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9 October 2009

By email: taxboard@treasury.gov.au

Review of Employee Share Schemes
The Board of Taxation
c/- the Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam,

Review into elements of the taxation of employee share scheme arrangements

Please find attached our submission relating to the Board of Taxation's review into elements of the taxation of employee share scheme arrangements.

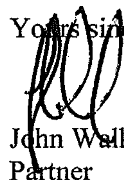
Our submission comments on the issue of how best to determine the market value of employee share scheme benefits. In summary, our submission argues that:

- a point in time market value should be used as the applicable value for shares listed on a prescribed stock exchange. This is the method which is used in all countries that we are aware of, except Italy and Australia;
- the taxing point for stock options should be at exercise. Accordingly, the market value of the underlying shares can be used in valuing the right. This is generally the practice used throughout the world; and
- if the taxing point for stock options is at vesting (which we do not agree with), then the employee should be taxed on the intrinsic value of the option at the point of vesting.

The submission has been prepared with the support and input from a number of our multinational clients (and some of these clients have agreed to be listed in Appendix 1) and focuses largely on the issues that are of great concern to multinational companies.

Should you have any questions regarding our submission, please do not hesitate to contact John Walker on (02) 8922 5206 or Erica Kidston on (02) 8922 5665.

Yours sincerely,



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Baker & McKenzie LLP Submission
Review into Elements of the Taxation of Employee Share Scheme Arrangements

In response to the Assistant Treasurer, Senator Nick Sherry's Press Release No. 17 on 24 July, 2009 and the Board of Taxation's (the ***Board's***) Press Release No. 28 of 7 September 2009 where the Board invited submissions for its review into elements of the taxation of employee share scheme arrangements, we provide our comments on the issue of how best to determine the market value of employee share scheme benefits.

In particular, we are focusing our comments on the valuation of shares and rights to acquire shares of publicly traded companies with a substantial trading volume on a prescribed stock exchange.

Baker & McKenzie LLP, a global law firm with over 3,900 lawyers in 67 offices in 39 countries, advises over 300 multinational corporations with regard to their global equity plans, most of whom make grants to Australian employees. In this regard, we maintain a current global database of the tax treatment of share plans in 53 countries. We also advise on a regular basis with regard to the taxation of internationally mobile employees and have direct ongoing experience with regard to the administrative issues relating to taxation of equity interests received by employees. Thus, we feel uniquely qualified to comment on the best way to determine the market value for employee share scheme benefits.

1. Type of Awards

In discussing valuation issues, we find it useful to separate the major types of equity awards granted to employees and other service providers by listed public companies. These fall generally into four categories:

(1) stock options;
(2) restricted stock;
(3) restricted stock units; and
(4) employee stock purchase plans.

(1) Stock options

Stock options are probably the most prevalent form of equity granted worldwide by public companies. They provide the employee with the right to purchase shares at a specific price (exercise or strike price) following a specified service period (vesting period) up until the option expiration date. The exercise price is typically the market value of the underlying shares on the date of option grant; the vesting period is normally from one to five years (often in tranches vesting annually or even quarterly) and the overall term of the option is typically 7-10 years.

(2) Restricted stock

Restricted stock are awards of actual shares for no consideration, but the shares are forfeited by the employee if he/she ceases employment before a specified vesting period. Like options, this vesting period is usually between one and five years, and is often in tranches.

(3) Restricted stock units

Restricted stock units awards are similar to restricted stock awards except that no shares are issued at grant of the restricted stock unit. Rather, following a specified vesting period, shares are issued. Until the specified vesting date(s) (again, typically one to five years), the employee has only a contractual right against the issuing company to receive shares at the specified vesting date(s), should he or she remain employed through that date.

(4) Employee stock purchase plans

Employee stock purchase plans offer employees the right to purchase shares from the company, typically at a discount of 5% - 15% from the market value. In some cases the price is determined by reference to the market value of the shares at the beginning and end of a specified purchase period (typically 3 or 6 months), whichever is lower.

There are of course variations on these types of awards (such as stock appreciation rights which are like stock options except the employee, on "exercise", receives only the appreciation in the underlying share value between grant and exercise) or matching share purchase program (in which employees purchasing shares at current market value receive matching shares from the company for no additional consideration).

