



CR 2004/102 - Income tax: employee share scheme - Allocation Share Plan: NRMA Insurance Group Limited

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Class Ruling

Income tax: employee share scheme – Allocation Share Plan: NRMA Insurance Group Limited

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Preamble

*The number, subject heading, **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **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 tax law(s) dealt with in this Ruling are:

- section 97 of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 100 of the ITAA 1936;
- section 139B of the ITAA 1936;
- section 139BA of the ITAA 1936;
- section 139C of the ITAA 1936;
- section 139CA of the ITAA 1936;
- section 139CC of the ITAA 1936;
- section 139CD of the ITAA 1936;
- section 139E of the ITAA 1936;
- section 139FA of the ITAA 1936;
- section 139G of the ITAA 1936;
- subsection 139GB(1) of the ITAA 1936;
- section 160AQT of the ITAA 1936;

- section 160AQW of the ITAA 1936;
- section 160AQX of the ITAA 1936;
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 104-25 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- section 109-55 of the ITAA 1997;
- section 115-5 of the ITAA 1997;
- section 115-10 of the ITAA 1997;
- section 115-15 of the ITAA 1997;
- section 115-20 of the ITAA 1997;
- section 115-25 of the ITAA 1997;
- paragraph 115-100(a) of the ITAA 1997;
- section 116-30 of the ITAA 1997;
- section 130-80 of the ITAA 1997;
- section 130-83 of the ITAA 1997;
- subsection 207-40(2) of the ITAA 1997;
- subsection 207-45(1) of the ITAA 1997; and
- section 207-50 of the ITAA 1997.

Class of persons

3. The class of persons to whom this Ruling applies is all Australian resident employees of relevant subsidiaries of NRMA Insurance Group Limited (NIGL, now known as the Insurance Australian Group Limited), who participated in the NIGL Allocation Share Plan (the Plan) described in the Arrangement section of this Ruling. In this Ruling this class of persons is referred to as the 'Participating Employees'.

4. The relevant subsidiaries of NIGL are:

- NRMA Insurance Limited;
- Insurance Manufacturers of Australia Pty Limited;
- NRMA Financial Management Limited;
- NRMA Asset Management Limited;
- NRMA Building Society Limited; and
- NRMA Information Services Pty Limited.

5. This Ruling does **not** apply to a person who, immediately after first participating in the Plan, either holds a legal or beneficial interest in more than 5% of the shares in NIGL, or is in a position to cast or control the casting of more than 5% of the maximum number of votes that might be cast at a general meeting of NIGL.

Qualifications

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

7. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is carried out in accordance with the arrangement described in paragraphs 12 to 28.

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

- 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
- this Ruling may be withdrawn or modified.

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Date of effect

10. This Ruling applies to the year of income ended 30 June 2001. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of a settlement dispute agreed to before the date of this Ruling (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Withdrawal

11. This Ruling is withdrawn and ceases to have effect from 1 July 2001. The Ruling continues to apply, in respect of the tax laws ruled upon to all persons within the specified class who entered into the specified arrangement during the term of the Ruling. Thus the Ruling continues to apply to those persons, even following its withdrawal, for arrangements entered into prior to the withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

12. The arrangement that is the subject of the 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:

- Revised Application for Class Ruling for the Allocation Share Plan dated 24 April 2001 (the Application);
- NIGL Bonus Equity Share, Allocation Share, Equity Share, NED Share and Performance Award Rights Plans Trust Deed, executed 12 February 2001 (the Trust Deed);
- Terms of the Invitation for Allocation Shares (Terms of Invitation);
- Letter from the Applicant dated 22 August 2001; and
- Letter from the Applicant dated 29 August 2001.

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

Features of the Allocation Share Plan

The Plan

13. The Plan is an employee share scheme offered by NIGL, the ultimate holding company of the subsidiaries listed at paragraph 4 (the NRMA Insurance Group, now known as the Insurance Australia Group).

14. In general, all full-time and part-time employees of the NRMA Insurance Group with at least 3 months continuous service as at 9 March 2001 were invited to apply for Allocation Shares valued at

5% of their total salary by 5pm EST on that date. No other persons were entitled to receive shares under the Plan.

15. A Participating Employee was not liable to make any payment on acceptance of an offer for Allocation Shares.

Allocation Shares

16. The Trust Deed defines Allocation Shares to mean ordinary fully paid shares in the capital of NIGL and certain Bonus Shares. This Ruling does **not** cover the taxation treatment of any Bonus Shares issued in respect of Allocation Shares.

17. Allocation Shares are allocated under this Plan on the terms set out in the Terms of Invitation and the Trust Deed, including Schedule 2 thereof.

18. NRMA Insurance Limited has made capital contributions to the Trustee (NRMA Share Plan Nominee Pty Ltd, now known as IAG Share Plan Nominees Pty Ltd). The Trustee acquired NIGL shares, which were registered in the name of the Trustee on acquisition.

