

IRAS Supplementary e-Tax Guide

**Tax Treatment of Employee Stock Option and
other forms of Employee Share Ownership
Plans – Alternative to the deemed exercise rule**



INLAND REVENUE
AUTHORITY
OF SINGAPORE

Published by
Inland Revenue Authority of Singapore

Published on 19 Aug 2004
Second edition published on 15 Apr 2011
[Updated the percentage from 10% to 25% in
the paragraph immediately after sub-paragraph
(b) of Annex 2, inserted new footnote 10 to
Annex 2 and replaced Annex 4 with the latest
version of Form IR21-Appendix 3 (updated as
at 15 Apr 2011)]

© Inland Revenue Authority of Singapore

All rights reserved. No part of this publication
may be reproduced or transmitted in any form
or by any means, including photocopying and
recording without the written permission of the
copyright holder, application for which should
be addressed to the publisher. Such written
permission must also be obtained before any
part of this publication is stored in a retrieval
system of any nature.

Table of Contents

Introduction	4
Tracking Option.....	5
Effective date	6
Qualifying Criteria	6
Requirements under the Tracking Option	7
Administrative Requirements	8
Enquiries	9
ANNEX 1 - Details of information to be furnished by the employer in order to satisfy the criteria that the employer's human resource and computer systems are able to track the ESOPs or shares under any ESOW plan	10
ANNEX 2 - Details of information to be furnished by the employer in order to satisfy the criteria that the company that employs the foreign employee has met adequate capital requirements.....	11
ANNEX 3 - Specimen of letter of undertaking for employers who would like to opt for the tracking option	12
ANNEX 4 - Details of unexercised or restricted ESOP or unvested or restricted shares under other forms of ESOW Plans as at date of cessation of employment/departure from Singapore and would be tracked by employer ..	14

IRAS SUPPLEMENTARY e-TAX GUIDE

TAX TREATMENT OF EMPLOYEE STOCK OPTION AND OTHER FORMS OF EMPLOYEE SHARE OWNERSHIP PLANS - ALTERNATIVE TO THE DEEMED EXERCISE RULE

INTRODUCTION

1 The “deemed exercise” rule was explained in paragraphs 34 to 38 of the IRAS Circular on “Changes to Tax Treatment of Employee Stock Options and Other Forms of Employee Share Ownership Plans” which was revised on 27 Dec 2002.

2 Briefly, under the “deemed exercise” rule, an individual who is:

- (a) neither a Singapore citizen nor a Singapore permanent resident (SPR);
or
- (b) a SPR leaving Singapore permanently upon cessation of employment in Singapore

(hereinafter referred to as a “foreign employee”) shall, at the time he ceases employment in Singapore, be subject to tax on a “deemed exercise” basis, for any unexercised or restricted¹ employee stock options (“ESOPs”) and any unvested² or restricted³ shares under any other form of employee share ownership (“ESOW”) plan granted to him on or after 1 January 2003 while he was exercising employment in Singapore. The foreign employee is deemed to have derived a final gain⁴ (also referred to as a “deemed gain”) in respect of the unexercised or restricted ESOPs, or the unvested or restricted shares under any ESOW plan, as the case may be, at the time he ceases

¹ Restricted employee stock options (ESOPs) refer to 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.

² Unvested shares granted under any other form of employee share ownership (ESOW) plan refer to shares 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.

³ Restricted shares granted under any ESOW plan refer to shares 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.

⁴ The amount of final gain is computed in accordance with the formula: $A - B$ where:
A is the open market price 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
B is

- exercise price of the shares under unexercised ESOPs; or
- exercise price of the shares under restricted ESOPs; 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.

employment in Singapore with the company which granted him the ESOPs or the shares under any ESOW plan (i.e. at the time of tax clearance).