2. Principles of Determining Market Value for Listed Company Employee Share Interests

Australia, like almost all countries around the world, determines market value of listed securities by reference to the current trading price on an established market. This is reflected in the guide titled "Market Value for Tax Purposes," issued by the Australian Tax Office (***ATO***), in several places.

First, as a general rule, the ATO's guide to the determination of market value states that "where a market exists for an asset, that market is widely considered to be the best evidence of market value of the asset." Further, with respect to listed ordinary shares traded on a daily basis, the ATO's guide provides that a taxpayer "may be able to rely on the appropriate share market as the source for valuing a listed ordinary share." If the stock is relatively liquid and does not exhibit price volatility, a taxpayer may, in certain circumstances, refer to a "point in time valuation (such as the closing price of a share)" to determine the appropriate market value.

We note that the Explanatory Memorandum to the Exposure Draft Bills (***Draft Package***[1]) released on 14 August 2009 indicates that the ordinary meaning of market value is used to determine the market value of ESS interests. However, in our view, this creates significant uncertainty for employers and employees.

With respect to the valuation, for tax purposes, of restricted stock, restricted stock units and employee stock purchase plans, all of which relate to the value of shares on a specified vesting or purchase date, we would submit that a point in time market value on the relevant date is the appropriate value. This is in fact the method used in all countries we are aware of, except Italy, which mandates use of the prior month's average price for tax purposes.

In this regard, and in a manner inconsistent with the overwhelming international practice, we note that Division 13A of the *Income Tax Assessment Act 1936* seemingly mandates that for listed shares market value is the weighted average trading price over a one week period ending on the relevant date of taxation.[2]

Although we understand, to some extent, the logic of an averaging approach, we believe it is ill-suited for valuing shares in an employee share plan for the following reasons:

(1) It does not reflect the value of the benefit the employee actually receives on the relevant day, as reflected by the price at which the employee could sell the shares on that day (which, in many cases, he or she will). For example, if the average weekly price was $12 per share, but the market price on the day of vesting was $10 per share and the employee sold the shares on that day at that price, he or she would have $12 of income and a $2 capital loss, which is not a desirable result from a standpoint of tax policy.

    It is true that a point in time price may be higher or lower than any number of averages, but it does reflect the very latest market factors. For example, if the company announces a new product, reports earnings or other significant events during the one week period prior to the taxing point, an average price (which includes pre-announcement trading prices) would not adequately or accurately reflect the updated market information. The fact of the matter is that an efficient market will have factored in, at any given point in time, all relevant information reflecting value.

(2) Use of a one week's weighted average methodology to calculate market value is hard for an employee to calculate and understand.

    An employee can easily grasp that, if he or she buys or sells or receives shares on a given day, the value of the shares on that day will apply. Making some

[1] The draft package consists of the following: (i) Exposure Draft for the *Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009* (Cth) and the *Income Tax (TFN Withholding Tax (ESS) Bill (Cth)* (the ***Bills***); (ii) Explanatory Materials (***EM***) for the Bills; and (ii) Exposure Draft for the *Income Tax Assessment Amendment Regulations 2009 (No.)* (Cth) and the EM for these regulations

[2] The Exposure Draft for the *Income Tax Assessment Amendment Regulations 2009 (No.)* (Cth) and the Explanatory Statement for these regulations released on 14 August 2009 still provides for the use of the weighted average trading prices when determining the market value of unlisted rights. However, the employee at least has a choice to determine the market value of the right according to ordinary principles.

arithmetical calculation of the prior week's weighted average trading value is an unnecessary and confusing complexity.

(3) As noted above, the rest of the world overwhelmingly uses a point in time value. A company with employee share awards in many countries finds it administratively difficult to administer and communicate to its employees an outlier method of valuation. It is preferable to permit a universal method of valuation, which is today possible (outside of Italy and Australia).

(4) With the new employer reporting (and, in some cases withholding) requirements in the proposed new draft legislation, it is even more critical to permit a uniform method of valuation, easily determined and communicated to employees.

