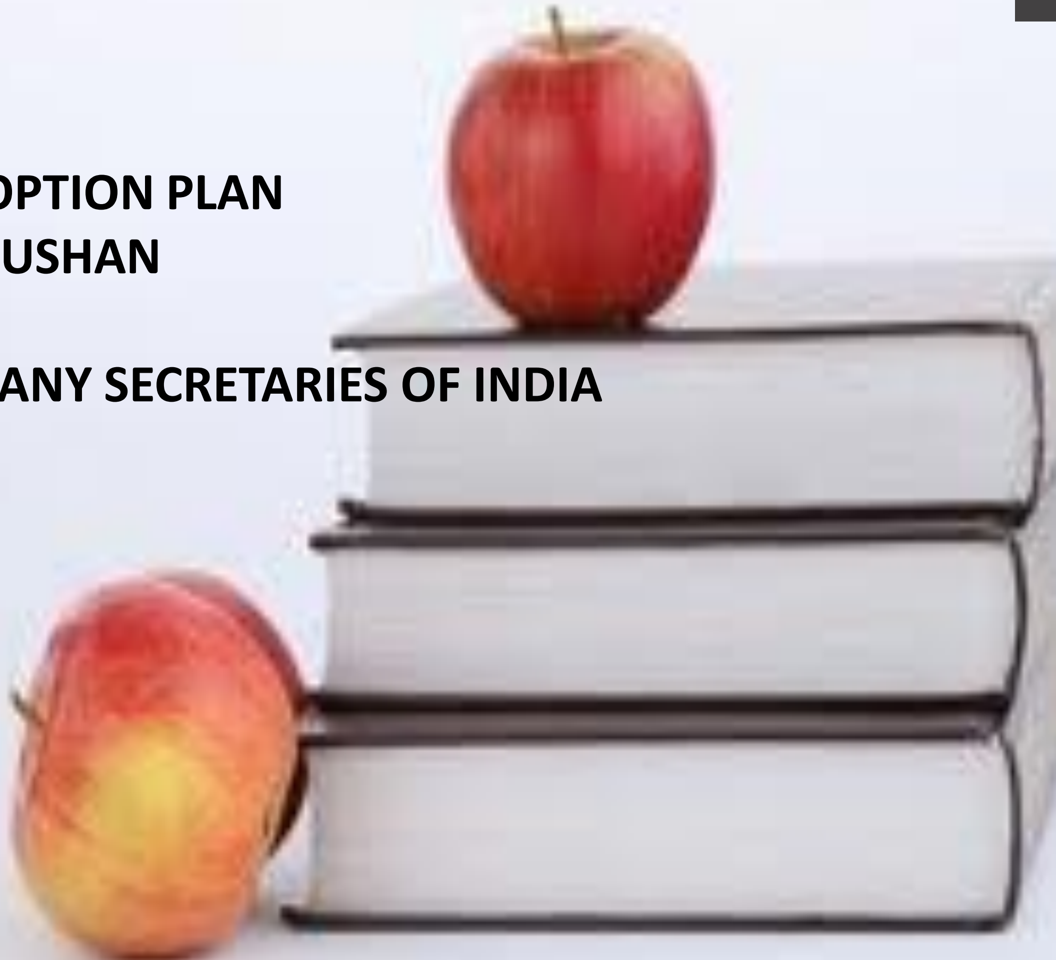
taxpert

EMPLOYEES STOCK OPTION PLAN
BY CA.SUDHA G. BHUSHAN
26th Oct 2012
INSTITUTE OF COMPANY SECRETARIES OF INDIA



TAXPERT PROFESSIONALS

Index

- Foreign Exchange Management Act , 1999
- Taxation Provisions
- International Financial Reporting System [IFRS]

