

# Dwyer Lawyers

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12 June 2009

The Hon Wayne Swan  
Treasurer  
Parliament House  
CANBERRA ACT 2600

Dear Mr Swan

### EMPLOYEE SHARE PLANS

As lawyers, we specialize in estate and succession planning. For some time, we have been examining the possible use of concessional Division 13A share plans in this process. Hence, my question at the Budget breakfast to your colleague, the Minister for Finance. Unfortunately, Mr Tanner did not seem to understand the point of my question.

Put simply, hundreds of thousands of small businesses in this country will close over the next 2 decades as baby boomers retire, if they cannot find buyers for their businesses. When those businesses close, many people will lose their jobs.

Employee share plans can, in theory, help solve these potential problems.

They can:

1. maintain and improve the productivity of the business;
2. offer the possibility of full sale to employees
3. preserve business goodwill and retirement equity
4. preserve the jobs of employees

Mr Tanner seemed quite unaware of these issues.

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Accordingly, we respectfully submit, first, that

- the Parliament be invited to amend the law to remove the 75%, 5% and ordinary shares rules as well as the 7 year rule in the case of small business.

These rules currently mean that concessional tax employee share plans cannot be used to facilitate employee buyouts and that other, non-concessional, share transfer or ownership plans must be used to assist employee buyouts. In a small business buyout, there will rarely be twenty buyers with 5% each and only a small percentage of employees may be buying. Further, the requirement to dispose of shares after 7 years to pay the tax defeats the purpose of an enduring buyout. Thus in the case of small business there needs to be a carve-out from these onerous conditions.

Turning to the technical issues in the Treasury's paper and the draft legislation, as we understand it, the current position is that benefits or discounts under employee share plans are taxed under the income tax law and taxed as required in the hands of the employee. They are therefore naturally excluded from fringe benefits tax. The real problem is how to value or treat the benefits and when they should be taxed in the hands of the employee.

In this regard, we submit that the Treasury's "real risk" concept is legally undefined and operationally meaningless. It will generate useless litigation and may even be manipulated. We also note deferral is nothing strange and should not be seen as inherently objectionable. For example, parliamentarians, judges and public servants are not taxed on accrual of their pension entitlements and only pay tax on their pension entitlements as and when received. The "receipt" principle is basic to tax law. Income tax is meant to be a tax on what *does* come in, not what *may* come in.

Further, we note that Australia is out of touch with US and UK treatment of employee share plans documented in the Treasury paper. Capital gains treatment should apply as in the USA to accretions in share value over purchase price and that deferral of tax on the discount is not a reason to deny capital treatment to the share itself.

We therefore submit that:

- Any discount on shares should only be taxed in the hands of the employee when the employee has first had the right to dispose of the shares *and receive the proceeds*. Any earlier taxing point creates the real risk that employees will be taxed on amounts they never get. (For example, the stock market crash has shown many people that paper values may not translate into cash 4 weeks later.)
- Any accretion in the value of shares over the purchase price be treated as a capital matter in regard to any tax on any gain.

We trust these comments are helpful to your review and that we may see a new concessional share plan tax treatment which is useful for small business succession.

If you or your officers have any further questions we should be happy to assist. If, on the other hand, you or your officers feel that we have not understood either the existing law or proposed law, we would appreciate correction so that we may advise future clients with precision.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Terence Dwyer', written in a cursive style.

Terence Dwyer  
Solicitor