Deloitte.

Global Employment Solutions

Global InSight

6 November 2015

In this issue:

Canada: Stock option deduction changes expected with new federal government

Overview

Canada's new Liberal majority government campaigned on a promise to change the tax treatment currently accorded to stock option benefits. How this promise will translate into legislative reality remains to be seen, but timely actions may help mitigate any adverse consequences – at least in the short run. This update reviews the current stock option rules, the campaign promises to change the current rules, who this will impact, and possible measures to mitigate the impact.

Current rules

Under the Canadian Income Tax Act (the "Act"), when an employee exercises a stock option pursuant to a stock option agreement made under section 7 of the Act, a taxable benefit equal to the difference between the fair market value (FMV) of the share and the price paid for the share will be included in the employee's taxable income for the year. However, the Act permits the employee to claim a corresponding deduction, referred to as the 110(1)(d) deduction, equal to 50% of the taxable benefit where certain conditions are met (namely, that the share is a common share and the price paid for the share is not less than the FMV of the share when the option was granted). Where the employer issues the employee shares, the employer will not be entitled to a corporate deduction. However, where the employee requests cash versus shares, the employer is allowed a corporate deduction for the expense, unless it elects to allow the employee to claim the 110(1)(d) deduction. In practice, cash-outs are rare. The 110(1)(d) deduction allows many employees to enjoy the equivalent to capital gains treatment from a tax rate perspective on potentially large amounts of compensation. Accordingly, many compensation packages are structured, at least in part, to include this form of incentive compensation.

It should be noted that where an employee exercises stock options granted by a Canadian-Controlled Private Corporation (CCPC), as defined by the Act, the timing of the taxable benefit and corresponding deduction are governed by a slightly modified regime under the Act, with an alternate deduction provided for in paragraph 110(1)(d.1) for CCPC option shares that have been held for at least two years.

Possible changes to the 110(1)(d)/(d.1) deduction?

The new Liberal government's platform included plans to amend the 110(1)(d)/(d.1) deduction. According to Liberal campaign literature, as part of a "wide-ranging review of complex tax expenditures," it will look for opportunities to reduce tax benefits that substantially benefit those earning in excess of $200,000 per year. The Liberals stated that a starting point for this review would be to cap how much an employee can claim under the 110(1)(d)/(d.1) deduction. Some comfort can be taken in the fact that they also said that any changes will recognize that stock options are a useful compensation tool for "start-up companies" and will ensure that employees having up to $100,000 in annual stock option benefits would be unaffected by the cap. We note that no guidance was provided on defining a "start-up company" for these purposes or how they would determine the $100,000 value of the stock option benefit.

To illustrate the impact of the change to the 110(1)(d)/(d.1) deduction, consider an individual who exercises an employee stock option which is subject to the top tax rates in Canada and Ontario, and due to the proposed rules, is not eligible for the 110(1)(d)/(d.1) deduction. In this case, the individual's top tax rate could increase from 24.77% to up to 53.53% on the income from the stock option (assuming the Liberal Party's proposed increase in personal income tax rates is implemented).

It is also not clear, at this time, what the effective date for any proposed changes may be (for example, whether they will apply to any options exercised as of the date of the Budget that introduces the above changes, or whether, the changes will apply retroactively, which is less likely).

Who may be impacted by the change

Depending on how any rule changes are implemented, the changes could impact a number of groups of people, including:

- Employees with vested yet unexercised stock options;
- Employees with unvested stock options;
- Employers and employees during compensation negotiations;
- Employer's withholding practices; and
- Non-resident employers with tax equalized employees who earn Canadian-source stock option benefits.

The accounting treatment of stock option benefits of public companies would also need to be reviewed for the potential impact.

Deloitte's view

How to mitigate the impact: Based on long-standing past practices of the federal government, Deloitte anticipates that any changes will likely be on a prospective basis only. That said, it is important for clients to consider the potential changes to the regime in a timely manner and companies may want to communicate with employees who may be affected to allow them to best manage their affairs. For instance, employees with vested yet unexercised stock options may want to consider the timing of future exercises of options and employers may want to provide employees with unvested stock options opportunities to exercise options in the current favorable environment through the acceleration of vesting of the options. Further, Deloitte can work proactively with employers to help them in the amending of their governance, accounting, and withholding practices to be compliant with the new laws as they come into force.

