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# VASAI BRANCH OF WIRC NEWSLETTER

June 2020



## CHAIRMAN'S COMMUNICATION

Dear Professional Companions,

"Seeds of faith are always within us; sometimes it takes a crisis to nourish and encourage their growth."

Our esteemed Institute of Chartered Accountant of India ("Institute") completes its 71 years of existence and it is a proud moment for all of us. The Institute is constantly innovating, upgrading and making itself enriched for all of us. In return, we as the members also have the responsibility, in fact duty towards our Institute and such responsibility can be shared if we take interest in Institutes various activities, interact

with each other and share our views.

1st July- Foundation Day was celebrated with lot of fanfare. Our branch has organized this time unique way to celebrate CA Day "VIRTUAL CA DAY CELEBRATION". In which we got more than 7,000 audience in virtual mode and 75 plus participants who have uploaded their videos.

With rapid recognition of growing pandemic COVID-19, the integrated and timely approach of Indian Government to encourage social distancing has continued to benefit the country. The countrymen tirelessly engaged in serving during these hard times deserve to be thanked.

With the ease and comfort that this home-stay comes up with, there arises a need to seek out and embrace the unfamiliar lifestyle in this sedentary state. It is therefore, necessary for all of us to stay motivated to be able to adapt to new way of living to achieve our personal, professional and social goals.

Where on one hand, social and physical contacts are absent; our Institute has been able to continue walking on the path towards and into the hearts of our various stakeholders with the use of various digital channels.

I pay my sincere thanks to the entire Vasai Branch Managing Committee Members, Past Chairperson and all coordinator for playing a key role in an digital ambit of sharing, participating and keeping in touch with the stakeholders to fulfil their requirements which are also our own top-most priorities.

Noteworthy initiatives have been taken by our team, have served in the welfare of our stakeholders and have been instrumental in winning the trust.

Hope you have a joyful journey reading this newsletter that will enhance your knowledge!

I look forward to your valuable suggestions and feedback. Feel free to interact with me at [vasaibranch@gmail.com](mailto:vasaibranch@gmail.com).

Wishing all of you a good health! Stay Safe, Stay Healthy, and take care.

With warm regards

**CA. Ankit Rathi**  
Chairman  
Vasai Branch of WIRC of ICAI

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## CONTENTS

Chairman's Communication .....	1
Photo - Hearty Congratulations to Winners in Quiz Competition - "Lockdown Champions" .....	2
Photo - Hearty Congratulations to Winners in WICASA Academic Quiz Competition - "Lockdown Champions" .....	2
Payment under protest under GST regime .....	3
Recorded Link of Virtual Meeting conducted by branch .....	6
GST on Director Remuneration .....	7
ESOP - Wanna Fly Together? .....	8
Photo - 5th Virtual CPE Meeting on Important provisions of Companies Act .....	10
Photo - 6th Virtual CPE Meeting on Important provisions of Companies Act .....	10
Photo - 7th Virtual CPE Meeting on Revised Code of Ethics .....	11
Photo - 9th Virtual CPE Meeting on RERA Opportunities for CA .....	11
Photo - 10th Virtual CPE Meeting on Impact of Covid 19 in Auditing Report .....	11
Photo - 11th Virtual CPE Meeting on Auditing Standard .....	12
Photo - 12th Virtual CPE Meeting on Equalization Levy on E Commerce .....	12



June 2020

## Hearty Congratulations to Winners in Quiz Competition - "Lockdown Champions" organized by Vasai Branch of WIRC from 21st April to 2nd May 2020



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## Hearty Congratulations to Winners in WICASA Academic Quiz Competition - "Lockdown Champions" organized by Vasai Branch of WIRC from 5th to 10th May 2020



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## Payment under protest under GST regime



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### A. Introduction

GST was introduced on 1 July 2017 and since then it has been evolving with each passing day through release of numerous notifications, circulars, advance rulings and various writ petitions. In the changing business scenarios and evolving GST law,

there is a high possibility that ambiguity may exist with regard to taxability of a transaction, valuation of a transaction, classification of goods / services under specific tariff heading, non-availability of an exemption and non-availability of Input Tax Credit (ITC) on certain procurements, etc. In order to avoid business exigencies, the taxpayer may want to pay GST / reverse ITC under protest without agreeing to the provisions contained in existing GST law. In this article, the author attempts to lay down the legal status of protest payments under the GST regime.

