ASIC

Australian Securities & Investments Commission

REGULATION IMPACT STATEMENT

Employee incentive schemes

October 2014

About this Regulation Impact Statement

This Regulation Impact Statement (RIS) addresses ASIC's proposals to make it easier for both listed and unlisted employers to offer financial products to their employees under employee incentive schemes, while still ensuring that there is adequate protection for employees investing in financial products through these schemes.

What this Regulation Impact Statement is about

1 This Regulation Impact Statement (RIS) addresses ASIC's proposals to review and update Regulatory Guide 49 *Employee share schemes* (RG 49). RG 49 sets out our policy on relief from the disclosure and licensing provisions of the *Corporations Act 2001* (Corporations Act) that we give to employee share schemes.

2 In developing our final position, we have considered the regulatory and financial impact of our proposals. We are aiming to strike an appropriate balance between:

- maintaining, facilitating and improving the performance of the financial system and entities in it;
- promoting confident and informed participation by investors and consumers in the financial system; and
- administering the law effectively and with minimal procedural requirements.

3 This RIS sets out our assessment of the regulatory and financial impacts of our proposed policy and our achievement of this balance. It deals with:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

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A Executive summary

What is the problem ASIC is trying to solve?

4 ASIC currently has a class order [CO 03/184] *Employee share schemes* that exempts in certain circumstances both listed and unlisted employers from having to comply with the disclosure, licensing, managed investment scheme, advertising, hawking and on-sale requirements and restrictions. This class order, and ASIC's policy position in RG 49, are now out-of-date and can no longer accommodate the broader range of employee incentive schemes that employers are seeking to offer their employees. In addition, [CO 03/184], like other legislative instruments, is set to expire (i.e. sunset) in 2015 unless it is re-executed.

Why is ASIC action needed?

5 ASIC provides relief to facilitate employee incentive schemes, and proposes to update and extend this relief, because employee incentive schemes create interdependence between an employer and its employees for their long-term mutual benefit.

6 While employee incentive schemes involve offering financial products (and are therefore caught by the raft of Corporations Act provisions applicable to such offers), these offers are distinctly different from most fundraising related offers. Most offers of securities targeting retail investors are designed to raise funds from the public so that the company can have sufficient equity to undertake its business. In contrast, the purpose of offering employee incentive schemes to employees is not to raise funds from the employees to inject capital, but rather to foster long-term interdependence.

7 An additional policy rationale for creating a 'light touch' regulatory regime for employee incentive schemes is that, because employees work for the particular company in which they are being offered financial products, they already have a degree of familiarity with the business, and therefore need less disclosure about the company and the financial products.

8 We are seeking to make it easier for both listed and unlisted employers to offer employee incentive schemes to their employees, while still ensuring that there is adequate protection for participants in these schemes.

What policy options have we considered?

9 ASIC has considered three options:

(a) Option 1: make substantive changes to our existing class order relief to accommodate the needs of employers, while strengthening conditions designed to ensure that employees are adequately informed about the risks and terms and conditions of the employee incentive scheme they are being offered;

(b) Option 2: make the substantive changes proposed in Option 1, but without imposing any conditions; and

(c) Option 3: make some minor or mechanical changes to our existing class order.

What is the likely net benefit of each option?

10 The net benefit of Option 1 is to enable more employers, both listed and unlisted, to offer employee incentive schemes to more of their personnel. The class order relief will make it easier for employers to offer such schemes because:

(a) it alleviates the need to prepare a disclosure document (i.e. a prospectus, offer information statement or Product Disclosure Statement);

(b) it alleviates the need to obtain a relevant licence to provide certain financial services, or, alternatively, to have to engage the services of an Australian financial services (AFS) licence holder to provide the relevant financial services;

(c) it enables employers to undertake the activities associated with advertising and discussing the terms of the schemes without the constraints imposed by the Corporations Act that otherwise curtail these activities; and

(d) it will reduce the procedural and administrative compliance requirements.

11 The net benefit of Option 2 would be even greater for employers because no conditions would be prescribed in the class order relief. This would leave the disclosure and terms of the employee incentive arrangements to private contractual arrangements without any regulatory protections for employees. This was not considered acceptable because it would disadvantage employees who would incur the substantial loss of a minimum standard of disclosure and other investor protection mechanisms. It would put employees out of step with non-employee investors when being offered financial products of an issuer. We think the effect of this would result in a net detriment to the market, industry, ASIC, employers, employees and the wider community.

12 Option 3 would result in a minor net benefit to employers but would not be broad enough to enable many employers to effectively offer employee incentive schemes to their employees. This means the cost of having to apply for individual ASIC relief, or abandon the prospect of offering an employee incentive scheme entirely, would continue. This would result in a net detriment to employers, employees, ASIC and the wider community.

Who will you consult about these options and how will you consult them?

13 We have consulted with stakeholders by undertaking informal roundtable discussions in Melbourne, Perth and Sydney. This information assisted our considerations which resulted in Media Release (MR 13-310) *ASIC to update its employee share scheme policy and class order* (14 November 2013), and our publication of Consultation Paper 218 *Employee incentive schemes* (CP 218) and draft updated RG 49.

