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# Restricted stock award for Wiproites

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BANGALORE: Employee stock option programmes (esops) are out, restricted stock awards are in. Wipro , on Friday, by announcing its decision to introduce an "innovative" restricted stock award scheme for employees, became the first listed company in the country to do so.

Wipro is following in the footsteps of global giant Microsoft and several other US companies, which today, prefer restricted stock award schemes over plain vanilla esops. Who knows, Wipro's move may prompt other companies in India to follow suit.

"Wipro's restricted stock award scheme falls within the Sebi requirements " states Suresh Senapaty, CFO and corporate executive vice-president (Finance), Wipro. Post approval by the shareholders at the annual general meeting, the nitty-gritty would be worked out.

The compensation committee would decide issues such as the parameters of eligibility for employees to be rewarded with restricted stock, the period over which shares would vest in the hands of employees, to name a few.

Right now, it appears to be a win-win situation for both the company and its eligible employees. Besides being a powerful retention tool, this scheme will reduce accounting hassles.

"Accounting for esops, based on the Black Scholes formula, means taking a hit on the P&L of a quantum that is higher than the perceived value to the employee," explains Senapaty.

"Accounting for restricted stock provides a more realistic picture of the employee benefit costs", he adds.

Analysts state that, in simple terms, accounting for restricted stock means factoring in the real market value of the shares, rather than a perceived value of the option. This leads to realistic presentation of the accounts.

Perhaps, what is more important is the benefits to eligible employees. And market indications are that the employees would be amply rewarded. KR Lakshminarayana, corporate treasurer, Wipro, told **The Economic Times** : "Restricted stock award would enable the compensation committee to arrive at a suitable predetermined price at which the eligible employees can buy the shares."

Wipro will be issuing fresh shares to cater to the needs of this scheme, he added. Today, the world over, restricted stock is being voted as the most powerful tool, when attrition is no longer an irritant but a serious problem.

Studies show that prompt ownership in the company, albeit as a shareholder, acts as a powerful motivational tool.

Unlike an esop scheme, which has four stages (of grant, vesting, exercise – conversion of option into shares by an employee – and its ultimate sale by the employee), a restricted stock scheme is much simpler. There is no process of exercising the option and converting it into a share.

Here is how a restricted stock scheme typically works. Eligible employees are vested with shares, eligibility could be based on performance criteria, seniority, number of years of service with the company or a judicious mix. On vesting, the employees have to pay for the shares at the predetermined price. They promptly become shareholders of the company.

If the employee does not accept the shares vesting in him/her by paying the predetermined price, the award scheme lapses. "Typically, legends/caveats are built in, which prevent the employee from immediately selling off the shares", explains an HR consultant.

Further, in times of market volatility, stock award schemes are more attractive than underwater options. While IT stocks are on a bull run in India, the scenario is slightly different in the US, thus making restricted stock schemes more popular.

"A stock option grant with an exercise price of $100 has no value when the stock is trading at $80. On the other hand, a restricted stock awarded when trading at $100 is still worth $80. The stock option has lost 100 per cent of its value, the restricted stock has lost just 20 per cent of its value," adds an analyst.

Restricted stock award schemes have a variant called the "Restricted Stock Award Unit". These are more useful for mature companies, says an analyst. This method is a hybrid variant of granting warrants and the shares can be awarded even at face value!

Here is an illustration, to depict the scene, if Wipro were to use this variant. Suppose Wipro decides to award A with 1,000 shares over a four year period. Then, in the first year, A will be able to acquire 200 shares for a face value of Rs 2 each. He would dole out just Rs 400 and would do the same for the next three years. A real bonanza for A!

What now of the tax implications for employees?

"The guidelines issued by the Ministry of Finance cover stock ownership plans. Thus, if a restricted stock scheme is formulated which is in accordance with central government guidelines and is filed with the appropriate authorities there should be no perquisite value in the hands of employees at the time of vesting, as per Section 17(2) of the Income-tax Act. Thus there will be no tax at this stage," explains **Daksha Baxi, advocate, Nishith Desai Associates**.

In such instances, there will be a capital gains tax only at the time of sale of shares, she adds. Capital gains are the difference between the sale consideration and the indexed cost of acquisition. The cost of acquisition, in those instances, where there is no tax on vesting, will be the price at which the employee acquired the shares. This will be indexed at the given index figure, provided by the tax laws for the year of sale.

If the sale consideration is Rs 150, the acquisition price is Rs. 80 (after indexation it is 90). Then the capital gain will be Rs. 60 only. If the shares have been held for one year, the capital gains would be long term in nature and taxed at the concessional rate of 10 per cent.

It is likely that Wipro's scheme, which has met Sebi requirements, would result in perquisite value exemption to employees.

"We have structured a tax efficient scheme, for our employees" is what Senapaty admits to, at this juncture. This is the icing on the restricted share award scheme.

Retaining employees would mean better profits and better dividends. Which shareholder would not agree with this? It is time to uncork the champagne at Wipro!