

# ***CR 2023/10 - Xero Limited - employee share scheme - Restricted Stock Unit and Option Plan***



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Status: **legally binding**

## Class Ruling

# Xero Limited – employee share scheme – Restricted Stock Unit and Option Plan

### **❶ Relying on this Ruling**

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

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

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### **What this Ruling is about**

1. This Ruling sets out the income tax consequences for employees of Xero Limited and its Australian employing entities (which are related or controlled entities) (Xero) who participate in the Xero Limited Restricted Stock Unit and Option Plan (Plan).
2. Details of this scheme are set out in paragraphs 14 to 36 of this Ruling.
3. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

**Note:** By issuing this Ruling, the ATO is not endorsing the Plan. Potential participants must form their own view about the Plan.

### **Who this Ruling applies to**

4. This Ruling applies to you if you are an employee of Xero who:
  - is granted a Restricted Stock Unit (RSU) under the Plan, and
  - is a resident of Australia as defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936).
5. This Ruling does not apply to anyone who is subject to the taxation of financial arrangements rules in Division 230 in relation to the scheme outlined in paragraphs 14 to 36 of this Ruling.

**Note:** Division 230 will not apply to individuals unless they have made an election for it to apply.

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**When this Ruling applies**

6. This Ruling applies from 1 July 2021 to 30 June 2026.

**Ruling**

7. The Plan is an employee share scheme as defined in subsection 83A-10(2).
8. An RSU is an ESS interest as defined in subsection 83A-10(1).
9. Subdivision 83A-C applies to the RSUs granted to you as the requirements set out in section 83A-105 for tax deferral are satisfied.
10. However, Division 83A will not apply if the RSU is settled with a cash payment, and the cash payment will be included in your assessable income in the income year you receive the payment (section 6-5).
11. Where an RSU allocated to you vests and converts into a Xero share, the ESS deferred taxing point (as determined in section 83A-120) will (subject to the 30-day period in subsection 83A-120(3)) be at the commencement of the first trading window after the vesting period ends. This is the time when you are no longer restricted from disposing of your Xero shares (subsection 83A-120(7)).
12. However, for the 2021–22 income year, where an RSU allocated to you vested and converted into a Xero share, if you ceased employment with Xero on or before the ESS deferred taxing point set out in paragraph 11 of this Ruling, former subsection 83A-120(5) will apply such that the ESS deferred taxing point will be when you ceased employment (subject to the 30-day period in subsection 83A-120(3)).
13. Your assessable income for the income year in which the ESS deferred taxing point occurs (as determined in section 83A-120) is the market value of the Xero share at that time (subsection 83A-110(1)).

**Scheme**

14. The following description of the scheme is based on information provided by the applicant. If the scheme is not carried out as described, this Ruling cannot be relied upon.
15. Xero Limited is listed on the Australian Securities Exchange and is a New Zealand-incorporated and domiciled company that operates globally.

**Xero Limited Restricted Stock Unit and Option Plan**

16. The purpose of the Plan is to, among other things, attract, motivate and retain employees by providing the opportunity to become shareholders in Xero, aligning the interests of employees who participate in the Plan with Xero shareholders.
17. The Plan is operated in accordance with the terms set out in the Plan (Plan Rules), together with the terms set out in the grant letter that Xero sends to employees (Grant Letter).

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18. Under the Plan Rules, the Grant Letter provided to employees at the time of the offer outlines:

- the number or value of RSUs being offered, or the method or formula for determining the number or value of RSUs
- details of any applicable conditions which must be satisfied and the time or times at which the conditions will be tested
- where the RSUs will be exercisable, the periods during which RSUs may be exercised, the manner of exercise of those RSUs, the applicable expiry date and the exercise price payable (if any) in order to exercise the RSUs
- details of any restriction on dealing Xero shares following vesting or exercise, whether on a mandatory or voluntary basis
- the time and circumstances in which RSUs lapse, and
- any other relevant terms and conditions attached to the RSUs or Xero shares acquired on vesting.

19. RSUs provide an employee with the right to receive a Xero share on a one-to-one basis.

20. Employees must accept or reject an offer within 2 weeks. Where an employee accepts an offer and is granted RSUs, they become participants in the Plan (Participant) and are bound by the terms and conditions specified in the Grant Letter, the Plan Rules and the Xero Share Trading Policy.

21. Unless the Board determines otherwise, a Participant is not required to pay for an RSU.

22. The number of RSUs granted is based on a percentage of a Participant's salary and the volume-weighted average price of Xero shares over the 30 trading days (or similar) immediately prior to the allocation date of the RSUs.

23. Grant Letters and RSUs are issued in July each year to all Participants who are employed as at 31 March.

24. For employees in their first year of employment with Xero, Grant Letters will be issued and RSUs will be allocated in or around July, November or January, depending on a Participant's start date. A Participant's allocation of RSUs may be prorated depending on their start date.

