

IRAS CIRCULAR

**CHANGES TO TAX TREATMENT OF
EMPLOYEE STOCK OPTIONS
AND OTHER FORMS OF
EMPLOYEE SHARE OWNERSHIP PLANS
(Revised Edition)**



INLAND REVENUE
AUTHORITY
OF SINGAPORE

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CHANGES TO TAX TREATMENT OF EMPLOYEE STOCK OPTIONS AND OTHER FORMS OF EMPLOYEE SHARE OWNERSHIP PLANS

INTRODUCTION

Following the recommendation by the ERC sub-committee¹, Deputy Prime Minister and Minister for Finance had, in his Budget Statement 2002, announced the following changes in respect of employee stock option (hereinafter referred to as “ESOP”) plans and other forms of employee share ownership (hereinafter referred to as “ESOW”) plans²:

- (a) change in the basis of taxation of gains from ESOP and ESOW Plans granted while an individual is exercising employment in or outside Singapore;
- (b) change in the timing of taxing the gains from ESOP and ESOW Plans with selling restrictions imposed;
- (c) extending the existing incentive schemes³ for ESOP to cover ESOW Plans;
- (d) requiring companies to track and collect taxes on gains from ESOP from employees who have exercised their ESOP after they leave Singapore.

¹ On 11 April 2002, the Sub-Committee on Policies Related to Taxation, the CPF System, Wages and Land (Sub-Committee) set up under the Economic Review Committee had among other things, recommended to the Government certain tax changes for equity-based methods of remuneration (for example, stock options, share awards etc). The recommendations put up by the Sub-Committee in its report “Restructuring the Tax System for Growth and Job Creation” are aimed at strengthening the entrepreneurial culture and encouraging remuneration packages that better link the interests of management and employees with the performance of the company in Singapore. The report is available at <http://www.erc.gov.sg>.

² Generally, ESOW Plans are plans, which allow an employee of a company to own or purchase shares in the company or that of its parent company. They include share awards and other similar forms of employee share purchase plans but exclude phantom shares and share appreciation rights (SARs) which merely use the share prices as a basis for computing the amount of benefits to be paid to the employees.

³ The incentive schemes are: Qualified ESOP Scheme, Entrepreneurial ESOP Scheme and the Company Stock Option (CSOP) Scheme.

2 The Government has since reviewed the announced tax change in paragraph 1(d) and decided not to proceed with it. Instead, the Government has decided that employees who are neither Singapore citizens nor Singapore permanent residents (hereinafter referred to as “SPR”) will be subject to tax on a “deemed exercise” basis on any unexercised/restricted ESOPs or unvested/restricted shares granted by any company under any ESOP/ESOW plans while they are exercising employment in Singapore, at the time they cease employment with the company. This change and the consequential details are further explained in paragraphs 34 and 35 of this circular.

3 This circular provides details of the above tax changes for ESOPs and ESOW Plans.

CHANGE IN BASIS OF TAXATION

ESOPs

4 Currently, an individual who exercises his ESOP while he is physically present in Singapore or exercising employment in Singapore is considered as having derived from Singapore, income amounting to the gains or profits computed based on the difference between the open market price of the shares at the time of exercise of the ESOP and the amount paid for such shares. The full amount of such gains or profits from ESOP exercised is taxable in Singapore under section 10(1)(g) of the Singapore Income Tax Act (SITA). Therefore in the case of an individual who was granted ESOP prior to his posting to Singapore but who exercises the ESOP while he is in Singapore or holds an employment in Singapore, he will be subject to tax in Singapore on the full amount of gains or profits derived from the exercise of the ESOP⁴.

5 Conversely, any gains or profits from ESOP exercised by any individual while he is overseas and not exercising employment in Singapore are not regarded as income derived from Singapore.

6 As announced in Budget Statement 2002, any gains or profits derived from any ESOP (hereinafter referred to as “ESOP gains”) would be taxed in Singapore to the extent that there is a nexus between that ESOP and the employment exercised in Singapore. An ESOP will be regarded as having a nexus with an employment exercised in Singapore, if it is granted while the individual is exercising employment⁵ in Singapore. Therefore for an individual who is granted ESOP while he is exercising employment in Singapore, the full amount of ESOP gains, irrespective of where the ESOP is exercised, would be regarded as gains or profits from employment derived by that individual from Singapore under section 10(1)(b) of SITA. Such gains constitute gains

⁴ Compass Article Vol 5 No.1 or E tax guide 1997/IT/2, and Compass Article Vol 7 No.3 or E tax guide 2000/IT/3.

⁵ If an individual is exercising employment in Singapore, any temporary absences from Singapore would be treated as incidental to his employment in Singapore.

derived by that individual in the year in which the ESOP is exercised⁶ and will be taxed as such in Singapore. This tax change will apply to ESOPs granted on or after 1 January 2003 while the individual is exercising employment in Singapore.

7 As a corollary, for an individual who is granted ESOP in respect of employment exercised overseas, any gains derived by him from the exercise of the ESOP are not regarded as income derived from Singapore and will not be subject to tax in Singapore as such. This tax treatment shall apply even if the above individual were to exercise the ESOP while he is exercising an employment in Singapore. This tax change would apply to such ESOPs, which are exercised by that individual on or after 1 January 2002. However, if the individual is a tax resident of Singapore, any amount of the gains or profits remitted to Singapore will be subject to tax as income received in Singapore from outside Singapore.

8 With the tax change in paragraph 7, Ministerial remission⁷ given under section 92(2) of SITA on a case-by-case basis to relieve a resident individual from any double taxation on the same ESOP gains would no longer be relevant and hence would be removed for ESOPs that are granted in respect of employment exercised overseas but exercised on or after 1 January 2002 while the individual is in Singapore or holds an employment in Singapore.

9 The examples in Annex 1 illustrate the effect of this change in basis of taxation of ESOP gains.

ESOW Plans

10 Currently, gains from shares granted under any ESOW Plan, other than those with vesting imposed⁸, accrue to an individual as income in the year during which the shares are granted. For shares under any ESOW Plan with vesting imposed, the gains accrue to the individual only on the date the beneficial interest from the ownership of the shares is vested to that individual (hereinafter referred to as “date of vesting”). Thus, for an individual who is granted shares under any ESOW Plan with vesting imposed while he is exercising employment in Singapore, and who is vested with the beneficial interest from the ownership of the shares only after he has left his employment in Singapore, he will generally not be assessed to tax on any

⁶Except for (1) restricted ESOP where any gains or profits arising from the exercise of such ESOP will under the new tax treatment constitute taxable gains only in the year in which the moratorium is lifted and (2) cases where the “deemed exercise” rule applies. Please refer to paragraph 15 for an explanation of the tax treatment of restricted ESOP, and paragraphs 34 and 35 for an explanation of the application of the “deemed exercise” rule.

⁷ Please refer to Compass Article Vol 7 No.3 or E tax guide 2000/IT/3. The remission is given on a case-by-case basis where ESOP is granted at the time an individual was exercising employment outside Singapore and the ESOP gains have been or will be subject to tax in a foreign country.

⁸ ESOW Plans with vesting imposed generally refer to those plans where the beneficial interest from the ownership of the shares does not accrue, either directly or indirectly, to the individual until the date of vesting.

gains derived by him in respect of such shares unless the gains are attributable to the individual's employment in Singapore.

11 With the change in basis of taxation of ESOPs as stated in paragraphs 6 and 7, the basis of taxation of shares granted under any ESOW Plan with vesting imposed will also be changed. Therefore, an individual who is granted shares under any ESOW Plan with vesting imposed, while he is exercising an employment in Singapore, will be assessed to tax in Singapore on the full amount of the gains derived in respect of these shares unless tax exemption under the respective incentive schemes as mentioned in paragraph 20 applies. This treatment shall apply regardless of whether the individual is in or outside Singapore as at the date of vesting. This tax change would apply to shares under any ESOW Plan with vesting imposed granted on or after 1 January 2003.

12 Conversely, an individual who is granted shares under any ESOW Plan with vesting imposed while he is not exercising an employment in Singapore, will not be regarded as having derived such gains from Singapore and will not be taxed on the gains as such⁹, even when that individual is either physically present in Singapore or exercising an employment in Singapore as at the date of vesting of such shares. In such cases, no tax deduction shall be allowed to the employer in Singapore for any cost borne, whether directly or indirectly, in relation to the vesting of such shares under any ESOW Plan. This tax change would apply to shares under any ESOW Plan with vesting imposed that vest on or after 1 January 2002.