FOREIGN EXCHANGE MANAGEMENT ACT, 1999

TAXPERT PROFESSIONALS

taxpert

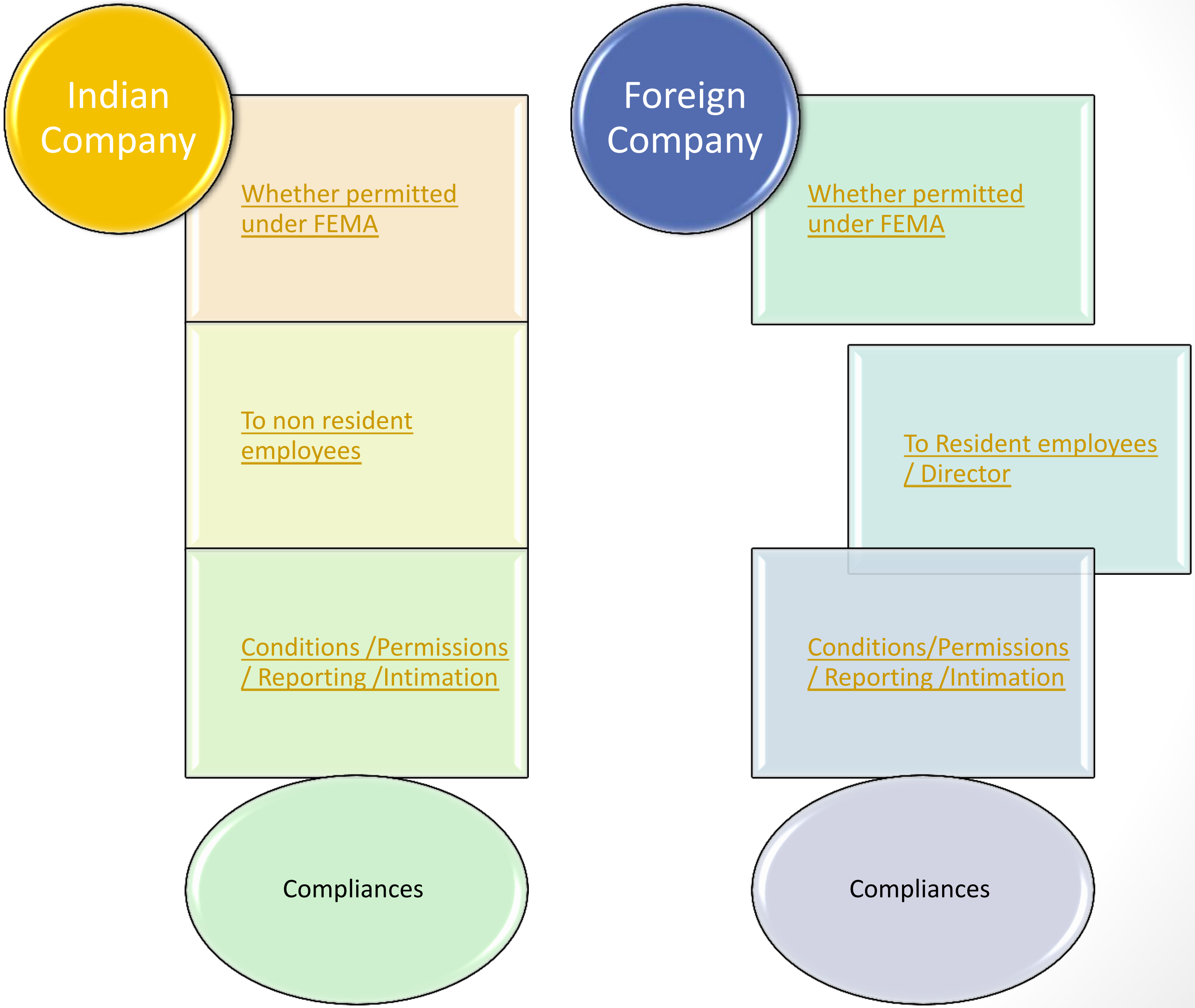
Governing Regulations

Foreign Exchange Management (Transfer or issue of security by a person resident Outside India) Regulation, 2000

Master Circular on Direct Investment by Residents in Joint Venture (JV)/ Wholly Owned Subsidiary (WOS) Abroad

Master Circular on Miscellaneous Remittances from India – Facilities for Residents

