


TD 2017/26EC - Compendium

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Public advice and guidance compendium – TD 2017/26

This is a compendium of responses to the issues raised by external parties to draft Taxation Determination TD 2017/D2 *Income tax: when will a dividend equivalent payment, made by a trustee under an employee share scheme that delivers ESS interests taxed by Subdivision 83A-B or 83A-C of the Income Tax Assessment Act 1997 be assessable as remuneration under section 6-5?*

This compendium of comments has been edited to maintain the anonymity of entities that have commented.

Summary of issues raised and responses

Issue No.	Issue raised	ATO Response/Action taken
1.	Scope and application	
1.1	<p>Sole activities test</p> <p>The Taxation Determination should refer to the sole activities test in subsection 130-85(4) of the <i>Income Tax Assessment Act 1997</i> (ITAA 1997).</p> <p>Dividend equivalent payments are similar to the distribution of dividends which are considered to be an incidental activity therefore dividend equivalent payments should be similarly treated. The employee is not provided with any additional benefit compared to a share plan, nor does the company obtain any additional tax deduction in respect of the payment.</p> <p>If a trust was used mainly to distribute cash payments to employees, rather than employee share scheme (ESS) interests, the 'sole activities' test would not be met.</p> <p>Generally, amounts are not contributed by employers to an employee share trust (EST) in order to pay cash amounts to employees, as this would breach the 'sole activities' test.</p>	<p>It is beyond the scope of this Taxation Determination to consider whether a trust is an EST that satisfies the sole activities test.</p> <p>We have recently consulted with the community in relation to ESS arrangements (consultation matter 201738) and sought feedback on issues that require guidance or clarification. In considering how we can best structure our public advice and guidance on ESS arrangements, we will consider whether the current guidance in ATO Interpretative Decision ATO ID 2010/108¹ needs to be updated or clarified.</p>

¹ ATO Interpretative Decision ATO ID 2010/108 *Income Tax: Employee share trust that acquires shares to satisfy rights provided under an employee share scheme and engages in other incidental activities.*

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	<p>To attribute dividend equivalent payments to employment, rather than arising in connection with the employee's interest in the underlying shares (acquired and held by a compliant EST), is therefore misleading and contradictory to the basis for arguing a trust satisfies the 'sole activities' test.</p>	
1.2	<p>CGT provisions The Taxation Determination should discuss the CGT implications (if any) of the arrangement and, in particular, outline that section 102-25 of the ITAA 1997 (CGT event E4 in accordance with section 104-70) applies.</p>	<p>The Taxation Determination concerns the characterisation of a dividend equivalent payment as for, or in respect of, services provided.</p> <p>It is beyond the scope of this Taxation Determination to consider the CGT implications for any participants in the arrangement.</p> <p>We have recently consulted with the community in relation to ESS arrangements (consultation matter 201738) and sought feedback on issues that require guidance or clarification. In considering how we can best structure our public advice and guidance on ESS arrangements, we will consider providing guidance on the CGT implications of ESS arrangements.</p>
1.3	<p>PAYG withholding The Taxation Determination should confirm whether the employer or the trust is required to withhold and remit the PAYG withholding.</p> <p>On the basis that PAYG withholding provisions apply to dividend equivalent payments, the Commissioner should accept that these obligations may be met by the recipient's employer, rather than the trustee as the payer.</p>	<p>The Taxation Determination concerns the characterisation of a dividend equivalent payment as for, or in respect of, services provided.</p> <p>It is beyond the scope of this Taxation Determination to consider the PAYG withholding implications for any participants in the arrangement.</p> <p>Whether PAYG withholding is required on a payment is determined in accordance with section 12-35 of Schedule 1 to <i>Taxation Administration Act 1953</i> (TAA). This provision requires an entity to withhold an amount from salary, wages, or bonuses it pays to an individual as an employee (whether of that or another entity). A trustee that makes a dividend equivalent payment (that is for, or in respect of, employment) is required to withhold an amount from the payment (even though the trustee is not an employer of the</p>