13 The examples in Annex 2 illustrate the effect of change in basis of taxation of gains from shares granted under any ESOW Plan with vesting imposed.

CHANGE IN TIMING OF TAXATION AND DETERMINATION OF TAXABLE GAINS FROM RESTRICTED ESOPS AND RESTRICTED SHARES GRANTED UNDER ESOW PLANS

14 Currently, an individual is regarded as having derived the ESOP gains at the time he exercises the ESOP. This treatment applies whether or not there is any restriction against the sale, within a certain period from the date the ESOP is exercised, of shares acquired under the ESOP (such a period is hereinafter referred to as "moratorium"). On the other hand, an individual is regarded as having derived gains from shares granted under any ESOW Plan, whether or not there is a moratorium, at the time of grant (in a case where there is no vesting imposed) or date of vesting (in a case where there is vesting imposed).

15 As announced in Budget Statement 2002, and subject to paragraphs 34 and 35, where there is a moratorium on shares acquired under any ESOP (hereinafter referred to as "restricted ESOP"), gains derived by an individual in respect of such ESOP only constitute gains accruing to him on the date the

⁹ However, if the individual is a tax resident of Singapore, any amount of such gains or profits remitted to Singapore shall be subject to tax as income received in Singapore from outside Singapore.

moratorium is lifted. The taxable gains will be determined based on the difference between the open market price of the shares on the date the moratorium is lifted and the exercise price.

16 Shares granted under any ESOW Plan with moratorium (such shares are hereinafter referred to as “restricted shares”) will also be treated in a similar way. That is, gains derived by an individual in respect of such shares will only constitute gains accruing to him on the date the moratorium is lifted, and the amount of taxable gains will be the difference between the open market price of the shares on the date the moratorium is lifted and the price paid or payable by the individual for the shares.

17 However for ESOPs and shares granted under any ESOW Plan without moratorium, the current treatment shall continue to apply i.e. such gains shall constitute taxable gains in the year the option is exercised (in the case of ESOPs) or in the year of grant or vesting of shares, as the case may be (in the case of shares granted under any ESOW Plan).

18 The tax change in paragraphs 15 and 16 will apply to restricted ESOPs or restricted shares under any ESOW Plan, which are granted on or after 1 January 2003. In the case where the restricted ESOPs or restricted shares under any ESOW Plan are granted to an individual who is neither a Singapore citizen nor an SPR and who ceases employment with the company for which he is exercising employment when he is granted such ESOPs or shares, the treatment in paragraphs 34 and 35 and not paragraphs 15 and 16 shall apply.

19 The examples in Annex 3 illustrate when the gains derived from restricted ESOPs and restricted shares under ESOW Plans are to be taxed.

EXTENDING THE EXISTING INCENTIVE SCHEMES FOR ESOPs TO RESTRICTED SHARES UNDER ESOW PLANS

20 As announced in Budget Statement 2002, shares granted under any ESOW Plan will now qualify for the existing incentive schemes for ESOPs, provided that there is a minimum holding period requirement for such shares under the ESOW Plan that achieves similar effect as the vesting period requirement¹⁰ in ESOPs. This is provided that all other qualifying criteria for the incentive schemes are also met. The existing incentive schemes for ESOPs are:

- (a) Qualified ESOP Scheme (introduced in the year 1999)¹¹;

¹⁰ The current vesting period requirement is pegged to that imposed by Singapore Exchange (SGX) on ESOP plans of companies listed on the SGX. It is as follows:

- (a) where the exercise price of the option to acquire share is equivalent to or exceeds the market value of the share at the time of grant of option, the option given on the share may not be exercised within 1 year from the grant of the option;
- (b) where the exercise price of the option to acquire share is at a discount to the market value of the share at the time of grant of option, the option given on the share may not be exercised within 2 years from the grant of the option.

Accordingly, if SGX were to change the above vesting period rules subsequently, an ESOP plan will have to comply with the amended rules from the date the change in rules take effect.

- (b) Entrepreneurial ESOP Scheme (introduced in the year 2000)¹²; and
- (c) Company Stock Option (CSOP) Scheme (introduced in the year 2001)¹³.

With the extension, the above incentive schemes would be renamed as Qualified Employee Equity-based Remuneration Scheme (“Qualified EEBR Scheme”), Entrepreneurial Employee Equity-based Remuneration Scheme (“Entrepreneurial EEBR Scheme”) and Company Employee Equity-based Remuneration Scheme (“Company EEBR Scheme”) respectively.

Minimum holding period requirement

21 The minimum holding period that is required for an ESOW Plan to qualify for the respective EEBR Schemes is as follows:

- (a) where the price payable by an employee to acquire a share is equivalent to or exceeds the market value of the share at the time of grant of the share under the ESOW Plan, a moratorium of at least ½ year must be imposed i.e. the share so acquired cannot be disposed of by that employee within ½ year from the date of grant;
- (b) where the price payable by an employee to acquire a share is at a discount to the market value of the share at the time of grant of the share under the ESOW Plan, a moratorium of at least 1 year must be imposed i.e. the share so acquired cannot be disposed of by that employee within 1 year from the date of grant.

Other qualifying criteria for incentives to apply to ESOW Plan

22 Besides the minimum holding period requirement stated in paragraph 21, restricted shares granted under any ESOW Plan must, unless otherwise specified in this circular, also satisfy all the other existing qualifying criteria and rules stipulated under the respective incentive schemes for ESOPs to qualify for the incentives under the Employee Equity-based Remuneration (EEBR) Schemes. For example, the shares granted under any ESOW Plan must also be ordinary shares and not redeemable or convertible shares or shares of a preferential nature. Once the minimum holding period and other stated qualifying criteria are met, an individual may -

- (a) defer the payment of tax on gains arising from ESOPs and shares under any ESOW Plans for up to 5 years subject to an interest charge, under the Qualified EEBR Scheme;

¹¹ Details of the scheme are available in the IRAS’ Press Statement on “Qualified Employee Stock Option Scheme” issued on 22 October 1999.

¹² Details of the scheme are available in IRAS circular on “Entrepreneurial Employee Stock Option Scheme” issued on 22 May 2000.

¹³ Details of the scheme are available in IRAS circular on “Company Stock Option Scheme” issued on 31 March 2001.

- (b) enjoy tax exemption of 50% of up to \$10 million of aggregate amount of gains¹⁴ from ESOPs and shares under any ESOW Plans over a period of 10 years under the Entrepreneurial EEBR Scheme; or
- (c) enjoy tax exemption on aggregate amount of gains¹⁴ from ESOPs and shares under any ESOW Plans of up to \$1 million over a period of 10 years under the Company EEBR Scheme as follows:
- full tax exemption on the first \$2,000 of gains from ESOPs and shares under any ESOW Plans
 - tax exemption of 25% on the remaining amount of gains from ESOPs and shares under any ESOW Plans

for each YA during the 10-year period.

23 The extension of existing incentive schemes to restricted shares granted under any ESOW Plan will apply to qualifying restricted shares, which are granted on or after 1 January 2002.

50% requirement under Company EEBR Scheme

24 Currently, an ESOP plan of a qualifying company can qualify to be a CSOP plan if the ESOP plan -

- (a) satisfies the vesting period requirement as prescribed by Singapore Exchange¹⁰;
- (b) offers stock options to at least 50% of the employees of the qualifying company at the end of each calendar year (hereinafter referred to as “50% requirement”) determined in accordance with the following formula:

$$\frac{\text{Total number of the qualifying company's employees offered stock options under ESOP plan during the year}}{\text{Total number of the qualifying company's employees as at 31 December of the year}}$$

Total number of the qualifying company's employees
as at 31 December of the year

25 In addition, where a qualifying company operates more than one ESOP plan, the 50% requirement under the CSOP Scheme is determined in respect of each ESOP plan. In other words, no aggregation of the plans is allowed for the purpose of determining the 50% requirement.

¹⁴ The gains exclude discount. In the case of shares granted under any ESOW Plan, the discount refers to the difference between the market value of the shares at the time of grant and the price paid or payable for the shares.

