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1.0 Executive Summary

This Submission was prepared in response to the terms of reference set out in the 1999 Parliamentary Inquiry on Employee Share Ownership. The Submission provides a brief background on Qantas and the characteristics of the airline industry in order to underscore the importance of schemes, such as employee share ownership, in securing the commitment of employees to the success of the airline.

The Submission also provides a discussion on the historical development of employee share ownership schemes in Qantas. The financial, operational, stock market and other performance measures of Qantas are discussed to show ongoing improvements in the airline since privatisation.

In conclusion, Qantas believes employee share ownership schemes to be:

- an important factor in bringing about cultural change in Qantas; and
- a good method of building an understanding of shareholder value amongst employees.

Qantas, therefore, supports the encouragement of employee share ownership schemes.

Suggested avenues towards encouraging greater levels of participation of Australian companies in employee share ownership schemes include:

- addressing the grey areas of the tax legislation that may act as disincentives for companies introducing employee share ownership schemes. An example is the dividend streaming issue; and
- further reforms to the Income Tax Assessment Act 1936, such as increasing current exemption concession and tax deduction levels.

2.0 An Overview of Qantas

Qantas was established in Queensland by private investors in November 1920. During the early years, the company expanded its air taxi business to include scheduled domestic passenger and mail services, as well as mail services to the UK in collaboration with Imperial Airways (a predecessor of British Airways). In 1934, Imperial Airways acquired 50 per cent of the company.

In 1947, Qantas became a Commonwealth entity when the Australian Government purchased all the shares in the company. During the same year, the Government-owned Trans-Australia Airlines (TAA) took over the Qantas domestic network, allowing the company to concentrate solely on its international services. In August 1986, TAA became Australian Airlines, with a new focus on customer service and the business market.

In June 1992, the Government accepted the Qantas bid for Australian Airlines and subsequently announced plans to privatise Qantas. In February 1993, the Government recapitalised Qantas with an injection of AUD 1.35 billion. A month later, the Government selected British Airways as the strategic airline partner to buy a 25 per cent stake in Qantas. In October 1993, the Qantas and Australian Airlines operations were merged under a single Qantas brand. The Public Share Offer was launched in June 1995 and Qantas shares were listed on the Australian Stock Exchange on 31 July 1995.

Today, Qantas is a profitable, world-class Australia-based airline, linking 104 destinations in 33 countries. The company employs around 29,000 staff, and is one of the top 50 public companies, by market capitalisation, in Australia. In relation to the financial year 1997/98, Qantas added value to the greater economy by providing AUD 2.2 billion towards salaries and staff related costs and AUD 215 million to the Australian Government through corporate tax. Qantas distributed AUD 158 million to the shareholders, and paid net interest charges of AUD 104 million.

Qantas is a prominent corporate citizen through active sponsorship of charities as well as cultural, sporting and community organisations. These include the Australian Opera, the Sydney Dance Company, the Commonwealth Games, Clean Up Australia, Clean Up the World and the Starlight Foundation.

3.0 Aviation Industry and Background

This section seeks to place the remainder of the submission in its historical and industry context.

3.1 Airline Industry Characteristics

The airline industry is characterised by high capital intensity, mobile assets and high fixed costs, which drive competitors towards marginal pricing. A result of this is an industry-wide trend of declining yields, which in turn requires constant vigilance over costs and efficiency. At the same time, the industry is highly reliant on the performance of front-line staff to deliver consistently high levels of personal service to customers. It is critical, therefore, for an airline to secure the commitment from its employees to strive for greater efficiency and productivity, whilst continually improving the quality of its services. Finally, all this must be accomplished with unquestioned commitment to safety.

3.2 Aviation Market Liberalisation

The past decade has seen significant changes in the policy and regulatory framework of the Australian aviation sector.

Within the domestic market, the abolition of the Two Airline Policy in October 1990 foreshadowed a period of strong price competition and enhanced service quality. Following deregulation, two start-up operators, Compass and Southern Cross, entered the domestic market in 1990-91 and 1991-92 respectively, but subsequently ceased operations.

The barrier between international and domestic air services was removed in 1992 and multiple designation in Australia's bilateral air service treaties was introduced. Multiple designation was a defining factor in Ansett Australia commencing international air services and the more liberal approaches to the negotiation of rights, which have occurred in recent years. Allied to these changes was the removal of aviation specific restrictions on equity investments between Australian airline operators, which opened the way for Qantas to buy Australian Airlines.

