DEVELOPMENTS IN EMPLOYEE SHARE OWNERSHIP PLANS IN AUSTRALIA

On 27 May the Australian House of Representatives gave second and third readings to some important amendments to employee share plan legislation. The changes improve the tax position for all companies operating employee share plans and introduce some new tax concessions targeted at start-ups. The Bill, which amends some damaging revisions to share plan taxation arrangements made in 2009, secured cross-party support. The changes take effect from 1 July 2015.

For all companies, there has been a full reversal of the option plan taxation position: any discount on options (and rights) will now be taxed at exercise rather than vesting. The 2009 changes had in effect shifted the tax point for discounts on the award of options and shares to the date of award (unless there was a real risk of forfeiture or a disposal restriction). In effect most options and rights plans were taxed at vesting rather than exercise. There was a possible $1,000 exemption if the plan operated with specific rules but this was available only to those earning $A180,000 or less. These changes reduced the attractiveness of employee share schemes generally, and had led to a steep decline in option-based plans.

Where an employee has not exercised previously awarded options because they are underwater (the exercise price for the option is higher the prevailing share price of the company), he or she can now get a full tax refund (previously this was not the case if it was the employees choice not to exercise). There has also been clarity about premium-priced options (options with an exercise price above the market share price at the time of grant). These options sit outside the ESS taxation legislation and some companies have used these to ensure that their plan fell into the CGT (capital gains tax) regime. There was some confusion, however, about whether these were subject to Fringe Benefit Tax. It has now been clarified that they do not.

Rights (options and rights, with no or nominal exercise prices) do not need to have a real risk of forfeiture just a disposal restriction. This opens the way for Non-Executive Directors to sacrifice their fees into plans again (using rights).

Finally, the potential to defer income tax on discounts has been extended from 7 to 15 years.

Safe harbour valuation methodologies have been created for unlisted companies to reduce the compliance burden. At this stage it looks like this will be based on Net Tangible Assets and this is currently being consulted with industry.

For start-ups a new, and very favourable, regime has been created. If a company meets the start-up test they are able to grant options (or shares with a discount of 15% or less), and the options and shares (that fall within the15% limit) are not subject to income tax. They are only subject to CGT on disposal and more importantly for options the CGT concession will apply as long as the options have been held for 12 months or more. This is a very significant change and a completely new structure in Australia. To qualify as a start-up, a company must be unlisted, incorporated for less than 10 years, resident in Australia for tax purposes (this can apply in certain cases to Australian subsidiaries of multinationals), and have aggregate turnover of less than $50 million. Private-equity controlled companies are not necessarily excluded from access to the concession. Eligibility is restricted to those employees holding less than 10% of the company's equity

Angela Perry, the Chair of Employee Ownership Australia, comments that "the Government should be applauded for the new start-up regime which is incredibly generous and places Australia on par with countries such as the UK. However, for listed companies the gains are minimal. In fact, for most companies it has added complexity. Companies now have three regimes to contend with: pre-2009, post-2009 and post-1 July 2015".

A remaining anomaly, is that share scheme members who are made redundant may be taxed on share plan discounts at the point of employment termination. In a series of recent meetings with MPs, Senators, and Ministers in Canberra recently, Angela Perry and Andrew Pendleton encountered considerable sympathy for amending this provision in employee share plan legislation.

Angela Perry and Andrew Pendleton
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