26 The Government has reviewed the above requirement and decided that for the purposes of determining the 50% requirement under the Company EEBR Scheme, ESOPs granted under different ESOP plans that satisfy the vesting period requirement or shares granted under different ESOW Plans that satisfy the minimum holding period requirement, can subject to paragraph 27, be aggregated on a company's basis, as shown in the formula below:

$$\frac{\text{Total number of the qualifying company's employees who are offered ESOPs under any ESOP Plan that satisfies the minimum vesting period requirement and/or shares under any ESOW Plan that satisfies the minimum holding period requirement during the year (N)}}{\text{Total number of the qualifying company's employees as at 31 December of the year (D)}}$$

Total number of the qualifying company's employees
as at 31 December of the year (D)

This change will take effect from 1 January 2002.

27 Where any of the ESOP Plans or ESOW Plans can meet all the qualifying conditions under both the Entrepreneurial EEBR and Company EEBR Schemes, the qualifying company can however opt for tax exemption under Entrepreneurial EEBR Scheme to apply in respect of gains from ESOPs or shares under any of these ESOP Plans or ESOW Plans. Once the option is made, the employees under such plans should be excluded from the numerator (N), for the purpose of determining the 50% requirement under the Company EEBR Scheme.

28 For ease of reference, some requirements presently applicable to the CSOP Scheme, which will similarly be applicable under the Company EEBR Scheme are provided in Annex 4. Full details of the requirement under CSOP Scheme are available in IRAS circular on "Company Stock Option Scheme" issued on 31 March 2001. Annex 4 also contains some examples on how the 50% requirement under the Company EEBR Scheme is to be determined.

Administrative requirements for EEBR Scheme

29 As is the case of the existing incentive schemes for ESOPs, companies do not have to apply for approval from the CIT to have their ESOP Plans or ESOW Plans considered as Qualified EEBR, Entrepreneurial EEBR or Company EEBR Schemes, whether the plans are operated by them or by their parent companies under a Group ESOP Plan or a Group ESOW Plan. However, companies that wish to operate ESOP Plans or ESOW Plans that qualify for the respective EEBR Schemes have to keep sufficient documentation to show, when required by the CIT, that their ESOP Plans or ESOW Plans satisfy the requirements of the respective schemes. In addition, they are required to comply with the administrative requirements as set out in paragraphs 30 to 33 of this circular and such other administrative requirements as the CIT may from time to time impose under the schemes.

30 If it were subsequently found that any of the qualifying criteria under the respective EEBR Schemes has not been met, the respective tax exemption will not be granted, or if previously granted, would be withdrawn on the ESOP or ESOW Plan gains derived by the employee. The CIT may also impose appropriate penalties on the company for non-compliance of any term or condition under the respective EEBR Schemes, or for giving any incorrect information unless this is due solely to incorrect declaration made by its employees.

31 Companies are currently required to provide details of all ESOP gains, segregating the gains, where applicable, into those qualifying for the existing Entrepreneurial ESOP Scheme; those qualifying for the existing CSOP Scheme and those that do not qualify for any tax exemption under any of the two schemes (including any amount of discount enjoyed by an employee on the ESOPs in a prescribed format¹⁵, that is to be submitted with the annual return of remuneration given to the employees no later than the date (usually on 1 March of the year following the year to which the employees' remuneration relates) that is stated in the gazette notice to employers. However, if the companies have made arrangement to transmit salary data electronically to the CIT for automatic inclusion, they would be allowed to provide their employees with details of the remuneration (including ESOP gains) in any format other than the prescribed format.

32 With the change in basis of taxation of gains derived in respect of any ESOP or shares granted under any ESOW Plan and the extension of the scope of the existing incentive schemes for ESOP to shares granted under any ESOW Plan, companies would henceforth also be required, to provide details of all such gains, derived by their employees or ex-employees¹⁶ (other than non-citizen, non-SPR employees where the "deemed exercise" rule as provided under paragraphs 34 to 35 would apply), segregating the ESOP gains and gains from shares granted under any ESOW Plan, and where applicable, further segregating the respective gains into:

- (a) those qualifying for the 50% income tax exemption under the Entrepreneurial EEBR Scheme;
- (b) those qualifying for the 25% income tax exemption (subject to the first \$2,000 of ESOP or ESOW Plan gains being fully tax exempt) under the Company EEBR Scheme; and
- (c) those that do not qualify for tax exemption under either the Entrepreneurial EEBR and Company EEBR Schemes (including any amount of discount enjoyed by an employee on the ESOP or shares granted under any ESOP or ESOW Plan respectively).

33 As is the case of the existing incentive schemes for ESOPs,

¹⁵ The prescribed format is Appendix 8B of Form IR8A.

¹⁶ This requirement would only apply to ex-employees who have been granted ESOPs under ESOP Plans or shares under ESOW Plans of companies in Singapore i.e. local ESOP/ESOW Plans.

- (a) where a qualifying company grants restricted shares to a qualifying employee under any ESOW Plan where the gains derived therefrom can qualify for the 50% tax exemption under the Entrepreneurial EEBR Scheme, the company is required to give, at the time of grant, a written confirmation to the employee confirming that the qualifying criteria of the EEBR Scheme have been met in respect of those shares granted under the ESOW Plan. Annex 5 provides a specimen of such written confirmation, which sets out the minimum information to be incorporated;
- (b) where a qualifying company grants restricted shares to a qualifying employee under any ESOW Plan where the gains derived therefrom can qualify for the 25% income tax exemption (subject to the first \$2,000 of ESOP or ESOW Plan gains being fully tax exempt) under the Company EEBR Scheme, the company is required to give a written confirmation within 4 weeks from 31 December of the year, to the qualifying employee confirming that the qualifying terms and conditions of the scheme have been met in respect of those shares granted under the ESOW Plan. Annex 6 provides a specimen of such written confirmation, which sets out the minimum information to be incorporated;
- (c) where a qualifying company is unable to determine definitively whether an employee has effective control of the company due to reasons such as the use of nominees for the purposes of Entrepreneurial EEBR Scheme or Company EEBR Scheme, it can require the employee to provide a declaration on his beneficial ownership, directly or indirectly, of such voting shares in the company. If the employee does not give the requisite declaration to the company, he cannot be considered as a qualifying employee under the scheme;
- (d) where an employee who is granted restricted shares under any ESOW Plan by a company that qualifies for the Entrepreneurial EEBR Scheme, works for the company for less than 30 hours per week at the time of the grant of the shares, he is required to make a declaration to the company on his total working time per week at that time to enable the company to determine whether he meets the 75% test to qualify him under the scheme.

DEEMED EXERCISE RULE

34 Instead of the earlier announced requirement for companies to track and collect the taxes on ESOP gains from employees who exercise their ESOPs after leaving Singapore, the Government has now decided that employees who are *:

- (a) ***neither Singapore citizens nor SPRs; or***
- (b) ***SPRs leaving Singapore permanently,***

**** updated as at 27 Dec 2002***

will be subject to tax on a “deemed exercise” basis (hereinafter referred to as “deemed exercise rule”) on ESOPs granted by any company under any ESOP Plan while they are exercising employment in Singapore, when they cease employment with the company for which they are exercising employment when they are granted the ESOPs. The “deemed exercise” rule applies not only to unexercised ESOPs which are granted while an individual is exercising employment in Singapore, but also to the following which are granted while an individual is exercising employment in Singapore:

- (a) restricted ESOPs where the moratorium has not been lifted on the date the individual ceases employment with the company for which he is exercising employment when he is granted the ESOPs;
- (b) shares granted under any ESOW Plan with vesting imposed where the beneficial interest from the ownership of the shares has not yet vested to the individual on the date he ceases employment with the company for which he is exercising employment when he is granted the shares;
- (c) restricted shares granted under any ESOW Plan where the moratorium has not been lifted on the date the individual ceases employment with the company for which he is exercising employment when he is granted the shares.

35 The “deemed exercise” rule shall apply to any ESOPs or shares under any ESOW Plan granted on or after 1 January 2003 to an individual while he is exercising employment in Singapore, and where that individual is *:

- (a) neither a Singapore citizen nor an SPR; or**
- (b) an SPR leaving Singapore permanently,**

on the date he ceases employment with the company for which he is exercising employment when he is granted the ESOP or shares under any ESOW Plan. Under the “deemed exercise” rule, the individual concerned is deemed to have derived a final gain in respect of ESOPs and shares granted under any ESOW Plan and the amount of gain is computed in accordance with the following formula:

$$A - B$$

where

A is the open market price¹⁷ of the shares as at one month before the date the individual ceases employment or the date of grant of the ESOPs or of shares under any ESOW Plan, whichever is the later; and

*** updated as at 27 Dec 2002**

¹⁷ Where the market price or open market value is not available, the net asset value of the shares could be used.