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		<p>employee who is in receipt of the payment), unless it is exempt or non-assessable non-exempt income of that employee.</p> <p>The amounts, formulas and procedures to be used to work out the amount required to be withheld are set out in the relevant withholding schedule (called tax tables). An entity that fails to withhold an amount as required by Division 12 of Schedule 1 to the TAA is liable to pay to the Commissioner a penalty equal to that amount.</p>
1.4	<p>Superannuation Guarantee</p> <p>The Taxation Determination should clarify whether a dividend equivalent payment would be included in Ordinary Time Earnings for the purposes of calculating the minimum Superannuation Guarantee contributions required to be made in respect of the recipient.</p> <p>On the basis that superannuation guarantee compliance is required in relation to dividend equivalent payments the Commissioner should accept that these obligations may be met by the recipient's employer, rather than the trustee as the payer.</p>	<p>The Taxation Determination concerns the characterisation of a dividend equivalent payment as for, or in respect of, services provided.</p> <p>It is beyond the scope of this Taxation Determination to consider the superannuation guarantee implications for any participants in the arrangement.</p> <p>We have recently consulted with the community in relation to ESS arrangements (consultation matter 201738) and sought feedback on issues that require guidance or clarification. In considering how we can best structure our public advice and guidance on ESS arrangements, we will consider providing guidance on any employment related obligations that may need to be satisfied by a trustee in an ESS arrangement.</p>
1.5	<p>Fringe Benefits Tax</p> <p>The Taxation Determination should outline that an employer is not liable for fringe benefits tax on dividend equivalent payments made by a trustee as part of an ESS arrangement as the definition of a 'fringe benefit' in section 136 of the <i>Fringe Benefits Tax Assessment Act 1986</i> (FBTAA) specifically excludes payments from which an amount must be withheld under section 12-25 of Schedule 1 to the TAA.</p>	<p>The Taxation Determination concerns the characterisation of a dividend equivalent payment as for, or in respect of, services provided.</p> <p>It is beyond the scope of this Taxation Determination to consider the fringe benefits tax implications for any participants in the arrangement. Where the provision of a benefit by the trustee as part of an ESS arrangement to an employee is a payment of 'salary or wages' that payment will not satisfy the definition of 'fringe benefit' in the FBTAA. Paragraph (f) of the definition of 'fringe benefit' in subsection 136(1) of the FBTAA specifically excludes the</p>

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		<p>payment of 'salary or wages'.</p> <p>'Salary or wages' is defined in subsection 136(1) of the FBTA to mean a 'payment from which an amount must be withheld (even if the amount is not withheld) under a provision in Schedule 1 to the TAA listed in the table, to the extent that the payment is assessable income.' Such payments would include dividend equivalent payments that have a sufficient connection with employment.</p> <p>We have recently consulted with the community in relation to ESS arrangements (consultation matter 201738) and sought feedback on issues that require guidance or clarification. In considering how we can best structure our public advice and guidance on ESS arrangements, we will consider providing guidance on any fringe benefits tax liabilities that may arise for an employer under an ESS arrangement.</p>
1.6	<p>Vested vs. unvested rights</p> <p>A distinction should be made in the Taxation Determination between the treatment of dividends paid in relation to unvested and vested rights and an example should be provided to that effect.</p>	<p>The principles that apply in determining if a dividend equivalent payment that relates to an unvested or vested right is for, or in respect of, employment are substantially the same. Separately dealing with each type in the Taxation Determination would increase its length and make it repetitive.</p>
1.7	<p>Commissioner's remedial power</p> <p>The Commissioner's Remedial Power (CRP) should be used to resolve the double taxation that results from the assessability of dividend equivalent payments to an employee despite the trustee also being assessed on the same amount. It would be unproductive for the business community to impose on the government an obligation to introduce amending law to resolve this issue.</p>	<p>The CRP is a discretionary power. The Commissioner can use this power in limited circumstances where law change would otherwise be required to address instances where the law is not operating as intended by parliament. The CRP is to be used as a last resort where alternative options, such as administrative or interpretive approaches, are not adequate to resolve an issue.</p> <p>The CRP may be applicable where the current law is producing unintended, negative impacts for entities, or is creating excessive compliance costs. In the context of dividend equivalent payments, it is considered that the intention of parliament is that the character of the payment is determined in the hands of the recipient. Where the nature of a dividend equivalent payment is remuneration, it will be</p>

