



Family of Companies

3 August 2009

Mr John Hawkins
Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

By email to: economics.sen@aph.gov.au

Dear Mr Hawkins

Inquiry into Employee Share Schemes

The Johnson & Johnson Family of Companies in Australia wishes to make a brief submission to the Committee supplementing its detailed submission to Treasury dated 12 June 2009. We attach that submission for the Committee's **reference**.

We note the further amended policy position set out in the Assistant Treasurer's **Policy Statement** dated 1 July 2009.

That policy position incorporated some positive amendments, however many of the concerns and questions noted in our earlier submission remain to be addressed. These include, but are not limited to, the following issues:

1. Employers not having visibility over total employee income;
2. Likely circumstances of taxation up-front when no benefit may be realised;
3. Uncertainty concerning the notion of "real risk of forfeiture test"; and
4. Implementation date for the amended policy arrangements.

In addition to these and other matters raised, we briefly express our concern in relation the practical implementation of the proposed \$5,000 cap for salary sacrifice based schemes (and note the submissions of other parties in this additional issue).

Our affected J&J employee share schemes remain suspended until clarity, viability and certainty are provided.

Thank you for the opportunity to be heard on these issues.

Please contact me should you seek any clarification or further information.

Yours sincerely

Tim James
Manager
Corporate & Government Affairs



Family of Companies

***Johnson & Johnson
Family of Companies in Australia***

Submission to Treasury

**Reform of the Taxation of
Employee Share Schemes**

12 June 2009

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Our Credo

We believe our first responsibility is to the doctors, nurses and patients,
to mothers and fathers and all others who use our products and services.

In meeting their needs everything we do must be of high quality.

We must constantly strive to reduce our costs
in order to maintain reasonable prices.

Customers' orders must be serviced promptly and accurately.

Our suppliers and distributors must have an opportunity
to make a fair profit.

We are responsible to our employees,
the men and women who work with us throughout the world.

Everyone must be considered as an individual.

We must respect their dignity and recognize their merit.

They must have a sense of security in their jobs.

Compensation must be fair and adequate,
and working conditions clean, orderly and safe.

We must be mindful of ways to help our employees fulfill
their family responsibilities.

Employees must feel free to make suggestions and complaints.

There must be equal opportunity for employment, development
and advancement for those qualified.

We must provide competent management,
and their actions must be just and ethical.

We are responsible to the communities in which we live and work
and to the world community as well.

We must be good citizens – support good works and charities
and bear our fair share of taxes.

We must encourage civic improvements and better health and education.

We must maintain in good order
the property we are privileged to use,
protecting the environment and natural resources.

Our final responsibility is to our stockholders.

Business must make a sound profit.

We must experiment with new ideas.

Research must be carried on, innovative programs developed
and mistakes paid for.

New equipment must be purchased, new facilities provided
and new products launched.

Reserves must be created to provide for adverse times.

When we operate according to these principles,
the stockholders should realize a fair return.

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The Johnson & Johnson Family of Companies

Worldwide

Caring for the world one person at a time inspires and unites the people of Johnson & Johnson.

We embrace research and science - bringing innovative ideas, products and services to advance the health and well-being of people.

Employees of the Johnson & Johnson Family of Companies work with partners in health care to touch the lives of over a billion people every day, throughout the world.

Our Family of Companies comprises:

- The world's premier consumer health company
- The world's largest and most diverse medical devices and diagnostics company
- The world's third-largest biologics company
- And the world's sixth-largest pharmaceuticals company.

We have more than 250 operating companies in 57 countries employing 119,200 people.

In 2007 we invested US\$7.68 billion in research.

Our worldwide headquarters is in New Brunswick, New Jersey, USA.

In Australia

Johnson & Johnson Pty Ltd became an Australian corporate entity in 1931.

Today there are more than 1500 Johnson & Johnson employees in Australia and New Zealand and annual turnover of more than AUD\$1.1 billion.

There are five health and medical care focused operating companies in Australia: Johnson & Johnson Medical; Janssen-Cilag; Johnson & Johnson Pacific; Tasmanian Alkaloids; and Ortho-Clinical Diagnostics.