We would suggest permitting, in the case of a company with a significant trading volume on a recognized stock exchange, the consistent use of a point in time market value on the relevant day, based on any consistently used reasonable method, *e.g.*, closing price, average high and low prices on the relevant day or prior day's closing price. For a variety of legitimate reasons, companies prefer one or other of these methods. So long as it is consistently applied, we see no reason not to permit any of these methods, as is allowed in the United States and almost all other countries of the world. This is also consistent with accounting rules governing the valuation of employee equity, which do not use averages over weekly or other periods.

3. Specific Considerations for Stock Options

For stock options (or stock appreciation rights), we have argued in our submission of 31 August 2009 in relation to the Draft Package for valuation to be made at exercise as is the overwhelming practice throughout the world (copy attached). If this is the taxing point, then there is no need to value the underlying right, just the market value of the share in excess of the exercise price, and no special valuation methods are required.

If for some reason Australia persists in taxing stock options at vesting, rather than exercise, then we would suggest permitting companies and employees to report and pay tax on the intrinsic value of the option at the point of vesting (*i.e.*, the positive difference between the market value of the underlying share and the exercise price). This method has several advantages.

First and foremost, it reflects the realizable benefit to the employee at the point of taxation, which appears to be a fundamental principle of share scheme taxation in Australia. That is, if the option is $2 in the money at vesting, an employee could exercise and sell and realize the $2 benefit. If the prescribed valuation method (such as the statutory formula currently in effect) requires recognition of a higher value, this may be a benefit the employee is never able to realize. We pointed out in our 31 August 2009 submission the highly undesirable effect of having an underwater option at vesting nevertheless taxable to the employee under the current statutory formula. This is enough of a negative factor to cause companies simply not to grant stock options to their Australian employees.

We do not believe other more sophisticated option valuation methods (such as the Black-Scholes and lattice methods used for accounting purposes) are appropriate to use in valuing employee stock options at vesting for the purpose of taxing the benefit. These methods are based on conditions not applicable under general tax concepts. An employee has no ability under the terms of almost all option grants, to transfer the option. Even if he or she could in theory transfer it, there is no market for an employee stock option. To value the option as though it were transferable to a willing buyer (or even an indifferent buyer) is simply not appropriate and would overstate the taxable benefit delivered to the employee.

We recognize that some form of formula may be necessary to value options taxed at grant, but the overwhelming majority of options issued by public multinational companies in Australia would not be taxable at grant (due to vesting conditions).

We reiterate that all of these above complications of valuations for stock options would be avoided if Australia were to line up with the rest of the world and tax options at exercise where the market value of the underlying shares can be used.

We note that there is a special rule that we recommend in the event the underlying shares are sold within 30 days of the taxing point of a stock option which is currently not provided for in the Draft Package.[3] As discussed in our submission of 31 August 2009, (at section 3 at page 5), we believe that the legislation should be clarified to make it clear that if an arm's length disposition of the shares is made within 30 days of the employee's taxing point, the employee should be able to take into account the exercise price to calculate his or her discount from the option exercise. Otherwise the discount would be overstated and the employee would receive no recognition for the fact that he or she has paid the exercise price.

4. Conclusion

In this era of globalization and increased employee mobility, it is very desirable to apply consistent methods of taxation to employee equity grants, many of which are made in Australia as part of larger worldwide employee share grants, absent some compelling tax policy reason to adopt a variation. Frankly we do not see any policy reason for Australia not to permit, for shares traded on an established stock exchange, the use of a point in time market value as the applicable share value for employee share interests.

Further, with regard to stock options, this point in time valuation method would be possible and desirable should Australia fall in line with the rest of the world and tax these awards at exercise.. If not, then the amount of taxable income should be based on the realizable benefit at the taxing point, which is the intrinsic value on the relevant day. Other valuation methods, resulting in greater value, will unduly penalize the employee, may result in phantom income being taxed (and never realized) and will be difficult for companies to administer.

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[3] We note that there is such a rule in Division 13A under s.139CC(3). This section applies where a share or right is disposed of at arm's length within 30 days of the cessation time. The amount of the discount is broadly the amount of the consideration received in respect of the disposal reduced by the amount paid for the share or right and, for a right that has been exercised, the exercise price.

Please note that under the Draft Package employers will be required to value these awards and report the taxable income to the ATO, unlike under the previous regime. This places even more importance on a valuation methodology that is easily administered and understood.

