



Class Ruling

Income tax and fringe benefits tax: IOOF Holdings Limited – Equity Participation Program

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① This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 21A of the *Income Tax Assessment Act 1936* (ITAA 1936);
- Division 13A of Part III of the ITAA 1936 ('Division 13A');
- section 139B of the ITAA 1936;
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- Part XIB of the *Fringe Benefits Tax Assessment Act 1986* (FBTAA).

All subsequent references in this Ruling are to the ITAA 1936, unless stated otherwise.

Class of entities

3. The class of entities to which this Ruling applies is all persons who are authorised representatives of Consultum Financial Advisers Pty Ltd (Consultum) and who receive an award under the IOOF Equity Participation Program (the Plan). In this Ruling, a person belonging to this class of entities is referred to as a 'participant'.

Qualifications

4. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 12 to 24 of this Ruling.

5. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

7. This Ruling applies from 1 July 2006. The Ruling applies to all entities within the specified class who enter into the specified scheme, subject to there being no change in the scheme or in the entities involved in the scheme.

8. The Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

9. If this Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

10. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

11. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

12. The following description of the scheme is based on information provided by KPMG (the applicant). The following documents, or relevant parts of them form part of and are to be read with the description:

- the application for a Class Ruling from the applicant dated 28 June 2007;
- the IOOF Equity Participation Program – 2006 Award Offer;
- the IOOF Equity Participation Program – Program Rules (Plan rules);
- the IOOF Equity Participation Program Information Booklet; and
- additional information provided by the applicant dated 31 July 2007, 24 August 2007, 11 September 2007, 25 September 2007 and 26 October 2007.

13. IOOF Holdings Limited (IOOF) is an Australian resident company listed on the Australian Securities Exchange (ASX) and conducts a financial services business through its various subsidiary companies, which includes Consultum.

14. The authorised representatives (individual advisers) of Consultum provide financial advice to clients of Consultum under agreements entered into with Consultum. Each individual adviser is a party to a contract with Consultum, either:

- directly under an individual adviser agreement;
- by being a party to a corporate agreement that the corporate has with Consultum; or

- by being a party to a partnership agreement that the partnership has with Consultum.

15. The applicant has advised that:

- neither IOOF nor Consultum have a pay as you go (PAYG) withholding obligation under Part 2-5 of Schedule 1 of the TAA in relation to any payments to individual advisers for services provided;
- neither the applicant nor IOOF are aware of which method of tax accounting (either receipts or earnings method) is used by each individual adviser; and
- where an award is satisfied by a cash payment, for the purposes of the earnings method, a recoverable debt will arise at the time of issue of a vesting notice to the participant.

16. IOOF has introduced the Plan to provide an incentive for individual advisers to maintain their relationship with the IOOF group. Under the Plan, and at the discretion of the IOOF board (the board), certain eligible individual advisers who are identified as key contributors to the business of the IOOF group will be offered an award based on their financial performance. Such offers, which are proposed to be made annually, will constitute an offer to participate in the Plan.

17. Participants in the Plan, who are eligible individual advisers who accept an offer, will be granted an award. An award, which is subject to vesting conditions, will entitle a participant to either acquire fully paid ordinary shares in IOOF (shares) or receive an equivalent amount in cash. An award does not confer any legal or equitable right or interest in shares.

18. The board has the absolute discretion to determine whether an award, granted to a participant that has met the vesting conditions, will be satisfied by the issue of shares or the payment of cash.

19. For an award to vest, a participant must, during the period of three years after the award is granted:

- attend not less than 85% of professional development days, unless non-attendance is with management's prior consent;
- not be placed on the monitoring and supervision program as a result of receiving a risk rating of extreme; and
- remain an authorised representative of Consultum, or be otherwise engaged by IOOF to provide financial planning services.

20. Where an award meets the vesting conditions, a vesting notice will issue to a participant advising them of:

- the number of shares to be issued or transferred to the participant; or
- the cash equivalent to be paid to the participant.

21. The issue or transfer of shares or a cash payment to a participant will be made after the issue of a vesting notice.

22. If an award does not meet the vesting conditions, the participant will not receive a vesting notice and, accordingly, will not be entitled to shares or cash in relation to that award.

