

COURT DECISION - TREATMENT OF STOCK APPRECIATION RIGHTS (SARS) BY MOBILE EMPLOYEES

GLOBAL EQUITY UPDATE - INDIA



Ruling suggests place of services rendered and residential status during vesting period not relevant for determining tax position of Stock Appreciation Rights (SARs).

BACKGROUND

Two employees of an Indian subsidiary of a US company received SARS in the US company. The employees were non-residents in India during the vesting period of SARS; however they were residents in India at the time they exercised the SARS.

At the time of exercise, the Indian subsidiary treated the SARS as a perquisite and deducted tax at source. The taxpayers contested this position claiming that the award should not be taxable in India as salary income.

The Tribunal found in the first instance that the SARS are not capital assets and therefore, are taxable as salary income. Secondly, the SARS are fully taxable in India as the taxpayers were Indian residents at the time of exercise. This is in spite of the fact that the taxpayers were non-residents during the vesting period. Further information on the Tribunal's rulings are described below.

TRIBUNAL RULING

The Tribunal held that the SARS represent a perquisite or benefit in lieu of salary and that the amount received is taxable as salary income in India for the following reasons:

- a) SARS were given to the employees because of their employment with the Indian subsidiary. It was to encourage employees to perform well and as a result the Indian subsidiary would directly benefit from this and the US entity would indirectly benefit.
- b) SARS cannot be treated as a capital asset because the incentive was given to the taxpayers as compensation for services rendered to the Indian subsidiary. The employees were conferred with the right to receive the appreciation value and it did not represent a transfer of a capital asset or termination of any source of income.
- c) The taxpayers were resident in India at the time of exercise and therefore, their residential status during the vesting period of SARS is not relevant.

The Tribunal noted that the taxpayers had not submitted any material evidence to support the claim that the value of SARS suffered tax in the US. Hence, the Tribunal remitted this matter back to the Assessing Officer to examine whether the taxpayers had paid tax in the US on the SARS benefit as per the India-US tax treaty.

ACTION POINTS

- ✓ Companies need to ensure that appropriate planning measures are in place for mobile employees who receive SARS in a foreign parent of an Indian subsidiary to avoid double taxation.
- ✓ The employer may wish to obtain expert advice given that the particular features of each scheme/plan may impact the Indian tax position.

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