B is

- exercise price of the shares under unexercised ESOP; or
- exercise price of the shares under restricted ESOP; or
- price paid or payable for shares acquired under an ESOW Plan with vesting imposed (with no moratorium); or
- price paid or payable for restricted shares acquired under an ESOW Plan,

as the case may be.

Annex 7 illustrates how the “deemed exercise” rule is applied.

36 Where the amount of gain computed based on the formula stated in paragraph 35 is higher than the actual gain derived by an individual as computed based on the following formula:

$C - B$

where

C is

- open market price¹⁸ of the shares on the date of exercise of ESOP;
- open market price¹⁸ of the shares on the date the moratorium is lifted in respect of shares acquired under restricted ESOP;
- open market price¹⁸ of the shares on the date of vesting in respect of shares acquired under an ESOW Plan with vesting imposed (with no moratorium);
- open market price¹⁸ of the shares on the date the moratorium is lifted in respect of restricted shares acquired under an ESOW Plan,

as the case may be;

and

B is

- exercise price of the shares under unexercised ESOP; or
- exercise price of the shares under restricted ESOP;
- price paid or payable for shares acquired under an ESOW Plan with vesting imposed (with no moratorium); or
- price paid or payable for restricted shares acquired under an ESOW Plan,

as the case may be;

the CIT may as an administrative concession and upon application of the affected individual, reassess the tax liability of that individual based on the

¹⁸ Where the market price or open market value is not available, the net asset value of the shares could be used.

gain computed in accordance with the formula [C – B] in the YA to which the year of deemed exercise relates.

Administrative requirements under the “deemed exercise” rule

37 In cases where an employer grants any individual any ESOP or shares under any ESOW Plan while that individual is exercising employment in Singapore, and where the “deemed exercise” rule *as explained in paragraph 35* is applicable to that individual, the employer is required to furnish details of the gains computed in accordance to paragraph 35 when it seeks tax clearance for such individual.

38 An individual whose actual tax liability is lower than that computed under the “deemed exercise” rule and who wishes to apply to the CIT to have a reassessment of his tax liability, must submit -

- (a) his application to the CIT within 6 years from the year of assessment following the year in which the deemed exercise rule is applied;
- (b) relevant documentation to show that the actual tax liability is lower than that computed under the “deemed exercise” rule e.g. a letter from the employer with the following details:

in the case of shares acquired under ESOP:

- the date of exercise of ESOP or the date the moratorium is lifted, as the case may be;
- the open market price of the shares on the date of exercise of ESOP or the date the moratorium is lifted, as the case may be;
- exercise price of the shares;

in the case of shares acquired under ESOW Plan:

- the date of vesting or the date the moratorium is lifted, as the case may be;
- the open market price of the shares on the date of vesting or the date the moratorium is lifted, as the case may be;
- price paid or payable for the shares.

ENQUIRIES

39 Taxpayers who have any queries concerning the above changes in respect of ESOPs and other forms of ESOW Plans may call our Taxpayer Services Division at 1800-252-8677 (**1800-356-8300 with effect from 1 Nov 2002*) for clarification.

Inland Revenue Authority of Singapore

** updated as at 27 Dec 2002*

EXAMPLES ILLUSTRATING THE EFFECT OF CHANGE IN BASIS OF TAXATION OF ESOP GAINS

Example 1

ESOP granted while an individual is exercising employment in Singapore

Mr Mahan, a Singapore citizen is granted ESOP on 25.02.03 by his employer, XYZ Company Ltd, which is a Singapore incorporated company. During his employment with XYZ Company Ltd, Mr Mahan performs his employment duties substantially in Singapore, but is required to travel out of Singapore occasionally to render services to XYZ Company Ltd's clients in the Asia Pacific region. Mr Mahan is seconded to work for a related overseas company from 1.1.04 onwards. During his secondment overseas, Mr Mahan exercises his ESOP on 15.11.04 and ESOP gains¹⁹ amount to \$100,000. His salary from his overseas employment of \$250,000 is not remitted to Singapore during the year 2004. Mr Mahan also does not have any other income from Singapore during the year 2004.

Assuming that Mr Mahan is a tax resident of Singapore for YA 2005 (i.e. he does not wish to avail himself of the concession to opt to be treated as a non-resident for YA 2005) and assuming YA 2003 tax rate structure applies:

Mr Mahan's Income Tax Computation Year of Assessment 2005

	\$
Salary from overseas employment (not remitted)	NIL
ESOP gains (derived from Singapore)	100,000
Assessable income	<u>100,000</u>
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>99,000</u>
Tax on first \$80,000	4,600
On the next \$19,000 @ 15%	2,850
Tax payable	<u>7,450</u>

¹⁹ With the tax change announced in Budget Statement 2002, any gains from the exercise of ESOP that are granted on or after 1 January 2003 while the individual is exercising employment in Singapore are considered to be gains derived from Singapore, irrespective of where the ESOP is exercised, and are to be brought to tax as income of the year in which the ESOP is exercised.

Example 2**ESOP granted while the individual is exercising employment overseas
i.e. prior to his posting to Singapore**

During his employment with EFG-US, Mr Bravo, an American citizen was granted ESOP by the US parent company on 15.7.99. Subsequently, he was seconded by EFG-US to head its related subsidiary in Singapore, EFG-Singapore from 21.5.01. On 15.1.02, Mr Bravo exercised the ESOP that was previously granted during his employment with EFG-US and derived ESOP gains amounting to \$250,000²⁰. Mr Bravo's salary (excluding the ESOP gains) for the full year of 2002 amounts to \$500,000. Mr Bravo has not remitted any foreign income to Singapore or derived any other income from Singapore during the year 2002.

As Mr Bravo is a tax resident of Singapore for YA 2003:

**Mr Bravo's Income Tax Computation
Year of Assessment 2003**

	\$
Salary	500,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	499,000
Tax on first \$320,000	47,000
On the next \$179,000 @ 22%	39,380
Tax payable	86,380

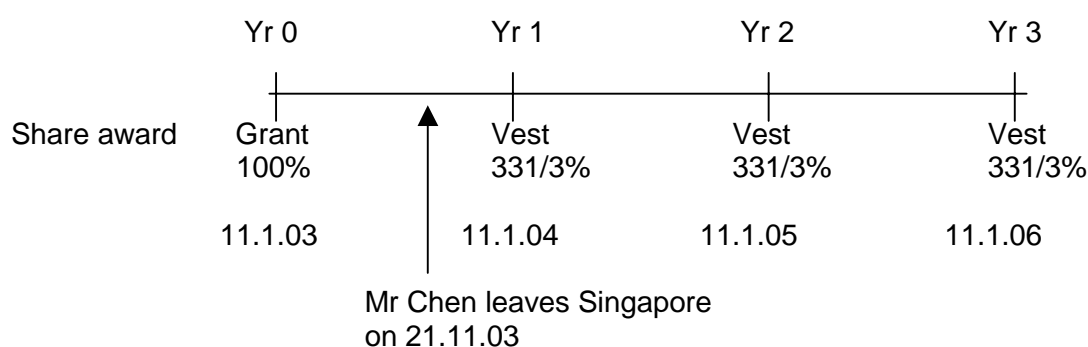
²⁰ With the tax change announced in Budget Statement 2002, any gains from the ESOP exercised on or after 1 January 2002 in respect of ESOP granted while the individual is exercising employment outside Singapore, are not regarded as income derived from Singapore and not be taxable as such in Singapore.

