

TECHNICAL DECISION SUMMARY > PRIVATE RULING

WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKATAUNGA  
TŪMATAITI

# Share scheme taxing date

Decision date | Rā o te Whakatau: 19 September 2024

Issue date | Rā Tuku: 18 December 2024

TDS 24/24

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## Subjects | Kaupapa

Income tax: Employee share scheme; vesting of shares to participants; share scheme taxing date

## Taxation laws | Ture tāke

All legislative references are to Income Tax Act 2007 unless otherwise stated.

## Summary of facts | Whakarāpopoto o Meka

1. The Applicant was a group of companies (the Group) that operated an employee share scheme (the Plan).
2. The Arrangement was the vesting of awards and transfer of shares to participants in the Plan.
3. Company A, as the parent company of the Group, invited certain employees to participate in the Plan. The invitation letter specified the number of awards granted, the date granted and the vesting conditions. Employees that took part in the Plan and were granted awards are referred to in this summary as "Members".
4. Each award represented the right to receive one share in Company A for nil two years from the date of the grant, subject to meeting the vesting conditions. There were two categories of vesting conditions. One category required continued employment over the two years, the other only required the passage of two years' time. No Member was entitled to vote or attend a meeting of the shareholders of Company A or receive any dividends by virtue of holding an award.
5. The awards were deemed exercised on the date on which all the vesting conditions were satisfied or waived by the Board, and this is when the awards vested to the Members. As soon as practicable after the deemed exercise of an award, Company A arranged for the Member to receive the requisite number of shares (Resulting Shares). PAYE was deducted from taxable value of the awards vested.
6. The awards (and in some circumstances the Resulting Shares) were subject to forfeiture or clawback in special limited circumstances under the Plan. Such circumstances could include termination of employment due to serious misconduct or a material breach of the terms of employment.

7. The Group maintained an employee share schemes trust (X Trust) for the purposes of holding shares on behalf of the Group in respect of various share schemes offered to employees.
8. Prior to the introduction of the Plan, the X Trust was primarily used to hold shares under schemes that provided shares to employees with restrictions attached. A clause of the deed establishing the X Trust (Trust Deed) provided that shares held by the trustee that were not for the time being allocated by the trustee under a scheme (Surplus Shares) may be retained by the trustee and held on trust until allocated or reallocated under a scheme, or may be sold or otherwise disposed of or dealt with at the direction of Company A.
9. On the day the awards are deemed to be exercised by a Member under the Plan (ie, on the date on which all the vesting conditions are satisfied or waived by the Board), Company A instructs the trustee to deliver the Resulting Shares out of its stock of Surplus Shares to the Members. The trustee communicates with the share registry service provider to transfer the Resulting Shares to the Member's personal account.

## Issues | Take

10. The main issue considered in this ruling was:
  - When did the share scheme taxing date arise under s CE 7B?

## Decisions | Whakatau

11. TCO concluded that:
  - The share scheme taxing date for a Member in the Plan arose on the date the awards vested to the Member under s CE 7B(1)(a), provided the awards had not been forfeited under the Plan prior to this date.

## Reasons for decisions | Pūnga o ngā whakatau

### Issue | Take: When does the share scheme taxing date arise under s CE 7B?

12. Section CE 7 defines employee share scheme for the purposes of the Act. The Plan met this definition by offering awards (rights to shares in Company A) to employees of the Group that were invited into the Plan. None of the exclusions in s CE 7(b) applied.

13. Where there is an employee share scheme, the employee has employment income under s CE 1(1)(d) of an amount equal to a benefit received under an employee share scheme. The amount of the benefit is calculated on the share scheme taxing date applying the formula set out in s CE 2(1).
14. The issue at hand was when the share scheme taxing date arises. This was important as this was the time the shares in Company A must be valued to calculate the Member's benefit under s CE 2(1).
15. Section CE 7B(1) defines share scheme taxing date. In summary, it sets out that the share scheme taxing date will arise on the earlier of the following dates:
  - Under para (a) the first date when shares are held by or for the benefit of the employee, and there are no provisions in the scheme that affect the employee's rights to shares as set out in subparas (i) to (iii). Relevantly:
    - An example of a provision that might defer the share scheme taxing date under s CE 7(b)(1)(a) is if there is a material risk that a right or requirement in relation to a transfer or cancellation of the shares might operate (as per subpara (i)).
    - When determining whether any such deferral occurs, certain rights or requirements as set out in sub (2) can be ignored. An example is a right or requirement to transfer shares for market value consideration at the time of transfer (as per para (a)).
    - The examples illustrate when there is a "material risk" that a right or requirement in relation to a transfer of shares might operate. If an employee forfeits their shares by simply resigning and leaving employment there is a material risk of forfeiture (example 1). However, if an employee only forfeits their shares if dismissed for serious misconduct, that that is not a material risk of forfeiture (example 2).
  - Under para (b) the date when the shares or rights are cancelled or transferred to a non-associate.