TAXPERT PROFESSIONALS


Indian Company
Whether permitted under FEMA
To non resident employees
Conditions /Permissions / Reporting /Intimation
Compliances
Foreign Company
Whether permitted under FEMA
To Resident employees / Director
Conditions/Permissions / Reporting /Intimation
Compliances

- Foreign investment in India is governed by sub-section (3) of Section 6 of the Foreign Exchange Management Act, 1999 read with Notification No. FEMA 20/2000-RB dated May 3, 2000 Foreign Exchange Management (Transfer or issue of security by a person resident Outside India) Regulation, 2000, as amended from time to time.
- As per the above mentioned notification Issue of shares under Employees Stock Options Scheme to persons resident outside India is permitted subject to conditions as prescribed.

Directly or Through Trust

An Indian Company may issue shares under ESOPs to

- its employees or
- employees of its joint venture or wholly owned subsidiary abroad who are resident outside India,
- other than to the citizens of Pakistan.
- Citizens of Bangladesh can invest with the prior approval of the FIPB.

TAXPERT PROFESSIONALS

Conditions

a) the scheme has been drawn in terms of regulations issued under the **Securities Exchange Board of India Act, 1992**; and

b) face value of the shares to be allotted under the scheme to the non-resident employees does not exceed **5% of the paid-up capital** of the issuing company.

The issuing company shall furnish to the Reserve Bank , **within thirty days** from the date of issue of shares under the scheme, a report giving the following particulars/documents, -

1. Names of persons to whom shares are issued under the scheme and number of shares issued to each of them;
2. a **certificate from the Company Secretary** of the issuing company that the value of shares issued under the scheme does not exceed 5% of the paid up capital of the issuing company and that the shares are issued in compliance with the regulations issued by the SEBI in this behalf.

At the time of conversion of options into shares the Indian company has to ensure reporting to the Regional Office concerned of the Reserve Bank in form FC-GPR, within 30 days of allotment of such shares. However, provision with regard to advance reporting would not be applicable for such issuances.

Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004,

taxpert

- Section 6 of the Foreign Exchange Management Act, 1999 provides powers to the Reserve Bank to specify, in consultation with the Government of India the classes of permissible capital account transactions and limits up to which foreign exchange is admissible for such transactions.

- Section 6(3) of the aforesaid Act provides powers to the Reserve Bank to prohibit, restrict or regulate various transactions referred to in the sub-clauses of that sub-section, by making Regulations.

- In exercise of the above powers conferred under the Act, the Reserve Bank has in supersession of the earlier Notification No.FEMA19/RB-2000 dated 3rd May 2000 and subsequent amendments thereto, issued Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 vide Notification No. FEMA 120/RB-2004 dated July 7, 2004.

- The Notification seeks to regulate acquisition and transfer of a foreign security by a person resident in India i.e. investment by Indian entities in overseas joint ventures and wholly owned subsidiaries as also investment by a person resident in India in shares and securities issued outside India.

General permission has been granted to a person resident in India who is an individual

Stock Appreciation Rights

taxpert

- To acquire shares under cashless ESOP issued by a company outside India

Provided it does not involve any remittance from India

- To purchase equity shares offered by a foreign company under its ESOP Schemes, if he is an employee, or, a director of an Indian office or branch of a foreign company, or, of a subsidiary in India of a foreign company, or, an Indian company in which foreign equity holding, either direct or through a holding company/Special Purpose Vehicle (SPV) irrespective of the percentage of the direct or indirect equity stake in the Indian company.

TAXPERT PROFESSIONALS

Conditions

(i) the shares under the ESOP Scheme are offered by the issuing company globally on a uniform basis, and

(ii) an Annual Return (Annex B) is submitted by the Indian company to the Reserve Bank through the AD Category – I bank giving details of remittances / beneficiaries.

taxpert

- A person resident in India may transfer by way of sale the shares acquired

Proceeds to be repatriated immediately on receipt thereof and in any case not later than 90 days from the date of sale of such securities.

TAXPERT PROFESSIONALS

Foreign companies are permitted to repurchase the shares issued to residents in India under any ESOP Scheme provided

- The shares were issued in accordance with the Rules / Regulations framed under Foreign Exchange Management Act, 1999
- The shares are being repurchased in terms of the initial offer document, and
- An annual return is submitted through the AD Category – I bank giving details of remittances / beneficiaries, etc.

