



TD 2014/D16 - Income tax: where a right to acquire a beneficial interest in a share is granted subject to shareholder approval, is the right an 'indeterminate right' within the meaning of subsection 83A-340(1) of the Income Tax Assessment Act 1997 ?

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This document has been finalised by TD 2014/21.

 There is a Compendium for this document: **TD 2014/21EC** .



Draft Taxation Determination

Income tax: where a right to acquire a beneficial interest in a share is granted subject to shareholder approval, is the right an ‘indeterminate right’ within the meaning of subsection 83A-340(1) of the *Income Tax Assessment Act 1997*?

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This publication is a draft for public comment. It represents the Commissioner’s preliminary view about the way in which a relevant taxation 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.

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Ruling

1. No. Where a right to acquire a beneficial interest in a share is granted subject to shareholder approval and the employee acquires only a right to have the matter put to the shareholders and nothing more, that right is not an ‘indeterminate right’ within the meaning of subsection 83A-340(1) of the *Income Tax Assessment Act 1997* (ITAA 1997).
2. For the avoidance of doubt, prior to shareholder approval being given, such a right is not an ESS interest within the meaning of subsection 83A-10(1) of the ITAA 1997, as it is not yet a right to acquire a beneficial interest in a share.
3. This ruling also applies for the purposes of section 83A-15 of the *Income Tax (Transitional Provisions) Act 1997* (ITTPA)

TD 2014/D16

Date of effect

4. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will not apply to employees to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 to 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation

24 September 2014

Appendix 1 – Explanation

① *This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.*

Explanation

5. An indeterminate right under subsection 83A-340(1) of the ITAA 1997 is a right an employee acquires that later becomes a right to acquire a beneficial interest in a share. Subsection 83A-340(1) of ITAA 1997 includes two examples:

Example 1:

You acquire a right to acquire, at a future time:

- (a) shares with a specified value, rather than a specified number of shares; or
- (b) an indeterminate number of shares.

Example 2:

You acquire a right under which the provider must provide you with either ESS interests or cash, whichever the provider chooses.

6. Subsection 83A-340(2) of the ITAA 1997 provides that Division 83A of the ITAA applies to such a right 'as if the right had always been a right to acquire a beneficial interest in a share'.

7. In the examples in subsection 83A-340(1) of the ITAA 1997, the original right is a right to receive property but the precise extent or nature of that property is yet to be determined at the time the original right is acquired. Such a right is capable of becoming a right to acquire a beneficial interest in a share because inherent in it is the capacity to acquire property. It remains to be determined whether the right ultimately becomes a right to acquire a specific number of shares or some other form of property, such as cash.

8. For a right to be an indeterminate right it must be appropriate for Division 83A of the ITAA 1997 to apply to it at the time it was granted. Difficulty in determining how a right might be valued may indicate that it is not a right to which Division 83A of the ITAA applies and therefore is not an indeterminate right. In *FC of T v. McWilliam* [2012] FCAFC 105; (2012) 204 FCR 478; 2012 ATC 20-339 the Full Federal Court implies at paragraph [84] that the ability to value a right pointed to whether it was a right to acquire a share for the purposes of former Division 13A of Part III of the *Income Tax Assessment Act 1936* (Division 13A of the ITAA 1936). Given the similarity in the structure and objects of Division 83A of the ITAA 1997 and former Division 13A of the ITAA 1936, the same conclusion can be applied also to Division 83A.

9. A right to acquire the beneficial interest in a share granted subject to shareholder approval is not a right to receive property where, in the absence of approval, the employee is not entitled to receive any benefit. For example, in *Fowler v. FC of T* [2012] FCA 1040; 2012 ATC 20-351 (a decision in relation to Division 13A of the ITAA 1936), Kenny J held at first instance that it was open to the shareholders to deny approval of the option issue to the employee. Her Honour stated at [54]:

It is only when the option-holder is in fact able to exercise the contractual right inherent in an option to acquire the shares that the option-holder can be said to have acquired the option. This cannot occur until the option is granted or 'vested'.