19. The Trustee allocated the shares acquired to the Participating Employees by crediting an account held for each. The Participating Employee acquired a beneficial interest in the Allocation Shares in their account.

20. While the shares are held on trust on behalf of the Participating Employee, dividends that accrue to the Allocation Shares are distributed to the Participating Employee.

21. The Application confirms that the Trust will be administered in a manner that ensures the sole activities of the Trust are to acquire shares and to provide such shares to employees of the NIGL Insurance Group. In this regard, any income or property to which a Participating Employee is not presently entitled will only be used for the administration of the employee share plan or for the purposes and operation of a successor employee share plan and powers in the Trust Deed that may permit the Trustee to do otherwise will not be so exercised.

The Restriction Period

22. The shares are held by the Trustee on behalf of the Participating Employee until a transfer or disposal is permitted under the Terms of Invitation and the Trust Deed. The date on which an employee may call for the shares or direct their disposal is governed in the main by the ending of the '**Restriction Period**'. The Restriction Period ends, on the earliest of:

- (a) the end of the day before the fifth anniversary of the allocation of the Share;
- (b) the day the Participating Employee is no longer employed by any of the following:

- (i) a member of the NRMA Insurance Group; or
- (ii) unless the Board of NIGL (the Board) otherwise determines, the employer of the Participating Employee at the date of allocation of the Allocation Shares; or
- (c) the day the Trustee notifies the Participating Employee that the Board has determined that an 'Event' (see paragraph 23) has occurred.

23. There are 5 'Events' which may end the Restriction Period. In general terms, these are:

- (a) a takeover bid being made to shareholders in NIGL;
- (b) a person acquiring 15 per cent or more of the voting rights in NIGL;
- (c) a court orders a meeting in relation to the reconstruction of NIGL or its amalgamation with any other company;
- (d) a resolution for the voluntary winding up of NIGL being passed; or
- (e) an order being made for the compulsory winding up of NIGL.

24. A Participating Employee suffering financial hardship may apply to the Board for an early release of Allocation Shares from the Trust. The Board may, in its absolute discretion, determine that the Shares be released.

25. With the exception of the Board's power to determine that an 'Event' has happened, or that the Participating Employee is suffering financial hardship, neither the Trustee nor the Board of NIGL has any discretion to release Allocation Shares before the end of the Restriction Period.

26. At the end of the Restriction Period, the Participating Employee has a period of 2 months in which to call upon the Trustee to transfer the Allocation Shares or to instruct the Trustee to sell the shares on their behalf. In the event that the necessary instructions are not given by the employee within the 2 month notice period, the Trustee is required to transfer the shares to the employee within a further month.

Forfeiture of the shares

27. Allocation Shares allocated to a Participating Employee will be forfeited to the Trustee if the Employee is no longer employed by any of the following before the second anniversary of the allocation:

- (i) a member of the NRMA Insurance Group; or
- (ii) unless the Board determines otherwise, the employer of the Participating Employee at the date of allocation of the Allocation Shares;

except for cessation caused by:

- (a) redundancy;
- (b) Retirement (at age 55 or over);
- (c) death; or
- (d) Total and Permanent Disablement as defined in the Trust Deed.

28. Allocation Shares allocated to a Participating Employee and held by the Trustee will be forfeited if the Participating Employee ceases to be employed due to serious misconduct involving dishonesty.

Ruling

[All legislative references are to the ITAA 1936 unless stated otherwise.]

Participating Employees who make an election under section 139E

Taxation of the discount

29. The discount given in relation to each Allocation Share acquired under the Plan is included in the Participating Employee's assessable income for the year of income during which the Trustee allocated the shares to the employee (subsection 139B(2) applies).

30. The amount of the discount to be included is the market value of each Allocation Share at the time that it was allocated to the Participating Employee by the Trustee (subsection 139CC(2) applies). The market value of an Allocation Share at this time is determined under section 139FA.

31. The amount included in assessable income is not subject to reduction under section 139BA.

Capital Gains Tax (CGT)

32. Where an Allocation Share is disposed of by, or on behalf of, the Participating Employee, a capital gain arises to the extent that the capital proceeds from the disposal exceed the cost base of the share. A capital loss occurs where the capital proceeds are less than the reduced cost base.

33. The first element of the cost base of an Allocation Share is the market value of the share at the time the Participating Employee acquired a beneficial interest in the share. The market value of the Allocation Share at this time is determined under section 139FA (refer subsection 130-80(3) of the ITAA 1997).

34. Where an Allocation Share is disposed of by, or on behalf of, the Participating Employee at least one year after the Participating Employee acquired a beneficial interest in the share, any gain on disposal will be a discount capital gain (section 115-5, section 109-55, and subsection 115-30(1) of the ITAA 1997 applies). The discount percentage for a discount capital gain is 50% (paragraph 115-100(a) of the ITAA 1997 applies).