These initiatives have been accompanied by a policy aimed at encouraging foreign carrier participation in Australia's international markets and the establishment of the single aviation market (SAM) with New Zealand which creates an 'open market' in air services within and between the two countries.

Following a recent report to the Government by the Productivity Commission, further liberalisation of the policy framework is under consideration.

3.3 Employee and Industrial Relations

The airline industry is traditionally highly unionised and the levels of union membership in Qantas reflect this. There is evidence, however, that union membership is declining within the company.

Since 1992, Qantas has successfully negotiated consecutive rounds of Enterprise Bargaining Agreements (EBAs) with the unions, with the latest agreement (EBA IV) completed in late 1998. Successive agreements have embodied greater flexibility and productivity improvement measures.

Qantas has increased its efforts to communicate directly with the staff and to influence their commitment to performance with a view to enhancing job security.

4.0 Restructuring and Cultural Change

A new Board and management group were installed in 1993. The early priority of the new management was to change the airline into a commercially driven organisation benchmarked by its performance against other major Australian companies and foreign airlines. In bringing about this change, the management team faced two tasks:

1) implementing a series of improvements in the products/services/operations of the company; and
2) changing the organisational culture.

In August 1994, Qantas initiated a major relaunch of its product and services with the support of a new marketing campaign. The relaunch included progressively refitting the fleet with new cabin interiors, new Business Class seats, new crew uniforms, enhanced catering and cabin services and redesigned airport lounges. A series of training programs and other initiatives were introduced to support a renewed focus on customer services. In addition, the employment of new scheduling techniques and strategies resulted in significant route and schedule changes.

Privatisation brought continuing improvements across the airline, including the introduction of new computer reservation and yield management systems. Further initiatives involved the introduction of a disciplined cost reduction/avoidance program whilst maintaining the Qantas reputation for safety. Competitive tendering was used to improve service and reduce costs in many key areas of the business, including airports, security and areas of engineering and maintenance.

Along with these initiatives, the management team faced the task of introducing an organisational culture more suited to the private sector. This entailed intensive communication with employees, highlighting the links between their contribution to the overall success of the company. Employees were encouraged to take ownership of their performance, whether measured through workplace-specific key performance indicators, customer satisfaction, cost, profit or shareholder value. The introduction of Qantas Service Standards in July 1997 is an example of this effort. The program introduced staff performance evaluation based on area-specific customer service requirements.

The Qantas employee share ownership scheme encouraged staff to take ownership of their work. By directly linking company performance to employee remuneration, the scheme underscored how individual contribution in the workplace relates to company performance, and ultimately, to remuneration. The employee share ownership scheme also endorsed a holistic view of Qantas through rewarding employees on the performance outcomes of the airline, rather than on the performance of individual business units.

5.0 Considerations

There are a number of factors in considering an employee share ownership scheme:

- appeal of share ownership schemes as a form of remuneration for employees;
- types of employee share ownership schemes;
- tax regime and accounting standards; and
- application of employee share ownership schemes within the airline industry.

5.1 Share Ownership Trends

Individuals are becoming increasingly comfortable with share ownership as a form of personal wealth. A 1999 study by the ASX indicated that 4.4 million Australians, or one quarter of the population, now own shares directly. Over half of those Australians with direct share ownership entered the market between 1995 and 1998, the increasing level of participation partly due to large-scale IPO’s of recent years. Moreover, employee share ownership schemes support this trend. A 1999 survey by AFR calculated the total capital raised from all shares issued under employee share ownership schemes during 1 April 1998 to 31 March 1999 to amount to AUD 1.19 billion.

5.2 Employee Share Ownership Schemes

There are four main types of employee share ownership schemes: loan plans; partly paid share plans; option plans; and employer funded plans, or bonus share plans. In Qantas, selecting an appropriate employee share ownership scheme involved evaluating the advantages and disadvantages of each scheme from the viewpoints of both the airline and employees. Bonus share plans were considered most appropriate, given the favourable impact on the financial accounts of the company, the relative ease of plan administration, and the low risk capital accumulation for employees.

5.3 Tax Regime and Accounting Standards

Employee share ownership schemes are subject to the Income Tax Assessment Act 1936. Prior to a further amendment to the Income Tax Assessment Act in 1996, Australian companies could issue up to $500 worth of tax-exempt bonus shares, provided that the employees did not trade their allocated shares over the ensuing five-year period (the 'trading lock' period). An additional condition was that at least three quarters of employees were entitled to participate in the bonus share plan.

