LEMBAGA HASIL DALAM NEGERI
INLAND REVENUE BOARD

PUBLIC RULING

EMPLOYEE SHARE OPTION SCHEME BENEFIT

Translation from the original Bahasa Malaysia text.

PUBLIC RULING NO. 4/2004

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DIRECTOR GENERAL'S PUBLIC RULING

A Public Ruling is issued for the purpose of providing guidance for the public and officers of the Inland Revenue Board. It sets out the interpretation of the Director General of Inland Revenue in respect of the particular tax law, and the policy and procedure that are to be applied.

A Public Ruling may be withdrawn, either wholly or in part, by notice of withdrawal or by publication of a new ruling which is inconsistent with it.

Director General of Inland Revenue,
Malaysia

1. This Ruling explains:

   i. the tax treatment in respect of a benefit arising from an employee share option scheme (ESOS) received by an employee from his employer by reason of his employment;

   ii. the circumstances in which the benefit from ESOS will arise;

   iii. determination of the amount or value to be taken as gross income from a source of employment of an employee; and

   iv. employer's responsibilities upon launching an ESOS and employee's responsibilities on receiving the ESOS benefit.

2. The related provisions in the Income Tax Act 1967 (*the Act*) which have relevance to ESOS are -

   - **Paragraph 13(1)(a)** - which provides that ESOS is a perquisite and forms part of the gross income from employment of an individual;
   - **Section 25** - for determining the basis period in which ESOS is to be related as income received by the employee;
   - **Section 77 -** the employee's responsibility to report to IRB the benefit from ESOS in the income tax return form (Form B or BE);
   - **Section 83** - the employer's responsibility to report to IRB the benefit from ESOS received by each employee in the Employer's Return (Form E); and
   - **Schedule (Rule 3) Monthly Income Tax Deductions** under the relevant Income Tax (Deduction from Remuneration) Rule - in respect of monthly income tax deduction on benefit arising from perquisites such as ESOS.

3. The words used in this Ruling have the following meanings:

   3.1 "Tangible asset" is an asset which is physical and material in nature such as land, building, motor vehicles, machinery and investments.

   3.2 "Intangible asset" is an asset which is not physical in nature but gives a right to its owner to receive cash payments or other interests, such as patents, goodwill or brand names.

   3.3 "Net tangible assets" means book value of assets less intangible assets and less liabilities.

   3.4 "Market value"- for companies listed on the Stock Exchange is the average price calculated by averaging the highest price with the lowest price on the date the option is offered.

   3.5 "Offer price " is the price to be paid by the employee for each share offered.

3.6 "Liability" is the obligation that arises due to loans, losses resulting from contingencies, payment commitments received or for goods or services supplied where payments are still owing.

3.7 "Employer" in relation to an employment, means-

a. the master, where the relationship of master and servant subsists;

b. where the relationship does not subsist, the person who pays or is responsible for paying any remuneration to the employee who has the employment, notwithstanding that the person and the employee may be the same person acting in different capacities.

3.8 "Option" is right offered in respect of a number of shares at a specific price to be exercised at a future date.

3.9 "Employee" in relation to an employment means -

a. the servant, where the relationship of master and servant subsists;

b. where the relationship of master and servant does not subsist, the holder of the appointment or office which constitutes the employment.

3.10 "Employment" means -

a. employment, in which the relationship of master and servant subsists;

b. any appointment or office, whether public or not and whether or not that relationship subsists, for which the remuneration is payable.

3.11 "Perquisites" means benefits that are convertible into money received by an employee from the employer or third parties in respect of having or exercising the employment.

3.12 "Monthly Tax Deductions or STD" means income tax deductions made in accordance with Rule 3 of the Schedular Monthly Deductions under the relevant Income Tax (Deduction from Remuneration) Rules.

3.13 "Date of offer of option" means the date the employer offers an employee the right to purchase a number of shares in the company, in its holding company or in its subsidiaries.

3.14 "Date of exercise of option" means the date the employee exercises the option by making payments (if any) for the shares offered.

