

# ***CR 2003/51 - Income tax: Brickworks Limited - Deferred Employee Share Plan***



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## Class Ruling

### Income tax: Brickworks Limited - Deferred Employee Share Plan

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#### *Preamble*

*The number, subject heading, and the **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains **Class Rulings** and **Taxation Rulings** TR 92/1 and TR 97/16 together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

#### **What this Class Ruling is about**

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

#### **Tax law(s)**

2. The taxation laws dealt with in this ruling are:

- 139B of the *Income Tax Assessment Act* (ITAA 1936);
- 139BA of the ITAA 1936;
- 139C of the ITAA 1936;
- 139CA of the ITAA 1936;
- 139CC of the ITAA 1936;
- 139CD of the ITAA 1936;
- 139CE of the ITAA 1936;
- 139E of the ITAA 1936;
- 139FA of the ITAA 1936;
- 139FB of the ITAA 1936;
- 139G of the ITAA 1936;
- 139GF of the ITAA 1936;
- 6-5 of the *Income Tax Assessment Act* (ITAA 1997);

- 104-75 of the ITAA 1997;
- 109-5 of the ITAA 1997;
- 130-80 of the ITAA 1997;
- 130-83 of the ITAA 1997.

**Note: On December 5<sup>th</sup> 2002 *Taxation Laws Amendment Bill (No. 8) 2002* was introduced into Parliament which amends the capital gains tax treatment of certain shares and rights acquired under employee share schemes in Division 13A. This ruling deals only with the law as presently enacted and which is not subject to the proposed amendments.**

## **Class of Persons**

3. The class of persons to whom this ruling applies is the Australian resident employees (participants/participating employees) of the Brickworks Group who participate in the Brickworks Limited Deferred Employee Share Plan (DESP/Plan) as described in the Arrangement part of this Ruling. The Brickworks Group comprises Brickworks Limited, The Austral Brick Company Pty Limited, The Austral Tile Company Pty Limited, The Austral Export Company Pty Limited, and Eureka Tiles Pty Limited.

## **Qualifications**

4. The Commissioner makes this Ruling based on the precise arrangement identified in this ruling.

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement described below at paragraphs 9 to 19 is carried out in accordance with the details of the arrangement provided in this Ruling.

6. If the arrangement described in this Ruling is materially different from the arrangement that is actually carried out:

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

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## **Date of effect**

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8. This ruling applies from the 2002/2003 year of income. However, this 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 (see paragraphs 21 and 22 of Taxation Ruling TR 92/20). Furthermore this Ruling only applies to the extent that:

- It is not later withdrawn by notice in the Gazette; or
- It is not taken to be withdrawn by an inconsistent later Public Ruling; or
- The relevant taxation laws are not amended.

## **Arrangement**

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9. The arrangement that is the subject of this Ruling is described below. The description is based on the following documents. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the arrangement are:

- Class Ruling Application, dated 1 July 2002;
- Brickworks Limited (ACN 000 028 526) Deferred Employee Share Plan Trust Deed (May 2002);
- Brickworks Limited (ACN 000 028 526) Deferred Employee Share Plan ('Deferred Plan') Information Booklet.

**Note: certain information received has been provided on a commercial-in-confidence basis and will not be disclosed or released under the Freedom of Information Legislation.**

10. The DESP was established as part of the employee share plan strategy of the Brickworks Group. Participation is offered to all Australian resident permanent full time or part time employees and directors of the Brickworks Group, who have completed at least 3

months employment with the Brickworks Group to salary sacrifice a part of their remuneration to acquire shares under the Plan.

Additionally, any bonus or incentive payments for participating employees will be automatically salary sacrificed into the DESP unless the employee otherwise elects to receive the bonus or incentive as salary prior to becoming entitled to it. For each non director participant, the Brickworks Group will also contribute an additional amount towards the purchase of shares in the DESP.

11. Special discretionary offers may also be made to select employees that have minimum service and performance conditions attached to aid in the retention and motivation of these employees.

12. The purchase of Brickworks Limited ordinary shares will be funded by way of an effective salary sacrifice arrangement within the meaning of paragraphs 19 to 23 of *Taxation Ruling* TR 2001/10. Participants will not be required to contribute any other funds in order to acquire the ordinary shares.

13. CPU Share Plans Pty Limited (CPU/Plan Trustee) has been appointed to act as trustee in the implementation and administration of the Plan. The Trust will be administered in a manner that ensures the sole activities of the Trust are to acquire Brickworks Limited ordinary shares and to provide such ordinary shares to participating employees of the Brickworks Group. In this regard any income or property to which a participant is not presently entitled cannot be used for the administration of the employee share plan. The Brickworks Group will meet the brokerage fees on share purchases, along with all other DESP expenses, costs and charges incurred by the Plan Trustee. Employees will only be responsible for brokerage fees on any share sales.