3 Since the implementation of the “deemed exercise” rule, the Government has received feedback from some companies that they prefer to keep track of when the foreign employee exercises the ESOPs that were unexercised or when the shares acquired under any ESOP plan are no longer subjected to any restriction or when the shares under any ESOW plan that were unvested or restricted at the time he ceases employment in Singapore vest or are no longer subjected to any restriction (hereinafter referred to as the “income realization event”) instead of allowing the foreign employee to be subjected to the “deemed exercise” rule at the time of tax clearance. These companies were also willing to undertake to pay the income tax on the actual gains⁵ at the time of the income realization event. In view of the representations received, the Government has now decided to allow the foreign employees of a company to be released from the “deemed exercise” rule, provided the employer is able to satisfy certain qualifying conditions.

TRACKING OPTION

4 This circular provides details on the alternative that allows a company the option to track when the income realization event of the foreign employee occurs. Upon the occurrence of such an event, the employer will compute and report the gains from the income realization event to Comptroller of Income Tax (CIT) and also undertake to collect and pay the tax on such gains to CIT. The above is collectively referred to as the “Tracking Option”. The “deemed exercise” rule at the time of tax clearance will not apply to any foreign employee whose employer has applied for and been granted approval to adopt the Tracking Option⁶.

⁵ The actual gains derived by an individual is computed based on the following formula: C – B

where:

C is

- open market price of the shares on the date of exercise of ESOPs;
- open market price of the shares on the date the moratorium is lifted in respect of shares acquired under restricted ESOPs;
- open market price 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 price 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 ESOPs; or
- exercise price of the shares under restricted ESOPs;
- 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.

⁶ This tax change has also been provided for under sections 10(7A) to (7C) of the Income Tax Amendment Bill 2004.

EFFECTIVE DATE

5 Any employer that grants ESOPs or shares under any ESOW plan on or after 1 Jan 2003 to any of its foreign employees is eligible for the Tracking Option, provided certain qualifying conditions and requirements as elaborated below are met. However, cases where the “deemed exercise” rule has been applied and the assessments already finalized will not be eligible for the Tracking Option.

QUALIFYING CRITERIA

6 An employer has to satisfy the following qualifying criteria in order to be considered for the Tracking Option:

i) Qualifying Employer

7 To qualify for the Tracking Option, an employer that grants ESOPs or shares under any ESOW plan to its employees must be a Singapore incorporated company or a branch of a foreign incorporated company registered in Singapore under the Companies Act and carrying on business activities in Singapore.

8 Where the ESOPs or the shares under any ESOW plan are not granted by the employer in Singapore but by its parent company who is operating a Group ESOP or ESOW Plan, the employer can still qualify for the Tracking Option if the employer satisfies the criteria stated in paragraph 7 and does not separately operate an ESOP or ESOW plan on its own at the time of the grant of the ESOPs or the shares, as the case may be.

ii) Employer’s Human Resource and Computer Systems are able to track the ESOPs/ Shares under ESOW Plans

9 The employer must have human resource and computer systems that are able to track the status of the ESOPs or the shares under any ESOW plan as well as the gains from the income realization event. Details of the information that an employer needs to furnish to satisfy this criterion are elaborated in Annex 1.

iii) The Company that Employs the Foreign Employee has met Adequate Capital Requirements

10 Please refer to Annex 2 for details of the information that an employer needs to furnish in order to satisfy this criterion.

iv) Excellent Taxpaying Record for the Past 3 Years

11 To satisfy this criterion, the employer must not have any record of late filing of tax returns, late payment of taxes, or have committed any offence under the Income Tax Act for the 3 years immediately before the date of application.

REQUIREMENTS UNDER THE TRACKING OPTION

12 Once the employer opts for the Tracking Option in respect of a particular foreign employee, it would need to track ALL unexercised or restricted ESOPs and unvested or restricted shares granted under any ESOW plan held by that foreign employee at the time the foreign employee ceases employment in Singapore. The employer will not be allowed to selectively apply the Tracking Option only to certain tranches of unexercised or restricted ESOPs or unvested or restricted shares granted under any ESOW plan held by that foreign employee or to subsequently opt out of the Tracking Option.