Master Circular on Miscellaneous Remittances from India – Facilities for Residents

- Resident individuals who are either employees or director of an Indian office or branch of a foreign company in which foreign holding is not less than 51 per cent are permitted to acquire foreign securities under ESOP Scheme without any monetary limit.
- They are also permitted to freely sell the shares provided the proceeds thereof are repatriated to India.

taxpert

GENERAL PERMISSION FOR INDIAN RESIDENTS

- Shares issued under **cashless scheme** of ESOP by a Foreign Company
- The following categories of persons
  - Employee / Director of Indian Office / Branch of Foreign Company
  - Employee / Director of subsidiary (at least 51% ?? &&##%%%) of a Foreign Company

  can Acquire shares in SPV / Step down subsidiary which owns shares of Indian company provided
  - Such shares should be issued globally on uniform basis
  - Annual Return to be submitted by the Indian Company (SPV / step down Indian subsidiary / Indian subsidiary) to the AD

taxpert

INCOME TAX ACT, 1961

TAXPERT PROFESSIONALS

Points of Taxation for Employees

Grant of options	At the time of Grant , taxable event does not arise
Vesting of options	At the time when the options are vested, Taxable Event does not arise
Exercise of options/Allotment of shares	Taxable Event (Taxable as Salary Income as **Perquisite**)
Sale of Shares	Taxable Event (Taxable as **Capital Gain**)

Perquisite

- Section 17(2)(vi)
- Value of Perquisite

Fair Market Value (FMV) - Exercise Price

- Taxable event :- Date of exercise

- ❖ Employer is required to withhold tax from the amount of perquisite ?
- ❖ Purchase of shares by Employer from Market / Fresh issue?
- ❖ Market price of share deductible expense?

Capital Gain

- Section 49(2AA)
- Value of capital Gain

  Difference between net consideration and FMV

- Taxable Event : Date of sale / disposal / transfer

TAXPERT PROFESSIONALS

LISTED COMPANY

Fair Market Value	Average High / Low of the Closing Prices at the Stock Exchange prevailing on the date of exercise
Capital Gain	Long Term : Exempt from taxation
	Short Term : Taxable at a flat rate of 10% plus securities Transaction Tax

UNLISTED COMPANY

Fair Market Value	FMV to be determined by a SEBI registered Category I Merchant Banker
	The FMV valuation should not be old by more than 180 days from date of exercise
Capital Gain	Long Term : Taxable at the rate of 20% after indexation benefits.
	Short Term : Taxable at the marginal rate of tax applicable to the concerned employee

taxpert

IFRS 2 : Share Based Payments

TAXPERT PROFESSIONALS

ACCOUNTING STANDARDS & GUIDELINES

Indian GAAP

- SEBI guidelines for listed companies
- Guidance accounting issued by ICAI (non mandatory)
- Intrinsic value method allowed with disclosures as per fair value method

IFRS

- IFRS 2 – **Share Based Payments** : Fair value method mandatory

IFRS 2 : Share Based Payments

A transaction in which the entity

a) Receives goods or services as consideration for **equity instruments** of the entity (including shares or share options), or

b) Acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price of the entity's shares or other equity instruments of the entity.

Equity instrument include share and share options

taxpert

Equity Settled Payment Transaction

- A share based payment transaction in which the entity receives goods or services as consideration for equity instruments of the entity.
- ESOPs

Cash Settled Payment Transaction

- A share based payment transaction on which the entity acquires goods or services by incurring a liability to transfer cash or other assets to the supplier of those goods or services for amounts that are based on the price (or value)of equity instruments (including share or share options) of the entity of another group entity.
- Share Appreciation Rights

Measurement of equity settled transactions

Can fair value of instruments granted be reliably measured

Yes

Measure at Fair Value

No

Measure at intrinsic equity instrument value

- Remeasure at each reporting period and settlement date
- Any change in intrinsic value to be recognised in Income Statement