### B. What is payment under protest?

The term 'protest' means a statement or an action expressing disapproval of or objection to something. Under Indirect Taxes, the payment made under protest would mean deposit of tax with the government without agreeing to the quantum of deposit already made. Further, it would mean that the person depositing the amount under protest would want to litigate / to contest the subject matter due to which the protest payment is made before the appellate authorities. The following is a list (not exhaustive) of scenarios, where there could arise a need for a protest payment under GST regime –

- Determination of value of a transaction;
- Taxability of a transaction;
- Applicability of type of tax (CGST + SGST or IGST) on a transaction;
- Classification of goods/services under a particular tariff heading;
- Non-availability of a prescribed exemption to a particular transaction;
- Reversal of ITC under protest in respect of certain procurements;
- Protest payment of tax against the assessment order issued by the GST authorities;
- Protest payment against the order of National Anti-profiteering Authority;
- Protest payment against the show cause notice issued in lieu of an advance ruling filed by the applicant and which got decided against it;

- Protest payment of GST and penalty to release the goods detained due to E-way bill issues;

The advantage of paying tax under protest is dual. One, the taxpayer deposits the tax amount with the government and second is if the case is decided in favour of taxpayer, the tax paid under protest can be obtained as refund subject to the fact that the burden must not have been passed to the buyers i.e. doctrine of unjust enrichment is applicable to protest payment too.

### C. Legality of protest payment of duties / taxes

#### Under erstwhile Indirect Tax regime

The payment of duty under protest was a common phenomenon in respect of a transaction exigible to Excise duty. The taxpayers made the payment of duty under protest mainly due to disputes in valuation and classification of goods. Rule 233B of the erstwhile Central Excise Rules, 1944 specifically provided for the procedure to be adopted where the duty was paid under protest.

Like 233B of the erstwhile Central Excise Rules, 1994, there was no corresponding provision under the amended Central Excise Rules, 2002. However, the CBEC (now CBIC) had implicitly expressed about the procedure to be followed where duty was paid under protest in the Central Excise Manual. In the manual, a similar procedure as prescribed in Rule 233B of the Central Excise Rules, 1994 was mentioned. The same procedure was followed by the taxpayers for making protest payment under Customs Act, 1962 and under the Finance Act, 1994 (for service tax related issues). Further, the provisions related to refund of the duty paid under protest were provided in Section 11B of the Central Excise Duty, 1944 and Section 27 of the Customs Act, 1962.

#### Under GST regime

Under the GST regime, neither the provisions of the CGST Act, 2017 nor any CGST Rules, 2017 provides for payment of tax under protest. Further, as per the Frequently Asked Questions (FAQs) on GST dated 15 December 2018 (3rd edition) released by CBIC, the concept of payment of tax under protest is not recognized under the GST regime. The extract of **FAQ No. 55 to the Chapter 14 – Refunds of such FAQs** is re-produced as under –

**“Q. 55. Does GST law recognize the concept of payment of tax under protest? Ans. No”**

Concept of protest payment continues to prevail under the GST regime as well

In author's view, the concept of protest payment continues to remain under the GST regime as well on account of the following reasons –

- It is a fundamental right bestowed to every taxpayer by the Constitution of India.**

- Article 19(1) (a) of the Constitution of India provides that all citizens shall have the right of freedom of speech and expression. The freedom of speech and expression means the right to express one's convictions and opinions freely by word of mouth, writing, printing,





pictures or any other mode. The payment of tax under protest is nothing but an expression of one's opinion, which is covered under Article 19(1) of the Constitution of India.

- The deposit of GST under protest would mean challenging the issue on merits, which is a fundamental right of every assessee. The fundamental rights bestowed to a taxpayer cannot be taken away unless specifically restricted by the Constitution of India itself.
- If the GST authorities do not allow the deposit of GST under protest then it would lead to gross violation of principles of natural justice as laid down in **Article 14 of the Constitution of India**. The principle of natural justice implies a duty to act fairly. i.e. fair play in action. The ultimate aim of principle of natural justice is to prevent injustice. Such principles do not supplant the law but supplement it. It implies that every taxpayer is given a fair chance of being heard and present his case for defence.
- Given the existence of fundamental rights under the Constitution of India, in author's view, the taxpayer should be allowed to deposit GST under protest.