Appendix I

General Electric Company

Tupperware Brands Corporation

CSC

Teradata Corporation

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Santiago
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Toronto
Valencia
Washington, DC

31 August 2009

By email: essreforms@treasury.gov.au

Manager
Philanthrophy and Exemption Unit
Personal and Retirement Income Division
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sir/Madam,

Draft laws to reform of the taxation of employee share schemes
Baker & McKenzie submission

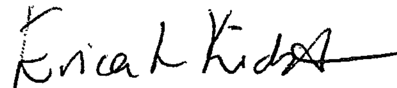
We refer to our previous submission dated 12 June 2009 in which we provided a comparison of the proposed changes with the taxation of employee share plans in 40 other countries. This submission showed that the proposed changes are out of step with other countries.

Please find attached our submission relating to the Government's draft laws regarding employee share schemes.

The submission has been prepared with the support and input from a number of our multinational clients (and some of these clients have agreed to be listed in Appendix 1) and focuses largely on the issues that are of great concern to multinational companies.

Should you have any questions regarding our submission, please do not hesitate to contact us.

Yours sincerely,



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Baker & McKenzie LLP Submission

Draft Package of Legislation Regarding Employee Share Schemes

We refer to the draft package of legislation released by the Assistant Treasurer, Senator Nick Sherry on 14 August 2009 ("Draft Package").[1] These remarks supplement our prior submission of 12 June 2009.

We are focusing these comments on six issues:

1. The need to have further consultation and a deferred effective date;
2. The taxation point at vesting for rights to acquire shares;
3. Disposal of shares acquired as a result of exercising rights within 30 days of exercise;
4. The taxation point for shares or rights to acquire shares at cessation of employment;
5. Valuation of market-traded shares;
6. Reporting and withholding requirements for employer or provider.

Baker & McKenzie LLP, a global law firm with over 3,900 lawyers in 67 offices in 39 countries, advises over 300 multinational corporations with regard to their global equity plans, most of whom make grants to Australian employees. In this regard, we maintain a current global database of the tax treatment of share plans in 53 countries. We also advise on a regular basis with regard to the taxation of internationally mobile employees and have direct ongoing experience with regard to the administrative issues relating to taxation of equity interests received by employees. Thus, we feel uniquely qualified to comment on the Draft Package.

1. The Need for Further Consultation and a Deferred Effective Date.

We note that the Economic References Committee Employee Share Schemes Report, August 2009, ("Committee Report") concludes as follows:

> "The committee recommends that the Government delay the implementation of the employee share scheme tax legislation in order to take note of the other reviews in this area, including the Productivity Commission and the Board of Taxation and the Henry reviews, to maintain legislative integrity and coherence." (Committee Report, Section 5.32, p. 36).

We strongly endorse this recommendation, and would add these further considerations:

Retroactive legislation (legislation covering grants made before the final legislation) is problematic in that it causes uncertainty and does not allow appropriate action to be taken to accommodate the proposed changes.

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[1] The Draft Package consists of the following: (i) Exposure Draft for the Tax Laws Amendment (2009 Budget Measures No. 2) Bill 2009 (C[th]) and the Income Tax (TFN Withholding Tax (ESS) Bill (C[th]) (the "Bills"); (ii) Explanatory Materials (EM) for the Bills; and (iii) Exposure Draft Regulations with EMs.

Many multinationals make global grants on the same date worldwide, and this is a significant undertaking of the Compensation Committee and/or Board of Directors. It is substantially problematic to carve out grants in a particular country pending a determination of the final legislative terms to be applied to the particular grant.

As noted below, if the final legislation in Australia persists in taxing stock options at vesting rather than exercise, many if not most multinationals will cease granting options to Australian employees (perhaps substituting other forms of equity awards). Similarly, even if they do grant options, employees may well not want to accept them if this results in disadvantageous tax treatment at vesting.

It is simply unsound policy to have this uncertainty concerning grants made since July 1, 2009 and up to final passage of the legislation.

Final legislation setting out such a fundamental change in the tax treatment of employee equity interests should be made prospective only, ideally with a delayed effective date.