Vesting Conditions

Market Based Vesting Conditions

- Included in FV of grant date.
- No periodic revision of vesting estimate

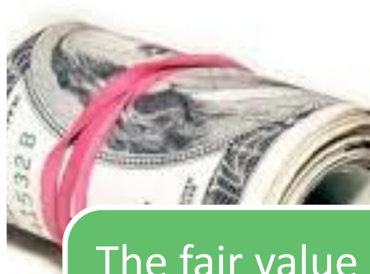
Non market based vesting conditions

- Not included in FV of grant date
- Revise vesting estimate periodically

Service Conditions |||| Performance Conditions

Measurement of cash settled SBP

At fair value of the liability incurred



The fair value of the liability is re measured at each reporting date until settlement date

Any changes in fair value recognized in Income Statement

Difference

Equity Settled SBP

- Transfer of equity instruments (EI)
- Accounting entry involves credit to share capital sooner or later
- Determination of FMV as on grant date
- Change in FV not to be accounted for at the end of each reporting period

Cash Settled SBP

- Creation of liability
- Accounting entry involves credit to liability account
- Determination of FV of liability at the end of reporting period
- Account for change in FV of liability on each reporting date through Statement of Comprehensive Income

taxpert

Thankyou for your kind attention

www.taxpertpro.com
sudha@taxpertpro.com ||sudhag999@gmail.com
09769134554 || 07738892291

TAXPERT PROFESSIONALS

Annex – B

ESOP Reporting

Statement of shares allotted to Indian employees / Directors under ESOP Schemes for the year ended March ________________
(to be submitted on the letterhead of the company through their AD bank)

We, ... (Indian company), hereby declare that:

a) M/s. .... (foreign company) has issued .... shares to our employees / Directors under ESOP Scheme during the year as under:
(i) No. of shares allotted :
(ii) Number of employees / Directors who accepted shares :
(iii) Amount of outward remittance (in FCY and equivalent INR, both):

b) The effective holding (direct or indirect) of the foreign company M/s. .... in the Indian company, as on March 31, ...(Year), is ....% and

c) The information furnished above is true and correct to the best of our knowledge and belief.

Signature of the Authorised Official :
Name :
Designation :
Date :