23. The allocation of shares or cash in relation to an award that vests is calculated using a formula based on brokerage/fees produced by a participant over the financial year prior to the granting of an award.

24. Participants do not pay any consideration for an award at the time of the grant of the award, or at the time the award is converted to shares or cash.

Ruling

Where an award is granted

25. Where a participant is granted an award under the Plan:

- the participant does not acquire a right to acquire a share under an employee share scheme for the purposes of Division 13A;
- the award at the time of grant does not give rise to a reportable fringe benefits amount for the participant for the purposes of Part XIB of the FBTAA; and
- the award is not a 'non-cash business benefit' for the purposes of section 21A.

Where a share is issued or transferred

26. Where a share is issued or transferred to a participant as a consequence of the vesting of an award granted to the participant under the Plan, the participant will acquire a share under an employee share scheme for the purposes of Division 13A.

27. Where a participant acquires a share under the Plan, any discount given on the share is included in the assessable income of the participant in the year of income in which the share is acquired, pursuant to subsection 139B(2).

Where cash is paid

28. Where a participant is paid an amount of cash as a consequence of the vesting of an award granted to the participant under the Plan, the amount of cash paid is ordinary income and is included in the assessable income of the participant in the year of income in which it is derived (pursuant to section 6-5 of the ITAA 1997).

29. Where a participant uses the receipts method of accounting for income, the amount of the cash payment is derived when it is actually paid to the participant or if not paid directly, when it is dealt with on their behalf or as they direct.

30. Where a participant uses the earnings method of accounting for income, the amount of the cash payment is derived when the vesting notice is issued to the participant.

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

Where an award is granted

A right for the purposes of Division 13A

31. The expression 'right' as used in Division 13A is not defined. However, as 'right' and 'right to acquire a share' are used interchangeably throughout Division 13A, the Commissioner considers that a 'right' should be taken to mean a 'right to acquire a share'.

32. Where, at the time a right is granted to a taxpayer:

- the taxpayer has a right to acquire a share on exercise of the right; and
- for the purposes of subsection 139B(2), the amount of the discount in respect of such a right can reasonably be determined,

the Commissioner considers the 'right' to be a right for the purposes of Division 13A.

33. However, where a taxpayer acquires a right under a scheme that purports to be a right to acquire a share, and the scheme operates so that it is not the taxpayer who makes the ultimate decision as to whether they actually receive a share (or cash in lieu of a share), the right granted will not be considered to be a right to acquire a share for the purposes of Division 13A.

34. Under the Plan rules, the board may, at its discretion, satisfy a participant's vested rights by either the payment of cash or the issue or transfer of shares.

35. Thus, the Commissioner considers that a participant will not acquire a right for the purposes of Division 13A at the time a right, in the form of an award, is granted to a participant under the Plan.

Fringe benefit

36. The definition of 'benefit' in subsection 136(1) of the FBTAA includes any right, privilege, service or facility.

37. Therefore, the grant of an award to a participant under the Plan, which is a right (albeit not a right to acquire shares for the purposes of Division 13A of the ITAA 1936), comes within the definition of a 'benefit' for the purposes of the FBTAA. However, for such a benefit to be considered a 'fringe benefit' for the purposes of the FBTAA, the primary criterion is that it must be provided 'in respect of employment' of an employee.

38. The expression 'in respect of' is defined in subsection 136(1) of the FBTA as 'in relation to the employment of an employee, includes by reason of, by virtue of, or for or in relation directly or indirectly to that employment'. The term 'in respect of employment' has been considered by the courts on numerous occasions. In *J & G Knowles & Associates Pty Limited v. Federal Commissioner of Taxation* (2000) 96 FCR 402; 2000 ATC 4151; (2000) 44 ATR 22; it was noted that the term 'in respect of employment' includes benefits where:

...there is a sufficient or material, rather than a causal connection or relationship between the benefit and the employment...