EXAMPLES ILLUSTRATING THE EFFECT OF CHANGE IN BASIS OF TAXATION OF GAINS FROM SHARES GRANTED UNDER ANY ESOW PLAN WITH VESTING IMPOSED (WITH NO MORATORIUM)

Example 1

Shares granted under any ESOW Plan (with vesting imposed but with no moratorium) while an individual is exercising employment in Singapore

Mr Chen, a Singapore citizen is granted share awards by his employer, TCF Singapore Pte Ltd under the TCF PLC group share ownership plan on 11.1.03. TCF Singapore Company Ltd is a Singapore incorporated company while TCF PLC is its UK parent company. Under the group plan, Mr Chen is only entitled to receive 33 1/3% of the share awards on the first anniversary from the date of grant, another 33 1/3% of the share awards on the second anniversary and the balance of the 33 1/3% of the share awards only on the third anniversary as shown below:



Mr Chen is seconded to work in a related subsidiary in China for a 5-year period from 21.11.03. During his secondment to China, Mr Chen does not derive any other income from Singapore nor remit any income to Singapore from outside Singapore. The share awards granted to him under the TCF PLC group share ownership plan while he is exercising employment in Singapore for TCF Singapore Pte Ltd continue to vest to him on the dates shown above. The gains from share awards²¹ accrue to him are \$70,000, \$75,000 and \$72,000 for the years 2004, 2005 and 2006 respectively.

Assuming that Mr Chen is a tax resident of Singapore for YA 2005, YA 2006 and YA 2007 (i.e. he does not wish to avail himself of the concession to opt to

²¹ With the tax change announced in Budget Statement 2002, any gains from shares granted under any ESOW Plan (with vesting imposed) that are granted on or after 1 January 2003 while the individual is exercising employment in Singapore are considered income derived from Singapore, irrespective of where the individual is on the date of vesting, and are to be brought to tax as income of the year in which the shares are vested to him. The gains from share awards in this example are computed based on the difference between the open market price of the TCF PLC shares as at the respective dates of vesting less any amount paid or payable by Mr Chen for the shares.

be treated as a non-resident for the mentioned YAs) and assuming YA 2003 tax rate structure applies:

**Mr Chen's Income Tax Computation
Year of Assessment 2005**

	\$
Gains from share awards (derived from Singapore)	<u>70,000</u>
Assessable income	70,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>69,000</u>
Tax on first \$40,000	1,000
On the next \$29,000 @ 9%	<u>2,610</u>
Tax payable	<u>3,610</u>

**Mr Chen's Income Tax Computation
Year of Assessment 2006**

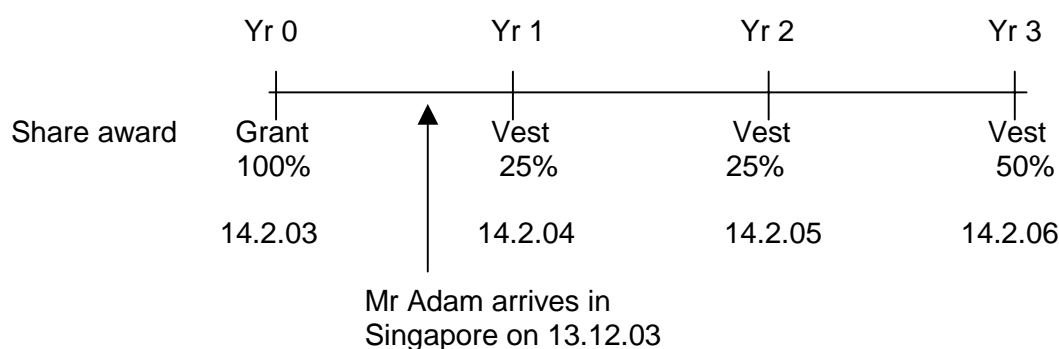
Gains from share awards (derived from Singapore)	<u>75,000</u>
Assessable income	75,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>74,000</u>
Tax on first \$40,000	1,000
On the next \$34,000 @ 9%	<u>3,060</u>
Tax payable	<u>4,060</u>

**Mr Chen's Income Tax Computation
Year of Assessment 2007**

Gains from share awards (derived from Singapore)	<u>72,000</u>
Assessable income	72,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>71,000</u>
Tax on first \$40,000	1,000
On the next \$31,000 @ 9%	<u>2,790</u>
Tax payable	<u>3,790</u>

Example 2**Shares under any ESOW Plan (with vesting imposed but no moratorium) granted while an individual is exercising employment overseas (i.e. prior to his posting to Singapore)**

Mr Adams, a British national is granted share awards under the OPQ group share ownership plan on 14.2.03 by his employer, OPQ-UK Inc. Under the OPQ group share ownership plan, all employees who are granted share awards are only entitled to receive 25% of the share awards on the first anniversary from the date of grant, another 25% of the share awards on the second anniversary and the balance 50% of the share awards on the third anniversary. In the case of Mr Adams, the shares are vested to him as follows:



Subsequent to the granting of the share awards under the OPQ group share ownership plan, Mr Adams is posted to work in OPQ-Singapore Pte Ltd for a 7-year period from 13.12.03. During his employment with OPQ-Singapore Pte Ltd, the share awards that are previously granted by OPQ-UK Inc. continue to be vested to him based on the above schedule stipulated under the OPQ group share ownership plan. Mr Adams derives gains²² from share awards which amount to \$250,000, \$280,000 and \$520,000 for the years 2004, 2005 and 2006 respectively. In addition to the above gains, Mr Adams also earns salaries of \$300,000, \$350,000 and \$400,000 from Singapore for the years 2004, 2005 and 2006 respectively. During the years 2004, 2005 and 2006, Mr Adams has not remitted any income to Singapore. He has also not derived any other income from Singapore during the said years.

As Mr Adams is a tax resident of Singapore for YA 2005, YA 2006 and YA 2007 and has not remitted any foreign income (including the gains from share awards) or derived any other income from Singapore during these 3 YAs and assuming YA2003 tax rate structure applies:

²² With the tax change announced in Budget Statement 2002, any gains from shares under ESOW Plans granted to an individual while he is exercising an employment overseas but vest to him on or after 1 January 2002 are not regarded as income derived from Singapore and therefore not taxed as such in Singapore, even if he is exercising employment in Singapore on the date of vesting.

**Mr Adam's Income Tax Computation
Year of Assessment 2005**

	\$
Salary	300,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	299,000
Tax on first \$160,000	16,600
On the next \$139,000 @ 19%	26,410
Tax payable	43,010

**Mr Adam's Income Tax Computation
Year of Assessment 2006**

	\$
Salary	350,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	349,000
Tax on first \$320,000	47,000
On the next \$29,000 @ 22%	6,380
Tax payable	53,380

**Mr Adam's Income Tax Computation
Year of Assessment 2007**

	\$
Salary	400,000
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	399,000
Tax on first \$320,000	47,000
On the next \$79,000 @ 22%	17,380
Tax payable	64,380

EXAMPLES ILLUSTRATING WHEN THE GAIN DERIVED FROM RESTRICTED ESOPs AND RESTRICTED SHARES UNDER ESOW PLANS IS TO BE TAXED

Example 1 (Restricted ESOPs)

Mr Lai, a Singapore citizen is granted restricted ESOP on 1.3.03 by his employer, YY Singapore Ltd. Under the YY ESOP plan, Mr Lai is given the option to acquire shares of YY Ltd at an exercise price of \$5 (same price as the open market price of the shares on the date of grant). On 4.5.04, Mr Lai exercises the ESOP to acquire 5,000 YY Ltd's shares at \$5 each, when the open market price is \$7.50.

Under the YY ESOP plan, Mr Lai is not allowed to sell the shares within 2 years from the date he exercises the ESOP to acquire the shares. On 4.5.06 (i.e. the date on which the moratorium is lifted), the open market price of YY Ltd's shares is \$7 per share. On 19.12.07, Mr Lai disposes all his 5,000 shares at \$8 per share.

At a glance

Open Market Price per share as at the date of grant (i.e. 1.3.03)	\$5.00
Exercise Price	\$5.00
Open Market Price per share as at the date of exercise (i.e. 4.5.04)	\$7.50
Open Market Price per share as at date the moratorium is lifted (i.e. 4.5.06)	\$7.00
Open Market Price per share as at the date of disposal (i.e. 19.12.07)	\$8.00
Number of Shares	5,000

With the tax change announced in Budget Statement 2002, gains from restricted ESOPs granted on or after 1 January 2003 in respect of employment exercised in Singapore will constitute taxable gains in the year the moratorium is lifted, even though Mr Lai has exercised the option on 4.5.04. Accordingly, gains derived by Mr Lai from the restricted ESOPs would only be brought to tax as income of the year 2006, as the moratorium is lifted on 4.5.06. The amount of ESOP gains made by him is computed as follows:

	\$
Open Market Price of YY Ltd's share as at date the moratorium is lifted (i.e. 4.5.06)	7.00
Less: Exercise price	5.00
ESOP gains per share	<u>2.00</u>
Number of shares acquired	<u>5,000</u>
Amount of ESOP gains (\$2 x 5,000 shares)	<u>10,000</u>

Assume that Mr Lai is a tax resident of Singapore for YA 2007. Besides ESOP gains, he also earns a salary of \$200,000 from Singapore for the year 2006.