Forfeiture

35. Where an Allocation Share is forfeited prior to the Participating Employee becoming absolutely entitled to it, no capital gain or loss will arise in relation to that share.

36. Where an Allocation Share is forfeited after the Participating Employee becoming absolutely entitled to it, a capital gain or capital loss may result. The capital proceeds in relation to the CGT event will be the market value of the Allocation Share at the time of forfeiture (section 116-30 of the ITAA 1997 applies). The first element of the cost base or reduced cost base will be the market value of the share as indicated at paragraph 33.

Participating Employees who do not make an election under section 139E***Taxation of the discount***

37. The discount given in relation to each Allocation Share acquired under the Plan is included in the Participating Employee's assessable income for the year of income in which the cessation time occurs (subsection 139B(3) applies).

38. The cessation time for an Allocation Share will be the earlier of when:

- the share is disposed of by the Trustee on behalf of the Participating Employee;
- the share is transferred to the Participating Employee by the Trustee;
- the share is forfeited; or
- the Participating Employee is no longer employed by any of the following:
 - a) a member of the NRMA Insurance Group, including NIGL; or
 - b) the employer, (specifically the employer in whom the Participating Employee was originally employed when the Allocation Share was acquired), of the Participating Employee.

39. Where a Participating Employee, in an arm's length transaction, disposes of the shares at the cessation time or within 30 days of the cessation time, the discount included in their assessable income is the amount or value of the consideration received on the disposal (subsection 139CC(3) applies).

40. Where an Allocation Share is forfeited, no amount of discount in relation to that share will be included in the Participating Employee's assessable income (subsection 139CC(3) applies).

41. Where a Participating Employee does not dispose of the shares in an arm's length transaction at the cessation time or within 30 days of the cessation time, the discount to be included in their assessable income is the market value of the shares at the cessation time (subsection 139CC(4) applies). The market value of an Allocation Share at this time is determined under section 139FA.

Capital Gains Tax

42. Where an Allocation Share is disposed of by, or on behalf of, the Participating Employee, a capital gain arises to the extent that the capital proceeds from the disposal exceed the cost base of the share. A capital loss occurs where the capital proceeds are less than the reduced cost base.

43. Where in relation to a CGT event A1 the disposal of an Allocation Share occurs under an arm's length transaction at or within 30 days after the cessation time, any capital gain or capital loss made from the disposal is disregarded (subsections 130-83(1) and (2) of the ITAA 1997 apply).

44. In circumstances where the disposal of an Allocation Share occurs under a non-arm's length transaction or not within 30 days after the cessation time, the capital gain or capital loss is calculated on the basis of the first element of the cost base or reduced cost base being the market value of the share at the cessation time (subsection 130-83(3) of the ITAA 1997 applies). The market value of the Allocation Share at this time is determined under section 139FA.

45. A capital gain on disposal will be a discount capital gain if the disposal of the Allocation Share occurs at least one year after the Participating Employee became absolutely entitled to it (section 115-5 of the ITAA 1997 applies). The discount percentage for a discount capital gain is 50 per cent (paragraph 115-100(a) of the ITAA 1997 applies).

Forfeiture

46. Where an Allocation Share is forfeited prior to the Participating Employee becoming absolutely entitled to it, no capital gain or loss will arise in relation to that share.

47. Where an Allocation Share is forfeited after the Participating Employee becoming absolutely entitled to it, a capital gain or capital loss may result. The capital proceeds in relation to the CGT event will be the market value of the Allocation Share at the time of forfeiture (section 116-30 of the ITAA 1997 applies). The first element of the cost base or reduced cost base is the market value determined under section 139FA at the cessation time. However, a capital gain or capital loss is disregarded if the share is forfeited at or within 30 days of the cessation time.

Dividends

48. A dividend received by the Trustee in respect of a Participating Employee's Allocation Share is assessable to the Participating Employee in the year of receipt (Division 6 of Part III applies).

49. Where such a dividend is franked, subject to the imputation rules in Part IIIA of the ITAA 1936 and Part 3-6 of the ITAA 1997, an additional amount will be included in the Participating Employee's assessable income and a franking rebate or tax offset allowed to the Participating Employee in the year of receipt of the dividend.

Explanation

Employee share schemes

50. Division 13A of Part III of the ITAA 1936 provides for the taxation treatment of shares acquired under employee share schemes. Under Subdivision B of Division 13A if a taxpayer has acquired a share or right under an *employee share scheme*, the assessable income of the taxpayer includes the discount given in relation to the share.

51. 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.

52. Clause 9.3 of the Trust Deed and Term 2.1 of the Terms of Invitation make it clear that the Participating Employee acquires a beneficial interest in an Allocation Share at the time of allocation. For the purposes of Division 13A, the Participating Employee acquired a share by it being allocated to their account by the Trustee.