14 In CP 218, we set out the proposed scope of revising our class order, including explicit details about the conditions we would require before we would grant class order relief. We provided for a 10-week consultation period and received 21 written responses, as well as a number of telephone inquiries about discrete issues in CP 218. In general, respondents supported our proposals and, in particular, supported Option 1 over the other options.

What is the best option from those you have considered?

15 We consider the best option is Option 1—that is, to make substantive changes to our existing class order relief to accommodate the needs of employers, while strengthening conditions designed to ensure that employees are adequately informed about the risks and terms and conditions of the employee incentive scheme they are being offered.

16 We have also taken the opportunity to update RG 49 to give clearer guidance on our policy settings, and to illustrate the factors that we will take into account if we are asked to grant case-by-case relief.

17 As mentioned above, respondents to CP 218 broadly supported Option 1 over any of the other options. They acknowledged that there was a need for ASIC to balance the requirements of employers with the information needs of employees.

How will you implement and evaluate your chosen option?

18 We intend to issue new class order relief to replace our existing class order [CO 03/184], and to publish a revised RG 49 to assist participants to understand our policy objectives and when individual relief may be granted.

19 The implementation will be undertaken by providing a transitional period. This will provide 'grandfathered' relief for employee share scheme arrangements that have been in operation in reliance on [CO 03/184], or that have been approved for operation before the commencement of the new class order relief. Because the new relief is broader in scope than our existing relief, we do not envisage that employers will incur substantive additional ongoing costs under the new class order regime.

B Introduction

Background

20 There is a large body of opinion, both in Australia and overseas, that considers employee ownership brings direct and indirect benefits to employers, employees and the wider community. While there is also some research that considers the empirical evidence is inconclusive,[1] the balance of evidence suggests that it is beneficial. We are prepared to assist by providing class order and individual relief to facilitate voluntary employee incentive schemes, provided that adequate safeguards are in place.

21 Commonly, an offer of financial products takes place in circumstances where the issuer is attempting to raise funds.

22 Employee incentive schemes are conceptually different to other fundraising activity. These arrangements aim to enhance the relationship between an employer and its employees, with the objective of improving business performance, engaging employees and strengthening employee commitment. They are not designed primarily for the purpose of raising funds, but rather to support interdependence between the body and the employee for their long-term mutual benefit.

23 Even in instances where the offer requires monetary consideration akin to fundraising, the majority of these are offered at some discount to the market price of the securities, or offer some other benefit or saving (e.g. no brokerage, interest free loans, or some additional benefit such as a top up of additional securities if held for a period of time).

24 ASIC is prepared to facilitate relief, because it is not specifically designed for the purpose of raising funds.

25 We note that, although issuing equity rather than paying wages reduces the amount of cash expenditure required, there is still a cost associated with doing this (i.e. the cost of equity) that employers need to take into account when weighing up the costs and benefits of offering an employee incentive scheme.

[1] I Landau, A O'Connell and I Ramsay, *Incentivising employees—The theory, policy and practice of employee share ownership plans in Australia*, 2012, p. 37.

Research supporting the benefits of employee incentive schemes

26 In 2009, the Employee Share Ownership Project[2] released the results of a survey into broad-based employee share ownership practices in ASX-listed companies. Under the study, the Employee Share Plan Survey was administered to 1,711 companies in October and November 2007. This sample accounted for all of the companies listed on ASX as at 12 September 2007 for which reliable contact information was available. One of the important findings relevant to ASIC's class order relief was that:

> 24.6 per cent of respondents either agreed or strongly agreed that the availability of relief from disclosure and fundraising requirements offered by ASIC influenced their decision to implement a plan and 25.4 per cent either agreed or strongly agreed that the availability of this relief influenced the design of the plan.

27 At a more general level, in July 2014, the expert panel of the Employee Ownership Australia and New Zealand[3] (EOA) published a research report,[4] highlighting that—in a study that was conducted over five years, using data that had been averaged across 11 companies—the companies that offered broad-based employee ownership, on average:

(a) outperformed the index by more than 5%;

(b) had better share price growth;

(c) had better price/earnings ratios; and

(d) had a higher dividend yield.

> Note: The report noted that there was limited research in Australia in relation to productivity, and that this study, although useful, had its limitations.

28 A recent international review was undertaken in July 2013 in the United Kingdom by the Minister for Employment Relations, Consumer and Postal Affairs who commissioned an independent review of employee ownership. The report produced was titled: *Sharing success: The Nuttal review of employee ownership*. Some of the benefits of employee ownership are discussed in this report, including case study evidence as well as other research undertaken. One such case referred to was the Employee Ownership Index, compiled by Field Fisher Waterhouse LLP. This tracks the share price performance of listed companies that are at least 10% owned by employees.

