

# THAT PESKY ESOPS!



VISTRA'S **KRZYSZTOF WÓJCIK**, HEAD OF LEGAL SERVICES, ATTORNEY AT LAW; AND **PIOTR PROKOCKI**, SENIOR TAX MANAGER, TAX ADVISOR & ATTORNEY AT LAW, WRITE ABOUT COMPLIANCE AND TAXATION ASPECTS OF EMPLOYEE SHARE OPTION PLANS.

Employee share option plans (ESOP) have recently become increasingly popular, especially in industries where talent acquisition and retention are fundamental success factors. The IT sector is a flagship example.

ESOPs are often organized at the group level and are international in scope. Yet, to participate in them, employees and B2B contractors in Poland must resolve many questions considering Polish tax law, labor law and regulatory restrictions.

## GENERAL CONCEPT

Under ESOPs, the beneficiaries (such as members of the management board, directors, key managers and consultants) have the right to acquire a fraction of shares in the company upon payment of a certain amount (strike price). ESOPs usually specify the conditions under which the beneficiary may receive share options, which, in turn, can be exchanged for shares. From the bene-

to employee stock option plans, granted as a result of the existence of an employment relationship and similar specified contracts. Due to these regulations, the moment of the recognition of taxable revenue (on the part of the beneficiary) is deferred until the disposal of the stock. To apply these specific rules, several conditions must be jointly met, including:

- the incentive program must be dedicated to employees (it does not apply to B2B contractors or board members without an employment contract);
- the incentive program must be established by a joint-stock company that is the employer of the beneficiaries or its parent company, which also operates as a joint-stock company.

When an ESOP meets the above conditions, determining when the tax revenue arises is relatively straightforward. Doubts arise where ESOP deviates from these conditions

ing shares (ref. no. 0115-KDIT1.4011.149.2020.3.MN). Fortunately, the aforementioned interpretation was revoked by the court, which indicated that the taxable income would only arise upon the sale of the shares (the judgment of the Regional Administrative Court in Gdańsk in the judgment of 16 December 2020, ref. no. I SA / Gd 819/20).

In many cases, the first two stages (i.e. subscription and acquisition of options) will not generate taxable revenue on the part of the beneficiaries. According to the general rules of the PIT Act, revenue comprises all kinds of cash payments and the monetary value of benefits in kind or their equivalents, regardless of the source of financing of these payments and benefits. In addition, according to the well-established jurisprudence of the Polish administrative courts, if the benefit received by Beneficiaries was to

contract of employment, it should be taken into account that certain parts of the scheme, such as "bad leaver" and "good leaver" definitions, need to be clarified under local law. Each legal system has specific labor law provisions, and the lack of precision is often resolved in favor of the employee. Provisions that do not comply with local labor jurisdiction or that are debatable, can cause local disputes with a high risk of loss for the employer.

## REGULATORY REQUIREMENTS

Another type of local legal risk is regulatory risk. It is not common knowledge that an ESOP based on shares in a joint stock company can be considered a public offering of securities in Poland. This in turn triggers registration obligations and may have further regulatory implications. In some cases, also an ESOP offering of a derivative may require

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fiary's perspective, such programs consist of three stages: the subscription, the acquisition of options and the vesting exchange of options for equity. The last step is the disposal of the company's shares—an exit from ESOP. In the case of the involvement of Polish employees or B2B contractors, the taxation rules and rights of the beneficiaries should be established in line with Polish regulations. This task can be difficult. In practice, ESOPs take very different forms, and often vary from the model schemes regulated in Polish provisions.

## TAXABLE REVENUE

In 2018, the Polish legislature introduced favorable tax rules applicable

(such as when B2B contractors are involved in it or its object shares in a limited liability company). In such circumstances, the moment when the tax revenue arises should be determined based on the general provisions regulating the moment when the profit is generated.

## ESOPs WITH NO TAX PREFERENCES

However, the application of the general rules may raise doubts. Their example may be an individual interpretation, in which the Director of the National Tax Information indicated that the income should be recognized three times: at the stage of obtaining rights to shares, exchanging options for shares and sell-

be considered taxable revenue, it must have a definitive character. In such situations, the taxable revenue may arise at the vesting stage and/or at disposal of shares. Appropriate application of tax law provisions will allow such situations to avoid double taxation of the same property gain.

## LOCAL LAW COMPLIANCE

Although international ESOP schemes are not in sync with the basis of Polish law, this does not mean that the Polish legal system can be completely disregarded when offering them to Polish beneficiaries. In particular, when offering ESOPs to beneficiaries employed under a

registration with the relevant official registers.

It is also worth noting other possible restrictions, such as the prohibition on offering shares in a limited liability company when the offer is to an unspecified addressee, which will take effect in Poland next year.

## CONCLUSIONS

As illustrated, offering an ESOP in Poland, even if it is based on well-tested international solutions and verified against the regulations governing it, requires local verification and sometimes relatively minor adjustments to tax, legal and regulatory requirements.