4. Employee Share Option Scheme (ESOS)

4.1 Generally, the granting of shares by an employer to its employees can be grouped into four (4) categories as follows-

4.1.1 Employee Share Option Scheme

4.1.2 Employee Share Purchase Plan

4.1.3 Warrant Scheme; and

4.1.4 Award Scheme.

4.2 The tax treatment on the granting of shares under categories 4.1.2 to 4.1.4 will be explained in detail under separate Rulings.

4.3 ESOS is the granting of shares in the company, in its holding company or its subsidiaries made by an employer to its employees. Shares offered under the category of ESOS are:

4.3.1 Employees Loyalty Scheme;

4.3.2 Stock Option Plan; and

4.3.3 other forms of share offers which have the characteristics of those schemes mentioned under paragraphs 4.3.1 and 4.3.2.

4.4 An ESOS has the following characteristics:

4.4.1 the existence of a 'by-law' to regulate the scheme;

4.4.2 the offer to purchase;

4.4.3 the price of the share offered is known at the time the offer was granted;

4.4.4 the date of the offer is also known; and

4.4.5 the date the option is to be exercised is stated clearly in the by-law of the scheme.

By-law refers to rules to administer a scheme, letters of offer, offer acceptance forms as well as specific features of a scheme which will then determine the type of scheme that is offered. Shares that are offered to employees by an employer can consist of shares in the company, shares in its holding company or shares in its subsidiaries, whether located in or outside Malaysia.

4.5 The main purpose for the grant of shares to the employees is to recognise the role of the employees through inculcating a sense of "belonging" amongst the employees in that they too have rights in the company by holding shares in that company.

5. Circumstances in which benefit from ESOS can arise and the method of calculation of the value of the benefit from ESOS

5.1 An employee has the benefit from ESOS when the employer offers to him-

i. shares issued free of charge; and
ii. shares issued at a discount that is at a price lower than the market value.

5.2 In short, the amount of benefit from ESOS which is to be assessed as a perquisite and included in the employment income under paragraph 13(1)(a) *of the Act* is as follows:

	RM
Market value of share at the date of the offer of the option	XXX
Less:	
Offer price of share at the date of the offer of the option (if any)	XXX
Perquisite under paragraph 13(1)(a) *of the Act*	XXX

Benefits from the grant of ESOS will arise on the date the option is exercised. For the purpose of tax computation, this benefit will be related back to the basis period for the year in which the option is offered.

Any subsequent changes in the value of the shares such as :-

i. fluctuations in the value of the shares;

ii. changes in the share price resulting from the grant of bonus shares based on the holding of ordinary shares by the employee; and

iii. gain or loss from the shares arising from the disposal of the shares;

will not influence or affect the taxable employment income.

5.3 Where an employer instead of paying remuneration in cash, issues shares free of charge to its employee, the shares constitute income of the employee under paragraph 13 (1)(a) *of the Act* being a perquisite of the employment. The shares are clearly payments otherwise than in money but are convertible into money. The amount of the income represented by the issue of shares is taken to be the market value of the shares at the date on which they are given to the employee. Any subsequent fluctuations in the value of the shares are capital fluctuations and do not give rise to any tax effects on the shareholder.

Example 1

On 1.3.2004, a managing director of a company was granted 1,000 shares in the holding company free of charge in addition to the salary received by him. The shares were traded in the Singapore Stock Exchange and the market value of the share at 1.3.2004 was equal to RM4.50 per share. On 30.4.2004, that director sold the shares at a price of RM5.00 per share.

The benefit taxable as perquisite on the employee determined at 1.3.2004 is the market value of the share at 1.3.2004 that is (1,000 X RM4.50) = RM4,500.

The benefit is taxable as part of the employment income of the employee for the Year of Assessment 2004. The gain obtained from the sale of the shares at 30.4.2004 does not have any tax consequences on the employee.

5.4 When an employer grants to its employees options to purchase shares under favourable terms, that is shares are offered to employees at:

- par value whereas shares have a premium value in the share market; or
- at a fixed price whereas the shares have a higher market value in the share market

the difference between the amount paid for obtaining the shares and the market value of the share at the date the option was offered is a benefit to the employee. This benefit is taxable as a perquisite under paragraph 13(1)(a) *of the Act* arising by reason of having or exercising an employment.