In 2005, Access Economics reported that during 2004, Johnson & Johnson in Australia accounted directly for gross value added of \$327 million, GDP of \$366 million and the employment of 1,313 full-time equivalents (FTE).

In addition, the flow on from inputs of domestically produced goods and services into Johnson & Johnson activities indirectly contributed additional gross value added of \$253 million, GDP of \$259 million and the employment of 2,772 FTE.

Combining the direct and indirect contributions, in 2004 Johnson & Johnson contributed gross value added of \$580 million, GDP of \$624 million and employment of 4,085 FTE to Australia.

We now outline the lines of business and companies within the Johnson & Johnson Family of Companies in Australia.

Pharmaceuticals

Janssen-Cilag Australia

Janssen-Cilag Pty Ltd (JCA) is a research-based company that markets pharmaceuticals for a range of conditions in mental health, neurology, haematology, gastroenterology, virology, and pain management. One of its key focus areas is biotechnology, which represents the promise of entirely new and highly targeted therapies for a range of diseases. At the same time, innovative genomics tools are already beginning to revolutionise and advance the discovery of pharmaceutical medicines.

Tasmanian Alkaloids

Tasmanian Alkaloids Pty Ltd is an advanced agricultural production and research & development company. It extracts alkaloids (morphine and thebaine extract) from poppies. Some of this product is converted to active pharmaceuticals (codeine phosphate and buprenorphine) with around 99% of the product exported.

In 1995, Tasmanian Alkaloids and another then J&J company initiated a project to develop a high-thebaine poppy. In sampling the alkaloid content of thousands of plants, one plant was found to have a high content of thebaine and no morphine, and the first commercial crop of these unique poppies was harvested in 1998. The new plant revolutionised thebaine production and today it has up to 80% of the worldwide market for Oxycodone raw materials.

Tasmanian Alkaloids is presently the largest manufacturer of active pharmaceutical ingredients in Australia and the largest exporter of codeine and thebaine in the world.

Medical Devices & Diagnostics

Johnson & Johnson Medical

Johnson & Johnson Medical Pty Ltd (JJM) is a major provider to the Australian health care system through both the provision of products and the development and implementation of support services for the medical community. Each year, JJM reinvests more than ten per cent of its sales in Australia to provide training and other assistance to local doctors. It is focused on a broad range of medical products and through a number of separate groups: Ethicon wound closure and wound management; Ethicon Endo-Surgery minimally invasive technology (Keyhole Surgery), laparoscopic instruments and mechanical staplers; Ethicon women's health products and antiseptic products; Cordis cardiology, endovascular, electrophysiology and neuro-radiology; and DePuy Australia, a leading developer of state-of-the-art technologies for joint reconstruction which markets a range of orthopaedic products.

JJM also supports clinical research programs in Australia across all business franchises. From involvement in global programs, first-in-human studies of new innovative technologies, to support original research ideas from Australian clinicians and specialists. JJM is particularly proud to have a long track-record of partnering with Australian surgeons to bring new and innovative devices to the global marketplace.

Ortho-Clinical Diagnostics

Ortho-Clinical Diagnostics (OCD) and Veridex LLC supply professional in vitro diagnostic instrumentation and related supplies to hospital laboratories, private pathology laboratories, and blood donor centres. Products include reagents used for determining patient blood groups and the compatibility of blood units prior to blood transfusions, screening of blood for infectious agents (eg. Hepatitis C), and reagents and instrumentation used for clinical chemistry, endocrinology, serology and oncology blood testing.

Consumer Healthcare

Johnson & Johnson Pacific

Johnson & Johnson Pacific Pty Ltd (JJP) is the largest over-the-counter supplier to retail pharmacy in Australia serving all community pharmacies and being in the top thirty suppliers for manufactured goods to grocery supermarkets. JJP is committed to providing the best service, programs and advice to consumers, customers and the community, and is dedicated to bringing to market innovative healthcare solutions.