With the passage of Taxation Laws Amendment Bill (No.4) 1996, the tax rules were amended to broaden access to and increase the benefits of participation in employee share schemes. Under an employer-funded plan, the amendment allowed Australian companies to issue up to $1,000 worth of tax-exempt bonus shares to employees, provided that the plan covered at least 75 per cent of permanent Australian employees. The period in which employees were required to hold their share allocation was reduced from five to three years.

Despite this favourable change in the tax laws, other aspects, such as the widely drafted dividend streaming prohibition in the current tax legislation, act as disincentives towards employee share ownership schemes. The ATO is unwilling to provide a clear indication on whether employee share ownership schemes are a form of dividend streaming, unless companies are willing to provide the taxation positions of the individual employees receiving the shares and those of the non-employee shareholders (refer to Appendix A).

Further participation in employee share ownership schemes by Australian companies can be encouraged through addressing grey areas of the current tax laws and by increasing the current employee exemption concession and company income tax deduction levels. The 'all employee share scheme' under the proposed Year 2000 UK Finance Bill provides an example of a further avenue in encouraging employee share ownership. Amongst other aspects, it provides flexible company and personal tax incentives for the granting of shares to employees (refer to Appendix B).

In addition to the operation of tax rules in Australia, a company with an overseas workforce, such as Qantas, must consider whether the scheme appeals to employees under different country tax regimes. The majority of the countries where Qantas has employees were found to impose income tax on the fair market value of the shares at the time of receipt. This made the Qantas employee share ownership scheme, with its trading lock of several years, less attractive to employees than a cash bonus. The argument is supported by higher rates of refusals from overseas staff who were invited to participate in the Qantas employee share ownership schemes.

Whilst companies are entitled to a tax deduction on the cost of shares issued under employee share ownership schemes, the cost of shares are not recorded as an expense in the Profit & Loss under the current accounting standards. This provides an incentive for companies to use employee share ownership schemes to remunerate staff. Changes to the current accounting treatment may affect company views on employee share ownership schemes.

5.4 Employee Share Ownership in Other Airlines

Employee share ownership schemes are becoming increasingly common within the airline industry. This section briefly examines a few examples of employee share ownership in selected major carriers.

5.4.1 British Airways

As a part of the privatisation of British Airways in 1987, special arrangements were made for eligible employees to acquire shares on favourable terms, including offers of free shares, two free shares for each share bought under the Offer for Sale Price, priority over applications and discount shares.

Post-privatisation saw British Airways implement a range of employee share ownership schemes. Eligible employees of British Airways are rewarded through a Profit Sharing Scheme, which provides a choice of cash or conversion of cash bonus to shares. In order to boost the shareholdings of employees, British Airways has introduced an additional bonus of 20 per cent for those who used their profit share payment to acquire shares. Employees are also offered an option scheme, which is bundled with a savings plan to assist employees to be able to pay the amount required to exercise their options.

5.4.2 United Airlines

Another success story of employee share ownership schemes within the airline industry is the recapitalisation of UAL Corporation (United Airlines) in 1994. A 1998 survey showed that United Airlines was the third largest company in the United States (measured by the number of employees) to have implemented a scheme which resulted in greater than 30 per cent share ownership by employees.

Despite its profitable operations in the late 1980's, United Airlines reported consecutive net losses during the early 1990s. As part of a turn-around of the company's operations, shareholders approved a stock repurchase program, amounting to approximately 55 per cent of the company, for its employees under an Employee Share Ownership Plan (ESOP). In exchange, the participating unions (Air Pilots Association, International UAL-MEC, and International Association of Machinists and Aerospace Workers) and salaried and management employees agreed to forgo significant pay and benefits, and agreed to work rule changes which were valued, in total, over USD 5 billion at the time of the agreement.

The post re-capitalisation performance of United Airlines saw the company report successive improvements in its net profit before abnormals.

5.4.3 Alitalia

After two unsuccessful restructuring programs in 1994 and 1995, Alitalia underwent a third under a new management group in 1996. Unlike its predecessor, the 1996 restructure addressed key issues, such as labour relations, which had plagued the company historically. As part of the restructure, an agreement was reached between the management and the unions to provide employees with equity in the company, in return for reduction in the number of employees, implementation of productivity initiatives and lower wages.