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[2] The Employee Share Ownership Project is a joint initiative of the Centre for Corporate Law and Securities Regulation, the Centre for Employment and Labour Relations Law and The Tax Group at the Melbourne Law School. It is funded by an Australian Research Council Discovery Project grant that was authored by I Landau, R Mitchell, A O'Connell, I Ramsay and S Marshall who published the report: *Broad-based employee share ownership in Australian listed companies: Survey report*, research report, Employee Share Ownership Project, 2009.

[3] Employee Ownership Australia and New Zealand (EOA) was formed in July 2011 out of the Australian Employee Ownership Association (AEOA)—a member-focused, non-profit association that was formed by 20 companies in 1986 to assist members with their employee ownership (or co-ownership) plan, employee engagement and involvement, and employee participation levels.

[4] EOA's expert panel's research report: *Employee share schemes— Their importance to the economy*, July 2014.

This study found that the Employee Ownership Index outperformed the FTSE All Share by an average of 10% annually since 1992 (Field Fisher Waterhouse, 2012).[5]

29 Another study looked at the implications of investing $1,000 in a tax-free employee share allocation, as opposed to investing in the All Ordinaries Index or paying off a home loan with the same value. Even if the employees were not issued the shares free of charge, but as part of a salary sacrifice program, the employees were 35.6% better off than if they had invested that money across the All Ordinaries Index of ASX Limited. If they had taken the $1,000 as part of their annual salary and used the money to pay off their standard home loan, they would still be 15% worse off than taking employee shares.[6]

30 While broad-based employee share ownership is relatively widespread in the listed company sector in Australia, it is estimated that only 3% of private and unlisted companies have 'all-employee' share ownership schemes, compared with 23% in the United States.[7]

31 In the Standing Committee on Employment, Education and Workplace Relations inquiry in 2000, the Australian Employee Ownership Association (AEOA) advised the committee that the prospectus requirements acted as a forceful disincentive to unlisted companies:[8]

> … while shares issued to employees of listed companies are covered by prospectuses required for the listing of company 'stock', unlisted companies face major prospectus hurdles. In order to issue shares to their employees, they must first meet ASIC prospectus requirements. Putting together a prospectus can be a daunting and excessively expensive business. As a result, the need to issue a prospectus has become the single greatest obstacle in the way of expanding employee ownership in the unlisted company sector of the economy.

32 The AEOA went on to say to the committee that, 'In practice, these measures [providing for employee share scheme offers using an offer information statement] have not helped. Further legislation will be required.'[9]

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[5] G Nuttall, *Sharing success: The Nuttal review of employee ownership*, July 2012, p. 23.
[6] EOA's expert panel's research report: *Employee share schemes—Their importance to the economy*, July 2014, p. 11.
[7] http://www.employeeownership.com.au/news-archives/employee-ownership-reform-could-significantly-boost-the-economy-new-report-shows-2/
[8] Standing Committee on Employment, Education and Workplace Relations, *Shared endeavours: Inquiry into employee share ownership in Australian enterprises*, 2000, p. 180.
[9] Standing Committee on Employment, Education and Workplace Relations, *Shared endeavours: Inquiry into employee share ownership in Australian enterprises*, 2000, p. 183.

Corporations Act obligations and current ASIC relief

33 The offer of securities and other financial products to investors, including to employees, constitutes an offer that is regulated under Ch 6D (securities) and Ch 7 (other financial products) of the Corporations Act. These provisions require that, unless a relevant exemption or ASIC relief applies, offers to participate in an employee incentive scheme must be made under a disclosure document. The purpose of the disclosure provisions in the Corporations Act is to ensure adequate investor protection and promote market efficiency even where offers are made by employers to employees. In addition, an employee incentive scheme may involve conduct that requires compliance with the licensing, managed investment scheme, advertising, hawking and on-sale provisions.

34 Currently, we provide class order relief for employee share schemes in [CO 03/184]. Under [CO 03/184], relief—subject to specified conditions—is available to certain bodies from the disclosure, licensing, managed investment scheme, advertising and hawking provisions of the Corporations Act, and on-sale relief is available under Class Order [CO 04/671] *Disclosure for on-sale of securities and other financial products*. We also provide relief on a case-by-case basis where our policy objectives are satisfied. RG 49 provides guidance on our current approach to relief and the underlying policy objectives.

35 Our relief is conditional on the aim of the offer not being fundraising; the offer sufficiently supporting the long-term interdependence between the employer and the employee; and adequate disclosure being provided to the employee-investor. These are fundamental requirements for ASIC relief because they differentiate the design and purpose of offers from those that warrant a more rigorous regime of regulated disclosure. There is an acknowledgement that the relationship between employer and employee means that employees have a higher level of information and understanding of their employer than an 'outside' retail investor would have in relation to the issuer.

36 ASIC's class order relief means that employees accepting offers of financial products under an employee incentive scheme that is relying on ASIC relief will not have recourse to the liability regime under Ch 6 or Pt 7.9 of the Corporations Act relating to statements in a regulated disclosure document. Employees will still have recourse to the general misleading or deceptive statements regime under the Corporations Act, which will apply to the offer document that their employer provides to them about the scheme.

