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31 August 2021

KPMG submission in relation to exposure draft legislation to provide regulatory and tax relief for employee share schemes released on 29 July 2021

Dear Directors

KPMG appreciates the opportunity to provide a submission to Treasury on exposure draft legislation and explanatory materials released on 29 July 2021 to provide regulatory and tax relief for employee share schemes, including:

- exposure draft inserts for the Treasury Laws Amendment (Measures for a later sitting) Bill 2021: Employee Share Schemes (**Draft ESS Regulatory Bill**); and
- exposure draft inserts for the Treasury Laws Amendment (Measures for a later sitting) Bill 2021: Employee Share Schemes – Removing cessation of employment as a taxing point (**Draft ESS Tax Bill**).

KPMG is broadly supportive of the proposed reforms having previously provided submissions on these issues and believes the reforms will make it easier for businesses – particularly unlisted companies – to offer employee share schemes in Australia.

In particular, we support the reforms to:

- remove disclosure, licensing, advertising and hawking requirements of the *Corporations Act 2001* (Cth) (**Corporations Act**) for ESS offers to employees and directors which do not require payment to participate;
- remove the offer value cap for ESS offers made by unlisted companies to employees and directors which do not require payment to participate and to increase the offer value cap for ESS offers made by unlisted companies to independent contractors or which require payment to participate;
- enable the use of loan arrangements as well as contribution plans to fund the acquisition of ESS interests offered by unlisted companies;
- extend regulatory relief to also cover the offer of non-voting ordinary shares, which are commonly offered by unlisted companies under an employee share scheme;

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- remove the quotation requirements currently applicable to listed companies seeking to rely on ASIC class order 14/1000; and
- remove cessation of employment as a taxing point.

While broadly supportive of the proposed reforms, KPMG welcomes the opportunity to comment on aspects of the Draft ESS Regulatory Bill in the **Annexure** to this submission. Most of these comments while technical in nature are intended to ensure that the legislation is harmonised and workable for businesses whilst remaining consistent with underlying policy. These include recommendations to:

- expand various references to an ESS interest being issued to also cover the transfer of an ESS interest (or alternatively the ESS interest being acquired) to ensure that the transfer of ESS interests (for example, a share) are not excluded from key concepts under the new regulatory regime;
- amend the definition of an 'ESS interest' applicable to a listed company and listed registered scheme to remove the requirement that no monetary consideration be payable for an option which is not able to be traded to be exercisable;
- amend the definition of an 'ESS loan' to allow the loan to be offered by an 'associated entity' of the body corporate or listed registered scheme; and
- amend the requirements applicable where a trustee is used to manage ESS interests to permit fees or charges being paid to the trustee provided that they are not paid by any ESS participant or out of the assets of the trust.

In addition, we note that the proposed amendment to the tax legislation would only apply to ESS interests acquired, at the earliest, from 1 July 2022. We urge the government to consider having the change apply to all ESS interests for which the deferred taxing point has not yet occurred, as of the date of the amended legislation receiving Royal Assent. This would accelerate the elimination of what is a considerable compliance burden for businesses and employees.

We appreciate Treasury considering this submission following the public consultation period closing on 25 August 2021.

In the meantime, please do not hesitate to contact us if have any questions or would like to discuss this submission.

Yours sincerely

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Annexure

KPMG submission in response to exposure draft legislation providing regulatory relief for employee share schemes

