ESPP & SOP
International Updates & Issues

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Topics Covered

Tax and Other Legal Developments in Following Regions:

Latin America

Europe

Asia Pacific

Latin America Region

Argentina

- Exchange Controls Further Liberalized
- Okay to Transfer up to $1 Million Per Month
- Includes all foreign currency transferred abroad, not only funds to purchase shares

European Region

EU Prospectus Directive 2003/71/EC

- Adopted 12/31/03
- 18 Months to Implement
- Non-EU Issuers can Trigger Home Member State Section with first admission for trading or first offering of securities after 12/31/03
- Maximum Harmonization Directive
- One Prospectus for all EU Member States
- Result: Companies Will No Longer Need to File Belgium Abbreviated Prospectus, French ESPP Prospectus, etc. when Directive Fully Implemented

European Region

EU Information and Consultation Directive No. 2002/14/EC (Works Council)

- Gives Ees Information & Consultation Rights
- Rights to Be Informed About Business Economic Situation & Consulted About Employment and Decisions Leading to Substantial Changes in Work Organization or Contractual Relations (RIFs, Transfers)
- Implement by March 23, 2005
- UK and Ireland Effected
- SOP/ESPP Modification or Discontinuation

European Region

Belgium – Timing of Taxation

- Stock options offered are taxable on the 60th day following the date they are offered, subject to a formal written acceptance of the beneficiary no later than on that 60th day.
- Stock options that are not properly accepted (accepted after the 60-day deadline or not explicitly accepted at all) qualify as deemed refused options ("DROs"), thus not taxable on that 60th day.
- Issue: How and when should DRO’s should be taxed?
- The Ministry of Finance has apparently determined that DRO’s should be taxed when exercised.
- Hence, if DROs are taxed at exercise, the taxable amount should be the difference between the stock fair market value upon exercise and the exercise price and will be taxed as earned income.

European Region

Belgium – Timing of Tax (Cont'd)

- So, if an employer sets up a process authorizing acceptance of the stock option beyond 60 days, employees could elect either:
  - an immediate tax charge on their option by accepting the offer in writing no later than on the 60th day following the offer, or
  - a tax charge on the spread at the purchase date of the shares by accepting the options after the 60-day deadline.
- Alternatively, though possibly slightly confusing for the employees, the employer could authorize a formal written acceptance of the option offer during a 60 day period and consider that those employees who would not have accepted the offer in writing within the 60 days - hence having refused the options from a tax perspective - have nevertheless **implicitly** accepted the options under the terms and conditions of stock option plan regulation.

European Region

Denmark

- Denmark's Parliament on 26 February approved a measure that increases the threshold for tax-free employee share distributions to DKK 20,000 (approximately US $3,300) per year.
- Under Danish tax law an employee generally is taxed when they receive vested shares at marginal tax rates of up to 63.3 percent.
- Danish law allows a company to distribute shares tax-free to their employees. Previously, the tax-free distribution could not exceed DKK 8,000 (approximately US $1,300) per employee, per year. The new rules increase that threshold and provide that it will be subject to an annual inflationary adjustment.
- Share plans must fulfill a number of conditions to qualify for the favorable tax rules. The plans must be offered to all employees, and once acquired, the shares must be held in trust with a depository bank for a period of five years for the first plan, and seven years for the second plan.

European Region

Denmark

- New Labor Legislation to Take Effect on July 1, 2004
  - Involuntary Terminated Ees Retain Options (Vested and Unvested) Granted in Year of Termination and Get Share of Any Grants in Year of Termination
  - If Voluntary Termination, Forfeit All Options (Vested and Unvested)
- March 11, 2004 – Supreme Court Upheld Novo Case Stating Section 17(a) Applied to Options and Ee Was Entitled to Pro-rata Share Post Termination. Applies to Options Linked to Past Performance
- Intel Case (Future Options) Pending

European Region

Ireland – Withholding Exemption

- The 2004 Finance Bill, published on February 4, 2004, narrows the exemption from income tax withholding and social security charges that applies to share based awards. Finance Act 2003 provided for a tax withholding exemption for "perquisites or profits whatever in the form of shares (including stock) in a company".
- However, Finance Act 2004 has tightened this exemption from “shares in a company” to “shares or stock in a) the company in which the employee holds his or her office or employment, or b) a company which has control” (*i.e.,* generally more than 50% of the share capital or voting power) of that company.
- The effect is to narrow the tax withholding exemption to shares in the employer company or its parent.

