After more than a month of detailed submissions on the proposed changes to the tax concessions for employee share plans, the Treasury has announced changes to the measures announced in the 2009 Budget.

The new provisions will apply from 1 July 2009 but the text of the new amendments is not yet available.

The main changes are:

- the threshold for eligibility for the tax concession for the $1,000 free grant of shares is to be increased to an adjusted taxable income of $180,000;
- the maximum time for the deferral of tax is reduced from ten years to seven years;
- apart from the $1,000 concession, tax will be paid as at the date of grant unless there is a real risk of forfeiture of the equity or the plan is a capped salary sacrifice plan satisfying the existing qualifying employee share plan rules;
- employers will be required to report to the ATO the market value of shares and rights acquired under a plan at an employee’s taxing point; and
- tax deferral will be limited to $5,000 worth of shares.

A major concern to the ATO has been the use in some plans of performance hurdles which do not provide a real barrier to vesting, and in some cases, make vesting subject only to a decision made by the participant alone. The new rules will provide for the risk of forfeiture in each plan to be scrutinised and assessed.

There are still problems in the management of grants of options and rights where tax may be paid as at the date of grant on the basis of an assessment of the potential value of the equity as at a future date. The first problem arises from the need to pay tax on a potential gain before it is received.

Many employees would not be able to fund the tax payment while most plans provide that the options or rights cannot be sold or mortgaged to raise the funds. Mention has been made of allowing partial sale to cover tax, but how this would be documented and managed is still to be worked out.

If at a future date the share price has gone down to the extent that the options are under water, and the participant decides not to exercise the options, it appears that the tax paid at vesting will not be refunded. In these volatile times, this will make the drafting of performance hurdles and the granting of options a very difficult task.

It seems that a number of the major concerns of the business and professional community have been addressed. Hopefully the drafting of the amendments will help clarify the situation. The Treasury has referred the rules for the valuation of equity to the Board of Taxation for review.

Egan Associates prepared a submission during the consultation process.

For an article based on that submission click here