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Let's chat

Employee incentives – November 2025

With:

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Information provided is general in nature; precise application depends on specific circumstances

Overview

- Employee share scheme considerations
- Payroll tax considerations
- Employer reporting and withholding
- Employee incentive arrangements
- Commercial considerations

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Division 83A

- ESS Rules
- Applies where shares or rights to acquire shares in respect of employment offered at a discount
- Intend to ensure such 'value' via the discount taxed as assessable ordinary income
- Concessions available include: 'start up' concession, discount concession and deferral concession

Start up concession

- Start up company (unlisted, Australian resident, incorporated less than 10 years)
- Meet employee incentive concessions
- Minimum holding period (earlier of 3 years/employment ceases)
- Discount cannot exceed 5% (if issuing shares)
- Capital gains tax discount for ESS interest under start up concession from original grant date rather than exercise of option date

Discount concession

- Reduce discount on receipt of ESS interest by $1,000 in any year
- Relates to ordinary shares held for at least 3 years (or until employment ceases)
- Taxpayer must be employed by company and hold no more than 10% interest (and voting rights)
- Taxpayer taxable income, reportable fringe benefits and superannuation…no more than $180,000
- Scheme is non-discriminatory (available for all full-time employees) and there must be **no risk** of forfeiture in respect of the ESS interest

Deferral concession

- ESS rules deferred until a later time (not triggered on issue or grant)
- Taxpayer employed and ESS interests relate to ordinary shares equal to less than 10% of the total interest
- At least 75% of permanent participants with more than 3 years of service have or are entitled to acquire such interest*
- Such interest at risk of forfeiture (need for employment of a reasonable period or dependent on real performance criteria being met)
- Plan rules allow concession to apply*

Deferral concession

- Deferral taxing point
- No real risk of forfeiture under the scheme and any restrictions no longer apply
- Time employment or relationship ends
- 15 years after acquisition of the interest

Other considerations

- FBT not applicable under an incentive plan subject to the ESS rules
- Non-equity plans (i.e. phantom share plans) result in participants paying tax on marginal rate on value of any benefits received
- Plans offering no discount not subject to ESS rules
- Division 7A and financial assistance considerations where company lends to prospective shareholder

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Available options

- Issue or transfer shares
- Options to acquire shares
- Performance rights plans
- Phantom share plan
- Loan funded share plan
- Flowering share scheme
- Employee share trusts

Cash bonus

- So simple as not to include in prior slide
- Measurable performance hurdles
- Cash flow dependent
- Avoids ESS rules

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Issue or transfer shares

- Employees issued or transferred shares
- Immediately subject to vesting conditions
- One amount or over various tranches
- ESS rules can apply if issued at a discount
- Funding considerations for employee if they required to be consideration

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Options

- Employees issued options which can be exercised on certain conditions being met
- Paying exercise price entitles employee to acquire shares in company
- Exercise price predeterminable and can be market value of shares at the time of grant
- Options less restrictive under ESS rules
- Allows company to remunerate employees without cash outflow
- At risk of non-exercise of option

Performance rights

- Performance rights exercisable on performance hurdles met
- Shares issued for no consideration
- Like options, allows remuneration without cash outflow and provides flexibility around taxing point
- Performance hudles can be a mixture of financial and non-financial

Phantom share plan

- Mimics employee share plan without the formal equity offering
- Growth met with cash bonuses upon a sale, liquidation or exit event
- As no shares offered, employees have no voting rights
- Protects equity holders without introducing additional shareholders
- Downside for employees in that they receive no shares and that cash bonuses subject to payroll tax and taxable as income

Loan funded share plan

- Share sale agreement conditional on loan agreement and shareholders agreement
- Vendor financed and limited recourse
- Shareholders agreement crucial for all parties
- If company assisting financing, consider other issues
- Consider FBT issues where loan is interest free or low interest

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Flowering share scheme

- Special class of shares issued immediately
- Rights suspended until milestones are met
- Market value lower initially given lack of rights, and accordingly, no discount
- Importance to obtain valuation of shares on outside and appropriate drafting of share rights
- More complex to understand and acknowledge

Employee share trusts

- Trust established to hold shares and rights for employees
- Employees buy into the trust
- Trust acquires shares in company
- Complicated as control of structure needs to be considered
- Valuing can be difficult to buy into the trust

What's best?

Objective

- What are the key objectives of the incentive plan?
- Attracting or retaining staff; or motivating performance?

Eligibility

- Will participation in the incentive plan be available to all employees, or only a specific few

Funding

- How much funding is available for the scheme?
- Will participants be required to pay in order to participate in the incentive plan?
- Will the company or other person fund?

Tax implications

- Consider tax implications for the existing participants and incoming

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What's best?

Vesting conditions

- Are any conditions required to be met?

Impact

- What is the impact on existing equity holders?

Implementation

- How will be plan be implemented

Ongoing administration

- How will the ongoing administration be managed

Exit strategy

- How will employees be able to sell or otherwise deal with their shares, rights or options?

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What's out there?

- Succession plans for the next generation
- Motivates key employees to stick around and grow the business
- Too many cooks can make the broth difficult when it comes to leaving
- Incoming equity holders being unreasonable with requests
- Rewarding the team
- Sceptism with performance milestones

Contact details

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