

EXPLANATORY STATEMENT

Select Legislative Instrument No. 63, 2015

Issued by authority of the Minister for Small Business

Income Tax Assessment Act 1997

Income Tax Assessment Amendment (Employee Share Schemes) Regulation 2015

Section 909-1 of the *Income Tax Assessment Act 1997* (the Act) provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Act.

The *Income Tax Assessment Amendment (Employee Share Schemes) Regulation 2015* (Regulation) amends the *Income Tax Assessment Regulations 1997* (ITAR 1997) as detailed below.

Purpose

The purpose of the Regulation is to amend the existing employee share scheme taxing rules to improve the international competitiveness and productivity of Australian companies, to assist companies to attract and retain staff, to encourage start-up companies to be established in Australia, to assist start-up companies to succeed, and to encourage further innovation in Australia. The Regulation will provide greater flexibility for taxpayers by extending the scope of the simplified valuation tables so that it covers unlisted rights that may be exercised between 10 and 15 years. The valuation tables will also be clarified through the inclusion of the assumptions used to determine the values listed in tables in the Regulations which have been updated to reflect current market conditions.

Context

An employee share scheme (ESS) is a scheme under which shares, stapled securities or rights to acquire them (ESS interests) in a company are provided to an employee or their associate in relation to the employee's employment.

Some companies encourage employees to participate in employee share schemes by offering employees shares, stapled securities, or ESS interests (including options) at a discount. ESS income tax rules apply to this discount.

The tax law contains specific rules about how tax applies to ESS interests. These rules apply to shares, stapled securities and rights to acquire them (including options), that have been provided to employees at a discount under an ESS.

Market value is generally used to determine the value of any ESS interest and any discount provided on its issue to an employee. However, valuation of ESS options can instead be determined by reference to rules set out in ITAR 1997. Division 83A of the

ITAR 1997 sets out alternate rules and valuation tables that can be used to determine the value of an ESS right. Use of these regulations by a taxpayer is voluntary, and taxpayers may instead choose to calculate market value using general principles. Further, if the rights are capable of exercise beyond 15 years, taxpayers will continue to be required to calculate market value using general principles, if a relevant taxing point occurs.

Application

This Regulation replaces the tables set out in subregulations 83A-315.08(1) and 83A-315.08(1) of the ITAR 1997 to reflect current market conditions. The full tables are set out in the Attachment and apply from 1 July 2015. The amendments made by Schedule 1 apply in relation to an ESS interest from commencement on 1 July 2015, even if the interest was acquired before that date.

In a report produced in 2009-2010, the Board of Taxation recommended that the Government should include the assumptions used to update the tables. The assumptions underlying the tables are set out in the Attachment.

This measure is part of the Government's Industry Innovation and Competitiveness Agenda.

Conditions

The Regulation is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The Regulation commences on 1 July 2015.

Description of Consultation

Public consultation was undertaken on the measure for 4 weeks commencing 14 January 2015 and concluding on 6 February 2015, through a release of the exposure drafts onto the Treasury website. No material concerns were raised regarding the changes made by this Regulation.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

The Legislative Instrument updates the existing option valuation tables under the employee share scheme taxing rules.

Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

Details of the *Income Tax Assessment Amendment (Employee Share Schemes) Regulation 2015*

Section 1 – Name of Regulation

This section provides that the title of the Regulation is *Income Tax Assessment Amendment (Employee Share Schemes) Regulation 2015* (Regulation).

Section 2 – Commencement

This section provides that the Regulation commences on 1 July 2015.

Section 3 – Authority

This section provides that the Regulation is made under the *Income Tax Assessment Act 1997*.

Schedule 1: Amendments

The Regulation replaced the tables set out in subregulations 83A-315.08(1) and 83A-315.09(1) of the *Income Tax Assessment Regulations 1997* (ITAR 1997).

Specifically, the purpose of the Regulation is to update the existing employee share scheme (ESS) taxing rules by updating the option valuation tables to reflect current market conditions.

Assumptions behind the valuation tables:

The Board of Taxation recommended in a report produced in 2009-2010 that when updating the tables, the Government should include the assumptions used to produce the tables. The assumptions used are:

- Risk-free interest rate – 4%
- Dividend yield – 4%
- Volatility – 12%

New valuation tables

To reflect current market conditions, the tables set out in subregulations 83A-315.08(1) and 83A-315.09(1) are to be replaced with the following tables:

Table 1—Table 1 percentages							
Calculation percentage 50% to 92.5%							
Exercise period (months)	Calculation percentage (%)						
	50 to 60	60 to 70	70 to 75	75 to 80	80 to 85	85 to 90	90 to 92.5
168 to 180	0.5%	1.3%	2.6%	3.5%	4.6%	5.8%	7.1%
156 to 168	0.42%	1.2%	2.5%	3.4%	4.4%	5.7%	7.1%
144 to 156	0.4%	1.0%	2.3%	3.2%	4.3%	5.5%	7.0%
132 to 144	0.3%	0.9%	2.2%	3.0%	4.1%	5.4%	6.8%

