



**TREASURER**

PARLIAMENT HOUSE  
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19 JUN 2000

Dr Brendan Nelson, MP  
Member for Bradfield  
Suite 8  
12-16 Tryon Road  
LINDFIELD NSW 2070

Dear Dr Nelson

A handwritten signature in cursive script that reads "Brendan".

Thank you for your letter of 21 February 2000 in your capacity as Chairperson of the Parliamentary Inquiry into Employee Share Ownership Plans regarding the implications of the reform of capital gains tax (CGT) and other business tax reforms for employee share schemes. You also enclosed a brief from Mr P. Thomas, Partner, KPMG. I apologise for the delay in replying to you.

As you appreciate, the taxation of capital gains on shares and rights is a general issue for all who may invest in shares and rights. The taxation of employee share schemes is a narrower question. The tax law presently has special rules for taxing discounts provided to employees under employee share schemes; otherwise, the acquisition of rights and shares by employees is treated the same for tax purposes as acquisition by others.

Division 13A provides concessional tax treatment of the discount received on qualifying shares or rights acquired under employee share schemes. Discounts under such schemes are appropriately treated as a form of remuneration, and any concession is offered relative to this benchmark rather than by comparison with the taxation of capital gains.

Under Division 13A, the taxpayer can elect to be taxed immediately on the discount. In this case only the amount of the discount that is in excess of \$1,000 will be included in assessable income. Alternatively, assessment of the discount is deferred for up to ten years. In this case the discount is calculated, at cessation time, as the market value of the share or right reduced by the amount of any consideration paid or given by the taxpayer.

Your letter noted that the 50 per cent CGT reduction may make deferral of assessment of the discount less attractive. The former CGT indexation and averaging arrangements also influenced the choice between paying tax on the discount immediately or deferring it for up to 10 years. Several factors will influence which option might be more attractive.

In general, the shorter the period of deferral, and the greater the rate of growth in the value of the share or right, the more attractive the immediate taxation of the discount. Conversely, the longer the period of deferral, and the smaller the rate of growth in the value of the share or right, the more attractive the deferral of tax on the discount.

In relation to Mr Thomas' comments regarding the application of the general anti-avoidance rule it should be noted that the rule is not generally intended to apply to concessions provided for in the Income Tax Assessment Act.

Mr Thomas also indicated that entity taxation might not be the appropriate treatment for trusts delivering employee share schemes. Legislation implementing unified entity taxation will be introduced into the Parliament this year. Prior to the introduction of that legislation, the Government is undertaking consultations with interested parties. Mr Thomas' views on this matter will be taken into account as part of that process.

I hope these comments are helpful to you and to the Committee.

Yours sincerely

A handwritten signature in cursive script, appearing to read 'P. Costello', written in dark ink.

PETER COSTELLO