M2K GST ALERT

M2K Advisors

GST Implications on Employee Stock options

The media has recently been highlighting instances where GST Authorities are requesting assessee to provide details about Employee Stock Options (ESOPs) and Employee Share Purchase Plans. Such requests are often based on the legal structures of these ESOP plans, particularly when they involve the granting of options between a parent and subsidiary company.

In certain transactions, the ESOPs are issued to employees of an Indian subsidiary, and the vesting of shares is associated with the parent foreign company. The tax authorities argue that the responsibility of making available shares as per the employment terms vest with the Indian company, which is then fulfilled by the foreign counterpart. According to this perspective, the fulfillment activity carried out by the foreign company could be seen as an import of services from the foreign entity.

Similarly, in respect of other transactions such as vesting of Restricted stock units, Phantom Stocks and Stock appreciation rights, the GST Authorities have been taking a position that there are no shares which are vested to the employees. Since the exclusion provided under the definition of goods and services is only restricted to securities, payment of considerations under these plans which are also contingent upon achievements of various milestones will qualify as a service.

Legal framework

According to the GST Act, the supply of goods and services is subject to taxation. Anything classified as movable property falls under the category of goods, while any activity that doesn't involve the supply of goods is considered a service. Notably, securities as defined by the Securities Contracts (Regulation) Act (SCRA) are explicitly excluded from the definitions of both goods and services. Consequently, the issuance of securities falls outside the scope of GST.

However, complications arise when these securities are part of a broader underlying transaction and are viewed as a concurrent condition for another obligation. The question then arises whether the fulfillment of such obligations and the associated satisfaction should be treated as a distinct activity, subject to independent taxation. Additionally, when one party undertakes certain actions on behalf of another (for instance, a holding company agreeing to issue shares to an employee of its subsidiary at a discounted rate), the question emerges whether the act and subsequent payment/creation of provisions in accounting records could imply that the holding company is tolerating or consenting to perform an action on behalf of the subsidiary.

Schedule II of the CGST Act deems that agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act is a service. The scope of this entry is very wide and the GST Authorities construes that various Stock options would fall under this category.

Independently, the GST Act also deems that any service provided by an employee to its employer is not a supply for the purpose of the Act. Hence, the vesting of the stock options at the hands of the employees is not usually viewed as a transaction liable to be taxed in the employees' hands. However, if the vesting is undertaken by a third party and the truncation does not get the color of a salary payment and is viewed in any other prism, the GST Authorities takes a concurrent position that the transaction is not towards the service provided in the course of the employment by the employer directly.

In this backdrop, it is now crucial that all ESOP transactions structured in any form must be viewed very cautiously as in the majority cases, it is the way the schemes are structured which leads to differing interpretations between the tax authorities and taxpayers. Hence, it is of paramount importance to vet these structures/ schemes and also incorporate specific clauses to protect the interest of both the company and the employee.

Our Key Publications

M2K Advisors

- UAE KNOWLEDGE SERIES
- STARTUP SERIES IN INDIA
- SUCCESSION PLANNING SERIES
- SINGAPORE KNOWLEDGE SERIES
- USA ANNUAL TAX KNOWLEDGE SERIES
- INSIGHT ON UNION BUDGET 2023

livemint

- THE RULES FOR BUYING IMMOVABLE PROPERTY
- NORMS IMPLIED FOR OVERSEAS INVESTMENT

businessline

- DISCLOSURE OF LTCG IN ITR
- SHORT STAY EXEMPTION
- EXPECTATIONS POST FILING THE TAX RETURNS
- TAXATION OF COVID RELATED FINANCIAL RELIEF

Join our Mailing list to receive the latest alerts and updates. Do not miss out!

CLICK HERE / SCAN THIS TO SUBSCRIBE TO OUR ALERTS

Feel free to write us back your thoughts at knowledge@m2k.co.in

Office Address:

M2K Advisors LLP,
7th Floor, Briley One,
No. 30/ 64 Ethiraj Salai, Egmore,
Chennai – 600 008, Tamil Nadu, India
www.m2kadvisors.com

Reach us at:

mukesh@m2k.co.in;
rahul.jain@m2k.co.in;