

3 March 2016

Commissioner of Taxation
Attn: Mr Haydn Daw
New Measures
IND LINCS
Australian Taxation Office

By email: haydn.daw@ato.gov.au

Dear Sir,

Re: Employee share scheme templates

Guerdon Associates appreciates the opportunity to respond to the Australian Taxation Office's (ATO) invitation to comment on the employee share scheme draft documents (the "documents") attached to your email of 17 December 2015.

Guerdon Associates welcomes the ATO's contribution to the program of making it easier, less costly and more efficient for start-up entities to implement an employee share scheme (ESS). We consider the ATO's existing ESS material that was developed earlier in 2015 to be a welcome step in simplifying a complex regime, particularly for start-up entities that do not have the resources or expertise enjoyed by larger listed entities. However, notwithstanding the high standard of product released by the ATO, start-up entities continue to find the way through the ESS maze to be difficult and costly.

The remainder of this submission provides brief information regarding our firm and then provides our comments on the documents and how they may be further refined to facilitate simpler adoption of ESS by start-up companies.

About Guerdon Associates

Guerdon Associates is an independent¹ executive remuneration and board governance consulting firm. Our clients include 20% of the ASX 50, a significant proportion of companies in the ASX 300, and private and pre-IPO companies. Offices are located in Melbourne and Sydney, with additional support located in offices in Chennai, India (database management and administration) and San Francisco (technology support), and affiliate firms in Los Angeles, New York, London, Zurich, Singapore and Beijing. The firm has worked with the boards of many of Australia's companies that have and utilise employee share scheme arrangements. The firm has and will continue to work with start-up companies to implement equity incentive arrangements that align employee interests with the investors.

The firm's submissions were among the most cited in the Productivity Commission's review of executive remuneration, and over the years it has contributed to Treasury and Australian Taxation Office consultations on numerous Corporations Act and taxation legislation changes.

¹ Independence is defined as a specialist provider of consulting services to boards to minimise conflicts of interest that may result from being a broad based supplier of multiple services to both management and boards.

Our comments are focused on the employer's handbook and the corporations law and regulatory requirements.

Employee share schemes – employer's handbook

The following observations and comments are provided for your consideration.

- ESS can be used by all types of employing entities but the implications vary significantly depending on the type of company (public – listed or unlisted – private, large, small etc) and structure used. While the handbook provides some excellent observations and commentary, companies may find they have a large range of issues to consider without necessarily knowing what the answer may be or where to find it. While the handbook states it “contains general information to help you decide whether an ESS is right for your company”, it is drafted in a way that identifies most of the issues to be considered rather than showing the way to a resolution.

The companies that will refer to the handbook are those smaller companies lacking the financial and human resources available to larger companies. This means that they will often require clear statements of the advantages for them and, equally relevant, the disadvantages for them of an employee share scheme in their particular circumstance.

It may, therefore, be useful to broadly describe the pros and cons of an employee share scheme arrangement for each of the different categories of company. A one page summary appendix could be included for each category.

- It may assist readers to understand the way forward by moving the section “What sort of company.....” on page 8 to the first page. In this way, the reader is being introduced to what follows.

This section currently refers to the fact that “...unlisted companies must take into account special regulatory provisions.” Since many such companies are likely to be the users of the handbook it may be useful to provide a checklist of those provisions at this point and how they may be resolved.

- The handbook identifies many of the benefits for employees and employers of introducing an ESS. As noted above, the companies with limited specialist or financial resources available to them, and in particular, private companies, will equally want to understand the implications for different types of companies of such a scheme. This would include commentary on, among other things:
 - Employees having the right to vote
 - Employees' equity holdings being subject to shareholders agreements
 - How unlisted companies deal with realisation of the ESS interests
 - Implications of the buyback provisions on forfeiture
 - The need to establish market value for grant and disposal purposes
 - Dilution of shareholder interests
- There is a trend to ensure more meaningful and accurate terminology not reflected in the handbook. For example, LTIP is increasingly being confined to grants of equity that are subject to explicit performance requirements (hence the use of “incentive”) for a period exceeding 12 months (hence the use of “long-term”). In many cases the allocation of equity to employees may be an inducement to join the company, or

remain with the company, rather than to achieve specified outcomes. Therefore, most times LTIP is used in the handbook it could be replaced with "employee equity plan".

- The different types of employee equity plans ("LTIPs") on page 9 should also include a reference to a "rights plan" being a right to acquire a fully paid ordinary share for no consideration. A "restricted share plan" is often understood to be a plan whereby the fully paid ordinary share is granted to the employee at date of grant. An example of this would be the \$1,000 tax exempt plan shares which are not subject to forfeiture.

In summary, while the employer's handbook does well in identifying most of the potential issues a company needs to address, the pathway to resolving those issues is less clear. It is appreciated that setting out the pathway for all aspects would lead to a much lengthier and more complex "handbook".

Many of the issues have significantly different outcomes depending on whether the company is a listed or unlisted public company, or a small or large private company. A variation of the handbook for each type would make presentation of the issues clearer.

Corporations Act and regulatory requirements

The commercial and taxation issues covered in the handbook and discussed above are quite distinct from the issues that arise for less well-resourced companies from the corporations law and related regulatory requirements.

It is appreciated that ASIC has a range of guides, class orders and related material that provide the specific rules or basis on which the law or relief will be applied. These present a significant barrier to the broader and deeper application of employee equity plans. Yet there is no equivalent handbook on these aspects to complement the ATO handbook.

However, given the extensive range of material that has to be considered it would facilitate a far more efficient, less costly and wider and deeper adoption of employee share schemes if there was an exclusive code in the Corporations Act covering all employee share schemes in all companies. Such a code would limit or eliminate many of the disclosure, self-dealing, hawking, licensing, and similar regulatory requirements that should not have application to employee share schemes.

Please do not hesitate to contact me if you would like to discuss any aspect of the above.

Sincerely,



Martin Morrow
Principal

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