**b) The concept of making the protest payment exists vide provisions of Section 174 of the CGST Act, 2017**

- Section 6 of the General Clauses Act, 1897 contains the provisions for effect of repeal of any act. The relevant extract is re-produced as under –  
*6. Where this Act, or any Central Act or Regulation made after the commencement of this Act, repeals any enactment hitherto made or hereafter to be made, then, unless a different intention appears, the repeal shall not —*  
(a) .....  
(b) .....;  
(c) *affect any right, privilege, obligation or liability acquired, accrued or incurred under any enactment so repealed;*
- Further, it would also be relevant to refer to the provisions of Section 174 of the CGST Act, 2017. The relevant extract is re-produced as under –  
(1) ...  
(2) The repeal of the said Acts and the amendment of the Finance Act, 1994 (32 of 1994.) (hereafter referred to as "such amendment" or "amended Act", as the case may be) to the extent mentioned in the sub-section (1) or section 173 shall not-  
(a) ....  
(b) .....; or

- (c) affect any right, privilege, obligation, or liability acquired, accrued or incurred under the amended Act or repealed Acts or orders under such repealed or amended Acts:

- On a conjoint reading of Section 6 of the General Clauses Act, 1897 and Section 174 of the CGST Act, 2017, it appears that the right / privilege acquired under the law purported to be repealed i.e. Central Excise Act cannot be taken away unless specifically notified through any notification or amendment in the act in this regard.
- Given that no notification has been released for taking away such right / privilege, in author's view, the right of depositing GST under protest is not repealed and is saved under the provisions of Section 38A of the Central Excise Act, 1944 read with Section 6 of General Clauses Act, 1897 and Section 174(2) (c) of the CGST Act, 2017.
- Given the above, in author's view, the taxpayer can deposit GST under protest.

**c) Section 54 of the CGST Act, 2017 allows for refund of GST deposited under protest**

- Section 54(1) of the CGST Act, 2017 provides that –  
*"Any person claiming refund of any tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the relevant date in such form and manner as may be prescribed:*
- In author's view, the term 'any tax' used in the above provision would mean any or all of the following –  
a) Taxes paid by the taxpayer while filing monthly GST returns;  
b) Taxes paid due to an outcome of any adjudication order issued against the taxpayer;  
c) Excess Tax paid inadvertently;  
d) Taxes paid under wrong head;  
e) Taxes paid due to outcome of a ruling which is against the taxpayer;  
**f) Deposit of taxes under protest.**
- Further, there is neither any provision in sub-sections of Section 54 of the CGST Act, 2017 nor in Chapter XI (Refunds) to CGST Act, 2017, which restricts refund of GST deposited under protest. Accordingly, the refund of GST deposited under protest should be allowed to the person applying for the same provided the outcome of the protest lodged before appellate authorities is decided in favour of such applicant.
- Additionally, in author's view, if there exists a provision to claim refund of the GST deposited under protest then it implies that the taxpayer can deposit GST under



protest. Given that the GST payment is to be online and the returns are required to be filed online, the procedure to lodge a protest under GST regime is a subsequent question, which should be clarified by CBIC at the earliest. Until clarification is provided, in author's view, adherence to the following procedure would ensure a good tax practice –

- a) Disclose the details of GST to be deposited under protest as outward tax liability / disclose as other reversal of ITC. Such details should be disclosed in **GSTR-3B** only.
- b) Deposit the GST through normal payment procedure.
- c) File a letter with the GST range officer along with a copy of the challan, return copy in FORM GSTR-3B. Also, file a letter with the office of the Deputy Commissioner / Commissioner as the case may be.
- d) The letter should contain the following details –
  - i. Brief description of the supply involved;
  - ii. Reason for making the depositing GST under protest;
  - iii. Period to which the deposit of GST under protest pertains;
  - iv. Details of taxable value and GST deposited;
  - v. Challan Number;
- e) It is advisable to get the letter acknowledged from the range officer and keep a copy of the same in the records of the taxpayer.
- f) At the time of filing an appeal before the appellate authorities, the cognizance of the letter filed should be considered in the appeal.

Glaring examples of protest payment made under GST regime–

- a) In one of the press release hosted by a large private sector bank on its website, they had mentioned about their intention to pay GST under protest on domestic money transfer program. The GST deposited under protest was INR 38.04 crores.
- b) In the case of *K. G. Unnikrishnan vs Assistant State Tax officer - 2 018-VIL-620-KER*, it was held by the Hon'ble Kerala High court that the assessee can pay tax demand and penalty under protest to release the goods in case of detention.

#### **D. Who is eligible to claim refund of GST deposited under protest?**

On perusal of the provision contained in Section 54(1) of the CGST Act, 2017 (supra), one can construe that 'any person' can file a

refund claim under GST. In author's view, the refund application can be filed by both the supplier or by the recipient but not by both at the same time.