In 1998, the employees owned 20.5 per cent of Alitalia, the largest proportion out of all major European airlines. Alitalia recorded a 50 per cent increase in productivity between 1993 and 1998. Further productivity gains are expected from the in-built flexibility of the current labour agreement. In addition, a decrease in total labour costs amounting to 25 per cent over the original budget is also expected by the year 2000.

5.4.4 Air France

In an effort to control costs prior to its float, the management of Air France proposed a shares-for-wage scheme to its pilots. Although the pilots' union accepted the shares-for-wage in principle, the union called a 10-day strike leading up to the soccer World Cup in June 1998 when the negotiation broke down. An agreement was eventually reached to provide pilots with an aggregate 10 per cent shareholding in the airline in exchange for a 15 per cent wage cut, on a voluntary basis. Those who accepted had their wage scale frozen over the following seven years. In addition, a two-tier wage scale, with lower wages for new pilots, was negotiated under the agreement.

5.4.5 Cathay Pacific

A recent example, with the outcomes yet to be determined, is Cathay Pacific's ongoing negotiations with its pilots. Having reported its first loss in 35 years during 1998, the management of Cathay Pacific proposed a 27 per cent reduction in wages for pilots in exchange for stock options in the company. The proposed reduction in wages is dramatic, considering that Cathay Pacific historically struggled with a shortage of pilots and gave expatriate pilots a 25 per cent raise in 1989 in order to attract and keep them in Hong Kong. The proposal was sent to each pilot in order to communicate directly with individuals, rather than through the union. To date, no agreement has been reached and the initial deadline of 9 April 1999 has been deferred until 30 May to provide the pilots with more time to study the proposal in detail.

6.0 Qantas Employee Share Ownership Scheme

Following the float, Qantas implemented an employee share ownership scheme which granted bonus shares to eligible employees. The link between company performance and the issue of shares was strengthened progressively. As the shareholding of individual employees has grown, anecdotal evidence suggests that staff have taken broader interest in the long-term financial performance of the group.

6.1 Qantas Staff Share Plan I (QSSPI)

There were two allocations made under QSSPI. The first allocation under QSSPI was in July 1995, followed by another in November 1996. In both instances, the allocation was approximately AUD 500 worth of ordinary shares, at market value on the respective issue dates. Permanent employees, or temporary and casual employees with 12 months continuous service, were considered eligible if they were employed by Qantas when the share offer was announced and at the time the shares were issued. The shares were issued with full ordinary shareholder rights.

6.2 Qantas Staff Share Plan II (QSSPII)

With the change in the Tax Assessment Act in July 1996, Qantas looked to update some of the terms and conditions under QSSPI. Minor modifications to the terms and conditions in QSSPI required shareholder approval and a re-signing of the contract with individual employees under the name of QSSPII.

The first allocation of bonus shares under QSSPII took place in February 1998. Approximately AUD 500 worth of ordinary shares at market value on the issue date were allocated to employees, using the same eligibility criteria as those specified under QSSPI. A trading lock period of five years was specified.

The second allocation of bonus shares under QSSPII took place in February 1999. Qantas allocated approximately AUD 1,000 worth of ordinary shares at market value on the date of issue. The trading lock for this grant was reduced from five to three years.

Qantas advised staff that the increase in the value of the share allocation was in recognition of their contribution to the airline's record profits in 1997/98. Accordingly, the eligibility criterion was tightened to those who were present for at least six months of the 1997/98 financial year. Specifically, employees (permanent full-time and temporary and casual employees with twelve months continuous service), employed continuously from 1 January 1998 to the allotment date, were considered eligible.

6.3 Qantas Profitshare Scheme

As the next progression towards linking share allocation to the financial performance of the airline, QSSPII was converted in December 1998 to the Qantas Profitshare Scheme. Unlike QSSPI & II, the new scheme introduced a pre-specified Performance Benchmark. Specifically, the Performance Benchmark is published so that employees are aware of the required return to shareholders prior to their participation in the share scheme.

The Board has set the Performance Benchmark for the 1998/99 financial year. If this Performance Benchmark is achieved, the eligible employees will be issued bonus shares calculated in a three-tier fashion (refer to Figure 1).