13 The employer is also required to provide a Letter of Undertaking (LOU) [a specimen is attached at Annex 3] to do the following in respect of each foreign employee covered under the Tracking Option:

- (a) to keep track of the occurrence of the income realization event, regardless of whether the foreign employee remains in the employer's employment;
- (b) to compute and report the amount of gains from any income realization event to CIT within 30 days from the occurrence of such event⁷;
- (c) to furnish an annual return by 31 January each year to CIT providing details of the status of the unexercised or restricted ESOPs or the unvested or restricted shares under any ESOW Plan as at 31 December of the previous year⁸;
- (d) to notify CIT at least 30 days in advance of the company's intention to cease carrying on business in Singapore due to corporate restructuring, merger etc.
- (e) to notify CIT immediately in the event of the death of the foreign employee
- (f) to collect and pay the income tax due on the actual gains that arise from the income realization event, upon receipt of the CIT's notice of assessment in respect of those gains.

14 In the event that an employer defaults on any of the requirements in paragraph 13 or where notice has been given under paragraph 13(d) and (e) above, CIT will raise an assessment based on the deemed gains computed under section 10(7) of the Income Tax Act ("ITA") and the deemed gains will be deemed to accrue in the year of default or notice, as the case may be. CIT may also impose a penalty on the employer of 200% of the tax assessed if the company defaults on any of the requirements in paragraph 13. In addition, the employer may also be disallowed from adopting the Tracking Option in future in respect of other foreign employees if it does not comply with any requirement under the Tracking Option.

⁷ Please refer to paragraph 20 for more details.

⁸ Please refer to paragraph 19 for more details.

15 For all other foreign employees whom the employer did not opt for the Tracking Option, the “deemed exercise” rule will continue to apply at the time such employees cease employment in Singapore with the employer.

ADMINISTRATIVE REQUIREMENTS

16 Where an employer wishes to opt for the Tracking Option, the employer is required to submit a written application to the Ministry of Finance (MOF) or CIT⁹, furnishing the details required under paragraphs 9 and 10 and confirming that the qualifying criteria under paragraphs 7, 8 and 11 have been met. The application has to be submitted at least 2 months before the foreign employee ceases employment with the employer.

17 Once the employer’s application for the Tracking Option is approved, the employer has to provide a Letter of Undertaking (LOU) for each foreign employee whom it is going to track, attesting to the fact that it has made an irrevocable option to track the gains from the ESOPs or the shares under any ESOW plan and pay over the tax on such gains to CIT in respect of those foreign employees. The LOU has to be submitted together with the foreign employees’ “Notification of a Non-Citizen Employee’s Cessation of Employment or Departure from Singapore” (Form IR21).

18 Despite the approval granted to the employer to adopt the Tracking Option in respect of a particular foreign employee, the employer is still required to seek tax clearance in respect of all other income of that employee and submit the Form IR21 within the stipulated period. The employer also has to complete the Form IR21-APPENDIX 3, which provides details on any unexercised or restricted ESOPs and any unvested or restricted shares under any ESOW plan, as at the date of cessation of employment, which the employer is going to track. Annex 4 provides a specimen of the Form IR21-APPENDIX 3.

19 By 31 January every year, the employer has to furnish to CIT complete details of the status of the unexercised or restricted ESOPs or the unvested or restricted shares granted under any ESOW plan held by that foreign employee as at 31 December of the previous year, until the occurrence of the income realization event.

20 On the occurrence of an income realization event, the employer is required to submit an additional Form IR21 to CIT, within 30 days, to report the gains from the ESOPs or the shares under the ESOW plan. IRAS will then raise an advance assessment in respect of such gains and send the Notice of Assessment (NOA) to the employer for it to make payment within the stipulated timeframe stated on the NOA.

⁹ Applications before the gazette of the Income Tax Amendment Bill 2004 will be submitted to MOF for approval while applications after the gazette date will be submitted to Comptroller of Income Tax for approval.