Example 2

On 1.4.2004, Employee A was granted an option by the employer to purchase 10,000 shares of the company valued at RM1.00 per share, at par during the company's "IPO" exercise to raise share capital. The share price on the same date in the share market was RM1.25. Employee A exercised that option on 1.4.2004.

Benefit from ESOS which is taxable as perquisite on the employee is determined at 1.4.2004 as follows:

	RM
Market value of share at 1.4.2004 (1,000 X RM1.25)	*1,250*
Share price under offer option 1.4.2004 (1,000 X RM1.00)	*1,000*
Perquisite under paragraph 13(1)(a) of the Act	*250*

This benefit is taxable as part of the employment income of the employee for Year of Assessment 2004.

Example 3

A company had launched a share purchase option scheme for its employees on 2.1.2004. Option to purchase shares at the price of RM1.45 per share was offered to the employees on 28.2.2004. The market price of the share at 28.2.2004 was RM1.65. The employees were given one year to exercise the option. On 31.1.2005, Employee B exercised that option by purchasing 1,000 company shares.

The benefit from ESOS which is assessable on Employee B is determined at 31.1.2005 as follows:

	RM
Market value of share at 28.2.2004(1,000 X RM1.65)	*1,650*
Share price under offer option at 28.2.2004(1,000 X RM1.45)	*1,450*
Perquisite under paragraph 13(1)(a) of the Act	*200*

This benefit is taxable as part of the employment income of the employee for Year of Assessment 2004.

Example 4

Using Example 3, assuming the share price offered to Employee C through this option is at a discount price of 25% of the market price. The benefit taxable for Year of Assessment 2004 which is determined on 31.1.2005 is as follows:

	RM
Market value of share on 28.2.2004(1,000 X RM1.65)	*1,650.00*
Share price under offer option on 28.2.2004(1,000 X {75% X RM1.65})	*1,237.50*
Perquisite under paragraph 13(1)(a) of the Act	*412.50*

5.5 In the circumstance where the option price is fixed only at the date when the option is exercised, the benefit as a perquisite under paragraph 13(1)(a) *of the Act* is calculated as follows:

	RM
Share price in share market at date of offer	XX
Less:	
Purchase price of shares in the share market at date of exercise	XX
Value of benefit as perquisite under paragraph 13(1)(a) *of the Act*	XX

Example 5

A company launched a share purchase option scheme for its employees on 2.1.2004. The option was offered to the employees on 28.2.2004 however without fixing the purchase price for each share required to be paid. The market price of that share at 28.2.2004 was RM1.65. The employees were given one year to exercise the option. On 31.1.2005, Employee D exercised the option by purchasing 1,000 shares of the company which was offered to him at the price of RM1.39 per share.

Benefit from ESOS assessable on Employee D is determined on 31.1.2005 as follows:

	RM
Share price in the share market at ***date of offer*** *28.2.2004 (1,000 X RM 1.65)*	*1,650*
Purchase price of share in the share market at ***date of exercise*** *31.1.2005 (1,000 X RM1.39)*	*1,390*
Perquisite under paragraph 13(1)(a) of the Act	*260*

This benefit is taxable as part of the employment income of Employee D for Year of Assessment 2004.

If the share price purchased under the option at 31.1.2005 is RM1.70 per unit, there is no benefit to be taxed on Employee D for Year of Assessment 2004.