2. The Taxation Period at Vesting for Rights to Acquire Shares.

The proposed taxation point for rights to acquire shares at the point at which there is no longer a real risk of forfeiture (what we will refer to herein as taxation of options at vesting) represents unsound tax policy for a number of reasons.

In this regard it is worth noting that stock options remain the most prevalent form of employee equity award worldwide, so this fundamental change in tax treatment is extremely significant (and troubling).

As we noted in our previous submission, taxation of options at vesting is a significant departure from international practice. Out of the 53 counties in our on-line database, only one, the Slovak Republic, effectively taxes options prior to exercise.[2]

We note that the Assistant Treasurer has referenced the deferral of tax from grant to vesting or beyond as a "deferral concession,"[3] and the concept that any taxation of employee scheme rights beyond grant is in effect a tax concession.

Frankly we question this conclusion as a matter of tax policy and certainly this concept has not found its way into tax policy considerations of employee stock options in other countries.

It is true as a general preposition that deferral of a taxable event may be viewed as concessionary, such as delayed taxation of superannuation contributions. However, when deferral comes at the cost of converting what might otherwise be tax-favored capital gains treatment into highly taxed regular income, the concessionary label becomes questionable.

A stock option may have little or no value at vesting, so taxing at that point, while leaving all appreciation in value between vesting and later sale after exercise to be taxed as a capital gain, might itself be considered concessionary where capital gains tax discount treatment is available (*i.e.*, if the shares acquired upon exercise are held for at least 12 months).

Under the current valuation tables, a 7 year option vesting after 3 years which is only at-the-money at vesting would be taxed at 9.5 % of the underlying share price. That option has four years of life left beyond the proposed taxing event. If the stock price goes up by 50% in the

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[2] This includes all OECD countries. It is true that, in theory, Belgium taxes options at grant and Switzerland (in some cantons) may tax options at grant or vesting. However, there exist readily available means for an employer issuing options in either country to effect taxation at exercise.

[3] The Hon. Senator Nick Sherry Assistant Treasurer, "Taxation of Employee Share Schemes," Press Release No. 011, 1 July 2009.

following 4 years when the option is exercised, the 40.5% additional gain will be taxed as a capital gains and if the shares acquired as a result of the exercise of the option are held for at least 12 months only half of the capital gain will be included, so in essence only 29.75% of the gain will be taxed at the normal marginal rate.

In the United States, for example, Section 83 of the Internal Revenue Code is at some pains to ensure that options will NOT be taxed until exercise. Only market-traded or freely transferable options are taxed prior to exercise (We are not aware of any company that has employee stock options that are market traded). The reason for this is to ensure government revenues are protected by precluding option gains from being converted into capital-gains income.

Any concession due solely to deferral is relatively modest, particularly in this interest rate environment. Whatever the concession is, it is more than offset by the additional taxes that would be collected at sale at regular tax rates, even with a modest stock appreciation between vesting and sale following exercise.

In fact, Australia, by not providing an employer tax deduction when the employer uses its shares to satisfy option exercises, already penalizes companies issuing stock options to employees compared to most countries which do permit such deductions. Adding harsh employee taxation on top of adverse corporate tax rules would put Australia even more adverse to use of employee stock options from a tax policy perspective.

Taxation of employee stock options at vesting is bad tax policy for another reason as well. The employee is taxed before the income is realized. Hence, tax is owed before funds are available to pay the tax. At best this may result in suboptimal economic choices by employees to exercise the option early to pay the tax (also defeating the purpose of the option to align employee and shareholder interests). Also taxing an underwater option just seems fundamentally unfair, in that the option may never have economic value. This is exacerbated by the proposal under the Draft Package that no refund will be available in these circumstances, but rather the employee will suffer a capital loss that can only be offset against capital gains. This could result in a taxpayer being out of pocket for a considerable period especially in times of falling share prices[4].

Third, by taxing options at vesting and being out of step with essentially all other countries, there are significant administrative and other problems associated with employees transferring into and out of Australia.

A mismatch of taxation timing on options is always a problem for internationally mobile employees. A mobile employee in Australia at vesting of an option will be subject to Australian tax at that time, but not home country tax (this is only due at exercise). This significantly complicates tax credit realization and tax equalization policies.

