


TD 2022/8 - Income tax: deductibility of expenses incurred in establishing and administering an employee share scheme

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Status: **legally binding**

Taxation Determination

Income tax: deductibility of expenses incurred in establishing and administering an employee share scheme

📌 Relying on this Determination

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

If this Determination applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Determination. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Determination.

Table of Contents	Paragraph
What this Determination is about	1
Ruling	4
<i>Establishment expenses</i>	4
<i>Amendment expenses</i>	7
<i>Ongoing expenses</i>	10
Date of effect	12
Appendix – Explanation	13
Not deductible under section 8-1 as capital or of a capital nature	13
Deductible under section 40-880	24
Ongoing expenses	30

What this Determination is about

1. An employer company may incur expenses in establishing and administering an employee share scheme¹ (ESS) as part of its remuneration strategy. This expenditure often includes establishing and administering an employee share trust² (EST) that holds shares or rights for employees participating in the ESS.
2. This Determination sets out the Commissioner's views on the deductibility of these expenses.
3. All legislative references in this Determination are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

¹ Has the meaning given by subsection 83A-10(2) of the *Income Tax Assessment Act 1997*.

² As defined in subsection 130-85(4) of the *Income Tax Assessment Act 1997*. See also Taxation Determination TD 2019/13 *Income tax: what is an 'employee share trust'?*

Status: **legally binding**

Ruling

Establishment expenses

4. Establishment expenses are not deductible to the employer company under section 8-1 because they are capital in nature.
5. Establishment expenses are deductible to the employer company in equal proportions over five years under section 40-880 to the extent that the business is carried on for a taxable purpose.
6. Establishment expenses are outgoings associated with the creation of an ESS and include:
 - legal fees incurred in establishing the EST and ESS plan rules
 - start-up costs; for example, trustee company commencement charges, and
 - registration fees with various authorities; for example, stamp duty and Australian Securities & Investments Commission fees.

Amendment expenses

7. Expenses incurred amending an ESS are not deductible to the employer company under section 8-1 because they are capital in nature.
8. Expenses incurred amending an ESS are deductible to the employer company in equal proportions over five years under section 40-880 to the extent that the business is carried on for a taxable purpose.
9. Examples of expenses that would be incurred amending an ESS include:
 - legal fees paid amending the EST and ESS plan rules, and
 - regulatory fees and stamp duty paid to authorities.

Ongoing expenses

10. Ongoing expenses associated with the administration of an ESS are deductible under section 8-1.
11. Examples of ongoing expenses include:
 - brokerage fees
 - audit fees
 - bank charges
 - making new offers to employees under an existing ESS, and
 - other ongoing administrative expenses.

Status: **legally binding**

Date of effect

12. This Determination applies both before and after its date of issue. However, this Determination will 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 this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10 *Public Rulings*).

Commissioner of Taxation

6 April 2022

Status: **not legally binding**

Appendix – Explanation

❶ ***This Explanation 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.***

Not deductible under section 8-1 as capital or of a capital nature

13. An expense is capital or of a capital nature if it relates to the business entity, structure or organisation established for the earning of profit as opposed to the process by which the organisation operates to obtain its income.³

14. In *Sun Newspapers*, Dixon J outlined three matters to be considered for determining whether an expense is capital or revenue in nature (emphasis added):

There are, I think, three matters to be considered, (a) **the character of the advantage sought**, and in this its lasting qualities may play a part, (b) **the manner in which it is to be used, relied upon or enjoyed**, and in this and under the former head recurrence may play its part, and (c) **the means adopted to obtain it**; that is, by providing a periodical reward or outlay to cover its use or enjoyment for periods commensurate with the payment or by making a final provision or payment so as to secure future use or enjoyment.

15. In *GP International Pipecoaters Pty Ltd v Commissioner of Taxation (Cth)*⁴, the High Court stated:

The character of expenditure is ordinarily determined by reference to the nature of the asset acquired or the liability discharged by the making of the expenditure, for the character of the advantage sought by the making of the expenditure is the chief, if not the critical, factor in determining the character of what is paid ...

16. An ESS sets up a strategy to remunerate employees to reward, motivate and retain staff while linking some of their personal remuneration to shareholder wealth creation.⁵

17. The ESS adds to the business structure of the employer company and is established to deliver benefits to its employees.

18. The establishment expenses are one-off in nature and used in setting up the ESS as part of the employer company's remuneration structure. The character of the advantage sought is the enduring benefit of having the ESS in its business structure to deliver ESS interests.