53. 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 provided to the taxpayer.

54. It is considered that Allocation Shares were acquired by Participating Employees in their capacity as employees and accordingly the 'employment' condition in subsection 139C(1) is satisfied.

55. 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 were not liable to make any payment on acceptance of an offer for Allocation Shares.

56. Therefore, Participating Employees acquired their Allocation Shares under an employee share scheme and the discount given is included in their assessable income, as required by Division 13A.

Election made under section 139E

57. Where an election is made under section 139E for a year of income, subsection 139B(2) applies to determine when the discount with respect to all the qualifying shares or qualifying rights acquired in that year is assessed. A section 139E election, once made, allows a Participating Employee to include the discount in their assessable income in the year that the Allocation Share is acquired.

58. 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. Notwithstanding this, paragraph 3 of Taxation Determination TD 97/23 provides that unless specifically requested to do so, taxpayers should not forward their section 139E elections to the Australian Taxation Office.

59. Where a taxpayer has acquired a share under an employee share scheme and subsection 139B(2) applies, the discount is included in the taxpayer's assessable income of the year in which the share is acquired.

60. Accordingly, a Participating Employee who has made an election under section 139E includes the discount given on their Allocation Shares in their assessable income in the income year *when* the shares were acquired.

Time of acquisition

61. Division 13A does not specify the time at which a share is taken to have been acquired. Section 139G describes the circumstances in which a person acquires a share.

62. The Explanatory Memorandum to the Taxation Laws Amendment Act (No. 2) 1995 (the EM), which inserted Division 13A into the ITAA 1936, states at paragraph 2.29:

For the purposes of the new Division, a share or right is taken to have been acquired by a person ... when:

- the share or right is transferred to that person;
- the share is allocated to that person; or
- the right is created in that person.

A person is also taken to acquire a share or right when a person acquires a legal or beneficial interest in a share or right.

63. The events listed in this passage of the EM are the same as those listed in the section 139G definition of 'acquires'. It is implied from the EM that the time of acquisition of a share for Division 13A purposes will be the time of the event referred to in section 139G. In the case of a Participating Employee this is when they acquired their beneficial interest which, as indicated above, was the time when the Allocation Shares were allocated to their account by the Trustee.

Amount of the discount where election made

64. If subsection 139B(2) applies, the amount of the discount is calculated under subsection 139CC(2). This provides that the discount is the market value of the share at the time when it was acquired, less any consideration paid or given by the taxpayer as consideration for the acquisition.

65. As the Participating Employee pays no consideration for the acquisition of their Allocation Shares the amount of the discount is the market value of the shares at the time of allocation. The market value of NIGL shares, being quoted on a stock market of an approved stock exchange, is determined under section 139FA.

Market value under section 139FA

66. The market value of an Allocation Share determined under section 139FA at a particular time is:

- if there is at least one transaction on the ASX in NIGL shares during the week up to and including the relevant time – the weighted average of the prices at which NIGL shares were traded during that period (paragraph 139FA(1)(a) applies);
- if there were no such transaction in the period specified – the last price at which an offer was made on the ASX in that period to buy a NIGL share (subparagraph 139FA(1)(b)(i) applies); or

- if there was no transactions in, or offers made to buy, NIGL shares on the ASX in the period specified – the arm's length value of the share as specified in a written valuer's report or calculated in accordance with an approved method under subsection 139FB(1) (subparagraph 139FA(1)(b)(ii) applies).

No tax-free threshold

67. As the Plan contains conditions that could result in a Participating Employee forfeiting ownership of Allocation Shares the exemption conditions in section 139CE are not satisfied in relation to the Allocation Shares. This means that a reduction under section 139BA of up to \$1,000 in the amount of the discount included in assessable income is not available to Participating Employees electing to be assessed in the year of acquisition under subsection 139B(2).

Election under section 139E not made

68. Under subsection 139B(2), the discount in relation to an Allocation Share is included in the Participating Employee's assessable income in the year in which the share was allocated to them, unless subsection 139B(3) applies.

69. Subsection 139B(3) applies where the Participating Employee has not made an election under section 139E and their Allocation Share is a *qualifying share* (refer to paragraphs 71 to 85).

70. If subsection 139B(3) applies, the discount is included in the Participating Employee's assessable income in the year of income in which the *cessation time* occurs.

Qualifying shares

71. Section 139CD sets out the six conditions required for a share to be a qualifying share.

Acquired under an employee share scheme

72. The first condition is that the Allocation Share must have been acquired under an employee share scheme. This condition is satisfied (refer to paragraphs 50 to 56).

Company or holding company is the employer

73. The second condition is that the company in which shares are being offered must be the employer, or the holding company of the employer of the Participating Employee.