10. Kenny J's decision was affirmed by the Full Federal Court in *Fowler v. FC of T* [2013] FCAFC 69; (2013) 212 FCR 149; 2013 ATC 20-398. In the reasons of the Full Federal Court at paragraph [94], Besanko J, with whom Dodds-Streeton J agreed at paragraph [163], described the employee's right prior to shareholder approval as 'a right that may have led to the acquisition of a right to acquire shares, but... not a right to acquire shares.' At paragraph [156] Gordon J stated that, prior to shareholder approval, 'Mr Fowler merely had the right to insist that Nexus put the issue of Options to him to its shareholders for their approval.'

11. In view of the findings of the Court, the right Mr Fowler held under the contract prior to gaining shareholder approval was a right that came to an end when shareholder approval was granted. It was the shareholder approval, rather than the original right, that produced the employee's rights to acquire shares in his employer company for the purposes of former Division 13A of the ITAA 1936.

12. Applying this analysis to indeterminate rights under section 83A-340 of the ITAA 1997, where an employee acquires a right subject to shareholder approval and that right is only a right to have the matter put to the shareholders and nothing more, the right is not a right that later *becomes* a right to acquire a beneficial interest in a share. Rather, it is the shareholder approval that produces a (new) right in the employee to acquire the beneficial interest in a share. The original right to have the matter put to the shareholders does not have inherent in it the capacity to acquire property. It is not capable of *becoming* a right to acquire a beneficial interest in a share. It is therefore not an indeterminate right within the meaning of section 83A-340 of the ITAA 1997.

13. This view is consistent with the view of the Commissioner that, where an employee is granted a right but the ultimate provision of a benefit is subject to the discretion of the employer, that right is not a right to acquire the beneficial interest in a share for the purposes of former Division 13A of the ITAA 1936 or of Division 83A of the ITAA 1997 until such time as the discretion ceases to apply or is exercised in the employee's favour.¹

14. Section 83A-15 of the ITTPA applies to a right acquired before 1 July 2009 that, on or after 1 July 2009, becomes a right to acquire a beneficial interest in a share. The section provides that Division 13A of the ITAA 1936 is taken to have applied as if such a right had always been a right to acquire the beneficial interest in the share.

15. For the reasons given above, where before 1 July 2009 an employee acquired a right that was subject to shareholder approval and the right was only to have the matter put to the shareholders and nothing more, that right will not be an indeterminate right for the purposes of section 83A-15 of the ITTPA.

Note: where a right is granted subject to shareholder approval on terms providing that if shareholder approval is not obtained the employee will receive an amount of cash as compensation, the right is a right to receive property and would be an indeterminate right within the meaning of section 83A-340 of the ITAA 1997. Where cash compensation is nominal or disproportionately small, it is necessary to consider whether that cash compensation truly relates to the grant or whether the general anti-avoidance provisions in Part IVA of the ITAA 1936 apply.

¹ Class Ruling CR 2006/101 *Income tax: BHP Billiton Limited – Employee Long Term Incentive Plan*, pars 24; 30-2 (in relation to former Division 13A of the ITAA1936); Class Ruling CR 2011/19 *Income tax: Barclays PLC Share Award Schemes*, pars 42; 55-57 (in relation to Division 83A of the ITAA 1997).

Appendix 2 – Your comments

16. You are invited to comment on this draft Determination. Please forward your comments to the contact officer by the due date.

A compendium of comments is prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments
- be published on the ATO website at www.ato.gov.au.

Please advise if you do not want your comments included in the edited version of the compendium.

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References

Previous draft:

Not previously issued as a draft

- ITAA 1997 Div 83A
- IT(TP)A 1997 83A-15

Related Rulings/Determinations:

TR 2006/10; CR 2006/101; CR 2011/19

Subject references:

- employee share schemes
- indeterminate rights

Legislative references:

- ITAA 1936 Pt III Div 13A
- ITAA 1997 83A-340
- ITAA 1997 83A-340(1)
- ITAA 1997 83A-340(2)

Case references:

- Fowler v. Federal Commissioner of Taxation [2013] FCAFC 69; (2013) 212 FCR 149; 2013 ATC 20-398
- Fowler v. Federal Commissioner of Taxation [2012] FCA 1040; 2012 ATC 20-351
- Federal Commissioner of Taxation v. McWilliam [2012] FCAFC 105; (2012) 204 FCR 478; 2012 ATC 20-339

ATO references

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