Recent legislative updates

This month's issue addresses recent tax and legal changes in various jurisdictions, namely:

- *Australia*— Potential tax withholding rate increase for employee share schemes
- *China*— Increasing scrutiny on equity based incentive plans may impact assignees and their employers
- *Hong Kong*— Inland Revenue Department provides clarification on the deductibility of equity compensation
- *India*— Long-term capital gains tax holding period requirements for unlisted shares
- *Singapore*— Approval requirements for ESPP deductions as a result of Employment Act amendments

Country summaries

For a more comprehensive discussion, please see *Country Discussions* starting on page 2.

Australia

Potential tax withholding rate increase for employee share schemes

A suite of Bills, including the Tax Laws Amendment (Temporary Budget Repair Levy) Bill 2014 were passed by the Australian Senate on June 17, 2014. This legislation is intended to implement the 2014-15 Federal Budget measure Temporary Budget Repair (TBR) Levy on high-income earning individuals effective from July 1, 2014 to June 30, 2017, and also the fringe benefits tax increase effective from April 1, 2015 to March 31, 2017. As part of the changes, employee share scheme (ESS) participants who do not provide their tax file number (TFN) to their employer will be subject to a withholding tax rate of 49% (formerly 46.5%) from July 1, 2014 to June 30, 2017. Please refer to this Tax Insights for further information. The information presented above will not be discussed below under Country Discussions.

China

Increasing scrutiny on equity based incentive plans may impact assignees and their employers

In China, listed companies implementing equity based incentive plans are required to register the plan with the in-charge local tax bureau. This requirement was first introduced in 2005 by Cai Shui [2005] No. 35 (Circular 35) and was reiterated in Guo Shui Han [2009] No. 461 (Circular 461). Over the years, the enforcement and implementation of this requirement has varied from one location to the other.

In recent months, we have observed that many local tax bureaus have started to tighten the tax registration requirements and related tax compliance administration concerning equity based income. Please see this Tax Insights for the latest developments in this area. The information presented above will not be discussed below under Country Discussions.

Hong Kong

Inland Revenue Department (IRD) provides clarification on the deductibility of equity compensation

The Inland Revenue Department (IRD) has clarified timing and corporate tax deductibility of stock options / share awards where the costs of such awards are recharged to Hong Kong. The IRD has confirmed that the maximum deductible amount for the Hong Kong company is the lower of the amount recharged or the market value of the shares acquired at the date when the stock option/ share award is exercised/ vested less the amount of consideration given by the grantee/ awardee, provided that certain specific conditions are satisfied. The IRD has also confirmed that the Hong Kong company can only claim a deduction in the year of vesting of the shares awards/ exercise of the stock options by employees.

India

Long-term capital gains tax holding period requirements for unlisted shares

On July 10, 2014, the Government of India presented the Union Budget for fiscal year 2014-2015 (the 'Budget'). As part of the budget proposals, unlisted shares and securities would now need to be held for more than 36 months to be treated as long term capital assets (currently 12 months). The extension of the holding period for unlisted shares will impact employees who acquire unlisted shares as a result of participating in an employee equity plan. Affected employees will now need to hold such shares for at least 36 months in order to benefit from the 20% long term capital gains tax rate. Otherwise, the gains arising on transfer of such shares will be taxed at marginal rates. Key features of the Budget proposals can be found in this Tax Insights. The information presented above will not be discussed below under Country Discussions.

Singapore

Approval requirements for ESPP deductions as a result of Employment Act amendments

The Singapore Employment Act (EA) has recently been amended to provide better protection for more workers and improve employment standards, while allowing flexibility for employers where there are practical business concerns.

As a result of the amendments, companies offering an Employee Stock Purchase Plan (ESPP) in Singapore need to now obtain approval from the Ministry of Manpower to make payroll deductions from employees earning a monthly salary of SGD 4,500 or less.

Country discussions

Hong Kong

Inland Revenue Department (IRD) provides clarification on the deductibility of equity compensation

Currently, where a foreign company recharges the cost of stock options or share awards granted to employees of its Hong Kong entity in order to claim a local tax deduction, the IRD's current practice is that the maximum deductible amount for the employing company is the lower of the amount recharged or the market value of the shares acquired at the date when the stock option/ share award is exercised/ vested less the amount of consideration provided by the participant, provided that certain specific conditions are satisfied. In this regard, the IRD has recently confirmed that:

(i) the amount deductible by the employing company will still be determined by the above formula; and

(ii) where the market value of the shares at the date of exercise/ vesting is below the amount recharged, claiming a deduction equal to the amount recharged may be considered by the IRD as excessive.

According to the IRD, in scenario (ii) above, a commercially realistic recharge agreement should safeguard the employing company's interest by allowing the amount of recharge to be adjusted according to the market conditions.

In relation to the timing of the deduction, the IRD also clarified that the Hong Kong employing company can only claim a deduction in the year of vesting of the shares awards/ exercise of the stock options by employees.

In addition, the IRD further clarified that if an employee is transferred from one local employer entity to another entity within the same group during the vesting period and the parent company recharges the costs accordingly to the two entities, the local employer entity can claim a deduction for its share of the recharge upon vesting / exercise of share award / option by the employee provided that the recharge arrangement is properly documented and the terms are at arm's length.

Singapore

Approval requirements for ESPP deductions as a result of Employment Act amendments

The Singapore Employment Act (EA) has been recently been amended to provide better protection for more workers and improve employment standards, while allowing flexibility for employers where there are practical business concerns.

Before the changes were introduced, employees in managerial or executive positions were not covered by the EA. Junior managers and executives earning SGD 4,500 basic monthly salary and below were only covered partially by the EA on basic salary payments.

However with effect from April 1, 2014, managers and executives earning a basic monthly salary of up to SGD 4,500 are covered under the general provisions of the EA, including sick leave benefits and protection against unfair dismissal. The changes also extend to making deductions, from the salaries of employees, which are not authorized under the EA.

As a result, companies offering an Employee Stock Purchase Plan (ESPP) in Singapore need to now obtain approval from the Ministry of Manpower to make payroll deductions from this group of employees. Although in the past companies have been able to avoid the approval requirement because the ESPP may have been offered only to employees in managerial and executive positions, approval is now required if such employees earn SGD 4,500/month or less.

Let's talk

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