Our broad product range spans across baby, beauty, oral care, smoking cessation, upper respiratory, gastro intestinal, eye care and general medicine categories. Among our most famous brands are the Johnson's Baby® range, Band-Aids®, Listerine® and Reach®.

Please note that each product referred to in this submission is the Registered Trademark of Johnson & Johnson.

Introduction

At Johnson & Johnson we recognise globally our responsibilities to bear our fair share of taxes and to provide adequate and competitive compensation programs for our employees. These responsibilities have been part of Our Credo for over 65 years.

Our compensation programs are designed to:

- Attract and retain talented employees in a globally competitive labour market;
- Encourage opportunities for broad based employee participation in the continued long-term success of their companies and our global enterprise as stockholders;
- Support the global movement and development of talent within and across our Family of Companies; and
- Help us cultivate a high-performance culture through performance-based remuneration plans, bonus and other incentive programs, determined by both individual performance and business results.

Johnson & Johnson particularly values the alignment, recognition and motivation of employees through the provision of employee share schemes (“ESS”).

In Australia, ESS represent an important element of Johnson & Johnson’s compensation programs and help us to achieve the four aims above. Our companies and staff operate in a highly competitive global marketplace and delivery of ESS provides a positive proposition that ensures our continuing contribution to the Australian economy through attraction and retention of superior talent in our businesses. In our view it is important that the local policy environment continues to support the sound and sustainable operation of such programs in the Australian market.

The measures announced in the Federal Budget on 12 May 2009 raised many concerns and created significant uncertainty for us. Those Budget measures, if implemented, would likely lead to the termination of some or all of our local ESS programs. The changes proposed both in the Budget and in Treasury’s Consultation Paper have potential to create considerable administrative and other burdens and pressures upon our organisations and people.

We nonetheless commend Treasury and the Government for consulting with the business community on further proposed policy changes in relation to ESS.

We are pleased to have the opportunity to comment on the revised proposed measures in the Treasury’s Consultation Paper received on 5 June 2009. We note the very limited time frame in which to respond.

This submission sets out our positions in principle and in brief. There remains substantial analysis and consideration before we can determine and act upon the particular impacts of the proposals on our ESS programs.

We have noted and broadly support the submissions made by Employee Ownership Group.

Direct Response to the Proposed Measures

We address the five key elements of the proposed measures as listed at point 6 of page 5 of the Consultation Paper.

1. Raise the income tax threshold for the \$1,000 tax exemption to \$150,000

Johnson & Johnson does not support the introduction of an income test to determine the application of the \$1,000 tax exemption. We understand the Government's rationale in proposing this change but do not consider it necessary nor likely to be effective in practice.

This proposal would add an unwarranted and increased level of complexity in company plan design and may lead to termination of some broad based employee share schemes.

Further, employers, appropriately, have no visibility over total employee income (inclusive of personal investment income) and as such will be ineffective in determining potential participation among their respective employee populations – this also may be viewed as a trigger for termination of plans.

An income test provides scope to create discrimination between participating employee populations at executive versus non executive levels which may be seen to defeat any purpose in providing share plans designed to encourage maximum participation, and on equal terms throughout an employee population.

It is noted that Division 13A already limits individual employees to only one tax concession in any one tax year, that is, a deferral concession or the current \$1,000 exemption concession.

2. Introduce limited deferral of the taxing point for some schemes

Johnson & Johnson supports the principle that taxation should not be payable until a benefit is realisable. We do not support the payment of tax on income that lies in paper only and may not be realised.

We note the proposed limited deferral of taxing point however we remain concerned that many employees will be taxed up-front when in fact no benefit may be realised. The possibility of subsequent refund of taxation would not necessarily represent adequate compensation for tax paid years prior.

Limiting deferral of the taxing point for grants awarded to employees (as opposed to purchases made under salary sacrifice arrangements) may give rise to employees having to pay tax on equities the value of which may not be realised in service. This is particularly true in a period where global share markets continue to be under stress and potentially creates short term cash flow issues for employees who may need to use retirement savings, or sell a parcel of shares to fund a tax liability arising from an "incentive" based program. This may work to defeat the purpose of plan design which otherwise encourages ownership in the company and a source of retirement saving for longer term employees.

