## Corporate Tax - Romania

# Tax treatment of stock option plans: navigating the grey areas

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### Introduction

In a competition-driven market, rewarding employees for their performance and commitment, as well as for aligning their interests with those of the company, involves equity plans, among other things. The use of such schemes in the Romanian market has become increasingly common in the past few years, considering both the presence of multinational corporations (most of which had already embraced equity plans) and the increasing interest of local companies. This interest is due to the fiscal advantages of such schemes and the possibility of attracting business financing through them. Nonetheless, implementing a stock option plan in Romania might prove challenging due to uncertainty over the applicable tax treatment, especially where the scheme involves employees of companies affiliated with or belonging to the same group as the issuer.

### Tax regime for stock option plans

Employee reward schemes are not specifically regulated under Romanian law, as the Fiscal Code refers solely to stock option plans. In accordance with the code, benefits allocated to employees under stock option plans are not taxable when granted or exercised. Where shares acquired under stock option plans are traded (ie, at a preferential price), capital gains are to be calculated as the difference between the share sale price and the preferential purchase price, deducted with the transaction costs. Despite these few stipulations, the code does not define the term 'stock option plan'.

The sole legal enactment that provides a definition of 'stock option plan' is an order issued jointly by the Ministry of Economy and Finance and the former National Securities Commission that regulates the income tax treatment of capital gains obtained by individuals from a transfer of securities. According to the order, a 'stock option plan' is:

> "*a program launched by a company listed on a regulated market or on an alternative trading system, whereby* its employees *are granted the right to acquire an established number of shares issued by that company for a preferred price*."

### Grey areas

Based on the above-mentioned definition of 'stock option plan', the structure envisaged in the order in question refers solely to stock option plans that involve the issuer's employees. Consequently, where shares are also offered to other employees (ie, those of a subsidiary or another company in the same group as the issuer), the tax impact on the relevant benefits is unclear. The applicable tax treatment is thus subject to debate and various interpretations by the tax authorities.

Due to the tax authorities' uncertainty over their approach to this situation, many are of the opinion that the safest strategy would be to treat the benefits received by an employee of a company other than the issuer as income assimilated into salary. This stance is based on the fact that under the Fiscal Code, the rules governing salary income apply to any other related amounts or salary-type benefits, including "any advantages received by the employee from third parties, or based on the provisions of the employment agreement, or on a contractual relationship between the parties, as the case may be". The main argument in treating the awards as salary-type benefits and

subjecting them to the same rules as salary income is that the employees would receive such benefits subject to – and as a consequence of – their employment with a company in the same group as the issuer. Based on such an interpretation, the benefits received under a stock option plan by employees other than the issuer's would be taxable on exercise of the option.

However, others have asserted that the benefits received under stock option plans are taxable neither when granted nor when exercised. Supporters of this stance consider that in the absence of a specific definition of 'stock option plan' in the Fiscal Code, the exemption provided therein with respect to stock option plans should apply to such schemes that fall under the general concept. Supporters of this interpretation also highlight the following points:

- The purpose underlying the provision of such incentives to group employees (including employees other than the issuer's) is the same in all cases.
- The relevant Fiscal Code provisions do not distinguish between the employees of the issuer and other employees qualifying in the plan.
- The order in question was issued for the enforcement of a Fiscal Code provision referring to withholding tax on investment income, rather than for the provisions specifically referring to stock option plans.
- Secondary legislation (eg, the order in question, which was an administrative enactment) should not limit the applicability of primary legislation (eg, the Fiscal Code, which was approved by law).
- Exceptions should be expressly provided by law, not inferred.

Some tax consultants have adopted a middle-ground approach whereby, save when re-charged to and thus borne by the direct employer, the benefits granted to employees by a company other than their employer should not be assimilated into salaries and consequently should not be taxed as such. However, the relevant advantage (ie, usually a share price discount) could be deemed as taxable income solely of the beneficiary thereof (ie, the relevant employee).

**Comment**

Considering recent practice, the tax treatment of stock option plans and employee reward schemes in general should be clarified in order to give companies a better perspective on their tax obligations and those of their employees. In this respect, it should also be considered that, from a tax perspective, treating similar situations differently would discriminate between taxable persons (eg, employees of companies in the same group), which would have a potentially unfavourable effect on the ultimate goals of such plans.

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