5.6 **Shares offered not listed on the Stock Exchange**

Where a company which is not listed on the Stock Exchange grants its shares or shares in its holding company or its subsidiary companies free of charge or offers the shares at a specific price, there is no market value that can be attached to the share concerned. In such circumstances, the computation of the benefit from ESOS is as follows:

	RM
Share value at date of offer of option*	XXX
Less:	
Share price offered under the option	XXX
Perquisite under paragraph13(1)(a) *of the Act*	XXX

*Share Value calculated as follows:

Share Value = $\dfrac{\text{Net Tangible Assets}}{\text{Number of Ordinary Shares}}$

Example 6

A company launched a company share purchase option scheme for its employees on 1.3.2004. The shares granted under the option were shares in a subsidiary company that was not listed in any Stock Exchange. On 1.4.2004, Employee E was offered option to purchase 1,000 company shares at the cost of RM0.80 per share. The option was exercised on 31.1.2005. The Audited Balance Sheet of the subsidiary company at 1.4.2004 reflected the following particulars:

Net tangible asset	RM3,750,000
Number of ordinary shares	4,000,000

Benefit from ESOS which is taxable as perquisite on Employee E is determined on 31.1.2005 as follows:

	RM
Share value at 1.4.2004(1,000 X RM0.9375)*	*937.50*
Share price under share option at 1.4.2004 (1,000 XRM 0.80)	*800.00*
Perquisite under paragraph 13(1)(a) of the Act	*137.50*

Share value calculated as follows:

**Share value* = $\dfrac{\textit{Net Tangible Asset}}{\textit{Number of Ordinary Shares}} = \dfrac{\textit{RM3,750,000}}{\textit{4,000,000}} = \textit{RM0.9375}$

This benefit is taxable as part of the employment income of Employee E for Year of Assessment 2004.

Example 7

Using Example 6, where the shares were given free of charge to Employee E, the benefit from ESOS which is taxable as perquisite on him for Year of Assessment 2004 is -

	RM
Share value at 1.4.2004(1,000 X RM0.9375)*	*937.50*
Share price under share option at 1.4.2004	*NIL*
Perquisite under paragraph 13(1)(a)of the Act	*937.50*

6. **Employee's responsibilities**

The employee is required to -

6.1 Report in the Income Tax Return Form (Form B or BE) of the employee, the amount in respect of benefits from ESOS that have been exercised;

6.2 Make assessment by including the benefit as stated above as income from employment for the basis period in which that benefit is offered; and

6.3 Ensure that income tax on the that benefit is paid -

6.3.1 by deductions from remuneration under the Schedular Tax Deductions scheme (STD) in the month the option is exercised or that total tax is paid by installment scheme based on the Schedular Tax Deduction scheme (STD) (the number of installments allowed is a maximum of 12 months); or

6.3.2 upon furnishing the Income Tax Return Form (Form B or BE).

6.4 Ensure that income tax on the benefit is paid upon furnishing the Income Tax Return Form(Form B or BE). Nevertheless, the employee can arrange with the Collection Branch to pay the amount of tax by way of installments in which case the employer is required to comply with the CP38 directives issued by the Branch/Collection Unit.

7. **Employer's responsibilities**

7.1 Where a company launches an ESOS scheme for its employees, the company as an employer is required within 30 days after the expiry of the period of acceptance of the offer as specified in the ESOS By-law, to notify IRB concerning the launch of the ESOS. At the same time, the employer is required to make the computation of the benefit per share that arises from the ESOS. IRB will not issue any letter of approval. The notification of the launch and the computation of the benefit must be made by completing Form BT/ESOS/2005 to be submitted with the following supporting documents:

7.1.1 The By-law of the ESOS;

7.1.2 Board of Directors' Resolution or the Resolution of the Extraordinary General Meeting which approves the launching of the ESOS;

7.1.3 A sample of the offer letter which states the offer price and the number of shares offered;

7.1.4 A sample of the letter of acceptance of the offer;

7.1.5 Market price at the date of the offer and the evidence (which can be obtained from newspaper cuttings or downloading from the website which shows the trading activity of the share on that day); and

7.1.6 In respect of company offering shares in the company not listed on the Stock Exchange-

i. Balance sheet of the company that offers shares to its employees. The balance sheet should be at the date of offer of the option and it must be audited; and
ii. A sample of the share certificate to be issued to the employee; and

7.1.7 Appendix A- details of employees accepting the offer.

7.2 Notification together with the supporting documents as above must be submitted to the address below:

Director,
Technical Department,
Inland Revenue Board Malaysia,
12th Floor, Block 9,
Government Building Complex,
Jalan Duta,
50758 Kuala Lumpur.