74. Clause 5.1 of the Trust Deed, read in conjunction with the definitions in Term 1 of the Terms of Invitation, makes it clear that shares under this Plan are only offered to Participating Employees of the NRMA Insurance Group.

75. The shares offered are shares in NIGL. NIGL is the holding company of the NRMA Insurance Group. Therefore, the second condition is satisfied.

Ordinary shares

76. The third condition is that all the shares available for acquisition under the scheme must be ordinary shares.

77. As the only shares available for acquisition under the Plan are ordinary shares in NIGL, this condition is satisfied.

At least 75% of permanent employees entitled to participate

78. The fourth condition is that at the time the share is acquired at least 75% of the permanent employees of the employer must have been entitled, or at some earlier time had been entitled, to acquire:

- shares under the scheme; or
- shares or rights in the employer, or a holding company of the employer, under another employee share scheme.

79. Subsection 139GB(1) defines a permanent employee to generally be a full-time or a permanent part-time employee of the company with at least 36 months of service.

80. All full-time and part-time employees of relevant subsidiaries of NIGL as at 9 March 2001 with at least 3 months continuous service were invited to participate in the Plan for the 2000-2001 tax year. Accordingly, at least 75 per cent of the permanent employees of the relevant employers (of Participating Employees) were entitled to acquire shares under the Plan.

Interest and power not to exceed 5%

81. The fifth condition is that, immediately after the acquisition of the share or right, the relevant Participating Employee does not hold a legal or beneficial interest in more than 5% of the company. The sixth condition is that, immediately after the acquisition of the share or right, the relevant Participating Employee is not in a position to cast, or control the casting of, more than 5% of the votes that might be cast at a general meeting.

82. While it is likely that these two conditions have been satisfied for most Participating Employees, it should be noted that this Ruling does not apply to any Participating Employee who does not satisfy these conditions (refer to paragraph 5).

83. Therefore, as these six conditions are satisfied for all persons to whom this Ruling applies, shares obtained under the Allocation Share Plan on 9 March 2001 for these persons will be qualifying shares for the purposes of Division 13A.

84. As neither NIGL nor the NRMA Insurance Group companies are investment companies the exception in section 139DF which may otherwise deny shares to be qualifying does not apply.

85. As the shares are qualifying shares, subsection 139B(3) applies where the Participating Employee has not made an election under section 139E. Under subsection 139B(3), the discount is included in the Participating Employee's assessable income of the year of income in which the *cessation time* occurs.

Cessation time

86. Cessation time with respect to shares is defined by section 139CA. Because the Plan contains restrictions preventing Participating Employees from disposing of Allocation Shares before a particular time and sets out conditions which could result in forfeiture of the shares, the cessation time is the earliest of the times specified under subsection 139CA(2). Under subsection 139CA(2) the cessation time is the earliest of:

- (a) the time the Participating Employee disposes of the Allocation Share;
- (b) the time when any restriction preventing disposal of the Allocation Share by the Participating Employee and any forfeiture condition that could result in the Participating Employee forfeiting ownership of the Allocation Share cease to have effect;
- (c) (taking into account subsection 139CA(3)), the time when the Participating Employee is no longer employed by any of the following:
 - i) a member of the NRMA Insurance Group, including NIGL; or
 - ii) the employer, (specifically the employer in whom the Participating Employee was originally employed when the Allocation Share was acquired), of the Participating Employee; or
- (d) 10 years after the share was acquired.

Restriction preventing disposal

87. The time that restrictions preventing disposal end depends upon the Trust Deed and the Terms of Invitation. Terms 12.1 and 12.2 of the Terms of Invitation (reflecting similar provisions in Schedule 2 of the Trust Deed) prohibit any dealings by both the Trustee and the Participating Employee in the Allocation Shares, including assignment,

transfer, sale, encumbrances or other dealing, except as permitted under Term 12 or as compelled by law. The restrictions on the disposal under these provisions *cease to have effect* at the earlier of when:

- the Trustee is given notice to sell the shares on behalf of the Participating Employee under Term 12.3(a) of Schedule 2 to the Trust Deed. This may occur up to 2 months after the end of the Restriction Period: (Term 12.3 of Schedule 2 to the Trust Deed);
- the shares are transferred to the Participating Employee under Term 12 of Schedule 2 to the Trust Deed. This may occur up to 3 months after the end of the Restriction Period: (Terms 12.3 and 12.5 of Schedule 2 to the Trust Deed); or
- the shares are forfeited under Term 13 of Schedule 2 to the Trust Deed or Term 13.2 of the Terms of Invitation.

88. Also, where an Allocation Share is transferred to a Participating Employee under Term 14 of the Terms of Invitation (and clause 14 of Schedule 2 of the Trust Deed) due to financial hardship faced by the Participating Employee, the restrictions on disposal contained in Term 12.2 of the Terms of Invitation (and clause 12.2 of Schedule 2 of the Trust Deed) will be of no effect as the Allocation Shares will no longer be registered in the name of the Trustee.