37 The licensing and associated relief provided by ASIC means that some of the regulatory requirements regarding the provision of general advice, dealing, providing custodial and depository services, hawking and advertising will be exempted. However, this must be viewed in circumstances where there is

already a relationship between the parties and the conditions of relief impose certain alternative obligations that are designed to safeguard the interests of employees (e.g. trusts, warning statements, and the requirement to use a licensed or authorised adviser).

Reliance on ASIC class order relief

38 While we do not collect data on how many employees have been offered an employee share scheme in reliance on our class order relief, our statistics revealed the following numbers of employers have notified ASIC of their reliance on [CO 03/184] (and its predecessors):

(a) *in the past seven years:* more than 4,910 employee share scheme notifications have been lodged with ASIC (45% Australian employers, 55% foreign employers);

(b) *in the past 10 years:* more than 6,160 employee share scheme notifications have been lodged with ASIC (45% Australian employers, 55% foreign employers); and

(c) *in the past 20 years:* more than 7,910 employee share scheme notifications have been lodged with ASIC (45% Australian employers, 55% foreign employers).

39 These figures indicate that a large number of employers have relied on, and continue to rely on, ASIC relief to offer employee incentive schemes. From the submissions we received in response to CP 218, we understand that many would like to avoid the costs of having to seek individual relief (see discussion below), and that, in wishing to avoid incurring the cost of seeking individual relief, many may also have refrained from implementing employee incentive schemes that would not otherwise currently qualify under a Corporations Act exemption.

Assessing the problem

ASIC's review of our relief and policy

40 We reviewed legal commentary, industry publications and government papers discussing employee incentive schemes, and have undertaken consultation with stakeholders to assess the extent of the issues. From our review, we identified a number of problems with [CO 03/184] and our current approach to relief for employee share schemes. It is evident that [CO 03/184] and our policy settings are now out-of-date. We are also aware that there are different views on the scope and operation of our class order relief, which have created risks and uncertainty in the market. In summary, our review indicated the following range of issues.

41 [CO 03/184] does not cover certain key features that are commonly used in many employee incentive schemes and that employers have been using outside of ASIC relief, or would like to implement using ASIC relief, including (among other things):

(a) offering employees a wider range of financial products that are not securities, such as incentive rights;

(b) the use of trusts to hold underlying financial products in a pool on behalf of their employees rather than specifically for a particular employee; and

(c) unlisted bodies offering securities and incentive rights.

42 This means that potential offers which meet our policy conditions (i.e. not being used for fundraising, promoting interdependence and providing adequate disclosure) are simply not able to use our relief because they include features that were not contemplated under [CO 03/184].

43 In addition, there is confusion about the operation of [CO 03/184], including, for example:

(a) whether incentive rights can qualify as zero exercise priced options;

(b) whether offers to non-executive directors are included in our relief;

(c) what the administrative and procedural requirements are (e.g. the frequency and timing of the lodgement with ASIC of employee incentive scheme offer documents);

(d) whether stapled securities can be offered; and

(e) whether offers can be made to associated bodies corporate of the issuer.

44 This confusion may have caused some potential offers not to be made because employers are uncertain about how ASIC would treat the offer. In addition, this confusion may also be causing some employers to push the boundaries and make offers that ASIC would consider may pose undue risk for employees.

Offers of employee incentive schemes under the Corporations Act

45 Employee incentive schemes involve the offer of financial products. Currently, the Corporations Act is designed so that offers of financial products require the use of a regulated disclosure document. This is to ensure that investors, who are being asked to subscribe, are appropriately informed and a liability regime exists for statements made in those disclosure documents.

46 In contrast, employee incentive schemes, which ASIC class order relief is intended to cover, are schemes that are not designed primarily to raise funds.

While the Corporations Act provides some exemptions to the disclosure requirement, these are limited in value and number, or are limited to a narrow range of persons. Employers who wish to offer employee incentive schemes more broadly would, without ASIC relief, still have to prepare a regulated disclosure document, and would be limited in the activities that they could undertake because some of these activities are either prohibited (advertising and hawking) or require the engagement of an AFS licensee.

47 From our work reviewing disclosure documents (i.e. prospectuses, offer information statements and Product Disclosure Statements), we understand that the cost of preparing such disclosure documents ranges from approximately $15,000 to in excess of $100,000. In our experience, employers occasionally make offers to employees using disclosure documents but, in these instances, they are seeking to raise funds from their employees, and the associated costs of preparing the disclosure documents are factored into the fundraising costs.

48 Our class order relief for employee incentive schemes is intended to apply where the purpose of the offer is not to raise funds, but to align the interests of the employee with those of the employer for longer-term mutual benefit. Where this is the motivation, the costs cannot be recouped in the same way, and because the benefits are less directly linked, this means that the threshold for deciding whether to offer an employee incentive scheme is also greater.