39. The applicant has advised that neither IOOF nor Consultum have a PAYG withholding obligation under Part 2-5 of Schedule 1 of the TAA in relation to any payments to participants (individual advisers) for services provided. As a consequence, it can be concluded that in relation to such payments by IOOF or Consultum, they do not have a sufficient or material connection with the employment of a participant.

40. Therefore, such a payment would not be considered to be made in respect of the employment of a participant within the meaning of the FBTA.

41. Further, where an award is granted to a participant under the Plan that, on vesting, may give rise to a payment of the kind mentioned above, the grant of the award will also not have the necessary connection with employment and, therefore, will not be a fringe benefit for the purposes of the FBTA.

42. Accordingly, the grant of an award to a participant under the Plan will not at the time of grant, or any other time, give rise to a reportable fringe benefits amount for the participant, for the purposes of Part XIB of the FBTA.

Non-cash business benefit

43. The definition of 'services' for the purposes of the non-cash business benefit provisions (subsection 21A(5) of the ITAA 1936) is virtually identical to the definition of 'benefit' for the purposes of the FBTA.

44. Therefore, where a participant is granted an award under the Plan which, as described in paragraph 37 of this Ruling, is a benefit for the purposes of the FBTA, it will also come within the definition of 'services' for the purposes of section 21A of the ITAA 1936.

45. Where an individual contractor is granted a right or rights to remuneration (pre-existing remuneration rights) that are an intrinsic part of a contract for services that ultimately results in the receipt by the contractor of remuneration which is subject to tax under the relevant tax laws as:

- ordinary income;

- as a non-cash business benefit (under section 21A); or
- as a discount on a share (under Division 13A),

the pre-existing remuneration rights, whilst it is accepted that they come within the definition of 'services' for the purposes of section 21A, are not treated as non-cash business benefits for the purposes of section 21A.

46. Thus, where a participant is granted an award under the Plan they will not receive a non-cash business benefit for the purposes of section 21A.

Where a share is issued or transferred

Acquiring a share under an employee share scheme

47. Section 139C effectively provides that a taxpayer acquires a share under an employee share scheme if the share is:

- acquired within the meaning of section 139G;
- acquired in respect of, or for or in relation directly or indirectly to, any:
 - employment of the taxpayer or an associate of the taxpayer (subsection 139C(1)); or
 - services provided by the taxpayer or an associate of the taxpayer (subsection 139C(2)); and
- acquired for less than market value (subsection 139C(3)).

48. A person will acquire a share when, amongst other things, the share is issued or transferred to them. Therefore, where the award vesting conditions have been met and the board decides to satisfy the award by the issue or transfer of shares to the participant, such shares will be acquired by the participant within the meaning of section 139G.

49. Further, where such shares are acquired by a participant as a consequence of an award vesting, it is accepted that the shares are acquired directly or indirectly in relation to (financial advisory) services provided (within the meaning of subsection 139C(2)) by the participant to Consultum.

50. The applicant has advised that where an award is converted to shares and the shares are issued or transferred to a participant under the Plan, the participant does not provide any consideration. Therefore, where a participant acquires a share under the Plan, they will acquire it for less than market value for the purposes of subsection 139C(3).

51. As the requirements specified in paragraph 47 of this Ruling are satisfied, the Commissioner accepts that where a participant acquires a share under the Plan, they will acquire a share under an employee share scheme for the purposes of Division 13A.

Inclusion of the discount on a share in assessable income

52. Where a taxpayer acquires a share under an employee share scheme, any discount given in relation to the share will be included in the assessable income of the taxpayer, pursuant to subsection 139B(1).

53. As a participant who acquires a share under the Plan will acquire the share under an employee share scheme, subsection 139B(2) will determine when the discount is to be included in the assessable income of the participant, unless the share is a 'qualifying share' in respect of which the participant has not made an election under section 139E.

54. In accordance with subsection 139CD(3), to be a 'qualifying share' a share must be in a company that is the employer of the taxpayer or a holding company of the employer. As shares acquired by participants under the Plan are shares in IOOF, which is not the employer of participants or a holding company of the employer of participants, the shares will not be qualifying shares.

55. Therefore, subsection 139B(2) applies such that the discount on a share is included in the participant's assessable income in the year of income in which the share is acquired by the participant under the Plan.