### ***When are shares held by or for the benefit of a Member***

16. TCO first considered when shares were held by or for the benefit of a Member under the Plan for the purposes of s CE 7B(1)(a).
17. At issue was whether the Surplus Shares could be considered held for the benefit of a Member. Case law such as *Gillespie v City of Glasgow Bank* (1879) 4 App Cas 632 (HL) and *Case D27* (1980) 4 NZTC 60,621 support the following propositions:
  - "For the benefit of" has been said to mean "in trust for".

- To hold shares for the benefit of someone means you are not beneficially the owner of the shares. The person for whose benefit you hold the shares is the beneficial owner.
18. Based on the Plan rules and the terms of X Trust, TCO did not consider the Surplus Shares were held for the benefit of any Members in the Plan prior to the awards vesting. This was primarily for the following reasons:
- The terms of the Plan did not state that there are any shares held anywhere for the Member, and the Member did not have any interest in any shares under the Plan until the vesting conditions were met. The Plan rules specified that no Member was entitled to vote or attend a meeting of shareholders of Company A, or receive any dividends declared by Company A, by virtue of holding an award.
  - The X Trust did hold shares for employees under some of the Group's other plans. Where it did so, the Trust allocated the shares to the relevant employee and a sub-register of shares was maintained with the employee's name allocated to those shares. Under the Trust Deed, the employee would then have a beneficial interest in those shares that had been so allocated.
  - None of the shares in the X Trust were allocated to Members in the Plan in this manner and the Trust Deed did not apply to any Members with awards under the Plan.
  - The Trust Deed recognised that the X Trust may hold Surplus Shares that are not allocated under the Trust Deed or a share plan at the particular time. The trustee was required to deal with those Surplus Shares at the direction of Company A. Dividends or distributions in respect of Surplus Shares were credited to the X Trust's cash fund (ie to be used for the purposes of the X Trust at Company A's direction).
19. In light of the above, a Member in the Plan could not be said to have any beneficial interest at all in the Surplus Shares held by the X Trust as they were not allocated to the Members under the Trust Deed or the Plan. The Plan itself specified that the Members had no rights to dividends or voting by virtue of holding an award. The Surplus Shares could be used for whatever purposes directed by Company A under the Trust Deed.
20. Accordingly, it was the view of TCO that the Surplus Shares were not held for the benefit of any Member in the Plan, at least prior to the vesting conditions being met.
21. TCO concluded that on the date the vesting conditions are met and the Member is deemed to exercise the awards, under the arrangement the trustee of X Trust will hold Surplus Shares at that point for the benefit of the Member. This is because Company A

has directed the trustee to deliver the Resulting Shares to the Member and the trustee has requested the share registry provider do this. Accordingly, from the vesting date, the X Trust will not be able to deal with the Surplus Shares in a way that is inconsistent with them being transferred into the Member's name – they are simply in wait to be transferred as soon as practicable. It was TCO's view that, at this point, they will be at the very least held by the trustee for the benefit of the Member.

### ***Risk of deferment***

22. TCO then considered whether any of the circumstances set out in subparas (i) to (iii) in s CE 7B(1)(a) applied to defer the share scheme taxing date.
23. After considering the clauses of the Plan rules and the limited circumstances in which the Resulting Shares could be forfeited or clawed back, TCO concluded that there was no material risk of forfeiture of the shares and therefore they did not result in the share scheme taxing date being deferred under s CE 7B(1)(a)(i).

### ***Overall conclusion***

24. Overall for this issue TCO concluded that on the facts of the arrangement:
  - Prior to the date the awards vest to a Member under the Plan, the X Trust was not holding the Surplus Shares for the benefit of an employee share scheme beneficiary of the Plan under s CE 7B(1)(a).
  - The Surplus Shares were held by or for the benefit of an employee share scheme beneficiary in respect of the Plan when the awards vest to the Member for the purposes of s CE 7B(1)(a).
  - That none of the deferral provisions in s CE 7B(1)(a) applied and the share scheme taxing date for a Member in the Plan arose on the date the awards vested to the Member under s CE 7B(1)(a), provided the awards had not been forfeited under the Plan prior to this date.