1. Issue of ESS interests

- 1.1. There are a number of definitions included in the Draft ESS Regulatory Bill which refer to ESS interests being issued.
- 1.2. For example, subsection 1100E(1) which defines an 'employee share scheme' and subsection 1100J(1) which defines an 'ESS offer' include one or more references to ESS interests being *issued*.
- 1.3. Similarly, an 'incentive right' is defined as "...a *right to be issued* a security or financial product or a right to be paid a cash amount (or a combination of these rights)..."
- 1.4. Subsection 1100E(5) which relates to the issue of ESS through a trust also refers to the ESS interests of a body corporate or responsible entity of a listed registered scheme being *issued* to another body corporate that is the trustee of a trust, for the purposes of that *trustee issuing* ESS interests of the body corporate or scheme to ESS participants. Subsection 1100E(7) also refers an ESS interest being *issued* to a trustee.
- 1.5. We are concerned that these references to ESS interests being issued, or in the case of an 'incentive right' the right to be issued a security or financial product, are too limiting and do not recognise that an ESS interest (in particular, a share) may be acquired by way of transfer (for example, to the ESS participant from an employee share trust). The reference to options in subparagraph (a)(ii) of the proposed definition of a 'contribution plan' recognises this and refers to "options, offered for no more than nominal consideration, for the *issue or transfer* of fully paid ordinary shares". Other references to options in the Draft ESS Regulatory Bill refer to "an option to *acquire* a fully paid ordinary share".
- 1.6. We also note that the existing definition of an 'employee share scheme' in section 9 of the Corporations Act while being limited in the interests that may be offered under an employee share scheme, does refer to those interests being "*acquired*" rather than issued.
- 1.7. Further, the definition of an 'offer' in ASIC class orders CO14/1000 and CO14/1001 includes "an offer to *transfer* the eligible product" and an 'incentive right' is defined as "a conditional right to *acquire* underlying eligible products..." in contrast to the new definition of an 'incentive right' proposed in the Draft ESS Regulatory Bill.
- 1.8. Given that the existing regulatory framework relating to employee share schemes recognises that ESS interests may be issued or transferred, we would recommend amending the relevant references in the Draft ESS Regulatory Bill to ESS interests being acquired or otherwise recognising such interests may be transferred (not only issued) and do not believe that this should raise any policy concerns.
- 1.9. We are also concerned with the references in subsections 1100E(5) and 1100E(7) of the Draft ESS Regulatory Bill to the trustee issuing ESS interests given that the trustee will not itself issue ESS interests, but rather hold the ESS interest on trust for the ESS participant



and transfer legal title to the ESS interest to the ESS participant when the ESS interest is released from the trust.

2. Meaning of ESS interest

2.1. An 'ESS interest' is defined in section 1100F of the Draft ESS Regulatory Bill. For a listed company or listed registered scheme it includes:

"a unit in, an incentive right granted in relation to, or an option to acquire an interest mentioned in any of paragraphs [(a) to (e)] to which either or both of the following applies:

- (i) the unit, right or option is able to be traded on a financial market operated by a market licensee or an approved foreign financial market;
- (ii) the unit, right or option is not acquired or exercisable (if applicable) upon the payment of monetary consideration."

2.2. We understand the policy rationale, as outlined in paragraph 1.38 of the explanatory materials for the Draft ESS Regulatory Bill, for such interests only being eligible if they are provided to ESS participants for free if they are not themselves able to be traded. However, the inclusion of the words "or exercisable (if applicable)" are problematic and should be removed, since an option will typically require the payment of an exercise price to be exercised.

3. ESS loans

3.1. Under subsection 1100J(1) of the Draft ESS Regulatory Bill, an employee share scheme can be eligible for relief if it has an associated loan, provided that the loan meets the definition of an 'ESS loan'.

3.2. The definition of an 'ESS loan' requires the loan to be "offered by a body corporate or a responsible entity of a listed managed investment scheme to an ESS participant of the body corporate or scheme". In our experience, loans are sometimes provided by a related body corporate of the issuer of the ESS interests (for example, an employing entity). Accordingly, we suggest that the definition of 'ESS loan' be amended to allow the loan to be offered by an 'associated entity' of the body corporate or scheme. This is in line with the existing requirements of ASIC class order 14/1000 which extends to loans provided by the listed body an associated body corporate.

4. ESS contribution plans

4.1. Under subsection 1100J(1) of the Draft ESS Regulatory Bill, employee share schemes can have contribution plans associated with the scheme and still be eligible for relief, provided that the contribution plan meets the definition of an 'ESS contribution plan'.