49 Financial statements must also be included with disclosure documents and must comply with Australian accounting standards and be audited. For foreign employers who do not prepare financial statements that comply with Australian accounting standards, the costs of preparing a relevant disclosure document will be even more than for an Australian employer. Depending on the size of the employer and its residency, these costs may be economically burdensome, or at worse, prohibitive.

50 Because the activities associated with offering an employee incentive scheme constitute financial services, it is also necessary for the employer to undertake additional compliance measures in order to make such offers in Australia without contravening the Corporations Act. This adds additional costs to the employer in having to obtain legal advice on what can and cannot be undertaken, and in ongoing compliance costs, while ensuring that human resource departments and administration functions that remain in-house do not breach the Corporations Act.

51 We have been told by one applicant that these costs would be in the vicinity of several hundred thousand dollars. The consensus from respondents generally was that ASIC's class order relief substantially alleviates the burden of complying with the Corporations Act when offering employee

incentive schemes, as demonstrated by ASIC receiving over 7,900 notifications of reliance on [CO 03/184] (and its predecessors) since 1993.

International perspective

52 Employee incentive schemes are more widely used in some foreign jurisdictions, including the United Kingdom, the European Union and the United States. Multinational employers have also wished to offer their Australian-resident employees participation in their global employee incentive schemes.

53 Under our current approach, Australian-resident employees may be disadvantaged. While they may receive a slightly higher salary as compensation for not being entitled to participate in an employee incentive scheme, they would not have exposure to the same potential employment-related benefits under employee incentive schemes that their overseas colleagues are being offered.

54 Some multinational companies consider that the cost of complying with the requirements in the Corporations Act in order to make an employee incentive scheme available to their Australian-resident employees would outweigh the benefits flowing from making these offers available to a small number of Australian-resident employees.

Offers of employee incentive schemes relying on case-by-case ASIC relief

55 We are aware that [CO 03/184] is no longer adequate to meet the needs of employers. In the past six years, there have been over 460[10] case-by-case applications for relief for employee incentive schemes. These individual relief applications were necessary because employers were unable to rely on [CO 03/184].

56 From an ASIC perspective, more resources are required to assess applications for relief and to provide relief. The aggregated time involved for a minor and technical relief application for an employee incentive scheme is estimated at an average of one to three days of a junior ASIC staff member's time.

[10] This calculation is based on the number of unique entity names and does not include instances where the entity has applied for the same relief on different occasions (e.g. the 2008 plan and the 2010 plan) or has applied for additional elements of relief not required on an earlier occasion where relief was granted. This calculation includes applications regardless of whether relief was granted or refused.

ASIC's objectives

57 Where we consider the benefits of an employee incentive scheme outweigh the risks to employees, and our policy objectives are satisfied, we are prepared to facilitate these schemes by relieving issuers from their obligations under the Corporations Act and reducing the compliance burden.

58 ASIC's overarching policy for facilitating relief relates to whether:

(a) the offer supports interdependence between the employer and its employees for their long-term mutual benefit by aligning their respective interests;

(b) there is adequate protection for participants in the scheme; and

(c) the objective of the offer is not fundraising.

C Options and impact analysis

Options

59 We are considering the following options to address the issues identified during our review of the policy applicable to employee incentive schemes:

(a) Option 1: make substantive changes to broaden the scope of our class order relief;

(b) Option 2: expand the scope of our relief (similar to Option 1) without imposing any conditions on such relief; and

(c) Option 3: maintain our existing approach to relief in line with [CO 03/184] but include some minor and technical changes and updates that are mechanical in nature.

60 We did not consider that allowing the class order to expire was a viable option, given the reliance that many employers currently place on our class order relief. Doing so would result in an exponential increase in the number of applications for case-by-case relief that would significantly increase the costs to industry, employers and employees, and be a significant and unnecessary resource drain on ASIC.

61 As discussed below, full compliance would cost approximately $15,000 or more per disclosure document and $30,000 or more to obtain any relevant licences. While large listed bodies may consider that the cost of preparing a disclosure document may justify the benefits, in a large number of cases, this would not be the case. In particular, foreign bodies with a limited number of Australian-resident employees have indicated that, without relief, the costs would outweigh the benefits. As such, the benefits of aligning the interests of employers and employees would not be realised because of the expense of having to prepare complying documents.

Option 1: Make substantive changes to the current guidance and relief (preferred option)

62 Under Option 1, we would publish a revised RG 49 and new class order relief, reflecting some substantive changes to our current policy and relief.

63 The intention is to make it easier for employers to implement appropriate employee incentive schemes which reflect market practices. We would also modify the conditions of relief to ensure that, while we make the relief easier to use for employers, it would also support the interests of employees by ensuring that they continue to receive adequate information about the offers that are being made to them.

64 We note that we will create two class orders—[CO 14/1000] *Employee incentive schemes: Listed bodies* and [CO 14/1001] *Employee incentive schemes: Unlisted bodies*. The reason we have created two class orders is because the recipients of relief do not overlap, and although there are a number of similarities including that our relief covers relief from equivalent obligations under the Corporations Act for both listed bodies and unlisted bodies, there are a number of conditions which are different between the class orders. These differences are necessary because in the case of relief granted in relation to listed bodies, there is a public market price relating to the underlying financial products, and a higher level of public disclosure and transparency about the listed body. The different conditions that we have imposed in relation to unlisted bodies are to protect participants in the less regulated and less transparent environment in which unlisted bodies operate. Also see paragraphs 128–133.