Forfeiture conditions

89. Conditions that could result in the Participating Employee forfeiting ownership of the Allocation Shares are contained in Term 13.1 and 13.2 of the Terms of Invitation and clause 13.1 of Schedule 2 of the Trust Deed. These conditions *cease to have effect* at the earlier of when:

- the shares are forfeited; or
- the shares are no longer held by the Trustee.

90. Taken as a whole then, the time when any restriction preventing disposal of the Allocation Share by the Participating Employee and any condition that could result in the Participating Employee forfeiting ownership of the Allocation Share ceases to have effect is the earliest time that that any one of the following events occurs:

- the Trustee on behalf of the Participating Employee disposes of the Allocation Share;
- the Allocation Share is transferred to the Participating Employee; or
- the Allocation Share is forfeited.

Cessation time for an Allocation Share

91. The potential cessation time 10 years after the share is acquired (set out in paragraph 139CA(2)(d)) will not be relevant to Allocation Shares. This is because, one way or another, the trust over the Allocation Shares must end within 5 years and 3 months from the date of allocation.

92. Accordingly, for an Allocation Share the cessation time will be the earlier of when:

- the share is disposed of by the Trustee on behalf of the Participating Employee under Term 12 of the Terms of Invitation (and clause 12 of Schedule 2 of the Trust Deed);
- the share is transferred to the Participating Employee under Terms 12 or 14 of the Terms of Invitation (and clauses 12 and 14 of Schedule 2 of the Trust Deed);
- the share is forfeited under Terms 13.1 or 13.2 of the Terms of Invitation (and Clause 13.1 of Schedule 2 of the Trust Deed); or
- the Participating Employee ceases to be employed by any of the following:
 - a) a member of the NRMA Insurance Group, including NIGL; or
 - b) the employer, (specifically the employer in whom the Participating Employee was originally employed when the Allocation Share was acquired), of the Participating Employee.

Amount of the discount where election not made

93. Where subsection 139B(3) applies the amount of the discount included in the Participating Employee's assessable income is calculated under either subsection 139CC(3) or subsection 139CC(4).

Disposal at arm's length within 30 days

94. Under subsection 139CC(3), if the shares are disposed of by the Participating Employee in an arm's length transaction at or within 30 days of the cessation time, the discount is the excess of the amount or value of any consideration received for the disposal, less any consideration paid or given by the Participating Employee to acquire the share.

95. As the Participating Employee provides no consideration for Allocation shares the amount of the discount in this instance will be the amount or value of any consideration received by the Participating Employee on the disposal of the shares (such as the proceeds of sale).

96. The amount of the discount in relation to an Allocation Share which has been forfeited will be calculated under subsection 139CC(3) if it can be said to have been disposed of by the Participating Employee in an arm's length transaction at the time of forfeiture.

97. In *FC of T v. Wade* (1951) 84 CLR 105; (1951) 5 AITR 214; (1951) 9 ATD 337, Dixon and Fullagar JJ, when considering the term 'disposed of' in another provision of the ITAA 1936, said (at CLR 110; AITR 219; ATD 340):

The words 'disposed of' are not words possessing a technical legal meaning, although they are frequently used in legal instruments. Speaking generally, they cover all forms of alienation.

98. In *Re Mal Bower's Macquarie Electrical Centre Pty Ltd (in liq)* (1974) CLC 27,771; [1974] 1 NSWLR 254 per LW Street CL in Equity at CLC 27,774; NSWLR 258, the concept of disposition was held to involve 'both a disponor and a donee'. Often, in cases of forfeiture, there will be no donee (see for example *Mosaic Oil NL v. Angari Pty Ltd (No. 2) and Another* (1990) 8 ACLC 780 at 782; (1990) 20 NSWLR 280 at 284). However, under the Plan Participating Employees will forfeit their Allocation Shares to the Trustee, who may be seen to be a donee.

99. The High Court held in *Henty House Pty Ltd (in liq) v. FC of T* (1953) 88 CLR 141 at 151; (1953) 5 AITR 557 at 560; (1953) 10 ATD 231 at 236, that the words 'disposed of' were not confined to a disposition by the taxpayer themselves. Notwithstanding this, under subsection 139CC(3) the relevant shares must be disposed of by the Participating Employee. Under the Plan any forfeiture will arise out of the contractual terms agreed to by the Participating Employee who, therefore, may be taken to have disposed of the Allocation Shares upon forfeiture.

100. If the disposal upon forfeiture occurred in the course of an arm's length transaction, the amount of the discount to be included in the Participating Employee's assessable income upon a forfeiture will be determined under subsection 139CC(3).