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		assessable to the relevant employee regardless of whether the trustee has paid tax on the amount in a previous year.
2.	Examples	
2.1	<p><i>Example 1²</i> Example 1 should be clarified to note that the payment would not cause an issue under the sole activities test in subsection 130- 85(4) of the ITAA 1997.</p>	<p>The Taxation Determination does not consider whether a trust is an EST but, we acknowledge that most ESS arrangements involving trusts will seek to operate as an EST.</p> <p>Whether a trust that makes dividend equivalent payments satisfies the sole activities test depends upon the terms under which the trustee is able to make such payments (including if the dividend equivalent payment can be provided to employees that do not receive the relevant shares on which the dividends were declared) and what other activities the trust engages in.</p>
2.2	<p><i>Example 2</i> Example 2 should clarify that that the sole activities test would be met where a trustee exercises their powers in the circumstances outlined, on the basis that the trustee exercising its discretion to deal with dividends is a merely incidental activity to holding shares for the purpose of providing ESS.</p> <p>From a practical perspective, it is extremely unlikely that a trustee would act without instruction from the company to make a distribution with no reference to the ESS interests granted and it results in the sole activities test not being satisfied.</p>	Refer to the response at Issue No. 2.1.
2.3	<p><i>Example 3</i> Example 3 should be clarified to note that the sole activities test would be met.</p>	Refer to the response at Issue No. 2.1.

² Paragraph, example and footnote references in this Column of the compendium are references to TD 2017/D2.

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2.4	<p>Additional example</p> <p>The Taxation Determination should include the following example:</p> <p>Employee A (“A”), an Australian tax resident, is granted 1,000 non-transferable rights to ordinary shares in her employer, Company B (“B”), which vest if the employee remains employed by the employer group for 3 years post the grant date of the ESS interests. The rights also entitle A to receive dividend equivalent payments based on dividends received by the Trustee for the period between the vesting of the rights and the exercise of those rights, provided those rights are ultimately exercised. The rights have no acquisition nor exercise price. The rights fall within the ambit of Division 83A of the ITAA 1997 as they are a right to a share and were granted at a discount to their market value in respect of the employment of A. The taxation of such rights is deferred under Subdivision 83A-C due to the real risk of forfeiture of the rights.</p> <p>Following the vesting of the above rights in 3 years’ time, A’s employer contributes funds to the B Company employee share trust which acquires 1,000 shares on market and which are held in the name of the Trustee of the EST.</p> <p>B pays dividends on its shares every 6 months. The Trustee receives such dividends, pays tax on them under section 99A of the ITAA 1936 less an offset for franking credits and accumulates the after-tax amount of the dividends. Between years 3 and 5, \$100 of fully franked dividends have been</p>	<p>This example is considered to be similar to Example 1 of the Taxation Determination. As the dividend equivalent payment will be made to Employee A because they have remained employed by Company B for three years, the \$73 payment has a sufficient connection with Employee A’s employment and would be assessable to Employee A under section 6-5 of the ITAA 1997.</p>