7.3 Where an employee who has been offered ESOS has exercised his right under the option, the employer must-

7.3.1 ensure that the tax to be charged on the benefit that arises from the ESOS is deducted from the employee's salary based on Schedule (Rule 3) of the Monthly Tax Deductions in the month in which the option is exercised; or

7.3.2 where the employee chooses to pay the tax by installments through the Monthly Tax Deductions, the employer must make the tax deductions from the remuneration of the employee each month (for a maximum of 12 months) commencing from the month in which the option is exercised. An example of the computation of deduction of income tax from the remuneration is shown in Appendix B.

7.3.3 In the case where an employee elects to pay by himself the income tax arising on the perquisite the end of the year, the employer must ensure that the election so made by the employee is done in writing.

[Where the Collection Branch has agreed to allow the employee to pay tax on the ESOS benefit by installments with the issuance of Directive of Tax Deduction CP 38, the employer must comply with the directive.]

7.4 The employer is also required to report this benefit in the EA Form of the employee for the year the option is exercised. At the same time, the employer is also required to submit to the Director, Technical Department, IRB a copy of the names of employees who have exercised their rights under an option as in Appendix C.

8. Employers are required to comply with the provisions of Section 82A *of the Act* in relation to the responsibility to keep documents for audit purposes.

9. This Ruling is effective for year of assessment 2004 and subsequent years of assessment.

Director General
of Inland Revenue

APPENDIX A

LIST OF NAMES OF EMPLOYEES ACCEPTING THE OFFER UNDER THE EMPLOYEE SHARE OPTION SCHEME (ESOS)

ESOS NAME :____________________________________
DATE LAUNCHED : _______________________________

No.	Name/ I.C. No./ Passport No.	Income Tax No.	Address	Market Value @ the Date of Offer of Option	Offer Price @ the Date of Offer of Option	Benefit Per Share	No. of Shares Offered

....
Signature **Name** **Designation**

Date: .... **Company's Seal**: ....

EXAMPLE OF COMPUTATION OF INCOME TAX DEDUCTION FROM REMUNERATION IN RESPECT OF BENEFIT FROM ESOS

Date Of Grant Of Option:	1 March 2004
Date Option Exercised:	2 May 2006
Offer Price (1 March 2004):	RM1.00
Market Value (1 March 2004):	RM2.00
Value of Benefit:	RM1.00

Where the employee is given right to purchase 50,000 shares, the total value of the benefit when the employee exercises his right on 2 May 2006 is:

50,000 x RM1.00 = RM50,000

Assume the employee has the following status :

Employee is married	
Wife is working	
2 children qualifying for deduction	
Monthly remuneration	RM3,600.00
EPF	RM396.00
Total benefit	RM50,000.00

Category referred to is Category 3/KA 2 of the STD Schedule

A. Amount of tax deducted in respect of the monthly remuneration (not including the ESOS benefit) is-

	RM
Monthly remuneration	3,600.00
Less: EPF	396.00 *
	3,204.00

STD on RM3,204,00 =RM48.00

B. Amount of tax deducted in respect of monthly remuneration where the ESOS benefit is included is-

(i) (1/*12 X Benefit) + Net monthly remuneration
(1/*12 XRM50,000) + RM3,204 = RM7,370
Note:
* The denominator for this example has taken into account salary up to a maximum of 12 months. This denominator can be reduced according to the number of months of deduction from salary that is required.

(ii) Amount of tax to be deducted on the amount determined in (i) -

STD on RM7,370 = RM616.00

(iii) Amount of STD in respect of ESOS per month = RM616-RM48 = RM568

(iv) Amount of tax to be deducted commencing from the month the benefit is received/ option is exercised is RM48 + RM568* = RM616.00

Note: * According to number of months of deduction as in (i) above.

Based on this rule, the employer must deduct RM616 from the remuneration of the employee each month for 12 months commencing from the month in which ESOS is exercised/share is given.

