

CR 2011/79 - Income tax: BHP Billiton Limited - Employee Long Term Incentive Plan



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Class Ruling

Income tax: BHP Billiton Limited – Employee Long Term Incentive Plan

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❶ This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 83A-15 of the *Income Tax (Transitional Provisions) Act 1997* (IT(TP)A 1997); and
- section 83A-340 of the *Income Tax Assessment Act 1997* (ITAA 1997).

All subsequent legislative references in this Ruling are to the ITAA 1997 unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies is employees of BHP Billiton Limited (BHP) and its subsidiaries (the BHP group) who:

- accept or are deemed to have accepted an invitation to participate in the Long Term Incentive Plan (the Plan);
- have been or will in the future be granted options and/or conditional rights to acquire fully paid ordinary shares in BHP (performance shares) under the Plan; and
- if they were granted performance shares under the plan prior to 1 July 2009, have not ceased employment with the BHP group prior to 1 July 2009 due to an uncontrollable event.

In this Ruling, a person belonging to this class of entities is referred to as a participant.

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 10 to 27 of this Ruling.

6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from the year ended 30 June 2005. The Ruling continues to apply until the year ending 30 June 2020 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Previous Rulings

9. The Commissioner has previously issued Class Ruling CR 2006/101 Income Tax: BHP Billiton Limited – Employee Long Term Incentive Plan in respect of the scheme described in paragraphs 10 to 27 of this Ruling. That previous ruling should now be read in light of this Ruling.

Scheme

10. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them form part of and are to be read with the description:

- The request for Class Ruling dated 8 June 2011;
- Rules of the BHP Billiton Limited Long Term Incentive Plan as approved by shareholders at the AGM on 22 October 2004;
- Amendments to the rules of the Long Term Incentive Plan as approved by BHP Billiton plc shareholders at the BHP Billiton plc AGM on 21 Oct 2010 and by BHP Billiton Limited shareholders at the BHP Billiton Limited AGM on 16 November 2010.
- Excerpt from Notice of General Meeting for the 2010 BHP Annual General Meeting.

Note: certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.

11. The operation of the plan is governed by the plan rules (rules). The rules were amended in 2010 with the amended rules applying to grants made under the plan from the year ended 30 June 2011.

12. References to the rules are a reference to the version of the rules that was in force at the time performance shares were granted.

13. As set out in the rules, the plan is aimed at creating a stronger link between performance and reward. Under the rules, eligible employees located in Australia who accept or are deemed to accept an invitation to participate in the plan are granted performance shares. The number of performance shares granted to a participant in respect of a performance year is determined by the Remuneration Committee of the Board of BHP (RemCo).

14. The rules give RemCo an overriding discretion to refuse to allow an eligible employee to participate in the plan even though the employee has accepted or been deemed to have accepted an invitation to participate in the plan. The applicant has advised that this discretion will not be exercised after the grant date of performance shares.

15. The first grant of performance shares under the plan was made in December 2004, in respect of the performance year commencing 1 July 2004. Performance shares have been granted each December since 2004, in respect of a performance year commencing on 1 July of the year of grant.

16. The vesting of performance shares granted to participants is subject to performance hurdles in respect of a 5 year performance period, commencing at the beginning of the performance year to which the performance shares relate. For example, the 5 year performance period for the performance shares granted in December 2004 commenced on 1 July 2004 and ended on 30 June 2009.

17. The performance hurdles compare the BHP group's total shareholder return (TSR) for the 5 year performance period against a 'median' TSR (weighted average TSR of a comparative group of companies in the same sector) for the performance period. For performance shares granted on or after 1 July 2010 the BHP group's TSR will be compared against companies in the same sector (to determine vesting of 67% of the performance shares) and against a broad stock market group, being the Morgan Stanley Capital Index World – a market capitalisation index that monitors performance of 1,500 stocks from around the world (to determine vesting of 33% of the performance shares). Performance hurdles are tested after the end of the 5 year performance period.