At this juncture, it would also be relevant to refer to the provisions of Section 54(8) of the CGST Act, 2017. The relevant extract is reproduced as under –

*(8) Notwithstanding anything contained in sub-section (5), the refundable amount shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to—*

- (a) ....
- (b) ....
- (c) ....
- (d) ....
- (e) *the tax and interest, if any, or any other amount paid by the applicant, if he had not passed on the incidence of such tax and interest to any other person; or*

On a conjoint reading of Section 54(1) and Section 54(8) of the CGST Act, 2017, one can construe that though the refund application can be filed either by the supplier or by the recipient, however, only the person who has not passed on the burden of taxes to any other person can claim it. For e.g. if the supplier of goods/service has deposited the tax under protest by collecting it from the recipient then the refund claim may not be sustainable for the supplier. In such a situation, the recipient can file a refund application and can succeed in obtaining the refund provided such recipient should not have passed on the burden.

#### **E. What is the time limit to file the refund application of GST deposited under protest?**

Every refund application must be filed before the GST refund authorities within the prescribed due date, else it would be time barred. Explanation 2 to Section 54 of the CGST Act, 2017 provides for the 'relevant date' within which a refund application is required to be filed.

It is a well-accepted fact that in case of protest payments, the right to file a refund application is crystallized only when the appellate authorities rules the case in favour of the person who has filed the protest.

In case of GST deposited under protest, it would be relevant to refer to clause (d) to Explanation 2 of Section 54 of the CGST Act, 2017 to determine the relevant date for filing the refund application. The extract is re-produced as under –

- (2) "relevant date" means – (a)....
- (b) ....
- (c) ....
- (d) *in case where the tax becomes refundable as a consequence of judgment, decree, order or direction of the Appellate Authority, Appellate Tribunal or any court, the date of communication of such judgment, decree, order or direction.*



On a conjoint reading of Section 54(1) of the CGST Act, 2017 (supra) read with Clause (d) to Explanation 2 of the Section 54 of the CGST Act, 2017, the relevant date to file a refund application in case of payment of tax made under protest would be before the expiry of two years from the date of communication of judgment, decree, order or direction.

#### **F. Whether the doctrine of unjust enrichment would apply to GST deposited under protest?**

Section 54(9) of the CGST Act, 2017 provides that –

*Notwithstanding anything to the contrary contained in any judgment, decree, order or direction of the Appellate Tribunal or any court or in any other provisions of this Act or the rules made thereunder or in any other law for the time being in force, no refund shall be made except in accordance with the provisions of sub-section (8).*

On perusal of the above provision, one can understand that the refund application would have to be filed by complying with the provisions of Section 54(8) of the CGST Act, 2017. In case of GST deposited under protest, clause (e) to Section 54(8) of the CGST Act, 2017 requires that the refund would be allowed if the applicant does not pass on the incidence of the tax to any other person.

Given the above, in author's view, it is clear that the doctrine of unjust enrichment would apply in case of GST deposited under protest too and it would be applicable to the applicant of refund application. In this regard, it would be relevant to refer to the decision ruled by the Hon'ble Supreme Court in the case of *Commissioner of Central Excise, Mumbai – II vs. Allied Photographics India Ltd. - 2004-VIL-01-SC-CE* wherein it was held that doctrine of unjust enrichment would be applicable to refunds of duty paid under protest.

Further, it must be noted that with regard to applicability of doctrine of unjust enrichment on protest payment, there are myriad of differing decisions ruled by various tribunals, various Hon'ble High courts and even Hon'ble Supreme court. Accordingly, the applicability of doctrine of unjust enrichment to protest payments can attract valid arguments from both the sides.

#### **G. Executive Summary and Conclusion**

The deposit of GST under protest should be allowed to be made by taking re-course to the fundamental rights available to a taxpayer.

Given that refund of GST deposited under protest is allowed, the deposit of GST under protest should be allowed.

While the fundamental rights can be enforced at any given point of time, however, in absence of specific provisions in GST law, the sustainability of GST deposited under protest would pose several issues especially when the payment is made online and the protest would be filed offline.

Prior to depositing GST under protest, it should be borne in mind by the taxpayer that he would have to deal with two types of litigation –

- Litigation for admissibility and sustainability of GST deposited under protest;
- Litigation for refund of GST deposited under protest.

The subject matter would also be prone to subjective interpretations that would be adopted by different officers and appellate authorities. A clarification by CBIC with regard to the procedure for depositing GST under protest is the need of the hour given that the assessments and department audits are going to commence soon.