Figure 1. Share Allocation Under the Profitshare Scheme for 1998/99 Financial Year

1999 Audited Profit Before tax and Abnormals as a Percentage of the Performance Benchmark (%)	**Market Value of Bonus Shares to be Issued Under the Qantas Profitshare Scheme ($)**
100	500
105	750
110	1,000

6.4 Participation Rate and Communication

Anecdotal evidence suggests that staff perceive the Qantas employee share ownership scheme to have been of significant direct benefit. Consequently, the four share allocations made to date have enjoyed a participation rate (as measured by the proportion of those eligible employees accepting the allocations over the total number of eligible employees) of over 99 per cent.

The eligible employees are initially advised of share offers via internal communication. This is followed by a letter from the Chief Executive and a pamphlet outlining the terms and the conditions of the offer. Subsequent communication includes a letter, confirming the allocation of the shares. In some cases, communication is customised for new or existing participants in the share offer.

As a constant reminder of the link between each employee and the performance of the company, an update on the price of Qantas shares is included in the staff newsletter sent to employees each week.

6.5 Performance of Staff Shares Since QSSPI

Figure 2. Return on Staff Shares

Date	Staff Share Scheme	Shares Issued per Employee	Issue Price	Value	Dividend Shares* per Employee	Total Shares per Employee	Value as at 18.5.99 $4.58	Return on Investment
		(No.)	($)	($)	(No.)	(No.)	($)	(%)
Jul-95	QSSPI	263	1.90	500	60	323	1,479	196
Nov-96	QSSPI	268	1.87	500	46	314	1,438	188
Feb-98	QSSPII	216	2.31	500	16	232	1,063	113
Feb-99	QSSPII	275	3.63	1,000	5	280	1,282	28
TOTAL		1,022		2,500	127	1,149	5,262	110

* Assumes dividends reinvested in shares

Figure 3. Total Employee Shareholdings

Date	Staff Share Scheme	Employees Participating	Shares Issued per Employee[1]	Total Shares Issued	Total Shares Outstanding[2]	Per cent of Share Capital[4]	Value of Shares Issued[5]
		(No.)	(No.)	(m)	(m)	(%)	($m)
Jul-95	QSSPI	28,532	263	7.5	1,036	0.7	14.3
Nov-96	QSSPI	29,457	268	7.9	1,112	0.7	14.7
Feb-98	QSSPII	27,686	216	6.0	1,177	0.5	13.8
Feb-99	QSSPII	26,529	275	7.3	1,205 [3]	0.6	26.5
TOTAL			1,022	28.7		2.5	69.3

(1) Excludes dividend re-investment

(2) Total shares outstanding at the end of the financial year

(3) Total shares outstanding at the end of April 1999

(4) Assumes all staff remain employess of Qantas since allocation of shares; actual 2.1%

(5) Share price at the time of issue

6.6 Links to EBA IV

The accumulation of shares from past allocations, combined with increased share price, has resulted in a sizeable value of free personal capital. Consequently, the Qantas employee share ownership scheme is increasingly recognised as a significant part of the remuneration package. Over the past two EBAs, Qantas has been able to negotiate wage increases lower than the prevailing EBA wage outcomes for the industry through the inclusion of the Qantas employee share ownership scheme.

Staff have come to understand that productivity improvement measures achieved through enterprise bargaining and other mechanisms such as competitive tendering result in increased profit, which is then distributed to staff through the employee share ownership scheme.

7.0 Performance Since Privatisation

Qantas has enjoyed considerable success since privatisation in mid 1995. The motivation and enthusiasm of staff and their identification with the commercial objectives of the company have played an important role. The Qantas employee share ownership scheme has been a valuable part of this transformation.

Qantas believes that the current levels of employee share ownership may influence and build understanding of shareholder value.

7.1 Financial and Operational Performance

Figure 4 shows the key financial and operating results of Qantas since the privatisation in 1995.

Figure 4. Key Performance Results

		Jun-95	Jun-96	Jun-97	Jun-98
Financial					
Operating Revenue	$m	7,163	7,600	7,834	8,132
Earnings Before Interest and Tax	$m	471	504	517	582
Operating Profit Before Tax and Abnormals	$m	320	401	421	478
Operating Profit After Tax	$m	180	247	253	305
Earnings per Share	cents	18.0	24.2	23.6	26.8
Operational					
Revenue Passenger Kilometres	m	51,204	54,627	59,199	58,619
Available Seat Kilometres	m	71,225	75,930	81,440	81,537
Revenue Seat Factor	%	71.9%	71.9%	72.7%	71.9%
Productivity					
RPKs(1) per Employee	000	1,793	1,844	1,968	2,026
ASKs(2) per Employee	000	2,496	2,563	2,707	2,818

Source: Qantas Annual Report 1998

(1) RPK: Revenue Passenger Kilometres - the number of paying passengers carried, multiplied by the number of kilometres flown.