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	<p>received by the EST Trustee on 1000 shares which results in tax payable of under section 99A of \$27 after allowing for the franking tax offset. After year 5, A exercises her rights, acquires an interest in the 1,000 shares held by the Trustee and is immediately paid out the after-tax amount of the dividends, that is, \$73 (\$100 -\$27) by the EST Trustee.</p> <p>A is taxable on the market value of the underlying shares at the time of exercise under Subdivision 83A-C of the ITAA 1997.</p> <p>The payment of the \$73 results from the exploitation of A's rights and, in turn, the interest in the shares acquired on exercise of those rights. It is therefore not regarded as remuneration assessable under section 6-5 of the ITAA 1997.</p> <p>The payment is not otherwise taxable to A but is subject to the provisions of section 104-70 (CGT Event E4). Whilst this CGT Event applies, the amount of the dividend equivalent payment does not reduce the CGT cost base of the interest in the shares held by A nor create a capital gain, as the dividend equivalent payment is sourced from dividends on which the Trustee has paid tax under section 99A of the ITAA 1936.</p> <p>In the above example, dividend equivalent payments are the product of exploiting an interest in a trust acquired through the exercise of vested right to shares. In Example 1 the dividend equivalent payments are payable based on meeting performance and service conditions.</p>	
3	Application of section 99B	

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3.1	<p>Footnote 14 is incorrect as there is no requirement that for section 99B of the <i>Income Tax Assessment Act 1936</i> (ITAA 1936) to apply, the trust must be a non-resident trust. Subsection 99B(1) of the ITAA 1936 applies to all trusts, and the subparagraph 99B(2)(c)(ii) 'carve-out', for income already assessed to the trustee, is relevant to determining if the amount is assessable to the employee (contrary to the position taken in paragraph 27).</p> <p>As by definition, a dividend equivalent payment is the after-tax amount of a dividend that the trustee has previously been assessed on under section 99A of the ITAA 1936, subparagraph 99B(2)(c)(ii) applies to reduce the amount assessable under subsection 99B(1) to zero.</p> <p>At the time of being introduced, section 99B of the ITAA 1936 was intended to apply to non-resident trust estates. However, on a strict reading of the legislation (without reference to the Explanatory Memorandum³), section 99B is not restricted to non-resident trust estates. Accordingly, the position at paragraph 27 is incorrect. The Courts would favour an approach that considered the legislative text without reference to the Explanatory Memorandum.</p>	<p>While subsection 99B(1) of the ITAA 1936 provides that certain property of a trust estate paid to, or applied for the benefit of, a resident beneficiary, is assessable to the beneficiary, the Commissioner considers that it does not apply unless the trust is or was a non-resident trust estate. Accordingly, neither it, nor the exception to it in subparagraph 99B(2)(c)(ii) of the ITAA 1936 (concerning amounts previously assessed to the trustee), generally applies to the arrangements described in this Taxation Determination.</p> <p>Although there is no decided case on point, the dicta of Hill J in <i>Traknew Holdings Pty Ltd v. Federal Commissioner of Taxation</i>⁴ (<i>Traknew</i>) is consistent with the approach in this Taxation Determination. See footnote 14 of the Taxation Determination.</p>
4	Characterisation of dividend equivalent payments as remuneration	
4.1	<p>Dividend paid to shareholders</p> <p>The fundamental character of dividend equivalent payments outlined, are that of a dividend.</p>	<p>The character of a dividend equivalent payment is determined in the hands of the recipient. Paragraphs 19 and 20 of the Taxation Determination outline the factors the Commissioner will consider in</p>

³ Explanatory Memorandum to the Income Tax Assessment Amendment Bill (No. 5) 1978 (Cth).

⁴ 91 ATC 4284; (1991) 21 ATR 1478.