Mr Lai has no other income in the year 2006. Assume YA 2003 tax rate structure applies:

**Mr Lai's Income Tax Computation
Year of Assessment 2007**

	\$
Salary	200,000
ESOP gains (derived from Singapore)	10,000
Assessable Income	<u>210,000</u>
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>209,000</u>
Tax on first \$160,000	16,600
On the next \$49,000 @ 19%	9,310
Tax payable	<u>25,910</u>

Example 2 (Restricted Shares Granted under ESOW Plans)

Mr Sri, a Singapore permanent resident is granted 10,000 shares with moratorium i.e. restricted share awards under the YC share award plan on 1.6.03 by his employer YC Singapore Pte Ltd. On 1.6.03, the open market price of the share is \$3.50. All share awards granted under the YC share award plan have 2-year moratorium from the date of grant. Therefore Mr Sri is not allowed to dispose of the shares any time prior to 1.6.05. On 1.6.05, the open market price of YC Singapore Pte Ltd's shares is \$3.20 per share. Mr Sri sells off all his 10,000 shares at \$4.20 per share on 1.2.06.

At a glance

Open Market Price per share as at the date of grant (i.e. 1.6.03)	\$3.50
Price paid by Mr Sri for the shares	NIL
Open Market Price per share as at the date the moratorium is lifted (i.e. 1.6.05)	\$3.20
Open Market Price per share as at the date of disposal (1.2.06)	\$4.20
Number of Shares	10,000

With the tax change announced in Budget Statement 2002, gains from shares under any ESOW Plan granted on or after 1 January 2003 in respect of employment exercised in Singapore will constitute taxable gains to Mr Sri on the date the moratorium is lifted i.e. 1.6.05, even though the shares under the ESOW Plan are granted to him on 1.6.03. Accordingly, gains derived by Mr Sri from the restricted shares under the ESOW Plan would only be brought to tax as income of the year 2005. The amount of gains made by him from restricted share awards is computed as follows:

	\$
Open Market Price of YC Singapore Pte Ltd's share as at the date the moratorium is lifted (i.e. 1.6.05)	3.20
Less: Price paid by Mr Sri for the shares	<u>NIL</u>
Share award gains per share	<u><u>3.20</u></u>
Number of shares acquired	<u>10,000</u>
Total share award gains (\$3.20 x 10,000 shares)	<u><u>32,000</u></u>

Assume that Mr Sri is a tax resident of Singapore for YA2006 and he only has salary income of \$120,000 for the year 2005. Assume YA 2003 tax rate structure applies:

**Mr Sri's Income Tax Computation
Year of Assessment 2006**

	\$
Salary	120,000
Share award gains (derived from Singapore)	32,000
Assessable Income	<u>152,000</u>
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>151,000</u>
Tax on first \$80,000	4,600
On the next \$71,000 @ 15%	10,650
Tax payable	<u>15,250</u>

SOME REQUIREMENTS²³ APPLICABLE TO COMPANY EMPLOYEE EQUITY-BASED REMUNERATION (COMPANY EEBR) SCHEME

1 In cases where ESOPs or shares are granted to employees of a qualifying company under any Group ESOP or ESOW Plan operated by its parent company, the determination of whether or not the 50% requirement under the Company EEBR Scheme has been met shall continue to be made with reference to the employees of the qualifying company, and not the employees of the Corporate Group.

2 Where an ESOP or ESOW Plan can concurrently meet all the qualifying conditions under both the Entrepreneurial Employee Equity-based Remuneration (Entrepreneurial EEBR) Scheme and the Company EEBR Scheme, the company can only avail itself of either one of the two schemes. Once the company has availed that plan to the Entrepreneurial EEBR Scheme, the effects of the Entrepreneurial EEBR Scheme shall apply to all tranches of ESOPs or of shares that are subsequently granted under that particular plan, as long as the qualifying conditions of the Entrepreneurial EEBR Scheme continue to be met. In addition, that plan will also not be allowed to come within the Company EEBR Scheme in respect of any subsequent tranches of ESOPs or of shares granted under that same ESOP or ESOW Plan, unless it can no longer meet the qualifying conditions under the Entrepreneurial EEBR Scheme (e.g. the aggregate market value of its gross assets has exceeded \$100 million). This is also provided that it is able to meet all the conditions of the Company EEBR Scheme.

3 Where the company mentioned in paragraph 2 of this Annex were to first avail the plan under the Company EEBR Scheme, the effects of the Company EEBR Scheme shall apply to all tranches of ESOPs or of shares subsequently granted under that same ESOP or ESOW Plan, as long as the qualifying conditions of the Company EEBR Scheme continue to be met. However, in such a case, any subsequent tranches of ESOPs or of shares granted under that same ESOP or ESOW Plan would no longer be allowed to come within the Entrepreneurial EEBR Scheme even if the qualifying conditions under the Entrepreneurial EEBR Scheme can be met. Accordingly, any gains arising from ESOPs or shares under ESOW Plans subsequently granted that can no longer meet the qualifying conditions of the Company EEBR Scheme shall be taxed in full.

4 In addition, under no circumstances can any equity-based plan operated by a company for its employees concurrently qualify for tax exemption under both the Entrepreneurial EEBR Scheme and Company EEBR Scheme.

²³ The requirements provided in this Annex are not exhaustive. Other requirements applicable to Company ESOP Scheme are set out in IRAS Circular on "Company Stock Option Scheme" issued on 31 March 2001, shall also apply with the necessary modification to Company Employee Equity-based Remuneration Scheme.

EXAMPLES ILLUSTRATING HOW THE 50% REQUIREMENT UNDER THE COMPANY EEBR SCHEME IS TO BE DETERMINED

Example 1

Sunshine Company Pte Ltd which is incorporated in Singapore, is a subsidiary of US-listed Sunshine Inc. Sunshine Inc operates the following equity-based remuneration plans that are offered to its own employees as well as employees of companies within the Sunshine's corporate group:

(a) Sunshine Group ESOP Plan A

This plan imposes a vesting period requirement similar to that imposed by the SGX rules;

(b) Sunshine Group Share Award Plan B

This share award plan that offers shares at no cost to selected employees, imposes a 1-year minimum holding period from the date of grant of the award;

(c) Sunshine Group Employee Share Purchase Plan C

This plan allows employee to acquire shares in the company at a 15% discount off the market price of the shares at the time of grant. Unlike plan B, there is no minimum holding period requirement for shares acquired under this plan.

At a glance

	Equity-based Remuneration Plan	Whether satisfies the minimum vesting or holding period requirement?
a	Sunshine Group ESOP Plan A	Yes, since the plan imposes a vesting period requirement similar to that imposed by the SGX rules
b	Sunshine Group Share Award Plan B	Yes, since the plan imposes a 1-year minimum holding period ²⁴ requirement
c	Sunshine Group Employee Share Purchase Plan C	No, since the plan does not impose minimum holding period requirement

During the year 2003, Sunshine Company Pte Ltd (i.e. the qualifying company) offers some of its employees the option to participate in the three plans operated by Sunshine Inc. The offers were made in 3 different tranches shown below:

²⁴ As set out under paragraph 21 of the main circular.

SUNSHINE GROUP ESOP PLAN A

<u>Categories of employees</u>	<u>Number of employees offered</u>			Total as at 31.12.03
	<u>Tranche A</u> 11.1.03	<u>Tranche B</u> 19.6.03	<u>Tranche C</u> 13.12.03	
Offered on				
Full time employees with 1 year or more service and non-executive directors	50	46	550*	646
Full time employees with less than 1 year service	-	-	-	-
Part time employees with 1 year or more service	2	-	3	5
Part time employees with less than 1 year service	-	-	-	-
Total	52	46	553	651

SUNSHINE GROUP SHARE AWARD PLAN B

<u>Categories of employees</u>	<u>Number of employees offered</u>			Total as at 31.12.03
	<u>Tranche A</u> 11.1.03	<u>Tranche B</u> 19.6.03	<u>Tranche C</u> 13.12.03	
Offered on				
Full time employees with 1 year or more service and non-executive directors	55	146	120	321
Full time employees with less than 1 year service	-	3	3	6
Part time employees with 1 year or more service	-	3	3	6
Part time employees with less than 1 year service	-	1	1	2
Total	55	153	127	335

*Includes 5 employees who are also offered share awards under the Sunshine Group Share Award Plan B within the same calendar year.