European Region

Italy – New Data Privacy Law

- Effective January 1, 2004
- Requires Data Protection Representative in Italy who will ensure compliance with law. Technically liable if non-compliant.
- Different approach to employee consent than other EU countries.
  - Necessary for performance of contract. If so, employee consent not necessary and inconsistent to ask for it. Must provide Informational Notice.
  - Consent only needed if data outside scope of contract.

European Region

Netherlands – Timing of Tax

- Existing rules generally tax options at vesting unless the employee elects to be taxed at exercise or unless the company required a cashless exercise and received a ruling permitting tax deferral.
- The Dutch Government Ministers has now concluded that employee stock options should be taxed only at exercise.
- The proposed changes are included in the 2005 Tax Plans. This means that any legislative changes will not take effect before January 1, 2005.
  - Information is not yet available as to whether transitional rules will be implemented. Furthermore, the Second Chamber of Parliament must still approve the proposed plans and can propose amendments.

European Region

Switzerland – Timing of Tax

- On October 1, 2003, the cantonal authorities of Zurich published a leaflet that compliments the federal information letter of May 6, 2003 with respect to the stock option taxation.
- The federal letter of May 6th, stated that options with a vesting clause are not subject to taxation at grant, and that such options should be taxed at exercise.
- According to the Zurich leaflet, options can be taxed at grant, vesting, exercise or sale, depending on the plan design. In order to ensure that the employee is aware of the tax consequences when accepting the option grant, it is now required that the tax consequences (which are agreed upon by the employer and the cantonal tax authorities) be included in the option agreement/certificate.

European Region

United Kingdom – The Dextra Case

- In the case of *MacDonald (Inspector of Taxes) v. Dextra Accessories Ltd.* ("the Dextra Case"), the Court upheld the Inland Revenue’s disallowance of a corporate tax deduction taken in advance of income recognition by employees.
- The Dextra Case involved a tax planning arrangement whereby employees deferred income tax while the employer claimed a tax deduction when contributions were paid into an employee benefit trust.
- While Dextra does not involve share schemes, the holding may impact companies operating a share plan where the company has accrued the tax deduction in advance of employees being subject to tax.
- In addition, where multinational companies operate recharge arrangements with respect to their international share plans, any accruals made in the UK employing subsidiary accounts for compensation that may be paid by the parent (either in the form of shares or cash) may be impacted by this decision.

European Region

United Kingdom

- The 2004 Budget contains no substantive provisions relating to share scheme taxation.
- Follows 2003 tax legislation which made significant changes to the equity plan taxation:
  - Withholding period extended from 30 to 90 days
  - Section 83(b)-type elections allowed with 14 days of restricted stock transfer
  - Unapproved exercises of approved options now subject to PAYE and NIC withholding
  - Eliminate "three year from previous exercise rule" for approved options, now only have to meet three year from grant rule
  - 1% NIC not subject to caps
  - Statutory deduction permitted for equity

European Region

Russia and Eastern Europe Doing Away With Exchange Controls

- Russia – New Law Proposed to Take Effect June 2004; Increase Currency Transfer Limit From $75,000 to $150,000; Proposal to End Limits Altogether in January, 2007
- Bulgaria – July 8, 2003, Declaration to Transfer Currency for Foreign Shares No Longer Required
- Czech Republic – Notification Requirements for Exchange Control Abolished
- Romania – Exchange Control Approval Abolished on January 1, 2003, but Repatriation Remains

Asia/Pacific Region

Australia – Payroll Taxes

- The state of New South Wales, which includes the city of Sydney, announced that it would impose an employer payroll tax of 6% on share plan discounts. The employer payroll tax will apply to discounted stock purchase plans, "free" share plans and stock options to the extent the option is granted at a discount. The tax will be imposed on companies who have employees working in NSW regardless of the company's location within the country.
- The legislation received assent on July 22, 2003 and was effective from July 1, 2003.

