


# ***CR 2003/67 - Income tax: Centennial Coal Company Limited - Exempt Employee Share Plan***

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## **Class Ruling**

### **Income tax: Centennial Coal Company Limited - Exempt 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**

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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 1936* (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;
- 130-80 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- 130-83 of the ITAA 1997.

**Note: On December 5th 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 all the Australian resident employees ('participating employees') of Centennial Coal Company Limited and all its associated companies (The Centennial Coal Group) who participate in the Centennial Coal Company Limited Exempt Employee Share Plan ('the Plan') as described in the arrangement part of this Ruling. The Centennial Coal Group comprises:

- Airly Coal Pty Limited;
- Berrima Coal Pty Limited;
- Centennial Angus Place Pty Limited;
- Centennial Fassifern Pty Limited;
- Centennial Hunter Pty Limited;
- Centennial Mandalong Pty Limited;
- Centennial Munmorah Pty Limited;
- Centennial Myuna Pty Limited;
- Centennial Newstan Pty Limited;
- Centennial Springvale Pty Limited;
- Centennial Springvale Holdings Pty Limited;
- Centennial Wyee Pty Limited;
- Charbon Coal Pty Limited;
- Clarence Coal Investments Pty Limited;
- Clarence Colliery Pty Limited;
- Clarence Coal Pty Limited;
- Coalex Pty Limited;
- Collieries Superannuation Pty Limited;
- Cook Coal Holdings Pty Limited;
- Elcom Collieries Pty Limited;

- Hartley Valley Coal Company Pty Limited;
- Huntley Colliery Pty Limited;
- Ivanhoe Coal Pty Limited;
- Japan Energy (Australia) Pty Limited;
- Mandalong Pastoral Management Pty Limited;
- Powercoal Pty Limited;
- Powercoal Employee Entitlements Company Pty Limited;
- Powercoal Superannuation Pty Limited; and
- Preston Coal 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;
- It is not taken to be withdrawn by an inconsistent later Public Ruling; or
- The relevant taxation laws are not amended.

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## Arrangement

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9. The arrangement that is the subject of this Ruling is described below. This 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 11 November 2002;
- Centennial Coal Company Limited (ACN 003 714 538) Exempt Employee Share Plan Trust Deed; and
- Centennial Coal Company Limited (ACN 003 714 538) Exempt Employee Share 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 Plan was established as part of the employee share plan strategy of the Centennial Coal Group. The Centennial Coal Group is the companies listed at paragraph 3. The initial offer to acquire shares under the Plan was made to all Australian resident permanent full-time and permanent part-time employees and directors of the Centennial Coal Group at 1 October 2002. Subsequent offers may be made each year at the discretion of the Board, in accordance with schedule 1 of the Plan Trust Deed.

11. Under the Plan the purchase of Centennial Coal Company Limited ordinary shares is funded by way of an effective salary sacrifice arrangement within the meaning of paragraphs 19 to 23 of Taxation Ruling TR 2001/10. Participating employees are not required to contribute any other funds to acquire the shares.

12. All offers to acquire shares under the Plan will be made on a non-discriminatory basis. No financial assistance in respect of the acquisition of the shares will be provided to participating employees.

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 Centennial Coal Company Limited ordinary shares and to provide such ordinary shares to participating employees of the Centennial Coal Group. In this regard any income or property to which a beneficiary is not presently entitled cannot be used for the administration of the Plan. The Centennial Coal Group will meet the brokerage fees on share purchases, along with all other share plan expenses, costs and charges incurred by the Plan Trustee. Participating employees will only be responsible for costs in relation to selling or transferring any shares.

14. The Plan Trustee uses the funds it receives from the Centennial Coal Group companies to purchase Centennial Coal Company Limited ordinary shares from new issues of shares by Centennial Coal Company Limited, from participating employees who have withdrawn shares from the Plan and wish to sell them or from dealings through the Australian Stock Exchange (ASX). The shares so acquired are registered in the name of CPU.