To,

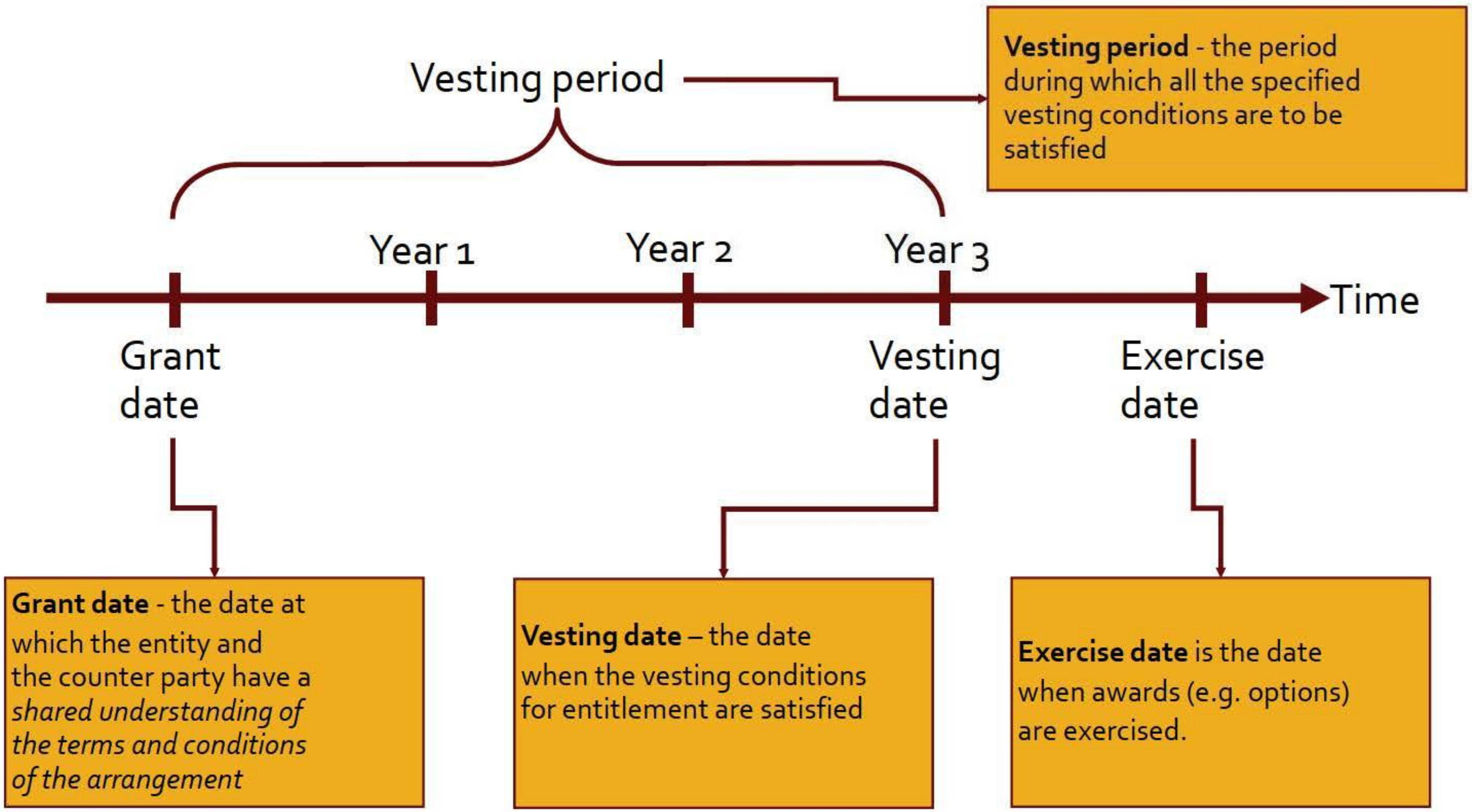
The Chief General Manager
Reserve Bank of India
Foreign Exchange Department,
Overseas Investment Division,
Central Office, Amar Bldg., 5th Floor,
Sir. P.M. Road, Fort, Mumbai 400 001.

individual may apply to the Reserve Bank for permission to acquire shares in a foreign entity offered as consideration for professional services rendered to the foreign entity and the Reserve Bank may, after taking into account certain factors, grant permission subject to such terms and conditions as are considered necessary	individuals to acquire shares of a foreign entity in part / full consideration of professional services rendered to the foreign company or in lieu of Director' s remuneration. The limit of acquiring such shares in terms of value shall be within the overall ceiling prescribed for the resident individuals under the Liberalized Remittance Scheme (LRS) in force at the time of acquisition.

Acquiring shares in a foreign company through ESOP Scheme

Regulation 22(2) of the Notification grants General permission to a resident individual to purchase equity shares offered by a foreign company under its ESOP Schemes, if he is an employee, or, a Director of an Indian office or branch of a foreign company, or, of a subsidiary in India of a foreign company, or, an Indian company in which foreign equity holding, either direct or through a holding company/Special Purpose Vehicle (SPV), is not less than 51 per cent.	It has now been decided that resident employees or Directors may be permitted to accept shares offered under an ESOP Scheme globally, on uniform basis, in a foreign company irrespective of the percentage of the direct or indirect equity stake in the Indian company subject to: ❖ the shares under the ESOP Scheme are offered by the issuing company globally on a uniform basis, and ❖ an Annual Return is submitted by the Indian company to the Reserve Bank through the AD Category – I bank giving details of remittances / beneficiaries, etc.

Accounting



Vesting period
Vesting period - the period during which all the specified vesting conditions are to be satisfied
Year 1
Year 2
Year 3
Time
Grant date
Vesting date
Exercise date
Grant date - the date at which the entity and the counter party have a *shared understanding of the terms and conditions of the arrangement*
Vesting date – the date when the vesting conditions for entitlement are satisfied
Exercise date is the date when awards (e.g. options) are exercised.