— Lorna Sinclair (Toronto)
Partner
Deloitte Canada
losinclair@deloitte.ca

Terri Spadorcia (Montreal)
Partner
Deloitte Canada
tspadorcia@deloitte.ca

Anne Montgomery (Toronto)
Partner
Deloitte Canada
amontgomery@deloitte.ca

Christina Diles (Vancouver)
Partner
Deloitte Canada
cdiles@deloitte.ca

Peter Megoudis (Toronto)
Partner
Deloitte Canada
pmegoudis@deloitte.ca

Norway:
Tax reform and Fiscal Budget 2016

Overview

The Norwegian Government has recently released the proposal for the fiscal budget for 2016. A tax reform is proposed together with the budget.

The tax reform implies a change in structure of the tax rates. Key changes:

- Reduced taxation of "ordinary income";
- Tax Bracket taxation is introduced;
- Adjustment factors for the taxation of ownership income is introduced;
- Reduced travel deduction;

- Reduced tax on net wealth; and
- Coordination of tax collector functions.

Ordinary income: The Government has suggested a reduction of the taxes on ordinary income (net income) from 27 % to 25 %. A further reduction of the taxes are expected for the income years 2017-2018 (22 %).

Bracket tax: The lower tax rate on ordinary income will result in a substantial tax loss for the Norwegian state.

In order to reduce the tax loss, the government is proposing to increase the tax on personal salary income (gross income). The current surtax is suggested to be replaced by bracket tax.

Compared to today's surtax, the introduction of two new brackets with a threshold of NOK 158,000 and NOK 224,900 and a tax rate of 0.8 % and 1.6 %, respectively, is proposed.

Surtax 2015	Threshold	Tax rate	Bracket Tax 2016	Threshold	Tax rate
			Bracket 1	158,800	0.8 %
			Bracket 2	224,900	1.6 %
Bracket 1	550,550	9 %	Bracket 3	565,400	10.6 %
Bracket 2	885,600	12 %	Bracket 4	909,500	13.6 %

Through the suggested alterations to the Norwegian tax rates, the marginal tax rate on salary income will decrease from 47.2 % to 46.8 %.

Taxation of ownership income: To prevent tax planning opportunities for company owners as a result of the lowering of taxes on ordinary income, a special tax regime for ownership income is suggested. This is meant prevent dividend income to be drawn by company owners as opposed to salary income. Ownership income consists of dividends, distributions from general partnerships, and gains and loss from sale of shares or equivalents.

To achieve this, the taxes on ownership income are suggested to be increased in line with the reduction in taxes on ordinary income. A scheme of upward adjustment of ownership income using an adjustment factor that is used to gross up the ownership income before calculating the taxes is proposed.

For 2016, an adjustment factor of 1.15 is introduced (tax rate ordinary income 25 %). Upon further lowering the taxes on ordinary income to 22 % in 2017 or 2018, the adjustment factor is planned at 1.44.

Reduced personal allowance for travel deduction: The Government proposes an increase of the lower threshold of the travel allowance from NOK 16,000 to NOK 22,000. The rates and number of kilometers remain unchanged.

Reduced personal allowance for travel deduction: The Government proposes an increase of the lower threshold of the travel allowance from NOK 16,000 to NOK 22,000. The rates and number of kilometers remain unchanged.

Wealth tax: The tax rate on net wealth is proposed to be reduced from 0.85 % to 0.8 %. Furthermore, the lower threshold is proposed to be increased from 1.2 million to 1.4 million. For married couples, the lower threshold will be 2.8 million.

Tax collection: The Government proposes a coordination of tax collector functions through moving the collection of taxes from each municipality to the Central Tax Authorities as of 01.06.2016.

The transfer of the collection of taxes will entail an expenditure cut of NOK 207 million in 2016, and a yearly expenditure cut of NOK 356 million as of 2017.

Deloitte's view

Through the suggested changes Norwegian taxation will take a significant step in moving from net taxation to gross taxation. This will imply a lower effect of actual deductions claimed.

The changes will generally result in a lower taxation of salary income.

Individuals who have significant ownership income (dividend income, income from the sale of stock or similar) may be imposed a higher taxation.

The taxation of ownership income will imply that such income is taxed at a higher rate than other capital income.

— Cecilie Bue (Oslo)
Senior Manager
Deloitte Norway
cbue@deloitte.no

Stig A. Sperre (Oslo)
Partner
Deloitte Norway
ssperre@deloitte.no

People's Republic of China:
New limit to be imposed on overseas Union Card cash withdrawals

Overview

China's State Administration of Foreign Exchange (SAFE) issued a notice on 18 September 2015 (Huifa [2015] No. 40 (Notice 40)) that aims to further strengthen the administration of overseas cash withdrawals (including in Hong Kong, Macao, and Taiwan) by Union Pay cardholders.