SUNSHINE GROUP EMPLOYEE SHARE PURCHASE PLAN C

<u>Categories of employees</u>	<u>Number of employees offered</u>			Total as at 31.12.03
	<u>Tranche A</u> 11.1.03	<u>Tranche B</u> 19.6.03	<u>Tranche C</u> 13.12.03	
Offered on				
Full time employees with 1 year or more service and non-executive directors	20	100	10	130
Full time employees with less than 1 year service	-	5	5	10
Part time employees with 1 year or more service	-	5	5	10
Part time employees with less than 1 year service	-	1	1	2
Total	20	111	21	152

As at 31.12.03, the Sunshine's Corporate Group has 300,000 employees worldwide. The subsidiary in Singapore, Sunshine Company Pte Ltd, has 2,200 employees comprising:

Full time employees with 1 year or more service and non-executive directors	1,580
Full time employees with less than 1 year service	250
Part time employees with 1 year or more service	220
Part time employees with less than 1 year service	150
Total	2,200

With the extension of the existing incentive schemes for ESOPs to shares granted under ESOW Plans that satisfy the minimum holding period requirement (explained in paragraph 21 of the circular), employees who are offered ESOPs under ESOP Plans that satisfy the minimum vesting period requirement or shares under ESOW Plans that satisfy the minimum holding period requirement may be aggregated to determine whether or not the 50% requirement under the Company EEBR Scheme is met. As the Sunshine Group Employee Share Purchase Plan C does not impose any minimum holding period requirement, the number of employees who are offered shares under such plan will not be included in the numerator of the formula for the

determination of the 50% requirement under the Company EEBR Scheme shown below:

Total no. of qualifying company's employees who are offered ESOPs under ESOP plans that satisfy the minimum vesting period requirement and/ or shares under ESOW Plans that satisfy the minimum holding period requirement during the year

Total no. of qualifying company's employees as at 31.12.03

$$\begin{aligned} &= [52+46+(553-5)+55+153+127] / 2,200 \times 100\% \\ &= 44.59\% < 50\% \end{aligned}$$

Since the 50% requirement under the Company EEBR Scheme is not satisfied, no tax exemption under the Company EEBR Scheme will be granted to any employee in respect of gains derived from the ESOPs or restricted shares granted under Sunshine Group ESOP Plan A or Sunshine Group Share Award Plan B respectively.

No tax exemption will also be given to employees in respect of gains derived from shares acquired under Sunshine Group Employee Share Purchase Plan C. This is because the plan has no requisite holding requirement, and therefore does not qualify for either the Entrepreneurial EEBR Scheme or Company EEBR Scheme.

Example 2

Same information as in example 1 except that Sunshine Group Employee Share Purchase Plan C has a 1-year minimum holding period requirement on the shares acquired under that plan.

In this case, the 50% requirement under the Company EEBR Scheme is satisfied as shown below:

Total no. of qualifying company's employees who are offered ESOPs under ESOP Plans that satisfy the minimum vesting period requirement and/ or shares under ESOW Plans that satisfy the minimum holding period requirement during the year

Total no. of qualifying company's employees as at 31.12.03

$$\begin{aligned} &= [52+46+(553-5)+55+153+127+20+111+21] / 2,200 \times 100\% \\ &= 51.5\% > 50\% \end{aligned}$$

As both the 50% requirement and the minimum vesting period requirement for ESOPs or the minimum holding period requirement for shares under ESOW Plans, as the case may be, are satisfied, tax exemption would be granted under the Company EEBR Scheme to qualifying employee in respect of

specified amount of gains²⁵ made from any of all 3 equity-based remuneration plans operated by the Sunshine corporate group. This is further provided that all other qualifying criteria for the Scheme are met.

Example 3

Same information as in example 2, except that:

- (a) the parent company, Sunshine Inc. is a Singapore incorporated company that carries on business in Singapore and the aggregate market value of the gross assets of the Sunshine corporate group does not exceed \$100 million, as at the date of the grant of the ESOP under Group ESOP Plan A, and offer of shares under the Group Share Award Plan B and Group Share Purchase Plan C;
- (b) all 3 Equity-based Remuneration plans are operated and granted by Sunshine Inc. to the employees of Sunshine Company Pte Ltd (“Qualifying company”);
- (c) all 3 Equity-based Remuneration plans operated by Sunshine Inc. can concurrently meet all the qualifying conditions under both Entrepreneurial EEBR and Company EEBR Schemes; and
- (d) as at 31.12.03, Sunshine Company Pte Ltd, has 1,500 employees comprising:

Full time employees with 1 year or more service and non-executive directors	1,080
Full time employees with less than 1 year service	250
Part time employees with 1 year or more service	120
Part time employees with less than 1 year service	50
Total	1,500

Assuming that Sunshine Company Pte Ltd opts for tax exemption under:

- (i) Entrepreneurial EEBR Scheme to apply in respect of gains made from “Sunshine Group Share Award Plan B”; and
- (ii) Company EEBR Scheme to apply in respect of gains made from “Sunshine Group ESOP Plan A” and “Sunshine Group Employee Share Purchase Plan C”.

For the purpose of computing the 50% requirement under the Company EEBR Scheme, the number of employees who are offered share awards

²⁵ Please refer to paragraph 22(c) of the main circular.

under the Sunshine Group Share Award Plan B should be excluded from the numerator and the 50% requirement would be computed as follows:

Total no. of qualifying company's employees offered ESOPs under the
"Sunshine Group ESOP Plan A and shares under the "Sunshine Group
Employee Share Purchase Plan C during the year

Total no. of qualifying company's employees as at 31.12.03

$$\begin{aligned} &= [52+46+553^{26}+20+111+21] / 1,500 \times 100\% \\ &= 53.5\% > 50\% \end{aligned}$$

In this case, given that the 50% requirement under the Company EEBR Scheme is satisfied, all qualifying employees who are offered ESOPs under the Sunshine Group ESOP Plan A and shares under the Sunshine Group Employee Share Purchase Plan and derive gains therefrom may enjoy tax exemption under the scheme (assuming that all other qualifying conditions are satisfied).

On the other hand, qualifying employees who are offered share awards under the Sunshine Group Share Award Plan B and derive gains therefrom may enjoy tax exemption under Entrepreneurial EEBR Scheme (assuming that all other qualifying conditions are satisfied).

In this example, as Sunshine Company Pte Ltd has availed the Sunshine Group Share Award Plan B to qualify for the Entrepreneurial EEBR Scheme, the effects of the Entrepreneurial EEBR Scheme shall apply to all subsequent tranches of share awards that are granted under that plan, as long as the qualifying conditions of the Entrepreneurial EEBR Scheme continue to be met. In addition, the Sunshine Group Share Award Plan B will also not be allowed to come within the Company EEBR Scheme in respect of any subsequent tranches of share awards granted under the same plan unless it can no longer meet the qualifying conditions under the EEBR Scheme (e.g. the aggregate market value of Sunshine corporate group's gross assets has exceeded \$100 million) and only provided that it is able to meet all the conditions of the Company EEBR Scheme.

On the other hand, as Sunshine Company Pte Ltd has availed the Sunshine Group ESOP Plan A and Sunshine Group Employee Share Purchase Plan C to qualify for the Company EEBR Scheme, the effects of the Company EEBR Scheme shall apply to all tranches of ESOPs or shares, as the case may be, that are subsequently granted under the respective plans, as long as the qualifying conditions of the Company EEBR Scheme continue to be met. However, any subsequent tranches of ESOPs or of shares, as the case may

²⁶ The numerator includes the 5 employees who are concurrently offered ESOPs under Sunshine Group ESOP Plan A and share awards under the Sunshine Group Share Award Plan B. Those other employees who are offered Sunshine Group Share Award Plan B are however excluded from the numerator since the company opts for tax exemption under Entrepreneurial EEBR Scheme to apply in respect of gains made from Sunshine Group Share Award Plan B.

be, that are subsequently granted under either plan would no longer be allowed to come within the Entrepreneurial EEBR Scheme even if the qualifying conditions under that Scheme can be met. Accordingly, any gains arising from any ESOPs or shares subsequently granted under either plans that can no longer meet the qualifying conditions of the Company EEBR Scheme shall be taxed in full.