#### **H. References**

- Study Paper on Unjust enrichment released by ICAI;
- CGST Act, 2017 and CGST Rules, 2017;
- 3rd edition of the FAQs dated 15 December 2018 released by CBIC (Page No 321);
- Central Excise Act, 1944;
- Central Excise Rules, 2002 and Central Excise Rules, 1944;
- Central Excise Manual;
- Press release by a private bank - <https://www.yesbank.in/media/press-releases/additional-payment-of-gst-under-protest>

[Date: 06.06.2020]

(The views expressed in this article are strictly personal)



### **Recorded Link of Virtual Meeting conducted by branch**

Virtual Meeting on Impact of Covid 19 in Auditing Report held on 23rd June 2020

<https://attendee.gotowebinar.com/recording/1968258162894759169>

Virtual Meeting on Auditing Standard held on 25th June 2020

<https://attendee.gotowebinar.com/recording/8620268326616742923>

Virtual Meeting on Equalization Levy on E Commerce held on 27th June 2020

<https://attendee.gotowebinar.com/recording/559999272086245644>



## GST on Director Remuneration



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### INTRODUCTION

Goods and Services Tax [GST] has been imposed on "supply of goods or services". That means for the purpose of imposition of GST there has to be supply, if there is no supply then no GST will be imposed. However government has specified the

certain activities in Schedule III which shall be treated neither as a supply of goods nor a supply of service. One of them is as under.

*"Services by an employee to the employer in the course of or in relation to his employment"*

Further GST shall be paid by forward charge (i.e. Supplier shall be liable to pay GST) or Reverse Charge (i.e. Receiver shall be liable to pay GST). Government has specified the certain goods & service, GST on which shall be paid by Reverse Charge (i.e. Receiver shall be liable to pay GST) one of them is as under.

*"Services supplied by a director of a company or a body corporate to the said company or the body corporate"*

Now before understanding the matter under the subject we need to know some definition of Director as per Company Act, 2013.

### DEFINITION

**Director:-** As per Section 2(34) of the Company Act, 2013 "Director" means a director appointed to the Board of a company.

**Managing director:-** As per Section 2(54) of the Company Act, 2013 "Managing director" means a director who, by virtue of the articles of a company or an agreement with the company or a resolution passed in its general meeting, or by its Board of Directors, is entrusted with substantial powers of management of the affairs of the company and includes a director occupying the position of managing director, by whatever name called.

**Whole-time director:-** As per Section 2(94) of the Company Act, 2013 "Whole-time director" includes a director in the whole-time employment of the company.

**Independent directors:-** The definition of "independent directors" under section 149(6) of the Companies Act, 2013, read with Rule 12 of Companies (Share Capital and Debentures) Rules, 2014 makes it amply clear that such director should not have been an employee or proprietor or a partner of the said company, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed in the said company.

### SUBJECT

Various doubts have been raised as to whether the remuneration paid by companies to their directors falls under the ambit of entry in Schedule III of the Central Goods and Services Tax Act, 2017 i.e. "services by an employee to the employer in the course of or in relation to his employment" or whether the same are liable to be taxed in reverse Charge i.e. "Services supplied by a director of a company or a body corporate to the said company or the body corporate".

### CLARIFICATION

In order to ensure uniformity in the implementation of the provisions of the law across the field formations, government has issued Circular No. 140/10/2020 Dt. 10th June, 2020 for Clarification in respect of levy of GST on Director's remuneration.

For the purpose of this matter company need to identify whether directors are employees of the company or not. To ascertain whether a director, irrespective of name and designation, is an employee or not, it would be pertinent to examine whether all the activities performed by the director are in the course of employer-employee relation (i.e. a "contract of service") or is there any element of "contract for service".

Sometime director who has also taken an employment in the company may be functioning in dual capacities, namely, one as a director of the company and the other on the basis of the contractual relationship of master and servant with the company, i.e. under a contract of service (employment) entered into with the company.

Further treatment of the Director's remuneration is also present in the Income Tax Act, 1961 wherein the salaries paid to directors are subject to Tax Deducted at Source ('TDS') under Section 192 of the Income Tax Act, 1961 ('IT Act'). However, in cases where the remuneration is in the nature of professional fees and not salary, the same is liable for deduction under Section 194J of the IT Act.

### CONCLUSION

#### ***If Directors are not an employees of the Company:-***

In respect of such directors who are not the employees of the said company, the services provided by them to the Company, in lieu of remuneration as the consideration for the said services, are clearly outside the scope of Schedule III of the CGST Act and are therefore taxable.

Accordingly, it is hereby clarified that the remuneration paid to such directors, by whatever name called, who are not employees of the said company, is taxable in hands of the company, on reverse charge basis.

#### ***If Directors are an employees of the Company:-***

It is clarified that the part of Director's remuneration which are declared as "Salaries" in the books of a company and subjected to TDS under Section 192 of the IT Act, are not taxable being consideration for services by an employee to the employer in the course of or in relation to his employment in terms of Schedule III of the CGST Act, 2017.