According to Notice 40, an annual limit will be imposed on overseas cash withdrawals, in addition to the daily limit of RMB 10,000. Effective 1 January 2016, the annual limit for overseas cash withdrawals will be RMB 100,000 or its equivalent in a foreign currency, per card. For the period 1 October to 31 December 2015, the limit is RMB 50,000 or its equivalent in a foreign currency, per card.

Individuals who violate the restrictions will be added to a watch list and banned from withdrawing further cash overseas.

Key implications

The cash withdrawal limit currently is RMB 10,000, or its equivalent in a foreign currency, per day. With the issuance of Notice 40, it appears that the annual withdrawal limit of RMB 3,650,000 will be reduced to RMB 100,000. However, it should be noted that the new rule does not affect the overseas purchase of goods using a Union Card.

Deloitte's view

The annual RMB 100,000 limit under Notice 40 applies on a per card basis, not on an individual basis. Based on our consultations with Union Pay, in theory, an individual who holds more than one Union Pay card could make withdrawals that exceed the established limit. Nevertheless, individuals should be aware that SAFE and banks are paying closer attention to foreign exchange control and the outflow of funds from China, so potential challenges could arise if an individual uses more than one Union Pay card to withdraw an amount of cash that exceeds the new annual RMB 100,000 limit. Individuals working outside of China should closely monitor future regulatory updates if they require frequent overseas cash withdrawals.

— Gus Kang (Beijing)
Partner
Deloitte People's Republic of China
gukang@deloitte.com.cn

Huan Wang (Beijing)
Partner
Deloitte People's Republic of China
huawang@deloitte.com.cn

Mona Mak (Hong Kong)
Partner/Principal
Deloitte People's Republic of China
monmak@deloitte.com.hk

Tony Jasper (Hong Kong)
Partner
Deloitte People's Republic of China
tojasper@deloitte.com.hk

Sandy Cheung (Shanghai)
Partner
Deloitte People's Republic of China
sancheung@deloitte.com.cn

Joyce W. Xu (Shanghai)
Partner
Deloitte People's Republic of China
joycewxu@deloitte.com.cn

Fei Fei Li (Shenzhen)
Director
Deloitte People's Republic of China
ffli@deloitte.com.cn

Irene Yu (Shanghai)
Deloitte People's Republic of China
Partner
iryu@deloitte.com.cn

South Africa:
Updated changes to the South African immigration legislation

Overview

In August 2015, the President set up the Inter Ministerial Committee to look at the unintended consequences and mitigating factors relating to the implementation of the Immigration Amendment Acts (2007 and 2011) and Immigration Regulations, 2014. The recommendations were presented to Cabinet, and the Department of Home Affairs (DHA) has now enforced some of these recommendations. It must be noted that the law, as amended, will remain with practical adjustments to be made in execution, to make it easier to comply to.

Important changes

Highlights: Changes to traveling with minors:

- Child travel requirements for outbound traveling will stay, including proof of parental relations through unabridged birth certificates, and, as necessary, parental consent.
- In respect of inbound travel where visas are required, it will still be required that original birth certificates and, as necessary, parental consent or certified copies are submitted during the visa application process.
- Requirements regarding unaccompanied minors will remain, like providing copies of the identity document or valid passport and visa or permanent residence permit of the person who is to receive an unaccompanied minor.
- For visa-exempt countries, a strong advisory directive will be issued, with travelers advised to have proof of relationship and consent from the absent parent/s or guardian/s, if in the event that they are asked to provide such on arrival.
- The DHA will consider extending the validity of the parental consent affidavit to six months.

Submission of applications:

- In terms of the decision, on the requirement for travelers to apply for visas in person, in countries where there is no SA mission, the DHA will receive applications, including by post.
- The biometrics details of travelers will be captured on arrival at ports of entry.

Other decisions that Cabinet have recommended and DHA will be looking at implementing: In the next three to twelve months:

- Implement the capturing of biometrics at ports of entry starting with a pilot at OR Tambo, King Shaka, and Cape Town airports;
- Consider a long-term multiple entry visa for a period exceeding three months and up to three years for frequent travelers (for business meetings), business people, and academics;
- Add visa facilitation centers, including in Zimbabwe, United Arab Emirates, and Botswana;
- Open two Corporate Visa Facilitation Centers in Durban and Port Elizabeth, in addition to the centre recently opened in Sandton;
- Consider visa exemption status for India, China, Russia, and other countries; and
- Consider granting a 10-year multiple entry visitor’s visa for a certain category of frequent travelers (business and academics) for countries on the African continent.