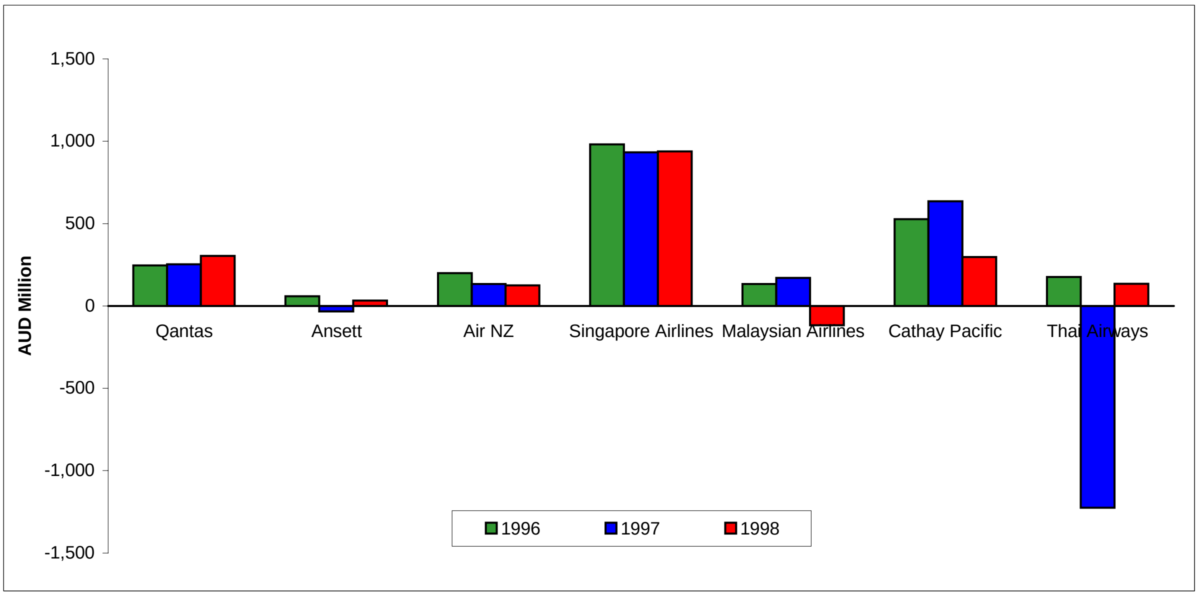
(2) ASK: Available Seat Kilometres - the total number of seats available for passengers, multiplied by the number of kilometres flown.

When 1998 results are compared to 1995, Qantas has recorded:

- 13.5 per cent increase in operating revenue;
- 49 per cent increase in operating profit before tax and abnormals;
- 49 per cent increase in the value of earnings per share; and
- 13 per cent increase in productivity, as measured by RPKs and ASKs per employee.

Despite the Asian crisis, Qantas has managed to improve profitability in contrast to many other Asian carriers (refer to Figure 5).