ENQUIRIES

21 Taxpayers who have any queries concerning the Tracking Option may contact:

IRAS Foreigner & Clearance Branch at 63513559/ 63514472 for clarifications.

Inland Revenue Authority of Singapore

DETAILS OF INFORMATION TO BE FURNISHED BY THE EMPLOYER IN ORDER TO SATISFY THE CRITERIA THAT THE EMPLOYER'S HUMAN RESOURCE AND COMPUTER SYSTEMS ARE ABLE TO TRACK THE ESOPS OR SHARES UNDER ANY ESOW PLAN

In order to satisfy this criterion, the employer has to furnish the following information to MOF or CIT, as the case may be:

A Written Description of the following:

- a) tracking mechanism and computer/ human resource (HR) system which effects the tracking;
- b) the number of years the employer has been tracking the ESOPs or shares under any ESOW plan of its employees including those employees who are overseas or are posted from one country to another. Only employers with at least 2 years of tracking experience will be eligible for the Tracking Option;
- c) how the system alerts the company's HR or Finance department when an employee's ESOPs or shares under any ESOW plan are exercised/ vested or when the restriction is lifted;
- d) how the system separately tracks those ESOPs or shares under any ESOW plan that are granted while the employee is exercising an employment in Singapore and those that are granted while the employee is not exercising an employment in Singapore;
- e) whether there are any mechanisms in place to ensure compliance with tax payments under the Tracking Option (e.g. compulsory sale of a portion of the ESOPs or shares under any ESOW plan to meet tax payments);

B Supporting Documents

- a) If the employer outsources the management of the ESOP or ESOW plan to an external entity, the company has to furnish a copy of the outsourcing agreement and documentation to show that the employer has regular audits of the management of the ESOPs or shares under any ESOW plan;
- b) The employer has to furnish samples of the entire tracking process. Examples of the samples could be copies of excel spreadsheet or any other documents showing the details of the ESOPs or shares under any ESOW plan being tracked.

DETAILS OF INFORMATION TO BE FURNISHED BY THE EMPLOYER IN ORDER TO SATISFY THE CRITERIA THAT THE COMPANY THAT EMPLOYS THE FOREIGN EMPLOYEE HAS MET ADEQUATE CAPITAL REQUIREMENTS

In order to satisfy this criterion, the Singapore-incorporated company that employs the foreign employee has to furnish to MOF or CIT, as the case may be:

- a) details of its capitalization. The employer has to furnish information to show that its capitalization is within the top 25% of market capitalization of companies in the Straits Times Industrial Index at the date of application; and
- b) details of whether it is listed and the name of the exchange where it is listed.

If the employer is a branch of a foreign-incorporated company registered in Singapore, it has to furnish information to show that the capitalization of its parent company is within the top 25%¹⁰ (prior to 15 Apr 2011, it was 10%) of capitalization of companies in one of the leading and universally recognized (by equity research houses) stock index in the parent company's country of incorporation at the date of application¹¹. The employer will also have to furnish details of whether the parent company is listed and the name of exchange where it is listed.

¹⁰ The market capitalization requirement has been reviewed following feedback from companies and takes effect from 15 Apr 2011.

¹¹ The list of acceptable indices are as follows:
 USA – Dow Jones Industrial Average, NASDAQ or Standard & Poors (S&P) 500
 Germany – Frankfurt Xetra DAX
 Britain – Financial Times Stock Exchange (FTSE) 100
 South Korea – KOSPI 200
 Japan – Nikkei 225
 Taiwan – Taiwan Weighted Index
 China – Shanghai Stock Exchange Composite Index
 Hong Kong – Hang Seng Index
 Australia – S&P / ASX 200 Index or the All-Ordinaries Index
 South Africa – Johannesburg All-Share
 Italy – Milan MIBtel
 Spain – IBEX 35
 France – Paris CAC 40
 Canada – Toronto 300 Composite
 Finland - Helsinki Stock Exchange Index (HEX 20)
 Sweden – SX All-Share
 Belgium – Bel-20
 Ireland – Ireland Stock Market Index
 India – Bombay Sensex
 Netherlands – Amsterdam AEX
 Switzerland – Zurich Swiss Market
 Denmark – Copenhagen Stock Exchange Index (KFX)
 Norway – Oslo Stock Exchange Index
 Israel – Tel Aviv 25