18. For performance shares granted prior to 1 July 2010 if, at the end of the performance period, the BHP group's TSR is equal to or less than the median TSR, all performance shares lapse. If the BHP group's TSR exceeds the median TSR by an outperformance target, 100% of the performance shares vest (that is in the case of performance shares granted in the form of options, the options become exercisable, and in the case of performance shares granted in the form of conditional rights, shares are issued or transferred to the participant). Vesting is pro rata between 0 and 100% if the TSR is between median TSR and outperformance.

19. For performance shares granted on or after 1 July 2010, the vesting outcomes are the same as for performance shares granted prior to 2010 except that 25% of performance shares vest if the BHP group's TSR is equal to the median TSR.

20. Participants are advised whether the performance hurdles for their performance shares have been satisfied on a date (the reporting date) determined by RemCo after the end of the performance period.

21. The rules give RemCo an overriding discretion to determine that performance shares will not vest notwithstanding that the performance hurdles have otherwise been met. The applicant has advised that this discretion will not be exercised after the reporting date or after the happening of an uncontrollable event.

22. For performance shares granted on or after 1 July 2010, the applicant has advised that RemCo only intends to exercise this discretion where it forms the view that the BHP group TSR does not properly reflect the financial performance of the BHP group over the performance period. The applicant has advised that it is anticipated that such discretion would only be used in exceptional circumstances.

23. For performance shares granted on or after 1 July 2010, RemCo may also determine that vesting not be applied for any particular participant, should they consider that individual performance or other circumstances makes this an appropriate outcome. The applicant has advised that it is anticipated that this power would only be exercised in exceptional circumstances.

24. For performance shares granted on or after 1 July 2010, RemCo may prevent the exercise of some or all of a participant's performance shares, determine that some or all of a participant's performance shares are forfeited or reduce the number of performance shares which vest, if the participant owes any amount to BHP or a BHP group company. It is expected that this power to adjust vesting or exercise of performance shares or determine that some performance shares are forfeited would only be used in circumstances where a participant left the BHP group unexpectedly while owing money to the BHP group, and no other arrangement was in place, or could be put in place, for repayment of the money owed by the participant. The applicant has advised that these circumstances would not be expected to arise very often.

25. If a participant with performance shares that are not yet vested (unvested performance shares), is made redundant or ceases employment by mutual agreement (good leavers) they may retain a pro rata number of their performance shares. Unvested performance shares that are retained are subject to the vesting conditions outlined in the rules.

26. Unvested performance shares held by a participant who ceases employment due to the happening of certain prescribed uncontrollable events, which include death or disability, vest regardless of whether the performance hurdles have been satisfied.

27. The rules provide that discretions available to RemCo must be exercised reasonably and in good faith.

Ruling

28. Section 83A-340 of the ITAA 1997 applies to performance shares granted on or after 1 July 2009 if and when those performance shares become rights to acquire shares in BHP on the reporting date or (if earlier) the date a participant ceases to be employed by a company in the BHP group because of an uncontrollable event.

29. Section 83A-15 of the IT(TP)A 1997 applies to performance shares granted before 1 July 2009 if and when those performance shares become rights to acquire shares on the reporting date or (if earlier) the date a participant ceases to be employed by a company in the BHP group because of an uncontrollable event that happens on or after 1 July 2009.

Commissioner of Taxation

24 August 2011

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

ESS interests

30. Under subsection 83A-10(1), an ESS interest in a company is either a beneficial interest in a share in the company, or a right to acquire a beneficial interest in a share in the company.

31. The rules give RemCo an overriding discretion to refuse to allow an eligible employee to participate in the plan even though the employee has accepted or been deemed to have accepted an invitation to participate in the plan. The applicant has advised that this discretion will not be exercised after the grant date of performance shares.

32. Vesting of performance shares granted to a participant is subject to performance hurdles in respect of a 5 year performance period, commencing at the beginning of the performance year to which the performance shares relate. The rules give RemCo an overriding discretion to determine that performance shares will not vest notwithstanding that the performance hurdles have otherwise been met. The applicant has advised that this discretion will not be exercised after the reporting date or after the happening of an uncontrollable event.