19. In working out whether an expense is capital in nature, there is also a need to identify a counterfactual. The High Court in *Commissioner of Taxation v Sharpcan Pty Ltd*⁶ opined that (emphasis added):

... specifically, whether the outgoing is calculated to effect the acquisition of an enduring advantage to the business. And the identification of what (if anything) is to be acquired by an outgoing ultimately requires a counterfactual, not an historical, analysis: specifically, **a comparison of the expected structure of the business after the outgoing with the expected structure but for the outgoing**, not with the structure *before* the outgoing.

³ *Sun Newspapers Limited v Federal Commissioner of Taxation* [1938] HCA 73 (*Sun Newspapers*).

⁴ [1990] HCA 25.

⁵ Paragraph 1.26 of the Explanatory Memorandum to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009 states:

Tax support is provided on the grounds that aligning the interests of employees and employers encourages positive working relationships, boosts productivity through greater employee involvement in the business, reduces staff turnover and encourages good corporate governance.

⁶ [2019] HCA 36 at [33].

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20. In comparing the business structure after the payment of establishment expenses with the expected structure but for the expense, an employer company would not have been able to offer its employees an ESS interest.

21. Therefore, the expense is capital or of a capital nature as it has an enduring benefit to the employer company. The purpose of setting up the ESS (being a one-off)⁷ was for it to be part of the employer company's business structure. Therefore, these expenses are capital or of a capital nature.

22. Further, any expense to amend the ESS is similarly of a capital nature.

23. Therefore, subsection 8-1(2) is satisfied and these expenses are not deductible under section 8-1.

Deductible under section 40-880

24. Broadly, section 40-880 allows deductions for certain business capital expenditure that fall outside the scope of the deduction provisions of the income tax law. It requires the expenditure to be capital and in relation to the business.⁸

25. As this expenditure relates to remuneration of employees of the employer company who work within that business, the expenditure must be incurred in relation to that business.

26. Section 40-880 contains limitations and exceptions in subsections 40-880(3) to (9) which may prevent a deduction being allowed.

27. Subsection 40-880(3) indicates that the expenditure is only deductible to the extent that the business is carried on is for a taxable purpose.

28. The other limitations and exceptions in subsections 40-880(4) to (9) do not prevent establishment expenses from being deductible under section 40-880.

29. Therefore, establishment expenses are deductible in equal proportions over five years under section 40-880 to the employer company to the extent that the business carried on is for a taxable purpose.⁹

Ongoing expenses

30. Ongoing expenses to administer and operate an ESS are regular and recurrent. They do not add to the business structure of the employer company nor are they one-off in nature.

31. Therefore, ongoing expenses are deductible under section 8-1.

⁷ *AusNet Transmission Group Pty Ltd v Federal Commissioner of Taxation* [2015] HCA 25 at [17]; *Commissioner of Taxation v Healius Ltd* [2020] FCAFC 173 at [57].

⁸ See Taxation Ruling TR 2011/6 *Income tax: business related capital expenditure – section 40-880 of the Income Tax Assessment Act 1997 core issues*.

⁹ Pursuant to subsection 995-1(1), 'taxable purpose' is defined in section 40-25.

Status: **not legally binding**

References

Previous draft:

TD 2022/D2

Related Rulings/Determinations:

TR 2006/10; TR 2011/6; TD 2019/13

Legislative references:

- ITAA 1997 8-1
- ITAA 1997 8-1(2)
- ITAA 1997 40-25
- ITAA 1997 40-880
- ITAA 1997 40-880(3)
- ITAA 1997 40-880(4)
- ITAA 1997 40-880(5)
- ITAA 1997 40-880(6)
- ITAA 1997 40-880(7)
- ITAA 1997 40-880(8)
- ITAA 1997 40-880(9)
- ITAA 1997 Div 83A
- ITAA 1997 83A-10(1)
- ITAA 1997 83A-10(2)
- ITAA 1997 130-85(4)
- ITAA 1997 995-1(1)
- TAA 1953

Cases relied on:

- AusNet Transmission Group Pty Ltd v Federal Commissioner of Taxation [2015] HCA 25; 255 CLR 439; 2015 ATC 20-521; 99 ATR 816
- Commissioner of Taxation v Healius Ltd [2020] FCAFC 173; 2020 ATC 20-766; 384 ALR 408; 112 ATR 306
- Commissioner of Taxation v Sharpcan Pty Ltd [2019] HCA 36; 2019 ATC 20-715
- GP International Pipecoaters Pty Ltd v Commissioner of Taxation (Cth) [1990] HCA 25; 170 CLR 124; 90 ATC 4413; 21 ATR 1
- Sun Newspapers Limited v Federal Commissioner of Taxation [1938] HCA 73; 61 CLR 337; 5 ATD 87

Other references:

- [Explanatory Memorandum](#) to the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009

ATO references

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