**CONFIRMATION BY COMPANY THAT ESOPS OR SHARES UNDER
EMPLOYEE SHARE OWNERSHIP (ESOW) PLANS GRANTED QUALIFY
FOR EXEMPTION UNDER ENTREPRENEURIAL EMPLOYEE EQUITY-
BASED REMUNERATION SCHEME**

Specimen

<Employee's name & identification number>

<Employee's address>

<Date: day/month/year>

Dear <Employee's name>

**QUALIFYING CRITERIA UNDER THE ENTREPRENEURIAL EMPLOYEE EQUITY-
BASED REMUNERATION SCHEME**

Pursuant to the <employee stock option/employee share ownership (ESOW) plan*> operated by <name of the company>, you have been granted on <date of grant>, stock options to acquire <number> ordinary shares / <number> ordinary shares under the ESOW plan in the company at any time during <effective period of option> at <exercise price/ price to be paid> per share.

This is to confirm that on the date of the grant of the above mentioned *option(s)/ shares under the ESOW Plan, the company has met the criteria to be a qualifying company and the company's *ESOP/ ESOW Plan has met the conditions²⁷ for an "Entrepreneurial Employee Equity Based Remuneration Scheme". Given that you *have / have confirmed to have met the criteria as a qualifying employee, as defined in the above IRAS' circulars, on the date of the grant of stock options/shares, you will be able to enjoy the 50% income tax exemption on gains derived by you from the exercise of the stock options/shares acquired under the ESOW plan. However, this is provided you have not already enjoyed the 50% income tax exemption on the aggregated amount of ESOP gains and the gains from shares acquired under the ESOW Plan exceeding \$10 million over a period of 10 years²⁸ commencing from the year the partial tax exemption is first enjoyed by you.

You should retain this letter and upon request by the CIT of Income Tax, produce it to him for verification.

Name, designation and signature
of Authorized Personnel of company

*Delete whichever is not applicable

²⁷ As set out in IRAS' circular on "Entrepreneurial Employee Stock Option Scheme" dated 22 May 2000 and IRAS circular on "Changes to tax treatment of employee stock options and other forms of employee share ownership plans" dated 31 August 2002.

²⁸ The 10-year period will commence from the year the tax exemption under the Entrepreneurial Stock Option scheme (renamed as Entrepreneurial Employee Equity-based Remuneration Scheme) is first enjoyed by you.

CONFIRMATION BY COMPANY THAT ESOPS OR SHARES UNDER EMPLOYEE SHARE OWNERSHIP (ESOW) PLANS GRANTED QUALIFY FOR EXEMPTION UNDER COMPANY EMPLOYEE EQUITY-BASED REMUNERATION SCHEME

Specimen

<Employee's name & identification number>

<Employee's address>

<Date: day/month/year>

Dear < Employee's name>

QUALIFYING CRITERIA UNDER THE COMPANY EMPLOYEE EQUITY-BASED REMUNERATION SCHEME

Pursuant to the <employee stock option/employee share ownership (ESOW) plan*> operated by <name of company>, you have been granted on <date(s) of grant> stock options to acquire <number> ordinary shares / <number> ordinary shares under the ESOW plan in the company at any time during <effective period of option> at <exercise price/ price to be paid> per share.

This is to confirm that on the date(s) of the grant of the above mentioned option(s)/shares under the ESOW Plan, the company has met the criteria to be a qualifying company under the Scheme. In addition, the <employee stock option/employee share ownership (ESOW) plan*> operated by the company has also met the terms and conditions²⁹ for a "Company Employee Equity Based Remuneration Scheme". Given that you *have/ have confirmed to have met the criteria²⁷ as a qualifying employee, on the date(s) of the grant of option/shares acquired under the ESOW plan, you will be able to enjoy tax exemption on the aggregated amount of stock option gains arising from the exercise of the options and/ or gains from shares acquired under the ESOW plan for each year as follows:

- full tax exemption on the first \$2,000 of aggregated amount of stock option gains and gains from shares acquired under the ESOW plan;
- tax exemption of 25% on the remaining aggregated amount of stock option gains and gains from shares acquired under the ESOW plan.

However, you will qualify for the above tax exemption provided that you have not already enjoyed the above tax exemption on aggregated amount of stock option gains and gains from shares acquired under the employee share ownership plan exceeding \$1 million over a period of 10 years, commencing from the year the tax exemption under the Company Employee Equity-based Remuneration Scheme³⁰ is first enjoyed by you.

²⁹ As set out in IRAS' circular on "Company Stock Option Scheme" dated 31 March 2001 and IRAS' circular on "Changes to tax treatment of employee stock options and other forms of employee share ownership plans" dated 31 August 2002.

³⁰ The 10-year period will commence from the year the tax exemption under the Company Stock Option scheme (renamed as Company Employee Equity based remuneration scheme) is first enjoyed by you.

You should retain this letter and upon request by the CIT of Income Tax, produce it to him for verification.

Name, designation and signature
of Authorized Personnel of company

* Delete whichever is not applicable

EXAMPLES ILLUSTRATING HOW THE “DEEMED EXERCISE RULE” IS APPLIED

Example 1

Mr Greg, an American, exercises employment in Singapore from 1.11.02 to 30.9.04. During his employment in Singapore, Mr Greg is granted ESOPs on 1.9.03 by his employer, TK Singapore Ltd. On 2.9.04, TK Singapore Ltd seeks tax clearance for Mr Greg. A Form IR21 is submitted to IRAS showing employment income of \$200,000. As at 2.9.04, Mr Greg has not exercised the ESOPs where he may acquire 50,000 shares of TK Singapore Ltd at an exercise price of \$1 per share. On 30.8.04 (one month before the date of cessation of employment), the open market price of the share is \$1.50.

Under the “deemed exercise rule” (see paragraph 35 of main circular), the ESOPs granted to Mr Greg are deemed to be exercised on 30.8.04 (one month before the date of cessation of employment) and the ESOP gains are computed as follows:

Open market price of TK shares as at 30.8.04	\$ 1.50
Less: Exercise Price	\$ 1.00
“Deemed” ESOP gains per share (derived from Singapore)	\$ 0.50
Number of shares	50,000
Total “deemed” ESOP gains (derived from Singapore)	\$25,000

Assume that Mr Grey has no other income in 2004 and YA 2003 tax rate structure applies:

Mr Greg’s Income Tax Computation Year of Assessment 2005

	\$
Employment income	200,000
“Deemed” ESOP gains	25,000
Assessable Income	<u>225,000</u>
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u>224,000</u>
Tax on first \$160,000	16,600
On the next \$64,000 @ 19%	12,160
Tax payable	<u><u>28,760</u></u>

Example 2

Same information as in example 1 except that Mr Greg was granted ESOPs by TK Singapore Ltd only on 15.9.04 instead of 1.9.03.

Under the “deemed exercise rule” (see paragraph 35 of main circular), the ESOPs granted to Mr Greg are deemed to be exercised on 15.9.04 (the later of the date of grant of ESOP or one month before the date of cessation of employment). Assuming that the open market price of TK shares as at 15.9.04 is \$1.20, the ESOP gains are computed as follows:

Open market price of TK shares as at 15.9.04	\$ 1.20
Less: Exercise Price	\$ 1.00
“Deemed” ESOP gains per share	\$ 0.20
Number of shares	50,000
Total “deemed” ESOP gains	\$10,000

Assume that Mr Greg has no other income in 2004 and YA 2003 tax rate structure applies:

**Mr Greg’s Income Tax Computation
Year of Assessment 2005**

	\$
Employment income	200,000
“Deemed” ESOP gains	10,000
Assessable Income	<u>210,000</u>
Less: Earned income relief (assume no other personal reliefs claimed)	1,000
Chargeable income	<u><u>209,000</u></u>
Tax on first \$160,000	16,600
On the next \$49,000 @ 19%	9,310
Tax payable	<u><u>25,910</u></u>