It is further clarified that the part of employee Director's remuneration which is declared separately other than "salaries" in the Company's accounts and subjected to TDS under Section 194J of the IT Act as Fees for professional or Technical Services shall be treated as consideration for providing services which are outside the scope of Schedule III of the CGST Act, and is therefore, taxable in the hand of the Company on reverse charge basis.

### SAC CODE

9983:- Other professional, technical and business services.

Rate:- 18%





## ESOP – Wanna Fly Together?



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### Introduction:

Employee Stock Option Plans (ESOPs) are a key part of the employee benefits offered by companies today. Start-ups, in particular, use ESOPs as an effective recruitment tool to attract and retain talent. However, employers and employees often

do not fully understand the terms and implications of such stock option schemes. From an employer's perspective, such a scheme enables them to offer an attractive compensation package while keeping the cash component of the employment offer low.

From the employee's perspective, such schemes help build a sense of belonging and ownership in the employer's company and investment in its growth and thereby foster long-term commitment. An introduction to employee stock option schemes and similar benefits, which are offered by companies in India to their employees, may provide helpful insights into current corporate employment offers. It is worth noting that limited liability partnerships cannot, generally speaking, offer similar employee schemes.

### What are ESOPs?

According to Section 2(37) of the Companies Act, 2013, *"The option given to the directors, officers or the employees of a Company or of its holding company or subsidiary company or companies, if any, which gives such directors, officers or employees, the benefits or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price."*

ESOPs are generally offered at a pre-determined price which is less than market price of the share which attracts employees to exercise their options and to become part of the growth of an organization.

### Eligibility Criteria for ESOPs in India

Any Company registered in India can issue ESOPs to its employees, directors or officers or any other person befitting into the definition as defined above.

However, there are some additional measures from the Ministry of Affairs and SEBI altogether to regulate ESOPs by Listed Entities through ESOP guidelines issue by them. These ESOP Guidelines provides detailed information for Employee Stock Options Scheme (ESOS) or Employee Stock Purchase Scheme (ESPS) as defined under clause 2.1 of Security Exchange Board of India (Employee Stock Options Scheme or Employee Stock Purchase Scheme) Guidelines, 1999 as below:

2.1. An "employee" means –

- a) a permanent employee of the Company working in India or out of India; or
- b) a director of the Company whether a Whole Time Director or not; or

- c) an employee as defined in sub-clauses (a) or (b) of a subsidiary, in India or out of India, or of a holding company of the company.

Provided, the following are not eligible to participate in ESOS under SEBI (ESOS and ESPS) Guidelines, 1999:

1. an employee who is a promoter or belongs to the promoter group;
2. a director who either himself or through his relative or through any Body Corporate, directly or indirectly, holds more than 10% of the outstanding equity shares of the company.

These kind of measures and restrictions protect minority interests and prohibit major dilution of promoter/promoters group's stake in the Company.

Companies that are not intent on adopting full-fledged ESOP schemes may prefer to choose a "phantom stock option scheme" where, instead of stock options and shares, employees / promoters are given the benefit of notional shares and appreciation in the value thereof. Some companies may also allot shares to an employee welfare trust upfront, which can then be transferred by the trust to employees. or as may be permitted by the trust and scheme documents.

### Benefits of ESOPs

Employer has benefits of granting ESOPs to its employees as follows:

1. **Retention tool:** Employees granted with ESOP options tend to remain longer in the Company than other employees. They look forward long relationship with the Company than other employees being more interest as an investor.
2. **Form of reward:** The Company grants ESOP options at lower rates than market price which enables employees to gain more by exercising options and acquiring shares. This is a kind of reward provided to hardworking employees who create wealth at lower cost than public at large.
3. **Building loyalty:** With granting options of ESOPs, employees tend to get attached with the Company and feel part of the growth of an organization which creates loyalty among the employee and the employer. This loyalty helps the company to achieve long term vision and goals.
4. **Performance improvement:** Reward and loyalty enhances performance of the employees as they understand growth of the Company will be growth of themselves which will help them generate wealth in long term.

While there are benefits on employer's part, there are benefits on the employee's part too.

1. **Financial benefits:** The employees are always piled with liquidity crunch and with these grants of ESOPs they enjoy greater financial benefits in the form of higher pay and wealth generation by getting shares in the company at discounted





rate to the market price which also ensures a comfortable retirement for employees in long term.

2. **Trust:** Employees after holding shares in the company feel more responsible towards the company. Employees take active participation in decision-making, which makes them optimistic, visionary and self-organized. Employees understand that growth of the company would benefit themselves only which make them trustworthy for an organization.
3. **Security:** ESOP provides great job security along with financial security by satisfying employees owning to the financial assets as well as non-monetary benefits.