25. RSUs are non-transferrable except as required by law and may only be registered in the name of the Participant. Where a Participant purports to transfer an RSU other than in accordance with the Plan Rules, the RSU will immediately lapse.

26. Immediately after the acquisition of the RSUs, no Participant will hold a beneficial interest in more than 10% of the shares in Xero and no Participant will be in a position to cast or control the casting of more than 10% of the votes that may be cast at a general meeting of Xero.

#### **Vesting of restricted stock units under the option plan**

27. RSUs are subject to satisfaction of vesting conditions (which are performance or service conditions to be met by a Participant) during the performance period.

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28. Participants must hold each RSU for a compulsory period (the Vesting Period). Different Vesting Periods may apply to the RSUs in a Participant's first year of employment depending on when they commenced employment.

29. Subject to the Board's discretion, a Participant's unvested RSUs will lapse on the date the Participant ceases to be an employee of Xero.

30. All RSUs allocated vest annually on or around 31 March (Vesting Date).

31. No cash consideration is required to be paid on vesting of the RSUs.

32. Some or all RSUs may be satisfied, at the discretion of the Xero Board, in cash rather than Xero shares, by payment to a Participant of the cash equivalent value in New Zealand dollars (or any other currency determined by the Board in its absolute discretion). The cash equivalent value is equal to the value of the Xero shares that would have been allocated or transferred to a Participant if Xero chose to settle their RSUs in Xero shares.

33. Where RSUs vest and the Board determines RSUs are to be settled with Xero shares, the vesting and issue process takes approximately 2 days with Xero shares available in Participant accounts on or around 1 April, annually.

34. Upon vesting, a Participant has legal ownership of their Xero shares, but Participants are prohibited from dealing with their shares pursuant to the trading restrictions imposed by Xero's Share Trading Policy. Participants are prohibited from dealing with their Xero shares during the Xero closed period, which occurs from the close of trade on 31 March until 10:00 am (times are in AEDT) on the next trading day after Xero's full-year financial results are released to the Australian Securities Exchange (usually early to mid-May).

35. Xero's general discretion to waive forfeiture, the Vesting Period or any other conditions that may have been imposed, which would allow Participants ceasing employment (for any reason except death) to have their RSUs vest, will not be exercised on a routine basis.

36. If a takeover or change of control occurs prior to the Vesting Date, the Board may determine in its sole and absolute discretion whether some or all of a Participant's unvested RSUs may vest, lapse or are forfeited. If it occurs after the Vesting Date, the vested RSUs must, if not converted into Xero shares, be so converted within 30 days of the change of control event or other such date determined by the Board. If the Board determines to settle an RSU in cash, Xero will be under no obligation to deliver any part of the vested RSU in the form of Xero shares.

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**Commissioner of Taxation****8 March 2023**

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Status: **not legally binding**


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## Appendix – Explanation

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**❶** *This Explanation 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.*

<b>Table of Contents</b>	<b>Paragraph</b>
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### **ESS interests and indeterminate rights**

37. An ESS interest in a company is a beneficial interest in a share in the company or a right to acquire a beneficial interest in a share in the company (subsection 83A-10(1)).

38. Under the Plan, RSUs acquired are only beneficial interests in rights that will later become rights to acquire beneficial interests in Xero shares. This is because the number of RSUs is not ascertained until the calculation occurs at a later point in time, as outlined in paragraph 22 of this Ruling. Upon completion of the calculation, the number of RSUs is ascertained and therefore become rights to acquire Xero shares.

39. Subsection 83A-340(1) applies where you acquire a beneficial interest in a right that later becomes a right to acquire a beneficial interest in a share which is referred to as an indeterminate right. A person will acquire an indeterminate right when they can enforce against their employer (under the terms of the contract) rights that will later become a beneficial interest in a share (refer to Taxation Determination TD 2016/17 *Income tax: in what circumstances does a contractual right, which is subject to the satisfaction of a condition, become a right to acquire a beneficial interest in a share for the purposes of subsection 83A-340(1) of the Income Tax Assessment Act 1997?*).

40. Therefore, where an RSU granted to you ultimately vests and is settled with a Xero share after the vesting date, section 83A-340 will apply to the RSU. The RSU will be treated as if it had always been a right to acquire a beneficial interest in a Xero share. That is, it will be treated as an ESS interest from when you acquired the RSU which is when the Plan becomes binding between you and Xero.

41. The Plan is an employee share scheme as defined in subsection 83A-10(2), as it is a scheme under which ESS interests in a company are provided to employees, or associates of employees, of the company, or a subsidiary of the company, in relation to the employee's employment (subsection 83A-10(2)).

42. The Plan provides that an RSU is issued for no consideration. This means the RSU was issued at a discount pursuant to subsection 83A-20(1). Subdivision 83A-B will apply to the RSU acquired by you under the Plan unless Subdivision 83A-C applies.