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	<p>It does not follow that, just because the trust ESS interest was issued 'in relation to' the employee's employment, that the income coming from the shares is properly characterised as income from providing services (and is assessable, as such, under section 6-5 of the ITAA 1997). Such payments would be characterised as income from the employee's beneficial interest in those shares (and assessed, as such, under section 44 of the ITAA 1936). If the ESS interest were a more obvious direct interest in shares, it seems likely that any dividends, paid to the employee, would be taxed as dividends (under section 44 of the ITAA 1936). Certainly, that would be the result of section 6-25 of the ITAA 1997, which gives non-core assessing provisions priority over section 6-5 assessment of 'ordinary income'. The result would be the same, if the ESS interest were a trust interest in particular shares, and the employee/beneficiary had an immediate beneficial right to any dividends declared and paid to the trustee, on those shares. The result would not be different, just because the trustee pays these dividend equivalent amounts out of an after tax amount, that it received in a previous year.</p> <p>Dividend equivalent payments result from the exploitation of ESS interests and are taxable under Division 83A of the ITAA 1997. In relation to dividend equivalent cash amounts distributed on vesting of the ESS interest, which are not subject to taxation under Division 83A of the ITAA 1997, those distributions should be subject to tax under the Division 6 of the ITAA 1936 trust tax regime and should not be characterised as employment income.</p>	<p>determining the nature of the connection between the payment and services provided.</p>
4.2	<p>Tax neutrality Dividend equivalent payments should be treated similar to</p>	<p>The character of a payment is determined in the hands of a recipient. In circumstances where the dividend equivalent payment</p>

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	<p>dividends paid through to employees and taxed in the same years derived by the trustee of the EST (that is, they should be taxable only once) and treated similarly to dividends paid to employees on unvested/allocated shares. This is because the two arrangements are the economic equivalent of each other. Subjecting the dividends to tax in the hands of the trustee and the dividend equivalent payments to tax in the hands of the employees violates the neutrality principle.</p>	<p>(which reflects the dividend the trustee received less tax paid) is connected to an employee's employment, the dividend equivalent payment retains the character of remuneration and is assessable to the employee as ordinary income. The principle of tax neutrality is not violated in this instance. If the dividend equivalent payment were not assessable to the employee (despite the payment being connected with the employee's employment) it would result in different treatment to what would occur if the employee's employer paid the amount directly to the employee in cash or if is paid by the employer or trustee in the form of discounted shares; resulting in the discount being assessable under Division 83A of the ITAA 1997. For example, see the Commissioner's views about a dividend reinvestment arrangement made in Class Ruling CR 2006/126.⁵</p>
5	Rule against double taxation	
5.1	<p>Application of section 6-25</p> <p>The mere fact that an amount is 'ordinary income' doesn't mean it can be assessed, as such, under section 6-5 of the ITAA 1997. Subsection 6-25(2) of the ITAA 1997 says:</p> <p style="padding-left: 40px;">"Unless the contrary intention appears, the provisions of this Act [1] (outside this Part [2]) prevail over the rules about ordinary income."⁵</p> <p style="padding-left: 40px;">[1] – both the 1936 and 1997 Assessing Acts; [2] – Part 1-3: 'Core Provisions' housing both Div 6 relating to 'ordinary income' and Div 8 'general deductions'</p> <p>It is far from clear that section 6-25 of the ITAA 1997, actually requires another provision to actually assess,</p>	<p>In the context of a trust arrangement, subsection 6-25(1) of the ITAA 1997 requires that the same amount only be assessed once to the beneficiary but does not operate where different amounts (one being part of the net income of the trust estate assessable to the trustee under section 99A of the ITAA 1936 and the other being ordinary income as remuneration) are included in different years by two different taxpayers. Where an amount is assessed in an earlier year to a trustee under section 99A of the ITAA 1936, this assessment does not prevent that amount (less tax) being assessed again to a beneficiary under another provision in a later year.</p>

⁵ Class Ruling CR 2006/126 *Income tax: Shell Group - Employee Performance Share Plan.*