### Vesting of an Option

Initially, the options are allotted or granted to employees, but cannot be exercised until certain conditions are met, after which time the options are said to be vested. Once the options are vested, the employee has the right to exercise the options, by paying either no consideration or a nominal amount, to the employer company in consideration of the allotted shares.

ESOPs are granted to the eligible directors or officers or employees which shall vest to them after certain vesting period. Such persons or their legal representatives or heirs may post completion of vesting period exercise these options to avail benefits of ESOPs.

### How companies adopt an ESOPs

The company will need to prepare an ESOP scheme, pass necessary resolutions and frame a separate stock option grant letter for each employee who can participate in the scheme. Such essential groundwork is often neglected by employers while offering employees their ESOP entitlements in the appointment letters. It is incumbent on companies, particularly those companies engaged in raising funds, to take the utmost care in ensuring the ESOP scheme is correctly put in place before the ESOPs are taken into account to calculate fully diluted capitalization tables.

The details of granting, vesting, and exercise of the stock options being offered, including the timelines, trigger events, lock-in period restrictions, and other conditions should be clearly spelt out in the ESOP scheme and/or the grant letters. Any variation in the terms of the originally approved ESOP would need shareholders' approval and comply with such other conditions as prescribed under the Companies Act, 2013 (and the rules enacted and amended thereunder).

### Laws governing ESOPs in India

Laws	Unlisted Private Company	Unlisted Public Company	Listed Company
The Companies Act, 2013	✓	✓	✓
Companies (Share Capital and Debenture) Rules, 2014	✓	✓	✓
SEBI (Share Based Employee Benefits) Regulations, 2014	X	X	✓

Laws	Unlisted Private Company	Unlisted Public Company	Listed Company
SEBI (Listing obligations and Disclosure Requirements) Regulations, 2015	X	X	✓
Income Tax Act, 1961	✓	✓	✓

### Tax implications when exercising the option

The taxation of ESOP has a typical structure. It is taxed in two stages. First stage is when the employee exercises the option to buy the shares at the exercise price. The second stage is when the shares are ultimately sold.

As and when the options under the ESOPs are exercised, the difference between the exercise price and the value of the security is treated as perquisite in the hand of the employee. The employer is required to deduct tax at source on the employee exercising the option, treating the same as perquisite. The value of the shares allotted to the employee shall be the average of market price (average of highest and lowest price) on the date the option is exercised in case the shares are listed on any stock exchange in India. In case the shares are not listed the fair market value of the same shall be as per the valuation certificate obtained from the merchant banker. The certificate of valuation of shares should not be older than 180 days from the date of exercise of the option. Even if the shares are listed outside India, the company will have to obtain the certificate from the Merchant Banker as such shares are treated as unlisted shares for ESOP purposes.

### Tax implications when the shares acquired under ESOP are disposed off

When the employee actually sells the shares, the incidence of sale will attract capital gains tax. The gains can be either long term or short term, depending on the period for which the employee has held the shares. The holding period requirement is different for listed shares as well as for unlisted shares. Listed shares shall become long term if held for more than one year. Unlisted shares become long term after three years. The period of three years has been proposed to be reduced to two years in the current budget.

The rate at which the short term or long term gains shall be taxed will depend on whether the shares have been traded on the platform of stock exchange on which the Security Transaction Tax has been paid. In case shares are traded through a broker, the long term capital gains are taxed under Section 112A at 10% over Rs. 1 lakh of capital gains. However, such short-term capital gains shall be taxed at a flat rate of 15% under Section 111A.

However, in case the shares are not sold through the platform of the stock exchange, the long term capital gains shall be calculated after applying the indexation to the original cost of purchase. Indexed gains so calculated shall be taxed at a flat rate of 20% plus applicable surcharge and education cess. You have the option to pay tax @ 10% on capital gains without applying indexation benefits. Such short-term capital gains are be treated like any other income and added to other income and taxed at the slab rate applicable.



For the purpose of computing the capital gains the fair market value as on the date of exercise, taken into account for the purpose of perquisites of the options, is treated as the cost of acquisition and not the price actually paid by the employee.

#### Taxation of Foreign ESOPs

In case the ESOPs are granted by foreign companies to the Indian resident, the same would be taxable in India. Moreover, the taxation provisions of the country of the company which grants the option as well as the double taxation avoidance agreement shall have to be looked into for understanding the exact tax implication. Moreover concessional tax on long term capital gains under Section 112A or concessional rate of 15% tax on short term capital gain in respect of such shares would not be available as these shares would not be sold on Indian stock exchanges as these are not likely to be listed in India.