The notion of a “genuine risk of forfeiture” test would create an additional layer of uncertainty and cannot possibly provide clarity in each contingency. Differing interpretations and positions would likely arise necessitating costly legal intervention.

In our view, the payment of any tax in advance of a benefit being realised raises concerns in relation to both equity and efficiency and policy measures that provoke such circumstances should be avoided.

3. Introduce an annual reporting requirement and associated withholding arrangements by companies that participate in these schemes

Johnson & Johnson supports the principle that people should pay the tax for which they are liable. Therefore we recognise the steps the government is proposing to take to ensure that the tax liabilities of individuals be appropriately reported and tracked.

We would positively view the implementation of a TFN based employer disclosure mechanism and the inclusion of share scheme income amounts as separate items on payment summaries and individual tax returns in achieving improved governance over the operations of ESS plans in the workplace. However we would anticipate that such reform does not change the burden of taxation from the employee onto the employer and bring the taxation of discounts into the PAYG withholding framework.

Enhanced reporting would be a more effective tool than utilising the blunt instrument of taxing grants up-front and is likely to yield the government greater tax revenue in the medium to longer term.

However, in seeking to achieve this, the Government needs to be mindful of any additional administrative burden this may place upon business. It therefore needs to design a scheme that achieves its goal of tracking individual liabilities while limiting the administrative burden upon companies. This would be in line with the Government’s stated goal of reducing the administrative and regulatory burden on business.

4. Review the existing rules for valuing discounted and deferred shares and rights

Johnson & Johnson supports the notion that general principles of market value apply in valuation.

A review of valuation rules, as proposed in the Consultation Paper, may be a helpful exercise and should be shaped by broad consultation and consideration among all stakeholders.

5. Modify the rules relating to the refund of income tax for forfeited benefits

In line with our comments above, Johnson & Johnson does not support the proposed modifications of the rules relating to the refund of income tax for forfeited benefits.

In particular, the proposal that no refund should apply where extinguishment, forfeiture or inability to vest occurs as a result of a choice the taxpayer makes would serve to enshrine the payment of tax in circumstances where no actual benefit has been received. For instance if a taxpayer opts not to exercise an option and that option lapses then no income will have been derived yet, under the proposed change, nor could that taxpayer seek a refund of tax paid up-front.

We support the maintenance of the current refund rules.

Other Submissions

6. Costs of Compliance

It is not clear at this stage whether the additional cost and complexity of compliance with the proposed new measures will outweigh the benefits to our organisations and staff of offering such schemes.

As noted, we urge the Government to ensure that compliance measures generate as little cost and administrative burden upon businesses as possible, particularly in the current difficult climate.

7. Global Competitive Dynamics

The Government speaks of the need for Australia to be internationally competitive. As part of this drive, Australia must also be internationally competitive for talent. As a global company, Johnson & Johnson is in the international market place for talent. This is in terms of both retaining Australian employees within the company and attracting international employees to Australia.

At present Johnson & Johnson has approximately 80 international employees on 457 visas working in its Australian operations. These employees make a valuable contribution not only to Johnson & Johnson, but to the Australian health care sector through bringing the benefit of international experience to this country. Importantly, these employees are across a range of incomes and are in no way confined to the highest level of income earners.

In determining whether to accept a position in Australia, our international candidates consider the implications for both their short and long term remuneration.

The counter is also true for Australian employees of Johnson & Johnson. As part of a global organisation many of our employees have the opportunity to work internationally. In considering these opportunities they take into account the implications for their short and long term remuneration. This is not only a factor in determining whether they accept an international opportunity, but whether they then return to Australia sometime in the future bringing with them the benefits of global experience back to their home country. This international experience makes a vital contribution to Australia's skill base and ongoing economic development.