Asia/Pacific Region

Australia

- Brokers administering or providing services for employee stock plans may be subject to licensing requirements under Financial Service Act.
- Transitional Relief ended March 11, 2004.
- No issue for Issuers offering cashless exercise if newly issued shares are used.
- B&M obtained relief from ASIC in January 2004 for 3 broker/ administrators based on theory services licensed under U.S. law and no broader than services to wholesale clients.

Asia/Pacific Region

Australia

- Class Order Relief for Share Plans changed in June 2003
  - Relief for Stock Option Plans and ESPP
  - Public Trading for 12 months (used to be 36)
- Note that restricted stock units with performance-based vesting may be considered a “derivative” and not subject to usual class order relief. Possible to apply for specific relief from ASIC.

Asia/Pacific Region

India Tax Guidelines and Exchange Controls

- Liberalization of Exchange Controls – February 4, 2004
  - General Permission for ESPP at Concession Rate/51% Ownership
  - $25,000 per year in Foreign Investments Per Year for Any Purpose; Cashless No Longer Required
- Tax Guidelines
  - 6 Months Rule – Sub-plan?
  - ESPP/SOP
  - Tax Advantages

Asia/Pacific Region

Indonesia

- Capital Market Supervising Board (BAPEPAM) Issued New Policy for Employee Stock Plans in April 2003
  - No registration statement is required for foreign issuer to offer options and shares to employees
  - Must comply with certain employee plan regulations
  - B&M obtained approval for ESPP in February 2004

Asia/Pacific Region

Japan

- The Tokyo High Court judgments have since been appealed to the Supreme Court by the individual taxpayers.
- About 100 similar cases are still pending, with the lower courts divided on the issue.
- See, *e.g.,* a Tokyo District Court decision on March 16 which held that income earned on the exercise of options given to Japanese employees of U.S. companies' Japanese subsidiaries is "extraordinary income" that should be taxed at lower rates than salary income. (Tokyo District Court Justice Toshihiko Tsuruoka upheld claims by a former Compaq Computer Japan employee and a former McDonalds Japan employee, filed with the court in 2000, that sought injunctions against Japanese tax authorities' deficiency assessments on stock option income earned in the late 1990s.)

Asia/Pacific Region

Japan

- Over the last several years there has been great debate in Japan as to whether stock option income should be taxed as salary at higher ordinary rates or as “occasional income” taxed at more favorable rates.
- Original judgments of two Tokyo District Courts held that stock option profits should be treated as occasional income since the income resulted from the market appreciation of the underlying shares, as opposed to a connection with any employment services rendered to the issuing corporation.
- In two rulings in February 2004, the Tokyo High Court reversed these judgments of Tokyo District Courts and held in favor of the National Tax Agency ("NTA"), ruling that stock option income should be treated as Employment Income rather than Occasional Income.
  – This decision followed a judgment made in January by the Yokahama District Court, in favor of the NTA.

Asia/Pacific Region

Korea – Cross Border Stock Options

- A South Korean court has rejected the requests of some locally hired employees of foreign multinationals seeking tax leniency on gains from global employee stock options granted by a parent company abroad.
- The Seoul Administration Court issued a ruling on January 12, 2004 stating that local recipients of international stock options should pay "earned income" tax due on the proceeds from exercised stock options.
  – In South Korea, the standard earned-income tax rates range up to 36 percent, while the alternative miscellaneous-income tax rate stands at 20 percent on a withholding basis.
- According to the text of the ruling, the court held that an employment agreement with a South Korean subsidiary should be sufficient to attribute company-sponsored stock options to service for its foreign parent firm.

Asia/Pacific Region

New Zealand

- Annual Sales Offering Report
  - Was Due on March 31, 2004
  - Securities Act (Overseas Employee Share Purchase Schemes) Exemption Notice 2002
  - Report all grants of options and shares issued for prior year
  - Not required for RS/U

Asia/Pacific Region

Thailand

- In 2004, new notification issued on filing fees for registering stock plan when private placement rules do not apply (35 or fewer Ees or value less than 20 million Baht in 12 months).
- Fee now fixed at 53,500 Baht per plan (used to be based on no. of shares and share price).
- Recent change in time registration statement takes effect. Now 15 days after approval given (not 15 days after statement submitted and documentation acknowledged).

Any Questions?

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