65 We will also create a new class order—[CO 14/978] *Employee incentive schemes: Personal offers*—which will entitle employers to continue to make personal offers under s708 of the Corporations Act, notwithstanding that they may have also made offers under an employee incentive scheme in reliance on [CO 14/1000], [CO 14/1001] or case-by-case relief of a similar kind.

66 Table 1 below summarises the key terms of relief under [CO 03/184], compared with our new employee incentive scheme class orders [CO 14/1000] and [CO 14/1001].

Table 1: Summary of current relief under [CO 03/184] compared with the new class order relief under [CO 14/1000] and [CO 14/1001]

Topic	Listed bodies: Relief under [CO 03/184]	Listed bodies: New relief under [CO 14/1000]	Unlisted bodies: Relief under [CO 03/184]	Unlisted bodies: New relief under [CO 14/1001]
Who can make offers?	• Issuer • Associated bodies corporate of the issuer (20% voting power)	Same as [CO 03/184]	• Issuer • Associated bodies corporate of the issuer (20% voting power)	• Issuer • Wholly owned subsidiaries of the issuer
Who can receive offers?	• Full-time employees • Part-time employees • Directors	Same as [CO 03/184] and in addition: • contractors—reduced to 40% of full-time equivalent • casuals—12-month prior history omitted • non-executive directors included	• Full-time employees • Part-time employees • Directors	Same as final relief for listed bodies [CO 14/1000]
What can be offered?	• Shares and stock, and units in them, on ASX or an approved foreign market • Options over shares and stock on ASX or an approved foreign market • Stapled securities on ASX	Same as [CO 03/184] and in addition: • beneficial (depositary) interests quoted on an approved foreign market • ASX-quoted managed investment schemes • ASX-quoted stapled securities • options and incentive rights over the above	• Options over shares	Changed to: • fully paid voting ordinary shares • units in ordinary shares • options over ordinary shares • incentive rights over ordinary shares
What structures can be used?	• Trusts (5% limit, audit obligation, all underlying eligible products must confer right to direct voting and right to dividends) • Contribution plans (no loans) • Loans (no contribution plans)	• Trusts (5% limit, no separate audit obligation, no voting if trustee is an associate of the unlisted body, reasonable charges can be claimed against trust funds, underlying eligible products held on an allocated or unallocated basis) • Contribution plans (opt-out notice period is 45 days, contributions cannot be collected for the acquisition of options or incentive rights (these must be issued for no more than nominal monetary consideration), new requirement that contributions used to acquire underlying eligible products confers a right to direct voting and a right to dividends) • Loans (requirement: no recourse or limited recourse only, no interest or charges)	Not applicable	• Trusts (same as for listed bodies except that the holding limit is 20%) • Contribution plans and loans not permitted

Topic	Listed bodies: Relief under [CO 03/184]	Listed bodies: New relief under [CO 14/1000]	Unlisted bodies: Relief under [CO 03/184]	Unlisted bodies: New relief under [CO 14/1001]
What conditions will apply?	• Quotation period (12 months) • Suspension period (2 days) • 5% offer limit (based on current offer and offers over last 5 years) • Certain prescribed disclosure about general advice warning, terms of loans, acquisition price • Provision of offer document and related documents to ASIC within 7 days	• Quotation period (3 months) • Suspension period (5 days) • 5% issue limit (current plus last 3 years and simplified formula) • Clear, concise and effective • Prominent general product warning, terms of any trust, contribution plans or loans • ASIC power to request copies of employee incentive scheme documents • Notice of reliance to ASIC (no later than one month after first reliance, certain minimum content reporting) • ASIC power to exclude a body from reliance on class order relief	• 5% issue limit (based on current offer and offers over last 5 years) • Certain prescribed disclosure about general advice warning • Requirement that on exercise of options, the underlying financial product must be quoted for 12 months without suspension for more than 2 trading days or being provided with a current prospectus	• Offers of fully paid voting ordinary shares, and units in, for no more than nominal monetary consideration (no other classes of shares under the offers) • Offers of options and incentive rights (over ordinary shares) for no more than nominal monetary consideration • Offers of all financial products must be no more than $5,000 per participant per year at the time of the offer • Basis of valuation as approved by directors disclosed • 20% offer limit (up from 5%) changed to current plus last 3 years and formula simplified (same formula as for listed bodies) • Clear, concise and effective • Prominent general product warning, terms of trust • Front page and prominent warning about liquidity and realisation value • Special purpose financial report to be provided unless statutory obligation to prepare audited accounts • Directors' solvency resolution • Obligation to provide future financial report if requested • Payment of more than nominal monetary consideration on exercise or vesting of the underlying ordinary shares is only permitted where the following alternative circumstances are included as terms of the offer:

Topic	Listed bodies: Relief under [CO 03/184]	Listed bodies: New relief under [CO 14/1000]	Unlisted bodies: Relief under [CO 03/184]	Unlisted bodies: New relief under [CO 14/1001]
				– quotation of the underlying ordinary shares for 3 months and not suspended for more than 5 trading days – a current disclosure document (offer information statement or prospectus) is provided no later than 14 days before exercise or vesting – written evidence of consideration paid if arm's length and not with an associate – an independent expert's report if not at arm's length or to an associate of issuer • ASIC power to request copies of employee incentive scheme documents • Notice of reliance to ASIC (no later than one month after first reliance, certain minimum content reporting) • ASIC power to exclude reliance on class order relief
What other relief applies?	• Licensing relief • Managed investment scheme relief • Advertising relief • Hawking relief • On-sale relief under [CO 04/671]	Same as [CO 03/184] and in addition: • trustees added to advertising and licensing relief for advice on incidental managed investment schemes	• Licensing relief • Hawking relief • On-sale relief under [CO 04/671]	Same as final relief for listed bodies [CO 14/1000] except incidental managed investment scheme relief not applicable

Impact on employers

67 The employers that either use, or would like to use, employee incentive schemes fall into three distinct groups relevant to Option 1:

(a) Listed and unlisted bodies that qualify under our current [CO 03/184] relief and currently have a scheme on offer—given the 'grandfathering' of existing schemes, the impact on these entities will be negligible. Based on lodgements in the past 10 years, there have been, on average, over 530 bodies per year that have lodged under [CO 03/184], with slightly less than half of these being Australian listed bodies or their unlisted subsidiaries, and the majority of the remainder being foreign listed bodies or their unlisted subsidiaries.

(b) Listed and unlisted bodies that would qualify under [CO 03/184] but do not currently have a scheme on offer—these bodies might have increased compliance costs because the proposed conditions are in some respects stricter than the conditions of our current relief, but may have reduced compliance costs in other respects where the conditions are more relaxed. We do not think it is possible to estimate how many of these bodies there may be, but as we consider that the net impact of the compliance costs would be neutral, we have not sought to estimate these numbers.

(c) Listed and unlisted bodies that do not currently qualify for relief under [CO 03/184] but would qualify under [CO 14/1000] or [CO 14/1001]—these bodies will have reduced compliance costs because they will be able to offer an employee incentive scheme without having to meet the Corporations Act requirements or will be able to avoid the costs of applying to ASIC for case-by-case relief. Based on the analysis below, we estimate that there would be in excess of 3,300 bodies that fall within this category.

68 We have estimated the 3,300 bodies falling under the third category in paragraph 67(c), based on the following:

(a) In the past 12 months, we have received in excess of 110 applications for individual relief. The majority of these employee incentive schemes would qualify for relief under the new class orders.

(b) There are 2,156 bodies listed on ASX.[11] We estimate that approximately 200 (10%) of these 2,156 do not currently fit into either the first or second groups that could now offer an employee incentive scheme in reliance on [CO 14/1000].

(c) In the past 10 years, we have had approximately 240 foreign listed bodies per year rely on [CO 03/184]. We estimate that the number of

[11] Source: ASX as at 26 August 2014.

foreign bodies seeking to rely on our new class order relief would increase by in excess of 40 (20%), with the additional classes of financial products as well as the lower level of compliance requirements.

(d) There are over 20,000 unlisted bodies registered with ASIC, some of which are local subsidiaries of foreign bodies.[12] Given the interest shown in the responses we received for substantially broadening the class order relief for unlisted bodies and the low cost of compliance with the new conditions of class order relief, we estimate that approximately 3,000 (15%) of these 20,000 would fall within the third category in paragraph 67(c).

69 Option 1 is designed to facilitate the widest scope for employers to utilise our class order relief when offering employee incentive schemes, while ensuring that employees still receive adequate information about the financial products they are being offered. The changes proposed to our class order relief will reduce or remove the costs for employers of having to:

(a) seek individual relief because the terms of their employee incentive schemes are outside the scope of [CO 03/184]. While it is unclear how much it costs an employer to obtain advice and to make an application to ASIC for individual relief, we estimate such costs to be approximately $10,000. This is based on:

(i) a prescribed application fee of approximately $1,000;

(ii) the cost of the employer's management time of approximately $2,000;

(iii) the costs of legal advice of approximately $6,000; and

(iv) processing and lodgement costs of $1,000.

Based on the 110 applications for individual relief that we received in the past 12 months, this costs employers in excess of $1.1 million;

(b) comply with the requirement to prepare disclosure documents for those that are ineligible for relief (e.g. unlisted bodies wishing to offer shares), or that do not wish to apply for individual relief. We estimate the costs of preparing a disclosure document to be approximately $15,000 and, while most employers are likely to decide not to implement employee incentive schemes through the use of a disclosure document, we have seen a few instances where this has been done. We estimate this to be approximately three in a year, at a cost of $45,000;

(c) comply with auditing obligations associated with operating a trust for the purposes of the employee incentive scheme. We estimate that, of the average of 540 lodgements we received in reliance on [CO 03/184] and the 110 applications for individual relief that we received in the past

[12] *ASIC Annual Report 2012–13*, p. 18.