14. CPU will use the funds it receives from the employer companies to purchase Brickworks Limited ordinary shares from new issues of shares by Brickworks Limited or from the Australian Stock Exchange (ASX). The shares will be registered in the name of CPU and held for the benefit of participants.

15. Shares will be notionally allocated, as a beneficial interest, to participants and CPU will ensure that each participant is notified in writing when ordinary shares are acquired and allocated to them. CPU will keep proper books and records of the ordinary shares allocated to each participant and provide a statement of account at least annually to each participant.

16. CPU will not hold fractions of shares for the benefit of participants. Amounts remaining after share purchases will be notionally carried forward on each participant's behalf to be used for future share purchases. Dividends paid by Brickworks Limited on shares held by CPU from year to year will be distributed to participants with reference to the number of shares notionally

allocated to them at the time that dividends are declared and paid. Dividends cannot be reinvested under the Plan.

17. The participant's beneficial interest in the shares is subject to:

- restrictions (shares must be held by CPU until at least 30 June after allocation, unless the participant ceases employment with the Brickworks Group before that date);
- the satisfaction of any relevant requirements (relevant requirements are minimum service periods and performance criteria); and
- forfeiture where the participant has committed an act of gross misconduct, theft or defalcation, or where the relevant requirements have not been satisfied and the participating employee is no longer an employee of the Brickworks Group.

18. Participants wishing to withdraw share benefits from the DESP must seek permission from the Brickworks Limited Board by completing and lodging with the Plan Trustee a Notice of Withdrawal of shares before a distribution can be made. The share benefits identified for withdrawal will be examined together with underlying service and performance criteria and any other restrictions affecting a distribution. If permission is granted, the shares will be transferred to the participating employee or sold on the participant's behalf by CPU.

19. At no time will a participating employee hold a legal or beneficial interest in more than 5% of the shares of Brickworks Limited. Also at no time will a participating employee be in a position to cast or control the casting of more than 5% of the maximum number of votes at a general meeting of Brickworks Limited.

## **Ruling**

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### **Where the participating employee does not make an election under section 139E**

20. Where a participating employee acquires shares under the Plan and does not make an election under section 139E, the amount of the discount on the shares will be included in assessable income in the year of income in which the cessation time occurs, pursuant to subsection 139B(3).

21. As there are restrictions and forfeiture conditions on the shares acquired under the Plan, the cessation time is determined under subsection 139CA(2).

22. In accordance with subsection 139CA(2), the cessation time for a share acquired by a participant under the Plan, will be the earliest of:

- The time when the taxpayer disposes of the share;
- The time when the Brickworks Limited Board has approved giving effect to a Notice of Withdrawal of the shares from the Plan by the participant; or
- The time when the participant ceases to be employed by a company in the Brickworks Group; or
- 10 years from when CPU notionally allocates the share to the participant.

23. Where the participating employee subsequently disposes of the shares in an arm's length transaction at the cessation time or within 30 days of the cessation time, the discount included in assessable income at the cessation time under subsection 139B(3) is calculated in accordance with subsection 139CC(3). The discount is the consideration received by the participating employee for the disposal of the shares.

24. Any capital gain or loss made as a consequence of such a disposal is disregarded pursuant to subsection 130-83(2).

25. Where the participating employee does not subsequently dispose of the shares in an arm's length transaction within 30 days of the cessation time, the discount included in assessable income at the cessation time under subsection 139B(3) is calculated in accordance with subsection 139CC(4). The discount is the market value of the shares at cessation time. The market value of the shares is worked out under section 139FA.

26. The first element of the cost base of such shares upon a capital gains tax (CGT) event happening is their market value at the cessation time pursuant to subsection 130-83(3).

27. Where an employee acquires shares under the DESP and does not make an election under section 139E in respect thereof, and the shares are subsequently forfeited under the Plan's rules, no amount is included in assessable income under subsection 139B(3) and there are no CGT consequences.

## **Where a participating employee makes an election under section 139E**

28. Where a participating employee acquires shares under the Plan and makes an election under section 139E, the discount on the shares is included in that employee's assessable income in the year of income in which the shares are acquired pursuant to subsection 139B(2). This

will be the year of income in which CPU allocates the shares to the participating employee.

29. The discount will be calculated in accordance with subsection 139CC(2). The amount of discount to be included in the participant's assessable income is the market value of each share at the time that it was allocated to the participant by CPU. The market value of a share at this time is determined under section 139FA.

30. As the Plan Rules do not satisfy the exemption conditions in section 139CE, subsection 139BA(2) does **not** apply to reduce the discount included in assessable income by up to \$1,000.