Table 1—Table 1 percentages							
Calculation percentage 50% to 92.5%							
Exercise period (months)	Calculation percentage (%)						
	50 to 60	60 to 70	70 to 75	75 to 80	80 to 85	85 to 90	90 to 92.5
120 to 132	0.2%	0.8%	2.0%	2.8%	3.9%	5.2%	6.6%
108 to 120	0.2%	0.7%	1.8%	2.6%	3.7%	4.9%	6.4%
96 to 108	0.1%	0.6%	1.6%	2.4%	3.4%	4.6%	6.1%
84 to 96	0.1%	0.4%	1.3%	2.1%	3.0%	4.3%	5.8%
72 to 84	0.1%	0.3%	1.1%	1.7%	2.7%	3.9%	5.4%
60 to 72	0.0%	0.2%	0.8%	1.4%	2.2%	3.4%	4.9%
48 to 60	0.0%	0.1%	0.5%	1.0%	1.7%	2.8%	4.2%
36 to 48	0.0%	0.0%	0.3%	0.6%	1.2%	2.1%	3.4%
24 to 36	0.0%	0.0%	0.1%	0.3%	0.6%	1.3%	2.4%
18 to 24	0.0%	0.0%	0.0%	0.1%	0.3%	0.9%	1.8%
12 to 18	0.0%	0.0%	0.0%	0.0%	0.1%	0.4%	1.1%
9 to 12	0.0%	0.0%	0.0%	0.0%	0.1%	0.2%	0.8%
6 to 9	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.4%
3 to 6	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%
0 to 3	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Calculation percentage 92.5% to less than 110%							
Exercise period (months)	Calculation percentage (%)						
	92.5 to 95	95 to 97.5	97.5 to 100	100 to 102.5	102.5 to 105	105 to 107.5	107.5 to less than 110
168 to 180	7.9%	8.6%	9.4%	10.3%	11.2%	12.2%	13.3%
156 to 168	7.8%	8.6%	9.4%	10.3%	11.2%	12.2%	13.3%
144 to 156	7.7%	8.5%	9.4%	10.3%	11.2%	12.2%	13.3%
132 to 144	7.6%	8.4%	9.3%	10.2%	11.2%	12.2%	13.3%
120 to 132	7.5%	8.3%	9.2%	10.2%	11.2%	12.2%	13.3%
108 to 120	7.2%	8.1%	9.1%	10.0%	11.1%	12.1%	13.3%
96 to 108	7.0%	7.9%	8.8%	9.8%	10.9%	12.0%	13.2%
84 to 96	6.6%	7.6%	8.5%	9.6%	10.7%	11.8%	13.0%
72 to 84	6.2%	7.2%	8.2%	9.2%	10.4%	11.6%	12.8%
60 to 72	5.7%	6.7%	7.7%	8.8%	9.9%	11.2%	12.5%
48 to 60	5.1%	6.0%	7.0%	8.2%	9.4%	10.7%	12.1%
36 to 48	4.2%	5.2%	6.2%	7.4%	8.6%	10.0%	11.4%
24 to 36	3.2%	4.1%	5.1%	6.3%	7.6%	9.0%	10.5%
18 to 24	2.5%	3.4%	4.4%	5.5%	6.8%	8.3%	9.9%
12 to 18	1.7%	2.5%	3.4%	4.6%	6.0%	7.5%	9.2%
9 to 12	1.3%	2.0%	2.9%	4.0%	5.4%	7.0%	8.8%
6 to 9	0.8%	1.4%	2.2%	3.3%	4.7%	6.4%	8.3%
3 to 6	0.3%	0.6%	1.3%	2.4%	3.8%	5.7%	7.8%
0 to 3	0.0%	0.1%	0.5%	1.4%	3.0%	5.1%	7.5%

Table 2—Base percentages		
Exercise period (months)	Column 1	Column 2
168 to 180	13.3%	0.5%
156 to 168	13.3%	0.5%
144 to 156	13.3%	0.5%
132 to 144	13.3%	0.6%
120 to 132	13.3%	0.6%
108 to 120	13.3%	0.6%
96 to 108	13.2%	0.6%
84 to 96	13.0%	0.6%
72 to 84	12.8%	0.7%
60 to 72	12.5%	0.7%
48 to 60	12.1%	0.7%
36 to 48	11.4%	0.8%
24 to 36	10.5%	0.8%
18 to 24	9.9%	0.8%
12 to 18	9.2%	0.9%
9 to 12	8.8%	0.9%
6 to 9	8.3%	0.9%
3 to 6	7.8%	0.9%
0 to 3	7.5%	1.0%