Figure 5. Comparative Profit after Tax

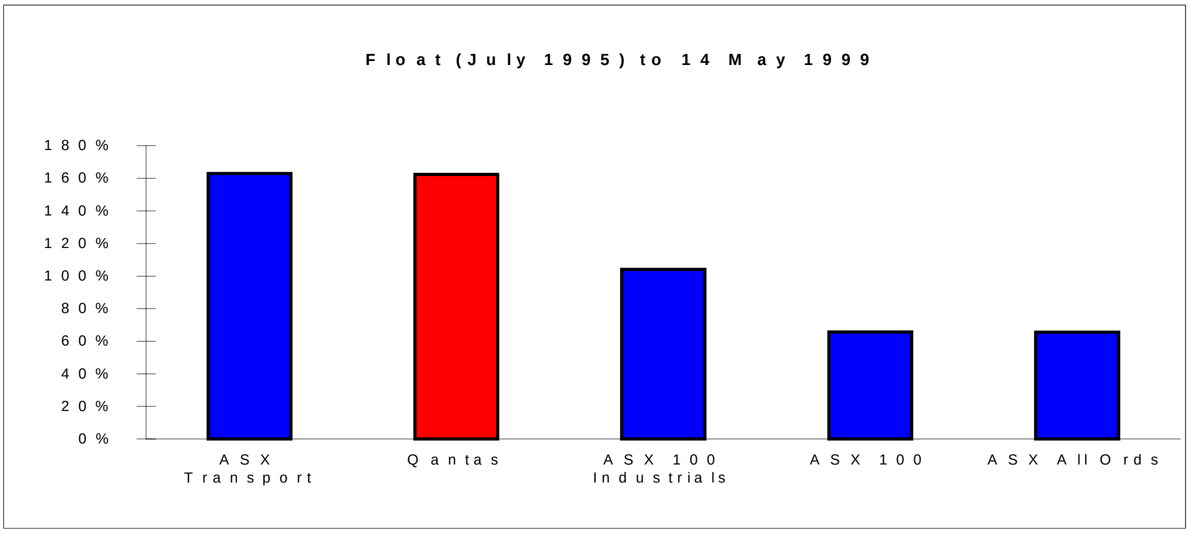


Source: Annual Reports 1996-1998

7.2 Stock Market Performance

The proven financial strength of Qantas over the past few years is reflected in its performance in the Australian stock market. Qantas shares have outperformed or equalled the relevant Australian Stock Exchange indices since privatisation, as illustrated in Figure 6.

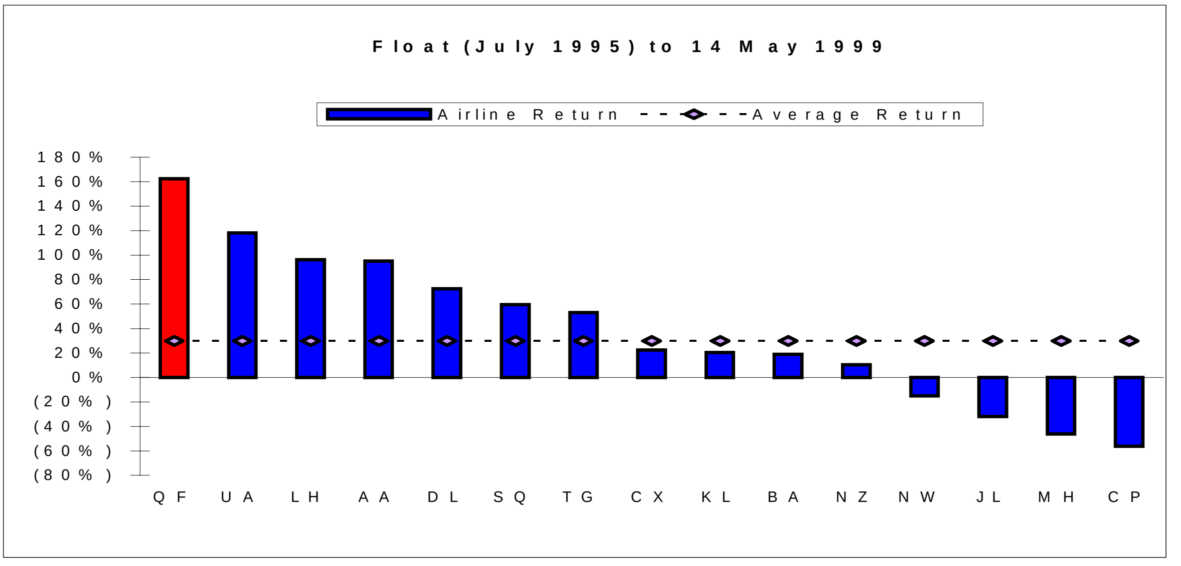
Figure 6. Qantas Total Returns versus Select ASX Indices.



Source: Bloomberg Equity Comp

A comparison of total shareholder returns against other major airlines (refer to Figure 7) shows that Qantas shareholders have enjoyed the highest total shareholder return since the float.

Figure 7. Qantas Return versus Selected Airlines



Source: Bloomberg Equity Comp.

Abbreviations: TG = Thai Airways; QF = Qantas; CX = Cathay Pacific; MH = Malaysian Airlines; SQ = Singapore Airlines; DL = Delta Airlines; JL = Japan Airlines; UA = United Airlines; LH = Lufthansa; AA = American Airlines; BA = British Airways; NW = Northwest Airlines; KL = KLM; CP = Canadian Airlines.

