

19 March 2020

Committee Secretary
Standing Committee on Tax and Revenue
PO Box 6021
Parliament House
CANBERRA ACT 2600

Via email: TaxRev.reps@aph.gov.au

Dear Sir/Madam

Inquiry into the effectiveness of the 2015 Employee Share Scheme (ESS) changes

Thank you for the opportunity to provide a submission to the Standing Committee on Tax and Revenue on the effectiveness of the 2015 Employee Share Scheme (**ESS**) changes.

The Australian Institute of Company Directors (**AICD**) has a membership of more than 45,000 including directors and senior leaders from business, government and the not-for-profit sectors. The mission of the AICD is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society.

Given our significant and diverse membership from a wide range of sectors, the AICD has a strong interest in enhancing the effectiveness of the ESS tax rules to ensure the ongoing promotion of share ownership by employees and directors - for start-up companies as well as a range of companies more broadly (in particular, early stage businesses that may not qualify for the start-up concessions).

The AICD was actively engaged in the consultation on the *Tax and Superannuation Laws Amendment (2015 Measures No.1) Bill 2015*, and we welcome the opportunity to provide comment on how the existing legislation could be further improved.

1. Removal of tax on cessation of employment

Equity interests under ESS arrangements are designed to align employee and shareholder interests, promote long-term ownership of shares and encourage future growth mindsets, rather than short-term risk taking. Indeed, there is a strong push by industry, investors and regulators to encourage employees to hold equity for extended performance and deferral periods.

Requiring employees to pay tax on equity that has not yet vested (in other words, value that they are unable to access or may never access) on cessation of their employment runs counter to these objectives and puts Australia out of step with the taxation treatment afforded under ESS regimes in the UK and US. This is also inconsistent with the taxation treatment of equivalent cash-based incentive arrangements, which are generally only taxed when an employee realises the cash payment, rather than the cessation of employment.

Moreover, these tax provisions work against regulatory initiatives such as the current Banking Executive Accountability Regime (**BEAR**) as well as the draft proposed Prudential Standard CPS 511 and Financial Accountability Regime (**FAR**) mandating deferral periods for performance-based remuneration. Notably, the Australian Prudential Regulation Authority (**APRA**) has taken the view it is preferable for deferral and vesting arrangements to remain

in place post cessation of employment and that cessation of employment as a taxation point for deferred share schemes 'has the potential to cause conflict between prudent deferral and taxation requirements'.¹ We note too that the Australian Productivity Commission in its report 'Executive Remuneration in Australia' has long recommended that employees' equity remain subject to full vesting requirements regardless of cessation of employment.²

Accordingly, the AICD strongly suggests that the ESS tax rules be amended to enable the taxing point to be triggered only on the vesting of equity (or, in the case of options, on exercise), not by an employee's cessation of employment. It is critical that the broader ecosystem of taxation policy, regulatory compliance and corporate governance practices works harmoniously so that it does not inadvertently discourage long-term share ownership by employees.

2. Greater flexibility for start-company concessions

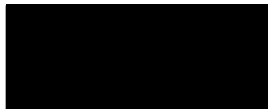
It is critical that ESS arrangements in Australia afford the right tax benefits to attract and retain top talent, particularly in the start-up context when viewed against market competitive compensation packages globally.

As raised in our previous submission on this issue, we are concerned that the conditions for start-ups to be eligible for the tax concessions are too restrictive. In order to be of greater benefit to start ups and to ensure that they can appropriately tailor their ESS arrangements for their business, we suggest removing the 3-year disposal restriction for start-up options and the requirement that a start-up company be unlisted.

3. Next steps

We hope our comments will be of assistance to you. 

Yours sincerely



LOUISE PETSCHLER
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¹ APRA, Prudential Practice Guide for Remuneration (2009), p.13.

² Australian Productivity Commission Inquiry Report: Executive Remuneration in Australia No. 49 (19 December 2010).