SPECIMEN OF LETTER OF UNDERTAKING FOR EMPLOYERS WHO WOULD LIKE TO OPT FOR THE TRACKING OPTION

To: The Comptroller of Income Tax
55 Newton Road, Revenue House, Singapore 307987

GUARANTEE AND UNDERTAKING TO TRACK GAINS FROM EXERCISE OR VESTING OR LIFTING OF RESTRICTION OF EMPLOYEE STOCK OPTION (ESOP) PLANS AND SHARES UNDER OTHER FORMS OF EMPLOYEE SHARE OWNERSHIP (ESOW) PLANS

IN CONSIDERATION of you acceding to our request not to apply the “deemed exercise” rule under section 10 (7) of the Income Tax Act (Cap. 134), in exercise of your discretion under section 10 (7B), to employee stock option (ESOP) plans or shares under other forms of employee share ownership (ESOW) plans (as the case may be) granted on (date)*, and listed in the annex attached hereto (annex 4), to (name of employee) of (address of employee) (Taxpayer identification no. _____) upon his departure from Singapore

NOW WE (name of employer) of (registered address) AGREE WITH YOU as follows:

- 1 We undertake to –
 - (a) track the gains from the exercise of the said ESOPs or lifting of restriction on the shares acquired under the said ESOP or the vesting of or lifting of restriction on the said shares under the ESOW plans (as the case may be) whether the said (name of employee) remains in our employment or otherwise;
 - (b) make a report annually by 31 January of each year as to whether the said ESOPs or the said shares under the ESOW plans (as the case may be) have been exercised/ vested/ or are no longer subject to restriction and such gains accrued to the said (name of employee);
 - (c) report the amount of any gains to you within thirty (30) days of the exercise of the said ESOPs or lifting of restriction on the shares acquired under the said ESOPs or the vesting of or lifting of restriction on the said shares under the ESOW plans;

* If there are more than 1 date of grant, please make reference to the dates listed in annex 4.

(d) give you at least thirty (30) days notice in advance if we are to cease to carry on business in Singapore, by reason of any corporate restructuring, merger or otherwise; and

(e) give you immediate notice in the event of the demise of the said (name of employee).

2 If we fail to comply with paragraph 1, you may assess the said (name of employee) to tax under the “deemed exercise” rule.

3 Where we have given you notice under paragraph 1(d) or (e), you may assess the said (name of employee) tax under the “deemed exercise” rule.

4 We undertake to collect and to pay over to you any tax assessed on any gains (whether upon actual exercise of the said ESOPs or lifting of restriction on the shares acquired under the said ESOPs or the vesting or lifting of restriction on the said shares under the ESOW plans or under the “deemed exercise” rule) on the said ESOPs or shares under the ESOW plans.

5 Notwithstanding paragraph 4, we irrevocably and unconditionally guarantee the immediate payment to you upon demand of the tax assessed on any gains (whether upon actual exercise of the said ESOPs or lifting of restriction on the shares acquired under the said ESOPs, the vesting or lifting of restriction on the said shares under the ESOW plans or under the “deemed exercise” rule) on the said ESOPs or shares under the ESOW plans.

6 If we fail to comply with our undertaking in paragraph 1 or fail to make payment to you within 30 days of your demand under paragraph 5, we will pay to you a penalty of two hundred per cent (200%) of any tax that may be payable by us under paragraph 5.

Dated this day of 20__.

Seal

Signature

(Full Name and Designation)