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	<p>before it can have precedence. It is open, and probable, that a provision, such as paragraph 99B(2)(c)(ii) of the ITAA 1936, would have precedence over section 6-5 of the ITAA 1997, so the dividend income is not double taxed.</p> <p>Capital receipts Dividend equivalent payments are capital receipts. Such characterisation is in line with decided case law and other ATO guidance. There are no other provisions of the income tax law that operate to include an amount in assessable income of the employees. Notably section 99B of the ITAA 1936 and section 104-70 of the ITAA 1997 (CGT Event E4) could potentially apply however the taxable amounts under those sections are reduced to zero under specific rules dealing with amounts previously taxed to the Trustee, for example under section 99A of the ITAA 1936.</p>	
5.2	<p>Distribution of corpus Dividend equivalent payments are not dividends. Whilst they are calculated by reference to the amount of dividends derived by the Trust, such dividends were derived in prior years by the Trust. Therefore, the dividend equivalent payments represent a distribution of corpus by the Trust and not 'net income' of the trust as defined in subsection 95(1) of the ITAA 1936.</p>	Agreed. This is reflected in paragraph 2 of the Taxation Determination.
5.3	<p>Double taxation If employees were taxed on dividend equivalent payments there would in our view be an element of double taxation. In most cases, dividends paid to Trustees of ESTs have already borne tax at the company level. In addition, Trustees of ESTs pay tax at the highest personal tax rate</p>	A trustee under an ESS arrangement pays tax on dividends it receives and to which no beneficiary is presently entitled. In circumstances where the dividend equivalent payment (which reflects the dividend the trustee received less tax paid) is connected to an employee's employment, the dividend equivalent payment retains the character of remuneration and is assessable to

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	<p>less an offset for any franking credits attached to the dividends. This ensures that once the dividend income has been derived by the Trustee it will have borne the full top personal tax rate. If further tax were levied on the subsequent payment to the employees there would be an element of double taxation, once in the hands of the trustee and once in the hands of the employees on amounts that essentially are being accumulated by Trustees of ESTs for the benefit of the specified employees. To subject employees to tax again on dividend equivalent payments is inconsistent with the law and represents a change to historical practice.</p> <p>It is a well-established principle that double tax should not apply unless the intention of the law in doing so is clear beyond doubt. In <i>Union Fidelity Trustee Co of Australia Ltd v. Federal Commissioner of Taxation</i>⁶ the High Court (in particular Menzies J at CLR 189) determined that Division 6 of the ITAA 1936, in conjunction with the other provisions of the Act, should not result in trustees or beneficiaries being subject to double taxation in respect of the income of a trust estate. The Commissioner's approach in this Taxation Determination results in the dividend income being taxed at a rate of 71.9% (for employees at the highest marginal tax rate of 47%).</p>	<p>the employee as ordinary income. No double taxation would result in this instance as there have been two separate amounts taxed at two separate points to two separate taxpayers. The imposition of tax on receipt of a payment of salary or wages by an employee does not depend upon whether the paying entity has previously paid tax on funds that are the source of that salary or wage payment.</p>
5.4	Application of section 6-5 to amounts already	In considering whether a trustee and beneficiary should be assessed on trust income, Dixon J observed in <i>Executor Trustee &</i>

⁶ (1969) 119 CLR 177; [1969] HCA 36; 69 ATC 4084; (1969) 1 ATR 200.

