

Period of holding of ESOPs shall be counted from date of grant even assessee didn't have vesting rights

Summary – The Bangalore ITAT in a recent case of N.R. Ravikrishnan, (the Assessee) held that where assessee earned profit from transfer of ESOP options, in view of fact that said options provided valuable right to assessee to exercise and have allotment of shares, they constituted capital asset from date of grant itself and since consideration was paid to assessee after expiry of three years under option transfer agreement, profit in question was liable to tax as long-term capital gain

Facts

- The assessee was an employee of Infosys, BPO Ltd.. He was granted ESOP options by employee company. During relevant year, assessee filed his return declaring long-term capital gain arising on transfer of ESOP options.
- The Assessing Officer took a view that the period of holding of those options for computation of capital gains could not be counted from the date of grant of ESOP options as prior to the vesting date, the assessee himself could not have exercised any such right. Therefore, according to Assessing Officer the capital gains on transfer of ESOP options was to be regarded as short-term capital gain.
- The Commissioner (Appeals) confirmed the order passed by Assessing Officer.
- On second appeal:

Held

- On an appraisal of the material on record, it is not disputed that the assessee, an employee of Infosys BPO Ltd., was granted ESOP options, of which 6000 options were subsequently *vide* Option Transfer Agreement dated 7-2-2007 transferred to/bought back by Infosys Technologies Ltd., with Infosys BPO Ltd., as a confirming party. These 6000 options comprised of 1250 options granted on 28-2-2003; 2500 options granted on 2-2-2004 and 2250 options granted on 1-6-2005. The options granted on 28-2-2007 and 2-2-2004 were held for a period of more than 3 years before their transfer on 7-3-2007 and therefore the assessee treated the gains as 'LTCG' and claimed exemption under section 54EC of the Act. The Assessing Officer, however, held that the options have no value without their exercise and the gains derived by the assessee by transfer thereof, essentially represents the exercise by the assessee of the rights that the options had rendered to him. The Commissioner (Appeals) held that as prior to the date of vesting the assessee himself could not have exercised right, the gains were short-term in nature *i.e.*, 'STCG'.
- It is seen that both the authorities below have ignored the important fact that 3750 options were sold to Infosys Technologies Ltd., without any exercise of option. If ESOP options had been exercised, and the shares allotted thereby would have been sold after their allotment, then

undisputedly the gains arising therefrom would have to be treated as STCG. In the case on hand, however, the 3750 options have been transferred as such, without any exercise of options. In the absence of exercise of options, no shares were allotted to the assessee. It is a case of buy back of ESOP options by Infosys Technologies Ltd., with Infosys BPO Ltd., the assessee's employer, as a confirming party.

- It is not in dispute that ESOP options provided valuable right to the assessee to exercise and have allotment of shares and, thus they were 'capital asset' held by the assessee from the date of grant *i.e.*, 28-2-2003 and 2-2-2004 for which a consideration was paid to the assessee under the option Transfer Agreement. The contention that the assessee cannot exercise option in the absence of vesting is not relevant as the options were transferred without any exercise in the case on hand.
- In view of the facts and circumstances of the case, it is held that the capital gain arising from the transfer of 3750 options should be considered as LTCG. The Assessing Officer is accordingly directed.