31. The first element of the cost base of the shares for the purposes of the capital gains tax provisions is determined in accordance with section 130-80. No advice is provided on the operation of this provision as it is currently subject to a retrospective legislative amendment contained in *Taxation Laws Amendment Bill (No. 8) of 2002*.

32. Where a participating employee acquires shares under the Plan, makes an election under section 139E and the shares are subsequently forfeited under the Plan Rules, the amount of the discount on the shares is included in assessable income under subsection 139B(2) as outlined above in paragraphs 28 and 29 above.

## **Explanation**

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### **Employee share schemes**

33. Where, as under this arrangement, a participant acquires a beneficial interest in a share under an effective salary sacrifice arrangement within the meaning given in *Taxation Ruling* TR 2001/10, there is an acquisition of a share for the purposes of Division 13A.

34. In this regard, section 139G provides that a person acquires a share in several circumstances, including by acquiring a beneficial interest in the share, or having a share allotted to them by another person.

35. Clause 4.7 of the DESP Trust Deed makes it clear that the participating employee acquires a beneficial interest in a share at the time the share is acquired under the Plan by CPU for the benefit of the participant. For the purposes of Division 13A, the participating employee acquires a share when it is allocated to him or her by CPU.

36. For Division 13A to apply, the beneficial interest in the share must be acquired under an employee share scheme. Subsection 139C(1) provides that a share is acquired under an employee share



scheme if the share is acquired in respect of, or in relation directly or indirectly to, any employment of the taxpayer (that is, of the participant).

37. Subsection 139C(3) provides that a share is not acquired under an employee share scheme unless it is acquired for less than its market value. This condition is satisfied under the Plan as the participant is not required to make any payment for the allocation of the shares.

38. A participant will therefore acquire shares under an *employee share scheme* within the meaning given by section 139C, as the shares will be acquired by that employee for less than market value and in respect of or in relation to their employment.

39. The discount given in relation to the acquisition is included in assessable income in accordance with section 139B. It is included in the income year in which the share is acquired where an election under section 139E is made by the participant (subsection 139B(2)) or, where no such election is made, in the income year in which the cessation time occurs (subsection 139B(3)).

40. In so far as the acquisition of shares under the Plan is concerned, the time at which the income is included in the participant's assessable income depends on two material factors. The first is whether the shares are 'qualifying shares' within the meaning of that term in section 139CD. The second is whether the taxpayer has made an election under section 139E to include the discount in assessable income in the year that the shares are acquired by him or her.

41. It is accepted that having regard to the conditions under section 139CD the shares acquired by participants in the Plan are qualifying shares.

#### **Where the participating employee does not make a section 139E election.**

42. Where a participating employee has not made an election under section 139E and as the shares are qualifying shares, the discount in relation to the shares is included in assessable income, pursuant to subsection 139B(3), in the year of income in which the cessation time occurs. As the shares are subject to forfeiture and there are restrictions preventing the participating employee from disposing of the shares, the cessation time is determined pursuant to subsection 139CA(2).

43. Under the plan the cessation time for a share acquired by a participant is the earliest of:

- the taxpayer disposes of the share;

- the later of the time when the disposal restrictions cease and the forfeiture conditions expire in relation to the share acquired by the participant. This will be when the Brickworks Ltd Board has approved the Notice of Withdrawal of the participant's share from the Plan;
- the time when the participant ceases to be employed by a company in the Brickworks Group; and
- 10 years after CPU allocates the share to the participant.

44. Where the shares are disposed of by the participating employee in an arms length transaction within 30 days of the cessation time, the discount included in assessable income is calculated pursuant to subsection 139CC(3). As the participating employee has given no consideration for the acquisition of the shares, the amount or value of any consideration received from the disposal will be included in the participating employee's assessable income.

45. As the shares are qualifying shares and no election was made under section 139E in the year of income that the share was acquired, any capital gain or loss made on the disposal, outlined above, will be disregarded in accordance with subsection 130-83(2).

46. A participating employee who does not dispose of the shares in an arm's length transaction at the cessation time or within 30 days of the cessation time will include the discount in their assessable income. The discount is calculated in accordance with subsection 139CC(4). The discount is the market value of the shares at cessation time as no consideration was paid by the participating employee to acquire the shares.

47. The ordinary shares in Brickworks Limited are listed on the Australian Stock Exchange (ASX), which is an approved stock exchange. The market value of the shares for the purposes of paragraph (a) of subsection 139CC(4) is determined in accordance with section 139FA. Section 139FA provides that the market value is:

- if there was at least one transaction on the ASX in Brickworks Limited shares in the week up to and including the valuation date - the weighted average of the prices at which those shares were traded during that week; or
- if there were no transactions in Brickworks Limited shares on the ASX in the period - the last offered price on the ASX for Brickworks Limited shares, or if no such offer was made, the value as determined under section 139FB.

