

## TAX ISSUES ENTRY SYSTEM (TIES) BRIEFING

<b>TIES Issue Number:</b>	0036-2009
<b>Submitted By:</b>	Email address:  Postal address:
<b>Concerning:</b>	Income tax – capital protected borrowings - Division 247 of the <i>Income Tax Assessment Tax 1997</i>
<b>Issue Raised:</b>	<p>The _____ is seeking to have the exclusion for employee share schemes in subsection 247-15(3) of the ITAA 1997 to all shares acquired by employees (where the scheme provides a loan to employees to acquire shares at a market value) rather than shares acquired under an “employee share scheme” (as defined in Division 13A)</p> <p>Currently, the exclusion from Division 247 applies to shares acquired under an “employee share scheme”. However, under Division 13A of the Income Tax Assessment Act 1936 (“ITAA 1936”), a share is only acquired under an employee share scheme if the share's acquisition price is less than the “market value” of the share as determined under the market value rules in section 139FA of Division 13A of the ITAA 1936.</p> <p>According to the _____, typically, under these types of plans, shares are acquired for market value, so the exclusion in Division 247 would not apply.</p> <p>The _____ claim that this is contrary to the stated intention of Division 247 (Explanatory Memorandum at paragraph 7.41 provides - "this measure is not to apply to CPB's under which a company provided limited recourse loans to employees to buy shares in their employer companies").</p>
<b>Treasury view:</b>	<p><i>Does Treasury agree that there is a problem with the law as described by the correspondent?</i></p> <p>No. Treasury does not agree that there is a problem with the law as it operates as intended.</p> <p><i>Does Treasury need advice from the ATO on the operation of the law?</i></p> <p>No. Treasury and the ATO agree that the law works as intended.</p> <p><i>Is the law operating appropriately? If not, how is it inappropriate?</i></p> <p>Yes. The law is operating appropriately. Subsection 247-15(3) of the ITAA 1997 is not ambiguous so that there is no need to consider the Explanatory Memorandum in interpreting the provision.</p> <p><i>Is this a care and maintenance issue or does it involve major policy?</i></p> <p>This is a major policy issue as it seeking to extend the exclusion for employee share schemes to arrangements not recognised as employee share schemes.</p>

	<p>Under these arrangements finance is provided by the employer but the employee has to pay market value for shares in the employer’s company. It is assumed that the loan would have to be at a discount rate or there would be no or little incentive for the employee to enter into such arrangement because it would be cheaper to borrow by increasing a home loan or by entering into a margin loan.</p> <p><i>Can the issue be addressed by a minor amendment?</i></p> <p>This issue is a policy issue which cannot be addressed by a minor amendment.</p> <p><i>What are the reasons for the view?</i></p> <p>This is a policy issue not a technical issue. The legislation is clear.</p> <p>It is not considered appropriate to extend the current FBT exclusion of ESS shares to the means by which ESS acquisitions are financed. That is, it is not considered appropriate to exempt from FBT discounted loans provided by employers to employees just because the loan will be used to purchase ESS shares.</p> <p>Similarly, it is not considered appropriate to exclude the capital protection premium which would normally be paid on limited recourse loans from FBT just because the loan is provided in connection with the purchase of ESS shares.</p> <p>A submission received during the development of the capital protected borrowing measures stated that there are a “great number” of companies which use limited recourse loans to finance the acquisition of ESS shares. Research by the Department of Employment and Workplace Relations found that only a small number of companies use limited recourse loans to finance ESS share acquisitions.</p> <p>There also does not appear to be a strong case that the aims of encouraging employee share ownership would be advanced by providing additional concessional treatment for ESS shareholders in relation to FBT.</p> <p>Consequently, based on these arguments, it is considered to be inconsistent with the principles of FBT, and the principles behind the current ESS exclusion from FBT, to provide a specific carve out for limited recourse loans to purchase shares under an ESS.</p> <p>There is no sound policy reason for extending the carve-out to arrangements where finance is provided at market interest rates or discounted interest rates to purchase shares at the market value. Such an extension of the carve-out would create an unlevel playing field between those investors borrowing as employees and those borrowing as non-employees. It would also undermine the integrity of the capital protected borrowing measures as taxpayers could avoid the application of the measures merely by structuring an arrangement using an employer loan.</p>
<b>Date of effect</b>	Not applicable.
<b>Explanation for correspondent</b>	As required, prepare an explanation for the correspondent of why the issue will not be pursued. This explanation should be similar to the content that would be included in a ministerial response. This will be included in the letter sent by the

	TIES Secretariat.
<b>Sensitivity</b>	Describe any sensitivities with the Treasury view – for example, the Government is considering its response to a report that raises the same issue.
<b>Drafting instructions</b>	Not applicable.
<b>Policy approval information</b>	Not applicable.