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By Email

Dear Treasury

Submission – Treasury Consultation Paper and Exposure Draft Legislation: Employee share schemes

1 Introduction

This submission is made by Herbert Smith Freehills (**HSF**) in response to Treasury consultation on a consultation paper, revised exposure draft legislation and explanatory materials published in December 2021 in respect of regulatory arrangements for employee share schemes (**ESSs**).

HSF is an international law firm with 27 offices located around the globe and which specialises in, amongst other things, financial services and financial services regulation. We regularly advise domestic and foreign, listed and unlisted entities who wish to make ESS offers to employees of their Australian subsidiaries.

In this submission we have provided our high level comments in respect of Treasury's consultation paper, revised exposure draft legislation and explanatory materials. We would be happy to discuss our comments with Treasury and provide any supporting explanation if that would assist.

2 Value cap

In our earlier submission we welcomed the increase in the value cap from \$5,000 to \$30,000 per employee per year and invited Treasury to consider increasing it further, to say \$50,000 per employee per year, so that small and start-up businesses which are growing rapidly are able to attract the best talent and invest in their businesses.

We note that the value cap provisions have been amended (in section 1100X(5)) to take into account 70% of any dividends and 70% of cash bonuses received by the ESS participant in the year.

The concession to take dividends and cash bonuses into account will assist larger and mature businesses but will not assist small and start-up businesses which tend to be cash poor and may not be in a position to pay any dividends or cash bonuses.

Given this we would like to repeat our invitation to Treasury to consider increasing the cap to say \$50,000 per employee per year so that small and start-up businesses are not disadvantaged by the application of this value cap.

3 Use of a trust account to hold application monies

A significant practical difficulty in relation to using a contribution plan is the requirement that before the participant acquires the ESS interests under the offer, the payments or deductions are held on trust in an account with an Australian ADI that is kept solely for that purpose.

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It is difficult to find an ADI that offers a trust account and when you do find one, the process to open a trust account with an Australian ADI is complicated and protracted.

- Opening a trust account is particularly difficult for foreign companies offering global incentive plans which extend to Australia for the benefit of the Australian employees in large international businesses.
- French incentive plans are commonly structured as a fonds communs de placement d'entreprise (**FCPE**) which is a non-corporate trust vehicle with a french trust deed. In our experience it is very difficult for Australian banks to be able to onboard and complete their AML/CTF and KYC checks for a FCPE and that they are usually in the position that they cannot offer a trust account to a FCPE at all.

The new section 1100Z requires an ESS participant's application money to be held in trust until the ESS interests are issued or transferred to them or the application money is returned to the ESS participant.

We assume, as section 1100Z does not refer to holding on trust in an account with an ADI, that the person offering ESS interests for issue or sale to an ESS participant is not required to hold the money in a trust account with an ADI and that the trust arrangement could be achieved by the person simply declaring a trust over the relevant money.

If our assumption is correct it would be helpful to clarify this in the explanatory memorandum. If our assumption is not correct then this trust requirement will have a disproportionate impact on international offerors of ESS interests, particularly FCPEs.

4 14 days between offer document and offer acceptance

The new section 1100V(a) provides (as one of the 'general rules') that the terms of an offer of ESS interests must provide that an ESS participant cannot acquire an ESS interest under the offer until at least 14 days after receiving the ESS offer document and any supporting information required under section 1100U (if applicable) for the offer.

We think that the explanation of this provision in paragraph 1.103 of the explanatory memorandum does not quite align with this and suggest that it is amended as follows:

1.103 For an offer that requires payment upfront, 14 days before [the offer is open for acceptance](#)~~making an offer~~, the participant must be provided with:...

5 Notice of intent

Under the proposed section 1100ZB and Schedule 3 of the Corporations Act, a failure to lodge a 'notice of intent' with ASIC in the 'prescribed form' before any ESS offers are made in connection with monetary or option ESS offers is an offence with a maximum penalty of five years' imprisonment.

We noted in our last submission that we considered that this level of penalty was inappropriately high for an administrative notice.

Five years' imprisonment is a high penalty level, like that which applies for failing to provide a disclosure document (which provides prescribed content to retail clients to assist them to make informed investment decisions).

The notice of intent is not a disclosure document but is an administration form, providing contact details and a notice of use to ASIC, similar to a form FS88, which is used to notify ASIC that a product disclosure statement is in use. We continue to submit that the penalty for failing to lodge an administration form (i.e. for failing to manage red tape) should be commensurate with the penalty for failing to lodge a form FS88, which is a maximum penalty of two years' imprisonment, rather than the penalty for a provide a prospectus under section 727 of the Corporations Act, which is a maximum penalty of five years' imprisonment.



We assume that the 'prescribed form' for a notice of intent will be similar to the *CF08 Notice of reliance on Class Order [CO 14/1000] Employee incentive schemes: Listed bodies; and Class Order [CO 14/1001] Employee incentive schemes: Unlisted bodies (CF08)*. We would again invite Treasury to consider prescribing either in a note in the draft legislation or in the explanatory materials that the 'prescribed form' is the CF08 to provide clarity on this, particularly given the proposed consequences of a failure to provide the prescribed form.

Yours sincerely

Sent electronically without signature

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