7.3 Other Performance Indicators

There are other performance monitors used in Qantas. The Customer Satisfaction Monitor studies, segregated into international and domestic operations, play an important role in gauging the service levels of the airline. Carried out successively over the past few years using comparable methodology and samples, the studies cover service levels attained on ground, in air, by class, by routes, and in the case of domestic operations, by flight frequency. Whilst many factors influence customer perceptions, the studies indicate that the relaunch of the international product and the implementation of customer service initiatives have had a positive effect overall on customer satisfaction. However, the bar is continually rising, with customers expecting ever-higher levels of service.

An external poll by the National Business Bulletin in January 1999 showed that Qantas remained Australia's corporate image leader. The airline has maintained its number one spot in the National Business Bulletin survey for ten consecutive years.

8.0 Conclusion

The employee share ownership scheme in Qantas has been an important component in the cultural change program which has contributed to the success of the airline since privatisation. This success can be measured in financial performance, productivity improvements, customer satisfaction and constructive industrial relations. The scheme is an effective means of communicating an understanding of shareholder value to employees and linking the performance of the airline to employee remuneration. This is wholly consistent with the long-term objective of Qantas of linking the fortunes of the company to an employee's own personal remuneration and to his or her own performance. Qantas needs the additional level of commitment this will engender as customer expectations rise and the level of competition in the aviation industry increases.

Government policy has an important role in encouraging greater levels of participation in employee ownership schemes by Australian companies. Specifically, the tax legislation should be examined for any ambiguity with respect to employee share ownership schemes. For example, Qantas recommends that further consideration be given to the dividend streaming issue to ensure the taxation laws and their administration by the ATO do not discourage companies from implementing employee share ownership schemes. In addition, Qantas recommends further reform to the tax legislation, such as increasing the tax-free threshold, which would encourage companies to participate in employee share ownership schemes. The 'all employee share scheme' under the proposed Year 2000 UK Finance Bill provides one example of how this can be done.

APPENDIX A

Dividend Streaming

There are a number of anti-avoidance provisions in the Income Tax Assessment Act 1936 which are designed to prevent streaming of distributions (either as dividends or capital) to certain shareholders in such a manner as to give rise to a tax advantage. The provisions are Sections 45, 45A, 45B and 160AQCBA.

Although the provisions are not intended to cover normal employee share acquisition schemes, they could potentially apply in circumstances where a company issues shares to employee shareholders only and not to other non-employee shareholders.

Qantas sought confirmation in the form of a binding private ruling from the Australian Taxation Office that these anti-avoidance provisions would not apply to QSSPII under certain commonly used procedures contained in the Taxation Administration Act 1953.

The ATO indicated that as a matter of policy it would not provide a binding private ruling to taxpayers including Qantas on these matters without an analysis of the taxation position of the individual employees receiving the shares (ie. approximately 30,000 employees) and its non-employee shareholders.

It is clearly impossible for Qantas to undertake an analysis of the tax position of each of its employees and its non-employee shareholders.

In recognition of this, the ATO provided a non-binding letter of comfort which indicated that "it is not envisaged that the Commissioner would make determinations that these sections would apply, provided the circumstances do not change".

However, this outcome is not satisfactory. The Government should remove the ambiguity in the widely drafted anti-avoidance provisions to facilitate the implementation of employee share ownership schemes.

APPENDIX B

Year 2000 Finance Bill (UK)

The recent budget announced a new "all-employee share scheme" to be introduced in the Year 2000 Finance Bill. The key features of the scheme include:

“Partnership Shares”

- allows employees to allocate up to GBP 1,500 each year of pre-tax income to shares in the employer's company (referred to as "partnership shares");
- may subject partnership shares to employee income tax when they are taken out of the scheme. The amount will depend on the timing; and
- provides employers with corporate tax deduction for partnership shares allocated.

“Matching Shares”

- permits employers to provide matching shares of up to two free shares for each partnership share (ie. up to GBP 3,000 in value each year);
- allows matching shares which are held in the scheme for three years or more to be tax-free for employees; and
- provides employers with corporate tax deduction for matching shares allocated.

“Free Shares”

- allows employers to provide free shares up to a value of GBP 3,000 each year;
- allows free shares which are held in the scheme for three years or more to be tax-free for employees; and
- provides employers with corporate tax deduction for free shares allocated.

Currently the UK Government is undertaking a consultation process in relation to the scheme.