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**Subdivision 83A-C**

43. Subdivision 83A-C provides that where certain conditions are satisfied, the discount in relation to an ESS interest is not included in a Participant's assessable income when they acquire the ESS interest. Instead, the assessable income of the Participant will include, at a later time, the market value of the ESS interest at the ESS deferred taxing point, reduced by the cost base of the ESS interest (section 83A-110).

44. Based on the description of the Plan, the Commissioner accepts, for the purpose of Subdivision 83A-C, that in relation to RSUs acquired by you under the Plan, the conditions set out in subsection 83A-105(1) are satisfied.

**Real risk of forfeiture**

45. One of the conditions satisfied for Subdivision 83A-C to apply is that there must be a real risk of forfeiture, under the conditions of the scheme, that the Participant will forfeit or lose the ESS interest (other than by disposing of it, exercising the right or letting the right lapse) (paragraph 83A-105(3)(b)).

46. RSUs allocated under the Plan will vest annually, in accordance with the Plan Rules. RSUs that have not vested will lapse if the Participant ceases to be an employee of Xero or its subsidiaries (for any reason except his or her death) during the Vesting Period.

47. Although Xero has discretion to waive conditions such as forfeiture and vesting conditions, this discretion will not be exercised on a routine basis and Participants cannot expect the discretion to be exercised.

48. While some RSUs will vest upon some Participants meeting a relatively short term of employment, the Plan operates such that an ESS deferred taxing point will occur for all Participants on the first day of the first trading period after the end of the Vesting Period. As the RSUs vest on an annual basis, a Participant needs to remain an employee for the entire Vesting Period, to obtain the benefit of the RSUs.

49. The Commissioner accepts that Participants will have a real risk, of forfeiting or losing the rights acquired under the scheme and an RSU will satisfy the condition in subsection 83A-105(3).

50. As a result, Subdivision 83A-C applies to an RSU, and Subdivision 83A-B does not apply. The taxation of an RSU allocated under the Plan will therefore be deferred until the ESS deferred taxing point occurs.

**ESS deferred taxing point**

51. When Subdivision 83A-C applies to an ESS interest, section 83A-120 applies in determining the ESS deferred taxing point.

52. Where an RSU allocated to you vests and converts into a Xero share, the ESS deferred taxing point (as determined in section 83A-120) will (subject to the 30-day period in subsection 83A-120(3)) be at the commencement of the first trading window after the vesting period ends. This is the time when you are no longer restricted from disposing of your Xero shares (subsection 83A-120(7)).

53. However, for the 2021–22 income year, where an RSU allocated to you vested and converted into a Xero share, if you ceased employment with Xero on or before the ESS deferred taxing point set out in paragraph 11 of this Ruling, former subsection 83A-120(5) will apply such that the ESS deferred taxing point will be when you ceased employment (subject to the 30-day period in subsection 83A-120(3)).

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**Amount to be included in assessable income**

54. In accordance with section 83A-110, the amount to be included as assessable income is the market value of the ESS interest at the ESS deferred taxing point, reduced by the cost base of that interest (if any).

55. As the RSUs and Xero shares were issued for nil consideration (and no consideration was required for any conversion of RSUs to Xero shares), the cost base will usually be nil. Therefore, the amount to be included in your assessable income, will be the market value of the Xero share at the ESS deferred taxing point (subsections 83A-110(1) and 110-25(2)).

**Where a cash payment is made**

56. Division 83A will not apply where your RSUs are settled with a cash amount instead of Xero shares.

57. Section 6-5 provides that assessable income includes income according to ordinary concepts derived during an income year. Ordinary income includes income from personal services such as employment income. Therefore, you include the cash amount you receive in your assessable income in the income year you receive it.



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Status: **not legally binding**

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## References

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### *Related Rulings/Determinations:*

TD 2016/17

- ITAA 1997 83A-105(1)
- ITAA 1997 83A-105(3)
- ITAA 1997 83A-105(3)(b)
- ITAA 1997 83A-110
- ITAA 1997 83A-110(1)
- ITAA 1997 110-25(2)
- ITAA 1997 83A-120
- ITAA 1997 83A-120(3)
- ITAA 1997 former 83A-120(5)
- ITAA 1997 83A-120(7)
- ITAA 1997 83A-340
- ITAA 1997 83A-340(1)
- ITAA 1997 Div 230

### *Legislative references:*

- ITAA 1936 6(1)
- ITAA 1997 6-5
- ITAA 1997 Div 83A
- ITAA 1997 Subdiv 83A-B
- ITAA 1997 Subdiv 83A-C
- ITAA 1997 83A-10(1)
- ITAA 1997 83A-10(2)
- ITAA 1997 83A-20(1)
- ITAA 1997 83A-105

### ATO references

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