In the long term, one year and beyond:

- Install systems for preflight checks at international airports;
- Upgrade Advance Passenger Processing systems and implement Passenger Name Record to enhance risk assessment; and
- Finalize automation of the visa and permitting system.

Please note that there are other changes and if you would like to enquire about what these changes are, kindly contact one of the resources below.

Deloitte's view

The birth certificate requirement: Although the current press releases advise that the requirement requesting presentation of an unabridged birth certificate for all minor children at the port of entry (in original or certified copy) has been relaxed this month. Deloitte is of the opinion that as a precaution, the requirement is still to be adhered to for the time being until the strong advisory is sent out and officials are up to speed with the changes. This is to avoid any queries at the port of entry that may delay entry into South Africa.

Lodgement in person: We would need to evaluate each case depending on where the application is to be lodged, to determine if the relevant mission is up to speed with the changes in the systems.

— Lino De Ponte (Johannesburg)
Partner
Deloitte South Africa
ldeponte@deloitte.co.za

Shivana Sewchuran (Johannesburg)
Senior Manager
Deloitte South Africa
ssewchuran@deloitte.co.za

Vishal Nundlall (Johannesburg)
Senior Manager
Deloitte South Africa
vnundlall@deloitte.co.za

Lesley Coetzee (Johannesburg)
Manager
Deloitte South Africa
lcoetzee@deloitte.co.za

Tanja Kesner-Reddy (Johannesburg)
Manager
Deloitte South Africa
tkesnerreddy@deloitte.co.za

Melicia Stuurman (Johannesburg)
Manager
Deloitte South Africa
mstuurman@deloitte.co.za

Sweden:
Foreign tax credit on incentive-based income not granted due to expired reassessment period of tax return

Overview

The Swedish Administrative Court of Appeal has held that a foreign tax credit on share based incentive income only can be granted the income year when the income is subject to tax in Sweden.

In the specific situation, Sweden taxed the income at vesting and the other country (Finland) at the subsequent exercise. The exercise occurred more than six years after the vesting, meaning that it was too late to reassess the tax return for the specific year with the vested benefit and include a claim for a foreign tax credit.

Background

A question has been raised to the Swedish Administrative Court of Appeal whether a foreign tax credit could be obtained due to double taxation of share-based incentive income in Sweden. Both Swedish and foreign tax was levied on the same income earned while performing work abroad.

Important facts in the current case are that the same income had different taxable events in Sweden (vesting) and the other country (exercise).

When the foreign tax on the income was known, a reassessment was filed with the Swedish Tax Agency claiming that a foreign tax credit should be granted in Sweden the same year as taxed abroad, i.e., not in the year the income was actually taxed in Sweden. This was not accepted by the Swedish Administrative Court of Appeal.

The ruling of the Administrative Court of Appeal

The Swedish Administrative Court of Appeal stated in its ruling that a foreign tax credit must be applied for the same income year that the double-taxed income is subject to tax in Sweden, i.e., point of vesting in this case. Considering that a reassessment of a tax return in Sweden must be filed no later than six years back in time, a foreign tax credit could not be applied for the tax returns filed prior to this. The fact that tax on the capital gain from the sale of the shares was due in Sweden in the same year as the exercise, it did not change this fact as it regards a different type of income (capital or investment income) than employment income (arising from an incentive-based benefit).

Deloitte's view

Although this case has unusual and specific elements, it serves as a reminder that it is important to keep the timing issue in mind for share-based incentive income when different countries apply different taxable events.

If the moment of taxation in another country is more than six years after the benefit was subject to tax in Sweden, it is too late to apply for a foreign tax credit for the double taxed income in Sweden.

Incentive programs issued to mobile employees are highly complex from a Swedish tax perspective. This is why Deloitte always recommends that companies with incentive plans ensures that sufficient processes are in place to avoid the situation as described in this case.

One question that was not tested by the Swedish Administrative Court of Appeal in this case was if the benefit value in the other country at the point of exercise could be seen as an acquisition cost of the shares and thereby reducing the Sweden taxable capital gain. It does not appear that the taxpayer made this claim, which is why the court did not rule on that question.

The judgment may be appealed to the Supreme Administrative Court (SAC). It is, however, uncertain if the case will be tried by the SAC even if it is appealed.

— Frida Haglund (Stockholm)
Partner
Deloitte Sweden
fhaglund@deloitte.se

Emilia Häggblom (Stockholm)
Consultant
Deloitte Sweden
ehaggblom@deloitte.se

Marcus Jönsson (Stockholm)
Senior Manager
Deloitte Sweden
mjonsson@deloitte.se