We note further that many companies utilize phased vesting for option grants. Annual, quarterly or monthly vesting is not uncommon. Some U.S. multinationals even have daily vesting. Taxation at vesting is extremely burdensome and complicated in this situation.

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[4] As an example, assume a 1,000 share option grant with an overall term of 10 years, full vesting after 3 years, and a fair market value of the shares at grant (and exercise price) of $10 per share. If the fair market value of the shares at vesting is $9.80 (the option is underwater by $0.20 per share), the employee will nevertheless be taxed under the statutory formula (Section 83A-315.02, 315.05 – 315.09) on $1.50 per share, or $15,000, notwithstanding the fact that there is no intrinsic value in the option and may never be. If the shares never rise above $10 per share during the option term, the employee will never have realized any economic benefit, but nevertheless will have been taxed on $15,000. This simply cannot represent sound tax policy and may well lead employers to resist granting options to Australian employees or to Australian employees rejecting the grant of the options.

Finally, we frankly find no logical or valid policy reason for taxing any employee share interest at cessation of employment, as discussed below.

3. Disposal of shares acquired as a result of exercising rights within 30 days of exercise.

There seems to be no rule in the Draft Package that replicates section 139CC(3) of the current rules. Section 139CC(3) applies where a share or right is disposed of at arm's length within 30 days of the cessation time (referred to as the 30 day rule). The amount of the discount is broadly the amount of the consideration received in respect of the disposal reduced by the amount paid for the share or right and, for a right that has been exercised, the exercise price.

Under the Draft Package, where the taxing point is deferred, the employee's assessable income includes the market value of the ESS interest at the ESS deferred taxing point reduced by the cost base of the interest (proposed section 83A-110). If the right is regarded as the relevant ESS interest, it is difficult to argue that the exercise price is included in the cost base of that asset. Under the current drafting, the 30 day rule is contemplated in working out the timing of the discount, but not in working out the amount of the discount. In our view, the draft bill should be amended to reflect the current position so that the exercise price is taken into account in calculating the discount in these circumstances. Otherwise the discount would be overstated and the taxpayer would receive no recognition for the fact that he or she has paid the exercise price.

4. The Taxation of Shares or Rights to Acquire Shares at Cessation of Employment.

The Draft Package proposes that cessation of employment be one of the taxation points for deferred rights and shares. Thus, both stock options and restricted stock units (RSUs), rights to acquire shares for no consideration after a specified vesting period, would be taxed at cessation of employment even if not vested and subsequently forfeited.

As noted in the submission of the Corporate Tax Association, and as quoted in the Committee Report (at page 45); this policy of taxation at termination of employment "stems from the misguided belief by policy makers" that the timing rules "are highly concessional and should therefore be withdrawn immediately when the employment relationship comes to an end."

This is simply layering one bad tax policy on top of another. As noted above, deferring taxation of an RSU until vesting, or a stock option until exercise, is not concessionary and may in fact increase government revenues by precluding regular income otherwise taxable at marginal rates from being converted to capital gains which may be eligible for CGT discount treatment.

Again, by taxing when the employee has realized no taxable benefit, this contains an element of unfairness and results in over-taxation in many instances.

We are aware of no other country that taxes employee shares or rights upon cessation of employment.

The only reasonable justification for this approach is to protect Australian tax revenue with respect to employees transferring out of Australia, but that issue is addressed by the new reporting requirement, which will result in the Australian source income being reported by the Australian employer.

5. Valuation of Market-Traded Shares.

The Draft Package does not adequately address the determination of market value for listed securities. As the concept of market value is such a crucial aspect of the Draft Package, we submit that the introduction of any changes should be deferred until the Board of Taxation has completed its review of valuation aspects.

Given the new requirement that employers report the market value of employee shares and rights at the taxing point, it is imperative to have simple and administrable valuation rules. Further, the proposal outlined in the draft explanatory memorandum to allow taxpayers to choose a valuation methodology that fits their circumstances merely introduces uncertainty and confusion.

We also note that proposed section 83A-315 appears to be inconsistent with the principles outlined in the draft explanatory memorandum. Section 83A-315 appears to dictate that if the regulations specify an amount for the purposes of the section in relation to the interest, that amount should be used rather than market value. The drafting of this provision does not appear to allow the taxpayer any flexibility to use market value in a case where the regulations specify an amount.