101. The case *Pontifex Jewellers (Wholesale) Pty Ltd v. FC of T* [1999] FCA 1822; 99 ATC 5324; (1999) 43 ATR 643 summarises the distinction between the two ways the term 'arm's length' is commonly construed. One construction refers to the relationship of the parties to a transaction (that is, whether the parties are related in some way) and the other refers to the terms of a transaction between the parties (that is, whether they are those that could be expected to arise between independent parties).

102. Here, it is the *transaction* which must be at arm's length. In determining whether a relevant transaction is at arm's length the entire circumstances surrounding the transaction must be considered: see *Granby v. FC of T* (1995) 129 ALR 503; 95 ATC 4240; (1995) 30 ATR 400 and *Collis v. FC of T* 96 ATC 4831; (1996) 33 ATR 438.

103. In the present circumstances, the forfeiture occurs under a term of the Plan which itself is an element of the total remuneration provided to Participating Employees. These remuneration agreements were negotiated at arm's length. Like the relevant sale agreements in *Granby*, the forfeiture here occurred under the 'umbrella' of arm's length negotiations, and therefore may be said to have occurred in the course of an arm's length transaction.

104. As no consideration is received on forfeiture under subsection 139CC(3) no discount will be included in a Participating Employee's assessable income in relation to a forfeited share where no election under section 139E is made.

Disposal not at arm's length or not within 30 days

105. Under subsection 139CC(4), if the shares are not disposed of by the taxpayer in an arm's length transaction at the cessation time, or within 30 days of the cessation time, the discount is the excess of the market value of the share at the cessation time over the amount or value of consideration paid or given by the taxpayer to acquire the share.

106. As the Participating Employee provides no consideration for Allocation Shares the value of the discount, in this instance, will be the market value of the Allocation Share at the cessation time. The market value at this time is determined under section 139FA, as set out in paragraph 66.

Capital Gains Tax

Acquired for CGT

107. For the purpose of the CGT provisions, you 'acquire' a CGT asset at the time worked out under Division 109 of the ITAA 1997. In relation to a CGT asset that is held under a trust the general acquisition rules provide that a beneficiary is considered to acquire the asset when they become absolutely entitled to it as against the trustee (see event number E5 in the table in subsection 109-5(2) of the ITAA 1997). This rule applies to shares held under employee share trusts subject to a limited exception applying where an election under section 139E has been made.

108. Where a share, being a qualifying share for Division 13A, was acquired from an employee share trust after 5 pm on 27 February 2001, the beneficiary is considered to have acquired the share for the purposes of determining the retention period under section 115-25 of the ITAA 1997 for discount capital gains at the time that they acquired their beneficial interest if the acquirer made an election under section 139E (see section 109-55, item 12 and subsection 115-30(1), item 8 of the ITAA 1997).

109. Participating Employees who make an election under section 139E to be taxed in the year of acquisition on an Allocation Share acquired after 27 February 2001 will be taken to have acquired that share on the date that it was allocated to them by the trustee for the purposes of determining whether a capital gain made after they become absolutely entitled to the share is a discount capital gain.

Disposal

110. A Participating Employee will make a capital gain on disposal of an Allocation Share if the capital proceeds from the disposal are more than the share's cost base.

111. If an Allocation share that has been acquired for CGT purposes is disposed of by, or on behalf of, a Participating Employee it will be a CGT event A1. Under subsection 104-10(4) of the ITAA 1997, the Participating Employee will make a capital gain if the capital proceeds from the disposal are more than the asset's cost base. A capital loss will occur where the capital proceeds are less than the reduced cost base. Capital proceeds are defined under Division 116 of the ITAA 1997 and include proceeds from sale.

Forfeiture

112. If an Allocation Share is forfeited before the Participating Employee is absolutely entitled to it no capital gain or loss will arise in relation to that share. This is because the share will not have yet been acquired for CGT purposes.

113. If an Allocation Share is forfeited after it has been acquired by the Participating Employee for CGT purposes it will be a CGT event C2. In this situation, under subsection 104-25(3) of the ITAA 1997, the Participating Employee will make a capital gain if the proceeds from the ending of the ownership are more than its cost base. A capital loss will result if the capital proceeds are less than the reduced cost base.

114. The proceeds from such an event will be deemed by section 116-30 of the ITAA 1997 to be the market value of the Allocation Share at the time of forfeiture. Market value for these purposes is the price that would be agreed to between willing, but not anxious, parties; see *Spencer v. The Commonwealth* (1907) 5 CLR 418; (1907) 14 ALR 253.

Whether discount Capital Gain

115. Under section 115-5 of the ITAA 1997, a capital gain will be a discount capital gain if:

- (a) it is made by an individual, trust, or complying superannuation fund (refer to section 115-10 of the ITAA 1997);

- (b) it is made from a CGT event occurring after 21 September 1999 (refer to section 115-15 of the ITAA 1997);
- (c) the cost base elements have not been indexed (refer to section 115-20 of the ITAA 1997); and
- (d) the relevant CGT asset was acquired at least 12 months before the CGT event (refer to section 115-25 of the ITAA 1997).