33. For performance shares granted prior to 1 July 2010, the applicant has advised that RemCo only intends to exercise this discretion where it forms the view that the BHP group TSR does not properly reflect the financial performance of the BHP group over the performance period. The applicant has advised that it is anticipated that such discretion would only be used in exceptional circumstances.

34. For performance shares granted on and after 1 July 2010, RemCo may also determine that vesting not be applied for any particular participant, should they consider that individual performance or other circumstances makes this an appropriate outcome. The applicant has advised that it is anticipated that this power would only be exercised in exceptional circumstances.

35. Thus, at the time performance shares are granted under the plan, they are both conditional and subject to the exercise of RemCo's discretion. In these circumstances the Commissioner does not consider that the participant has acquired a right to acquire shares on grant of the performance shares.

Indeterminate rights

36. Section 83A-340 provides that where you acquire a beneficial interest in a right that later becomes a right to acquire a beneficial interest in a share, Division 83A will apply as if the right had always been a right to acquire the beneficial interest in the share.

37. In order for section 83A-340 to apply:

- the right acquired must be capable of becoming a right to acquire a beneficial interest in a share; and
- the right must become a right to acquire a beneficial interest in a share.

38. Section 83A-340 provides examples of rights which later become rights to acquire a beneficial interest in a share:

Example 1: You acquire a right to acquire, at a future time:

- a. shares with a specified total value, rather than a specified number of shares; or
- b. an indeterminate number of shares.

Example 2: You acquire a right under which the provider must provide you with either ESS interests or cash, whichever the provider chooses.

39. In both examples the right is a right to receive property but the precise extent or nature of that property has not yet been determined at the time of acquisition of the right. Such rights are capable of becoming a right to acquire a beneficial interest in a share because the capacity to acquire property is inherent in the nature of the right originally acquired. It merely remains to be determined whether the original right ultimately becomes a right to acquire a specific number of shares or some other form of property, such as cash.

40. At the time a participant is granted a performance share, the right that the participant obtains is a right to acquire a beneficial interest in a share:

- if service conditions and performance hurdles are satisfied; and
- RemCo does not exercise its overriding discretion (which must be exercised in good faith) to prevent the performance shares from vesting.

41. Whilst the rights that the participant obtains are the subject of a discretion, the rights which the participant obtains are considered to be rights to property. These rights can be distinguished from the rights that a discretionary beneficiary obtains when they become the object of a discretionary trust.

42. Where the trustee of a discretionary trust has an absolute discretion to apply the income and capital of a trust, the beneficiary's only rights are discrete, fixed and fully determined at the time of grant. As was noted in Class Ruling CR 2011/19 the Commissioner considers such rights cannot be indeterminate rights as they are not capable of becoming rights to acquire a beneficial interest in shares.

43. By contrast, where a participant is granted performance shares under the plan, the Commissioner considers the rights obtained are rights to property which are capable of becoming rights to acquire beneficial interests in shares.

44. Thus, where performance shares are granted to a participant on or after 1 July 2009 and those performance shares become rights to acquire shares in BHP on the reporting date or (if earlier) the date a participant ceases to be employed by a company in the BHP group because of an uncontrollable event, section 83A-340 of the ITAA 1997 will apply to those performance shares.

45. Similarly, where performance shares are granted to a participant before 1 July 2009 and those performance shares become rights to acquire shares on the reporting date or (if earlier) the date a participant ceases to be employed by a company in the BHP group because of an uncontrollable event that happens on or after 1 July 2009, section 83A-15 of the IT(TP)A 1997 will apply to those performance shares.

Appendix 2 – Detailed contents list

46. The following is a detailed contents list for this Ruling:

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; CR 2006/101;
CR 2011/19

Subject references:

- employee share schemes & options

Legislative references:

- ITAA 1997
- ITAA 1997 Div 83A
- ITAA 1997 83A-10(1)
- ITAA 1997 83A-340
- IT(TP)A 1997
- IT(TP)A 1997 83A-15
- TAA 1953
- Copyright Act 1968

ATO references

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