4.2. Given that the term 'contribution plan' is also defined in the Corporations Act, it would appear that the contribution plan must also meet the definition of a 'contribution plan'. This would seem to be supported by paragraph 1.51 of the explanatory materials to the Draft ESS Regulatory Bill which states that the ESS contribution must "only relate to fully paid shares or units in, incentive rights granted in relation to or options to acquire fully paid shares".



- 4.3. Paragraph (a) of the definition of 'contribution plan' currently covers regular deductions from the wages or salary of an employee or director (the contributor) to acquire financial products.
- 4.4. It is proposed that paragraph (a) will be repealed and substituted with a new paragraph (a) which will limit the financial products that may be acquired under the contribution plan to:
 - (i) fully paid ordinary shares;
 - (ii) options, offered for no more than nominal consideration, for the issue or transfer of fully paid ordinary shares; and
 - (iii) units in fully paid ordinary shares.
- 4.5. The definition of an 'ESS contribution plan' is broader than the definition of a 'contribution plan' and refers to the issue of 'ESS interests'. It also refers to an 'ESS participant' participating in the plan, not only employees or directors unlike the definition of 'contribution plan'.
- 4.6. If the definition of an 'ESS contribution plan' is not intended to be limited by the definition of a 'contribution plan', we suggest this be made clear in the Draft ESS Regulatory Bill.
- 4.7. If it is intended to be limited by the definition of a 'contribution plan', we suggest that paragraph (a) of the definition be expanded to also cover incentive rights to acquire fully paid shares as intended (refer to paragraph 1.51 of the explanatory materials to the Draft ESS Regulatory Bill). We also submit that the definition should cover all ESS participants (including independent contractors) for consistency with the other provisions of the Draft ESS Regulatory Bill and in light of the additional requirements for offers made to independent contractors under the Draft ESS Regulatory Bill.

5. Trustees managing an employee share scheme

- 5.1. Subsections 1100E(5) and 1100E(6) of the Draft ESS Regulatory Bill allow a body corporate or responsible entity of a listed registered scheme to use a trustee to manage ESS interests under an employee share scheme provided the trust meets certain requirements.
- 5.2. The requirements broadly reflect the existing requirements that must be met in order to rely on ASIC class orders 14/1000 and 14/1001. However, paragraph (c) of subsection 1100E(6) requires that the trustee must not charge any fees or charges for administering the trust, other than reasonable disbursements. The equivalent requirement under paragraph 20(c) of both CO 14/1000 and 14/1001 only prohibits fees or charges for administering the trust that are payable directly by any eligible participant or out of the assets of the trust.
- 5.3. We suggest amending paragraph (c) of subsection 1100E(6) to only prohibit fees or charges that are payable directly by any ESS participant or out of the assets of the trust. Professional trustee service providers will typically charge fees for administering employee share trusts. This amendment would allow the body corporate or responsible entity of a listed registered scheme utilising a trust to manage ESS interests to directly pay any such administration fees to the trustee, while still minimising financial risk for ESS participants and not compromising the trustee acting in the best interests of ESS participants.



6. Consequential amendment to definition of 'employee share buy-back'

- 6.1. It is proposed that the existing definition of an 'employee share scheme buy-back' in section 9 of the Corporations Act will be repealed and replaced with the new defined term 'employee share buy-back' with the same meaning.
- 6.2. The proposed definition of 'employee share buy-back' covers "a buy-back under a scheme that:
- (a) has as its purpose the acquisition of shares in a company by, or on behalf of:
 - (i) employees of the company, or of a related body corporate; or
 - (ii) directors of the company, or a related body corporate, who hold a salaried employment or office in the company or in a related body corporate; and
 - (b) has been approved by the company in general meeting."
- 6.3. In other words, it is limited to employees and salaried directors (and does not cover non-executive directors or independent contractors). We submit that this definition should be amended to cover 'ESS participants' in line with other provisions of the Draft ESS Regulatory Bill, and do not believe that this should raise any policy concerns.