#### Importance of the fine print in ESOPs

Both employees and employers must pay close attention to the manner in which ESOPs will be dealt with, in the event that the employer company undergoes an acquisition or merger.

Employees must also clearly understand the terms of vesting of the company's ESOP, and its granting and vesting schedule, all of which affect their actual benefit from the scheme. Further, the employee

must be clear on the rules governing her ESOP in the event that she resigns/retires, or her services are terminated by the employer. It is likely that the employee will still be able to exercise the stock options for a certain period after the employment has ended, depending on the terms of the scheme.

#### Few limitations of ESOPs

The Company may have to forego additional premium on shares while granting options to its employees which might be an expensive tool for the Company. On other side, Employee may not create wealth and incur huge loss when the Company turns out to be a failure.

#### Re-evaluating ESOPs in the COVID-19 crisis

As with all things equity, the impact of the current pandemic and resultant restrictions on ESOPs remains to be seen. However, employees must carefully consider the value of their stock options, and the terms of the ESOP of their employer company, in the event that they consider resigning from their job or the employer company is likely to downsize and offer a severance package. Uncertain times need certain cautions.

*Till then Stay Safe by Staying Home !*



### 5th Virtual CPE Meeting on Important provisions of Companies Act held on 8th June 2020



Speaker- CS. Gaurav Pingle. Welcome note - CA. Xavier Rajan (Immediate Past Chairman, Vasai Branch of WIRC), Session Chairman - CA. Ankit Rath (Chairman - Vasai Branch of WIRC) & Coordinator – CA. Vijendra Jain (Secretary – Vasai Branch of WIRC)

### 6th Virtual CPE Meeting on Important provisions of Companies Act held on 10th June 2020



Speaker - CA. Rajiv Khandelwal, Welcome note - CA. Dayaram Paliwal (Past Chairman, Vasai Branch of WIRC), Session Chairman - CA. Ankit Rath (Chairman - Vasai Branch of WIRC) & Coordinator – CA. Abhishek Tiwari (Vice Chairman – Vasai Branch of WIRC)



## 7th Virtual CPE Meeting on Revised Code of Ethics held on 12th June 2020



Speaker- CA. Durgesh Kabra (Central Council Member), Welcome note - CA. Pramod Dhamankar (Past Chairman, Vasai Branch of WIRC), Session Chairman - CA. Ankit Rath (Chairman - Vasai Branch of WIRC), Coordinator – CA. Vijendra Jain (Secretary – Vasai Branch of WIRC) & CA. Lokesh Kothari (Treasurer – Vasai Branch of WIRC)

## 9th Virtual CPE Meeting on RERA Opportunities for CA held on 20th June 2020



Speaker - CA Ramesh Prabhu, Welcome note - CA. Ramanand Gupta (Past Chairman, Vasai Branch of WIRC), Session Chairman - CA. Ankit Rath (Chairman- Vasai Branch of WIRC) & Coordinator – CA. Abhishek Tiwari (Vice Chairman – Vasai Branch of WIRC)

## 10th Virtual CPE Meeting on Impact of Covid 19 in Auditing Report held on 23rd June 2020



Speaker - CA. Amarjit Chopra (Past President, ICAI), Welcome note - CA. Xavier Rajan (Immediate Past Chairman, Vasai Branch of WIRC), Session Chairman- CA. Ankit Rath (Chairman - Vasai Branch of WIRC) & Coordinator – CA. Lokesh Kothari (Treasurer – Vasai Branch of WIRC)





June 2020

### 11th Virtual CPE Meeting on Auditing Standard held on 25th June 2020



Speaker - CA. Padmashree Vinod Crasto, Welcome note - CA. Umesh Mestry (Past Chairman, Vasai Branch), Coordinator – CA. Amit Agarwal (Committee Member – Vasai Branch of WIRC) & CA. Tarun Dhandh also presence CA. Vijendra Jain (Secretary – Vasai Branch of WIRC)

### 12th Virtual CPE Meeting on Equalization Levy on E Commerce held on 27th June 2020



Speaker - CA Shailesh Monani & CA Amit Agrawal Welcome note - CA. Kishor Vaishnav (Past Chairman, Vasai Branch of WIRC), Session Chairman - CA. Ankit Rathi (Chairman - Vasai Branch of WIRC) & Coordinator – CA. Abhishek Tiwari (Vice Chairman – Vasai Branch of WIRC) & CA. Vijendra Jain (Secretary – Vasai Branch of WIRC)

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**Vasai Branch of WIRC**

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