Reminder: **In the case where the date of this exercise involves prior years, the employer is required to remit the payments by using a separate CP39 stating the year of assessment concerned (one list for each year of assessment) to facilitate payment details to be recorded by the Collection Branch based on the year of assessment concerned.**

As in the above example, as the date of grant is 1 March 2004 whereas the date of exercise of option is 2 May 2006, therefore the deductions as in (ii) above will commence in the month of May or June 2006. The employer is required to prepare two copies of CP39 that is for Year of Assessment 2004 and Year of Assessment 2006. The amount of deduction for the current year (RM48) must be reported in the CP39 list for Year of Assessment 2006, while the amount of deduction for the prior year (RM568) is reported in the CP 39 list for Year of Assessment 2004.

APPENDIX C

LIST OF NAMES OF EMPLOYEES WHO HAVE EXERCISED THE OFFER UNDER THE EMPLOYEE SHARE OPTION SCHEME (ESOS)

ESOS NAME:____
DATE SCHEME LAUNCHED:_________________________

No.	Name:/ I.C. No./ Passport No.	Income Tax No.	Address	Market Value @ Date of Offer of Option	Offer Price @ Date of Offer of Option	Benefit per Share	No. of Shares granted	No. Of Shares Exercised

....

Signature **Name** **Designation**

Date:.............................. **Company's Seal**: ....

NOTIFICATION BY EMPLOYER
UNDER SECTION 83 INCOME TAX ACT 1967
IN RESPECT OF
BENEFITS RECEIVED BY EMPLOYEES FROM
EMPLOYEE SHARE OPTION SCHEME

(This form must be completed by the employer in one (1) copy and submitted to the following address within 30 days after the expiry date of the offer acceptance period by the employee as provided for in the By-law of the ESOS)

DIRECTOR,
TECHNICAL DEPARTMENT,
INLAND REVENUE BOARD MALAYSIA
BLOCK 9, 12th FLOOR,
GOVERNMENT BUILDING COMPLEX,
JALAN DUTA,
50758 KUALA LUMPUR.

1. Name of the Employee Share Option Scheme (ESOS) launched:
   ____

2. Date of launch scheme
   ____

3. Duration of scheme:
   ____

4. Number of schemes launched prior to this date (if any):
   ____

5. Number of shares offered under the scheme:
   a. Quantity: ____(unit)
   b. Percentage compared to the paid-up share capital of the company:_______(%)

6. Information relating to the company launching the ESOS:
   a. Name of company:____
   b. Address of company:____
   c. Telephone No. :____
   d. Facsimile No.: ____
   e. Company's Income Tax No.:_____________________________________
      i. IRB Branch: ____
      ii. Employer's Income Tax No.: E _____________________________
7. Name of companies whose shares are granted
   ____

8. Information of company if it is different from the company which launches the abovementioned scheme
   a. Name of company: ____
   b. Country of origin: ____

c. Address:____
d. Telephone & Facsimile No.:____
e. Income Tax No.(if any): ____
f. Employer Income Tax No.:____
g. IRB Branch: ____

9. Names of subsidiary/related companies participating in the ESOS above:

No.	Name	Address	Tel No. & Fax. No.	Income Tax No.	Employer Income Tax No.

10. **Summary of the scheme launched:**

The summary should include the objectives and main features of the scheme, eligibility criteria, the source of funding including other benefits offered to the employees in connection with the scheme such as a discount given on the share price at the time of purchase, contributions from the employer to fund the purchase, allowance to bear the tax on the benefits arising from the ESOS, etc.

____
____
____(Please prepare a separate sheet of attachment.)

11. Date of grant of option:

____

If options are granted in stages, state the number and basis for ascertaining the respective option dates:

____
____

12. Date of exercise of option:

____

13. Calculation of ESOS benefit

Date of Grant of Option (A)	Market Value At Date of Grant of Option (B)	Offer Price At Date of Grant of Option (C)	Benefit from ESOS (B)-(C)

14. **Declaration by Employer:**

I hereby confirm that all information furnished in this notification form is true and correct.

Signature: ____

Name: ____

Designation: ____

Company's Official Seal: ______________________________________