15. Under the Plan shares are notionally allocated, as a beneficial interest, to the participating employees. The Plan Trustee notifies each participating employee in writing when ordinary shares are acquired and allocated to them, keeps proper books and records of their interest and provides them with an annual statement of account.

16. The Plan Trustee will not hold fractions of shares for the benefit of participating employees. Amounts remaining over from share purchases are notionally carried forward on the employee's behalf to be used for future share purchases. Dividends paid by Centennial Coal Company Limited on shares held by CPU are distributed to participating employees with reference to the total number of shares notionally allocated to them at the time that dividends are declared and paid. Dividends cannot be reinvested under the Plan.

17. Each participating employee's beneficial interest in the shares is:

- subject to a restriction (shares must be held by the Plan Trustee for three years from the date of their allocation to the participant, unless the employee ceases to be employed within the Centennial Coal Group before the three years has elapsed); and
- **not** subject to any conditions which would result in the forfeiture of any shares.

18. Participating employees wishing to withdraw share benefits from the Plan must give the Plan Trustee a Withdrawal Notice. Whilst an employee continues in employment with the Centennial Coal Group, this can only be done after three years from the date of allocation of the shares to them. This Withdrawal Notice can be in respect of some or all of the shares if the employee holds at least \$2,000 worth of Plan Shares. If the employee has less than \$2,000 worth of Plan Shares then the Withdrawal Notice must be for all the shares. If the participant ceases to be an employee of the Centennial Coal Group, including within the first three years of allocation of the shares to the participant, the participant must give the Plan Trustee a Withdrawal Notice for all the shares if they have at least \$2,000 worth of shares. Where an employee has less than \$2,000 worth of shares, or they have more than \$2,000 worth of shares but do not give the Plan Trustee a Withdrawal Notice within 30 days of ceasing to be an employee of the Centennial Coal Group, the Plan Trustee will sell the shares and distribute the proceeds to them.

19. At no time will a participating employee hold a legal or beneficial interest in more than 5% of the shares of Centennial Coal Company 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 Centennial Coal Company Limited.

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## **Ruling**

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

20. Where a participating employee makes an election pursuant to section 139E for the year of income in which they acquire shares under the Plan, the discount given in relation to the shares is included in their assessable income in the year of income in which the shares are acquired pursuant to subsection 139B(2). This is the year of income in which the Plan Trustee allocates the shares to the employee.

21. The discount is calculated in accordance with subsection 139CC(2). The amount of discount included in the participating employee's assessable income is the market value of each share at the time that it is allocated to them by the Plan Trustee. The market value of a share at this time is determined under section 139FA.

22. Provided that the Plan is operated in a manner that continues to satisfy the exemption conditions in section 139CE only the amount of discount in any one year of income in excess of \$1,000 is included in the participating employee's assessable income pursuant to subsection 139BA(2).

23. The first element of the cost base of the shares for the purposes of the capital gains tax (CGT) provisions is determined in accordance with section 130-80 of the ITAA 1997. No advice is provided on the operation of this provision as it is currently subject to a legislative amendment contained in *Taxation Laws Amendment Bill (No. 8) of 2002*.

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

24. Where a participating employee does not make an election under section 139E for the year of income in which they acquire shares under the Plan, the discount given in relation to the shares is included in their assessable income in the year of income in which the cessation time occurs, pursuant to subsection 139B(3).

25. As the shares acquired under the Plan are subject to restrictions preventing a participating employee from disposing of them before a particular time, the cessation time is determined pursuant to subsection 139CA(2). The cessation time for a share acquired under the Plan will be the earlier of:

- three years after the share is acquired by the participating employee; or
- the time when the participating employee ceases to be employed by a company in the Centennial Coal Group.

26. Where the participating employee 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 amount of consideration received by the employee for the disposal of the shares.

27. Any capital gain or loss made as a consequence of such a disposal is disregarded pursuant to subsection 130-83(2) of the ITAA 1997.



28. Where a 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 the cessation time. The market value of the share is worked out under section 139FA.