56. The amount of the discount to be included in a participant's assessable income is determined by subsection 139CC(2), and is the market value of the share (worked out under Subdivision F of Division 13A) at the time it was acquired (as no consideration is provided by the participant).

Where cash is paid

Inclusion of cash in assessable income

57. Under subsection 6-5(1) of the ITAA 1997, an amount is assessable income if it is income according to ordinary concepts (ordinary income).

58. In determining whether an amount is ordinary income, the courts have established the following principles:

- what receipts ought to be treated as income must be determined in accordance with the ordinary concepts and usages of mankind, except in so far as a statute dictates otherwise;

- whether the payment received is income depends upon a close examination of all relevant circumstances; and
- whether the payment received is income is an objective test.

59. Relevant factors in determining whether an amount is ordinary income include:

- whether the payment is the product of any employment, services rendered, or any business;
- the quality or character of the payment in the hands of the recipient;
- the form of the receipt, that is, whether it is received as a lump sum or periodically; and
- the motive of the person making the payment. Motive, however, is rarely decisive as in many cases a mixture of motives may exist.

60. In consideration of the above factors, where a participant is paid a cash amount under the Plan, the cash amount is paid by Consultum either directly or indirectly in relation to services rendered by the participant and is contingent on the participant meeting the award vesting conditions which relate to the provision of those services. Therefore, cash received by a participant under the Plan is assessable as ordinary income for the purposes of section 6-5 of the ITAA 1997.

61. Under subsections 6-5(2) and (3) of the ITAA 1997, taxpayers must include in their assessable income the ordinary income derived during the income year.

62. The question of when ordinary income is derived by a taxpayer is determined by reference to the method of accounting that, in the circumstances, is appropriate for the taxpayer.

Receipts method

63. Under the receipts method (or cash received basis), income is derived when it is actually received, or when it is received constructively, for the purposes of subsection 6-5(4) of the ITAA 1997. The effect of that subsection is that income is taken to be derived by a person, even if it is not actually paid over, when it is dealt with on their behalf or as they direct.

64. Therefore, where a participant accounts for income using the receipts method, they will derive the cash amount when it is actually paid to the participant or if not paid directly, when it is dealt with on their behalf or as they direct.

Earnings method

65. Under the earnings method (or accruals method), income is derived when it is earned. The point of derivation occurs when a recoverable debt is created.

66. The applicant has advised that for the purposes of the earnings method, where an award granted to a participant is to be satisfied by a cash payment, a recoverable debt will arise at the time of the issue of a vesting notice to a participant.

67. Therefore, under these circumstances, a participant will derive ordinary income for the purposes of section 6-5 of the ITAA 1997 at the time that a vesting notice is issued to them and such amount will be included in their assessable income in the year of income in which the vesting notice is issued.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Subject references:

- employee share scheme
- fringe benefit
- income derived
- non-cash business benefit
- rights

Legislative references:

- ITAA 1936 21A
- ITAA 1936 21A(5)
- ITAA 1936 Pt III Div 13A
- ITAA 1936 139B
- ITAA 1936 139B(1)
- ITAA 1936 139B(2)
- ITAA 1936 139C
- ITAA 1936 139C(1)
- ITAA 1936 139C(2)
- ITAA 1936 139C(3)
- ITAA 1936 139CC(2)
- ITAA 1936 139CD(3)
- ITAA 1936 139E

- ITAA 1936 Pt III Div 13A Subdiv F
- ITAA 1936 139G
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 6-5(2)
- ITAA 1997 6-5(3)
- ITAA 1997 6-5(4)
- FBTAA 1986
- FBTAA 1986 Part XIB
- FBTAA 1986 136(1)
- TAA 1953
- TAA 1953 Sch 1 Pt 2-5
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968

Case references:

- J & G Knowles & Associates
Pty Limited v. Federal
Commissioner of Taxation
(2000) 96 FCR 402; 2000 ATC
4151; (2000) 44 ATR 22;
[2000] FCA 196

ATO references

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Fringe Benefits Tax ~~ Liability to tax