Most of the valuation problems in the Draft Package, as applied to companies whose schemes are traded on an established stock exchange, relate to the ill-advised attempt to tax stock options prior to exercise. If employee stock options are taxed at exercise, then there is no need to undertake the difficult task of placing a value on a non-transferable and non-traded employee stock option. Instead, the market value of the share on the stock exchange on the date of exercise (or sale price if the employee exercised and sells in a same-day sale transaction) can be used.

We note the provision in current law requiring use of a prior one-week average to value traded securities is itself out of synch with global practice, and potentially over- or undervalues shares which have had a significant shift in market value during the prior week. Unless trading in the shares is very thin, we see no reason not to allow use of the market price on the relevant day (or prior day's close) as the appropriate market value.

6. Reporting and withholding requirements for employer or provider

We note that in relation to the proposed withholding and reporting rules, the exposure draft bill refers to the provider of shares or rights having obligations, while the draft explanatory memorandum refers to the employer of the employee having those obligations. Although imposing those obligations on the provider is consistent with other provisions of the *Taxation Administration Act* (Cth) 1953, it is not appropriate in all cases in relation to the provision of shares or rights under an employee share scheme. Where the provider of a share or right is a non-resident holding company of an Australian employer, for example, a U.S. or U.S. multinational making grants to employees of its Australian subsidiary, it is not appropriate to impose withholding and reporting obligations on the non-resident especially if the non-resident holding company does not have a taxable presence or permanent establishment in Australia. In these circumstances it would be more appropriate to impose the obligations on the Australian resident employer as the employer would have the infrastructure in place to pay any TFN withholding tax, would have an ABN, would have received notification of employees' TFNs and would be able to access all of the relevant information.

CONCLUSION

We strongly urge a delay in the adoption of these significant changes to the taxation of employment equity awards set forth in the Draft Package to allow more complete analysis of all the relevant considerations. Also, as these matters are considered, we urge the Australian

government to consider adopting taxation at exercise for employee stock options to come in line with uniform global practice. We do not believe this represents any tax concession and, particularly when combined with employer reporting requirements, will likely increase tax revenues.

Further, given that, under the Draft Package, the tax consequences for an employee of acquiring ESS interests depend upon the structure of the employee share scheme, any changes to be introduced should be legislated well before the application date to allow ample time for the relevant documents to be drafted or amended (and where relevant, allow shareholder approval to be obtained) and for the employee to obtain advice on the tax implications in respect of their participation.

As a final note, we have shared this submission with clients over the last few days and, despite the short time frame for them to review it, the list of clients attached as Appendix I have subscribed to our comments. We have heard no objections or contrary views to those expressed herein from any of our clients.

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Appendix I

Asia Pacific
Bangkok
Beijing
Hanoi
Ho Chi Minh City
Hong Kong
Jakarta
Kuala Lumpur
Manila
Melbourne
Shanghai
Singapore
Sydney
Taipei
Tokyo

Europe & Middle East
Almaty
Amsterdam
Antwerp
Bahrain
Baku
Barcelona
Berlin
Brussels
Budapest
Cairo
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Geneva
Kyiv
London
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Milan
Moscow
Munich
Paris
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Riyadh
Rome
St. Petersburg
Stockholm
Vienna
Warsaw
Zurich

North & South America
Bogota
Brasilia
Buenos Aires
Cancun
Caracas
Chicago
Chihuahua
Dallas
Guadalajara
Houston
Juarez
Mexico City
Miami
Monterrey
New York
Palo Alto
Porto Alegre
Rio de Janeiro
San Diego
San Francisco
Santiago
Sao Paulo
Tijuana
Toronto
Valencia
Washington, DC

Cisco Systems, Inc.

Computer Sciences Corporation

Donaldson Company, Inc.

EMC Corporation

ENVIRON Australia Pty Ltd

General Electric Company

Genzyme Corporation

Hess Corporation

Kinetic Concepts, Inc.

NetSuite Inc.

Qualcomm Incorporated

Quantum Corporation

Schlumberger Limited

Sun Microsystems, Inc.

Teradata Corporation

The Walt Disney Company

Tupperware Brands Corporation