29. The first element of the cost base of such shares upon a CGT event happening is their market value at the cessation time pursuant to subsection 130-83(3) of the ITAA 1997.

## **Explanation**

### **Employee share schemes**

30. Where, as under this arrangement, a participating employee 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 under an employee share scheme for the purposes of Division 13A.

31. For the purposes of Division 13A, 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.

32. A participating employee acquires a share when it is allocated to them by the Plan Trustee in accordance with Clause 5.5 of the Exempt Employee Share Plan Trust Deed.

33. 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. This condition is satisfied with respect to shares acquired by participating employees under the Plan.

34. 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 participating employees are not required to make any payment for the allocation of the shares.

35. Therefore, participating employees acquire shares under an ***employee share scheme*** within the meaning in section 139C, as the shares are acquired by them for less than market value and in respect of or in relation to their employment.

36. Where a taxpayer acquires shares under an employee share scheme the discount given is included in assessable income in accordance with section 139B.

37. The time at which the income is included in the participating employee'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 employee has made an election under section 139E to include the discount in assessable income in the year that the shares are acquired.

38. A share is a qualifying share for the purposes of Division 13A if it meets the six conditions specified in section 139CD. Shares acquired under the Plan are qualifying shares because:

- they are acquired under an employee share scheme;
- the share is a share in a company that is the employer or the holding company of the employer of the participating employee;
- the shares are ordinary shares;
- at least 75% of the permanent employees of the employer have been eligible to acquire shares under the Plan;
- the restriction on ownership not exceeding 5% is complied with; and
- the restriction on voting power not exceeding 5% is complied with.

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

39. 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 is acquired.

40. An election under section 139E must be made in writing in a form approved by the Commissioner, before the taxpayer lodges their 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.)

41. 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 and qualifying rights acquired by them in that income year is included in their assessable income in the income year of acquisition.

42. The amount of the discount is calculated in accordance with subsection 139CC(2). As a participating employee does not provide any consideration for the acquisition of shares acquired under the Plan, the discount is the market value of each share, as determined by section 139FA, at the time it was acquired by the employee.

43. The ordinary shares in Centennial Coal Company Limited are listed on the Australian Stock Exchange ('ASX'), which is an approved stock exchange. Accordingly, the market value of the shares for the purposes of subsection 139CC(2), determined under section 139FA, is:

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

### ***\$1,000 tax-free threshold***

44. 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 exemption conditions are:

- the first condition is that the scheme does not contain any conditions which could result in an employee forfeiting ownership of any shares that were acquired under the Plan, subsection 139CE(2);
- the second condition is that the scheme is operated so that no employee is permitted to dispose of shares acquired under the Plan until the earlier of;
  - (a) three years after their acquisition; or
  - (b) the time when the employee is no longer employed by the company that was their employer at the time the shares were acquired,

unless the employee, on cessation of that employment is then employed by a member of the Centennial Coal Group, in which case, the time when they are no longer employed within the group, subsections 139CE(3) & (5); and

- the third condition is that the scheme is operated on a non discriminatory basis; subsection 139CE(4).

45. As the reference to 'the scheme' in subsections 139CE(2) to (4) is a reference to the mechanism by which the participating employees acquire qualifying shares, the exemption conditions must, initially, be satisfied at the time an offer of shares is made to employees. On the basis of the arrangement as described above, it is accepted that this is so. However, as the purpose of subsection 139CE(3) is to ensure that qualifying shares are held for the nominated period in order to access the concession in section 139BA, satisfaction of the conditions at the time of the offer, alone, is not enough. If, for instance, a subsidiary leaves the Centennial Coal Group taking with it employees who have shares under the Plan and as a result all or some of them are permitted to dispose of their shares, it will be necessary to reconsider whether the exemption conditions are still satisfied with respect to those shares.

46. For the exemption to be maintained, the Plan needs to continue to be operated in a manner that satisfies the exemption conditions. Subject to this necessary proviso, section 139BA applies to shares acquired under the Plan, so that where a section 139E election is made only the amount of the discount in excess of \$1,000 for the year of income is included in the participating employee's assessable income.