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	<p>assessed</p> <p>Recent cases have specifically doubted that section 6-5 of ITAA 1997 can apply to amounts that have already been assessed (refer to Hill J's comments in <i>Traknew</i>⁷).</p> <p>An outcome that results in double taxation is inconsistent with the policy of the Act and should not be adopted.</p> <p>Policy considerations</p> <p>Dividend equivalent payments made by a trustee under an ESS that delivers ESS interests to an employee are not assessable as remuneration. It is unclear, from a policy perspective, why such payments when made by a trust, as outlined in the Taxation Determination, are assessable as remuneration. There is no tax mischief involved with the arrangements outlined in the Taxation Determination (there is no loss to revenue or taxation advantage to taxpayers compared to if they had been paid the dividends in the year that they are declared) and they are commercially based arrangements aimed at aligning employees with their employer and shareholders alike. An interpretation that promotes the policy intent of the law is required.</p> <p>The purpose of the relieving provisions in subparagraph 99B(2)(c)(ii) of the ITAA 1936 and paragraph 104-71(1)(c) of the ITAA 1997 relating to amounts taxed to the trustee under section 99A of the ITAA 1936 are designed to prevent double taxation on distribution of trust corpus</p>	<p><i>Agency Co of SA Ltd v. Federal Commissioner of Taxation</i>⁸:</p> <p>No interpretation of a taxing Act should be adopted which results in the imposition of double taxation unless the intention to do so is clear beyond any doubt. The arrangement and the substance of the provisions contained in sub-sec. 1 and in sub-sec. 2 of sec. 31 suggest very strongly that they were intended to be complementary and mutually exclusive. The object of sub-sec. 1 is plainly to define the liability of the beneficiary in order to ensure that, whether it reaches his hands or not, all income to which a person is presently entitled shall be included in his assessment so that it may not escape aggregation.</p> <p>In the context of an EST arrangement, the Full Federal Court in <i>Cajkusic v. Commissioner of Taxation</i>⁹ in rejecting the Commissioner's argument that contributions made to the ERT were distributions of income in satisfaction of section 101 of the ITAA 1936, noted that:</p> <p>This is not to say that in the case of a trust, where the trustee has no active duties to perform and incurs no outgoings in deriving the income of the trust, the payment by the trustee to a beneficiary during a year of income of a receipt which is income in the hands of the trustee will escape tax in the hands of the beneficiary. Clearly it will not. It will be included in the beneficiary's assessable income as ordinary income or statutory income...¹⁰.</p> <p>It is considered that it is the intention of legislature that the character of a payment is determined in the hands of the recipient.</p>

⁷ 91 ATC 4272 at 4284; (1991) 21 ATR 1478 at 1492.

⁸ (1932) 48 CLR 26, 44; [1932] HCA 25.

⁹ (2006) 155 FCR 430; [2006] FCAFC 164; (2006) 64 ATR 676; 2006 ATC 4752.

¹⁰ At FCR 439; FCAFC [35]; ATC 4760; ATR 684.

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	<p>which is taxed under section 99A of the ITAA 1936. Accordingly, given the absurd outcomes that could arise, an interpretation that promotes the purposes of these provisions and relieves double taxation should be preferred.</p>	<p>In the context of a dividend equivalent payment, whether or not the trustee has paid tax on this amount in a previous year does not impact on the assessability of this amount in the hands of the employee recipient.</p>
5.5	<p>Capacity</p> <p>It is not sufficient to make an amount paid out of a trust fund retain its character as employment income merely because it</p> <ul style="list-style-type: none"> • can be connected to another amount which might have been employment income or • would not have been derived by the person if they had not been an employee. <p>Such circumstances arose in <i>Constable v. Federal Commissioner of Taxation</i>¹¹ (<i>Constable</i>) where it was held that the amounts came to him by virtue of his rights under the terms of the Deed despite the presence of the above factors. Employees receive the dividend equivalent payments in their capacity as beneficiary. This ensures that they receive the same tax and after tax cash outcome as compared to dividends paid on allocated shares.</p>	<p>In <i>Constable</i>, the employee received a significant lump sum benefit from a fund established by the employer to deliver payments to employees as a result of retirement. The High Court was asked to consider whether payments from the fund were payments to which former paragraph 26(e) of the ITAA 1936 applied. <i>Constable</i> became entitled to the payments because the terms governing the fund stated that where an alteration was made to the terms and that alteration resulted in a curtailing of the rights of members (<i>Constable</i> was a member) or increasing their obligations, then any member was entitled to withdraw amounts in their account in the fund. Such an alteration was made and <i>Constable</i> became entitled to withdraw amounts. Chief Justice Dixon, McTiernan, Williams and Fullagar JJ stated:</p> <p style="padding-left: 40px;">It appears to us that the taxpayer became entitled to a payment out of the fund by reason of a contingency (viz: an alternation of the regulations curtailing the rights of members) which occurred in that year enabling him to call for the amount shown by his account. It was a contingent right that became absolute. The happening of the event which made it absolute did not, and could not, amount to an allowing giving or granting to him of any allowance, gratuity, compensation, benefit, bonus or premium.¹²</p>

¹¹ (1952) 86 CLR 402; [1952] HCA 64.