116. Conditions (a) to (c) will be satisfied by a Participating Employee in relation to Allocation Shares acquired under the employee share scheme.

117. Therefore, any gain made on the disposal of an Allocation Share by or on behalf of a Participating Employee will be a discount capital gain if the share was held for at least 12 months after the time it was acquired for the purposes of Division 115 of the ITAA 1997.

Capital Gains Tax consequences – election made under section 139E

118. Subdivision 130-D of Part 3-3 of the ITAA 1997 sets out specific rules in regard to shares acquired at a discount under an employee share scheme. Where the Participating Employee has made an election under section 139E 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 of the ITAA 1997.

119. Under section 130-80 of the ITAA 1997, the first element of the cost base or reduced cost base will be the market value of the Allocation Share at the time it is acquired (when the Participating Employee acquired a beneficial interest in it). The market value at this time is determined under section 139FA, as set out in paragraph 66.

120. If the proceeds on disposal of an Allocation Share acquired for capital gains tax purposes exceed this cost base the Participating Employee will make a capital gain. This will be a discount gain, as set out in paragraph 117, if the Allocation Share was held for at least 12 months after the Participating Employee acquired their interest in the share.

Capital Gains Tax consequences – election not made under section 139E

121. Section 130-83 of the ITAA 1997 provides that if the share is a qualifying share (which an Allocation Share is – refer to paragraph 83), an election is not made under section 139E, and CGT event A1, C2, E1, E2 or E5 happens in relation to the share in an arm's length transaction at, or within, 30 days of the cessation time any capital gain or capital loss the Participating Employee makes on the disposal is disregarded.

122. Therefore, if the Allocation share is disposed of in an arm's length transaction at, or within, 30 days of the cessation time no capital gain or loss will arise in relation to that share. This also applies to a forfeiture occurring at or within 30 days of the cessation time.

123. Where a Participating Employee does not make an election under section 139E and the Allocation Share is not so dealt with at, or within 30 days, of the cessation time the effect of section 130-83 of the ITAA 1997 is that the first element of the cost base or reduced cost base of the Allocation Share is its market value at the cessation time. The market value at this time is determined under section 139FA, as set out in paragraph 66.

124. If the capital proceeds for the CGT event exceed this cost base the Participating Employee will make a capital gain. This will be a discount gain, as set out in paragraph 117, if the Allocation share was held for at least 12 months after the Participating Employee became absolutely entitled to it.

Tax consequences of payment of a dividend by NIGL

125. The Trust Deed provides that while Allocation Shares are held on trust for Participating Employees all dividends received in respect of those shares will be distributed to such employees.

126. Dividends received by the Trustee with respect to a Participating Employee's Allocation Shares will be fully assessable to the Participating Employee in the year of receipt under section 97 or section 100, as is appropriate.

Gross-up and tax offset from 1 July 2002

127. Where the relevant dividend is franked the assessable income of the trustee, for the year in which the distribution is made, includes an amount equal to the franking credit on the dividend under subsection 207-40(2) of the ITAA 1997. This additional amount grosses-up the dividend received to take account of the company tax already paid in respect of that dividend.

128. In this case, subsection 207-45(1) of the ITAA 1997 operates to include the Participating Employee's share of the franking credit in assessable income, while section 207-50 of the ITAA 1997 generally allows the Participating Employee a tax offset equal to this amount if they are a qualified person under Division 1A of Part IIIAA.

Gross-up and franking rebate prior to 1 July 2002

129. Where the relevant dividend is franked the net income of the trust estate includes an additional amount under section 160AQT if the Trustee is a qualified person under Division 1A of Part IIIAA. This additional amount grosses-up the dividend received to take account of the company tax already paid in respect of that dividend.

130. In this case, a share of the additional amount will be included in the Participating Employee's assessable income under section 160AQW (or included in the section 100 amount if the Participating Employee is under a legal disability). In addition, the Participating Employee will be entitled to a franking rebate under section 160AQX if they are also a qualified person under Division 1A of Part IIIAA in relation to the relevant franked dividend.

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*Previous Rulings/Determinations:*CR 2001/1; TR 92/1; TR 92/20;
TR 97/16; TD 97/23*Subject references:*

- absolute entitlement
- acquisition of shares
- capital gains tax
- CGT cost base
- CGT discount
- CGT event
- CGT event A1
- CGT event C2
- CGT event E1
- CGT event E2
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- cost base
- dismissal of employees
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- employee share ownership
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- imputation credits
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- income
- resignation of employees
- share discounts on employee share schemes
- shareholders
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- trust distributions
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