In summary, the government should take account of global competition for talent and the implications that personal taxation policies have on Australia's ability to compete in the international employment market place. Any steps that the government may take to lessen Australia's international competitiveness in this area will have both short and long term implications.

8. Addressing Uncertainty

The Government needs to address the current uncertainty in the marketplace as soon as is possible. In response to the current level of uncertainty, Johnson & Johnson suspended its employee share purchase scheme after the Budget announcement. It is not feasible to reinstate this scheme until the Government delivers certainty as to the longer term arrangements. This suspension is not only an inconvenience to employees, but also has imposed additional administrative costs and burdens upon our companies.

9. Rollover Relief

Existing Australian tax rules provide rollover relief for employees of companies that are subject to takeovers or restructures under which shares or rights they hold under an employee share scheme are disposed of and they receive replacement shares or rights that reflect the new corporate structure.

These rules are important in ensuring that employees of companies undergoing such transactions are not disadvantaged, from a tax perspective, as a result of such transactions being undertaken.

Johnson & Johnson considers it important that any proposed amendments provide certainty to companies considering undertaking such transactions. This can be achieved by clarifying that the proposed amendments will not apply to awards made after the announcement of the proposed changes where those awards qualify for the rollover relief, it is important that certainty is provided to companies that may be undertaking takeovers or restructures so as not to adversely impact on those transactions.

10. Consultation Processes

The disruption that the Government's budget announcement has caused highlights the benefit to government and the community of government undertaking appropriate consultation on measures that have the potential for wide spread impact.

Had the Government initiated even some form of informal consultations with the business community on this issue, it would have been rapidly evident that the original budget proposals were ill considered and likely to be detrimental to millions of Australians.

Employee share schemes provide incentives and connect people with their employer across a wide range of incomes. They are in no way restricted to a small number of very highly paid executives that the government appeared intent upon targeting. This reflects the changes that have occurred in the Australian workplace over the previous two decades and the need for Australia to become more internationally competitive in the battle for global talent. Engaging with the business community on key initiatives will not only result in better policy being delivered, but also deliver a broader political dividend.

11. Timing

Having regard to the considerable analysis, deliberation, and compliance necessary in relation to the proposed changes, we would suggest that implementation commence at a time that permits us to fully register and respond to the changes in our organisations.

The proposed 1 July 2009 implementation date is unlikely to facilitate sufficient time for due consideration and preparation at a range of levels: government; company; and individual.

Johnson & Johnson would suggest implementation at a time after the current calendar year to ensure sound and smooth planning and implementation.

Recommendation

The Government should take account of business, community and individual views and inputs in relation to employee share schemes and complete timely and adequate consultation before setting a firm policy agenda.

Any policy that would reduce the prevalence and impact of employee share schemes, as we believe the proposed measures would, should be avoided and a policy agenda set that has regard to continued development and improved integrity of such schemes in the national interest.

Johnson & Johnson holds a range of concerns in relation to the current proposed measures and recommends that the Government further consult and consider options for reform before finalising and implementing major policy change in this important area.

Conclusion

The Johnson & Johnson Family of Companies in Australia is committed to providing competitive compensation programs for employees. We are also pleased to work with governments towards an effective policy balance to attract, develop and retain talented people while meeting taxation requirements in an equitable and effective manner.

In this spirit, we thank Treasury for the opportunity to submit and we are pleased to commend this feedback to the Government for consideration.

We reiterate our position and recommendation below:

Recommendation

The Government should take account of business, community and individual views and inputs in relation to employee share schemes and complete timely and adequate consultation before setting a firm policy agenda.

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Johnson & Johnson holds a range of concerns in relation to the current proposed measures and recommends that the Government further consult and consider options for reform before finalising and implementing major policy change in this important area.

The Johnson & Johnson Family of Companies in Australia would be pleased to assist and work with the Treasury and the Government to:

1. Amplify and/or clarify these submissions;
2. Attend hearings to speak to these submissions;
3. Provide expert advice in relation to these submissions; and
4. Otherwise contribute to the development and implementation of a more effective tax system in Australia.

To do so please contact:

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