¹² At CLR 418; HCA [11].

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		<p>After referring to (and distinguishing) the decision in <i>Constable, Edmonds J in Blank v. Federal Commissioner of Taxation</i>¹³ held that the amounts paid to Blank were deferred compensation connected to his employment income and retained the character of remuneration even though he was no longer an employee when the amounts were paid from the plan.</p> <p>In what capacity an entity receives a benefit is a matter of fact and will be determined with regard to the individual factual circumstances of each case. Miscellaneous Taxation Ruling MT 2019¹⁴ outlines when a benefit provided to a shareholder who is also an employee receives the benefit in respect of their employment and in their capacity as an employee.</p>
6	Date of effect	
6.1	<p>Reliance on CR 2013/15</p> <p>Many public companies have relied on the view in Class Ruling CR 2013/15¹⁵ and guidance on the ATO website that until further notice CR 2013/15 would be followed by the ATO, to treat dividend equivalent payments as not assessable as remuneration. This approach should continue to be followed.</p>	<p>Class Ruling CR 2013/15 applies to the defined class of entities who take part in the scheme as described in that Ruling. Refer also to the response provided at Issue No. 6.2.</p>
6.2	<p>Grandfathering</p> <p>The date of effect should be extended to either 1 January 2018, 1 March 2018, 31 March 2018 or 1 July 2018. This should give companies sufficient time to ensure that current intended grants of ESS interests are adequately grandfathered and allow companies</p>	<p>In considering an appropriate date of effect for this Taxation Determination, we took into account a number of matters:</p> <ul style="list-style-type: none"> • Industry had been following the views in CR 2013/15 (despite the fact that it only applies to the class of entities specified). • Our position on the Advice under development

¹³ [2014] FCA 87, [98]; 2014 ATC 20-442,15913; (2014) 95 ATR 1, 32.

¹⁴ Miscellaneous Taxation Ruling MT 2019 *Fringe benefits tax: shareholder employees of family private companies and directors of corporate trustees*.

¹⁵ Class Ruling CR 2013/15 *Income tax: Leighton Holdings Limited Equity Incentive Plan*.

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	<p>appropriate time to adjust their existing arrangements without adversely impacting ESS grants relating to the 2017 financial year.</p>	<p>program that should our view be unfavourable we would only apply it prospectively and would not apply it to 'arrangements that had been entered into prior to publication' of our view.</p> <ul style="list-style-type: none"> • The entitlement to a dividend equivalent payment generally arises from the terms and conditions in the Invitation given to an employee to participate in a particular ESS arrangement. As such our view should not apply to ESS interests that have already been granted. • Having a set date provides certainty. <p>We have revised the date of effect at paragraphs 12 and 13 of the Taxation Determination to allow an additional transitional period for impacted clients to alter their arrangements where they determined that they did not want to include dividend equivalent payments in their ESS arrangements going forward, or if they wanted to update their employee handbooks to reflect our position in relation to the assessability of dividend equivalent payments.</p> <p>The Taxation Determination applies to dividend equivalent payments where they are paid under the terms and conditions attached to ESS interests issued on or after 1 January 2018. This timeframe allows for the necessary processes to be completed in relation to ESS interests offered to employees for the 2017-18 income year.</p>
6.3	<p>Clarification of the term 'issued' We understand the term 'issued' in this context to refer to ESS interests granted to participants on or after 1 October 2017.</p>	<p>The term issued is used to refer to ESS interests offered or granted to employees.</p>