48. The cost base of the shares for the purposes of the CGT provisions is determined in accordance with subsection 130-83(3), the first element being the market value of the shares worked out under section 139FA at cessation time. This is the market value determined in paragraph 47.

49. Where a participating employee acquires shares under the Plan which are subsequently forfeited under the Plan rules, the discount to be included in assessable income pursuant to subsection 139B(3) will be nil. As the Plan rules apply equally to all participating employees, the forfeiture is considered to be arm's length for the purposes of subsection 139CC(3). As the participating employee will receive no consideration upon forfeiture of the shares, nor paid anything for them, the discount calculated in accordance with subsection 139CC(3) is nil.

50. Likewise, the forfeiture of shares will have no CGT consequences because there will have been no acquisition of those shares by the employee as required by section 130-80. Pursuant to the rules for CGT event E5 in section 109-5 and section 104-75, the employee will not have acquired the shares because he or she did not become absolutely entitled to them.

#### **Where a participating employee makes a section 139E election**

51. A participating employee can elect under section 139E that subsection 139B(2) applies for a year of income. Subsection 139B(2) includes the discount in assessable income in the year of income in which the share was acquired.

52. An election under section 139E must be made in writing in a form approved by the Commissioner, before the taxpayer lodges his or her return of income for the year of income or within such further time as the Commissioner allows. Taxpayers should not forward their section 139E elections to the Australian Taxation Office unless specifically requested to do so. (See paragraph 3 of *Taxation Determination TD 97/23*.)

53. Where an election is made by a participating employee under section 139E for a year of income, the discount given on all the qualifying shares or rights acquired is included in the participant's assessable income in the income year of acquisition.

54. The discount is calculated in accordance with subsection 139CC(2). The discount is the market value of the share, as determined by section 139FA (see paragraph 47), at the time it was acquired by the participant as no consideration was provided for the acquisition of the share by the participant.

55. Section 139CE contains three exemption conditions that must be satisfied by the Plan for the participating employees to have access to the \$1,000 tax free threshold provided for in subsection 139BA(2). The Plan does not satisfy these exemption conditions as it:

- contains conditions which could result in participating employees forfeiting ownership of shares that were acquired under the Plan - thus failing to satisfy subsection 139CE(2);
- permits participating employees to dispose of shares acquired under the Plan within three years of their acquisition - thus failing to satisfy subsection 139CE(3); and
- is not operated on a non discriminatory basis, as specified under subsection 139GF, because it permits the making of special discretionary offers of shares to select employees - thus failing subsection 139CE(4).

As the Plan does not satisfy all the exemption conditions in section 139CE, subsection 139BA(2) will not apply to reduce the discount to be included in the participant's assessable income by \$1,000.

56. This discount is still included in assessable income even where in a subsequent year of income the shares are forfeited under the rules of the Plan.

57. The first element of the cost base of the shares for the purposes of the CGT provisions is determined in accordance with section 130-80. No advice is provided on the operation of this provision as it is currently subject to retrospective amendment contained in *Taxation Laws Amendment Bill No. 8 of 2002*.

## **Detailed contents list**

58. Below is a detailed contents list for this Class Ruling:

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**Commissioner of Taxation**9 July 2003

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	- ITAA 1936 139CC
<i>Previous draft:</i>	- ITAA 1936 139CC(2)
Not previously issued in draft form	- ITAA 1936 139CC(3)
	- ITAA 1936 139CC(4)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 139CD
TR 92/1; TR 92/20; TR 97/16;	- ITAA 1936 139CE
TD 97/23; TR 2001/10; CR 2001/1	- ITAA 1936 139CE(2)
	- ITAA 1936 139CE(3)
	- ITAA 1936 139CE(4)
<i>Subject references:</i>	- ITAA 1936 139E
- employee share schemes	- ITAA 1936 139FA
	- ITAA 1936 139FB
<i>Legislative references:</i>	- ITAA 1936 139G
- ITAA 1936 Div 13A	- ITAA 1936 139GF
- ITAA 1936 139B	- ITAA 1997 6-5
- ITAA 1936 139B(2)	- ITAA 1997 104-75
- ITAA 1936 139B(3)	- ITAA 1997 109-5
- ITAA 1936 139BA	- ITAA 1997 130-80
- ITAA 1936 139BA(2)	- ITAA 1997 130-83
- ITAA 1936 139C	- ITAA 1997 130-83(2)
- ITAA 1936 139C(1)	- ITAA 1997 130-83(3)
- ITAA 1936 139C(3)	- Copyright Act 1968
- ITAA 1936 139CA	- TAA 1953 Pt IVAAA
- ITAA 1936 139CA(2)	

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ATO References

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