47. The first element of the cost base of the shares for the purposes of the CGT provisions will be determined in accordance with section 130-80 of the ITAA 1997. 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*.

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

48. Where a participating employee does not make an election under section 139E for the year of income in which the shares are acquired, the discount given in relation to the shares is included in the employee's assessable income in the year of income in which the cessation time occurs, pursuant to subsection 139B(3). The cessation time is determined under subsection 139CA(2) as the shares are subject to disposal restrictions.

49. According to subsection 139CA(2), the cessation time for a share acquired by a participating employee under the Plan will be the earliest of:

- the time when the Plan Trustee, on the employee's behalf, disposes of the share;
- the time when the disposal restrictions cease to have effect. Under the Plan rules the restriction period effectively ends three years after the employee acquires the share or when they cease to be employed by a company in the Centennial Coal Group, as from that date, they can lodge a Withdrawal Notice which must be complied with by the Plan Trustee;
- the time when the employment in respect of which the share was acquired ceases. This is the time when the employee is no longer employed by the company that was their employer at the time the shares were acquired, unless the employee, on cessation of that employment is then employed by a member of the Centennial Coal Group, in which case, the time when they are no longer employed within the group; and
- 10 years after the Plan Trustee allocated the share to the employee.

In light of the disposal restrictions and the procedures under the Plan concerning withdrawal from the Plan, the participating employee's cessation time for shares acquired under the Plan will be the earlier of the second and third abovementioned times.

***Disposal within 30 days of cessation time***

50. The amount of the discount included in assessable income is calculated under subsection 139CC(3) where the shares are disposed of by the participating employee in an arm's length transaction within 30 days of the cessation time. There being no consideration paid or given for the acquisition of the shares, the amount of the discount consists of the consideration received from the disposal of the shares.

51. 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, is disregarded in accordance with subsection 130-83(2) of the ITAA 1997.

***No disposal within 30 days of cessation time***

52. A participating employee who does not dispose of the shares in an arm's length transaction within 30 days of the cessation time includes in their assessable income the discount calculated in accordance with subsection 139CC(4). The amount of the discount is the market value of the shares at the cessation time as no consideration was paid or given by the employee to acquire the shares. The market value of the shares for the purposes of paragraph (a) of subsection 139CC(4) will be determined in accordance with section 139FA as outlined at paragraph 43.

53. The cost base of the shares for the purposes of the CGT provisions will be determined in accordance with subsection 130-83(3) of the ITAA 1997, the first element being the market value of the shares worked out under section 139FA at the cessation time. This is the market value determined in paragraph 43.

**Detailed contents list**

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

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**Commissioner of Taxation**

13 August 2003

<i>Previous draft:</i>	- ITAA 1936 139CC(2)
Not previously released 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; CR 2001/1; TR 2001/10	- ITAA 1936 139CE(2)
	- ITAA 1936 139CE(3)
	- ITAA 1936 139CE(4)
<i>Subject references:</i>	- ITAA 1936 139CE(5)
- Employee Share Schemes	- ITAA 1936 139E
	- ITAA 1936 139FA
<i>Legislative references:</i>	- ITAA 1936 139FB
- ITAA 1936 Div 13A	- ITAA 1936 139G
- ITAA 1936 139B	- ITAA 1997 130-80
- ITAA 1936 139B(2)	- ITAA 1997 130-80(2)
- ITAA 1936 139B(3)	- ITAA 1997 130-83
- ITAA 1936 139BA	- ITAA 1997 130-83(2)
- ITAA 1936 139BA(2)	- ITAA 1997 130-83(3)
- ITAA 1936 139C	- TAA 1953 Part IVAAA
- ITAA 1936 139C(1)	- Copyright Act 1968
- ITAA 1936 139C(3)	- Taxation Laws Amendment Bill
- ITAA 1936 139CA	(No.8) 2002
- ITAA 1936 139CA(2)	
- ITAA 1936 139CC	

## ATO references

NO: 2003/10152

ISSN: 1445-2014