12 months, at least 30% of these would operate through a trust. We estimate that the audit costs for each trust would be approximately $2,000 per year, totalling $1.3 million; and

(d) comply with more detailed administrative requirements, such as having to provide ASIC with copies of anonymised offer documents, along with the offer document, trust deeds and plan rules. Based on an estimate from a high-volume lodging respondent, we understand the cost is approximately $1,000 per lodgement. With an average of 650 lodgements a year, this would cost approximately $650,000.

70 The aggregated estimate of compliance cost savings in paragraph 69(a)–69(d) under the new class order relief would be approximately $3.095 million per year.

71 Some of the proposed benefits of our class order relief, which we have not sought to quantify, include:

(a) being able to offer a wider range of financial products, particularly incentive rights (very commonly offered by US-based employers);

(b) being able to offer the employee incentive scheme to a broader range of personnel (i.e. contractors, casual employees and non-executive directors);

(c) listed bodies being able to offer loans in conjunction with contribution plans;

(d) unlisted bodies being able to offer shares and use trust arrangements; and

(e) reducing the amount of paperwork and administration associated with lodging documents with ASIC.

72 As noted at paragraphs 26–32, there is strong evidence that employee incentive schemes are beneficial for both employers and employees. We have not quantified the benefit to those employers (and their employees) who were previously outside the scope of our relief, but will now be able to offer employee incentive schemes under our class orders.

73 There is also a subset of listed bodies and unlisted bodies, which either currently rely on [CO 03/184] or will rely on the new class orders, that are, or would be, prevented from making personal offers under s708(1) of the Corporations Act. Relief under [CO 14/978] would permit these bodies to continue to rely on s708(1) to make personal offers rather than having to prepare a regulated disclosure document to make such offers. While the cost savings would be in excess of $15,000 if they had to prepare a disclosure document—given that they could not rely on s708(1), we have not estimated this amount because we expect such employers would consider this cost prohibitive and would simply not make such offers.

Impact on employees

74 The impact on employees is that our class order relief will enable more employees (i.e. contractors, casual employees and non-executive directors) to be eligible to participate in their employer's employee incentive schemes, and to acquire an interest in a broader range of financial products.

75 In the case of unlisted bodies, employees will, for the first time, be eligible to participate in direct ownership of the unlisted body because they will be eligible to be offered fully paid ordinary voting shares of the body. They will also be eligible to be offered options and incentive rights in a wider range of circumstances than is available under [CO 03/184].

76 While this will benefit employees who were previously prevented from being made offers in reliance on ASIC relief, the risk is that more employees will be exposed to the potential financial and economic success and failure of their employer. Employees may also not engage in appropriate diversification of their investment portfolios, or otherwise over-invest in their employer, depending on their outlook. While there is a risk that some employees may limit their investments to financial products offered by their employer, for employees who may never invest their discretionary funds in financial products at all, the benefit would be to provide them with an investment in a financial product outside of superannuation that they may not otherwise undertake.

77 The relief also imposes a number of conditions that are designed to provide some risk mitigation for employees, including a requirement to expressly warn that employees should seek independent financial advice as well as a number of other measures (e.g. see paragraph 80).

78 Another cost, and benefit, is that because the employee incentive scheme is generally a feature of an employee's remuneration package, employees will be offered less cash than remuneration arrangements without employee incentive schemes. While this is part and parcel of the risk–return trade-off, there is the additional risk that some employers may seek to take advantage of relief by offering remuneration arrangements that result in being more adverse on this risk–return trade-off because employers are in a better bargaining position than their employees. The overall impact is somewhat mitigated by the fact that employee incentive schemes are generally voluntary, leaving it to an employee to determine whether they wish to participate. Market forces relating to commercial arrangements will generally shape the attractiveness of including or excluding certain terms in an employer's employee incentive scheme.

79 Our new class order relief is designed to ensure that the financial risk employees face is limited (particularly in the case of unlisted bodies), and

the information they receive about the employee incentive scheme is adequate.

80 For unlisted bodies, unlike in a fundraising situation, under our class order, the employer is not permitted to seek funds from the employee—the offers must be for no more than nominal monetary consideration, limited in value to no more than $5,000 per year; and limited to no more than 20% of the issued capital of the unlisted body. This limits the financial exposure of an employee. In addition, there are requirements regarding solvency, preparation of financial information and prominent warnings about the speculative nature of holding shares in an unlisted body.

81 In the case of both listed and unlisted bodies, employers will still:

(a) provide employees with an offer document, which must be presented in a clear, concise and effective manner;

(b) have trust arrangements (if employers choose to utilise them) that recognise and protect the interests of employees; and

(c) provide general product warnings and caution employees to seek independent financial advice.

82 For listed bodies, there is a restriction from requiring payment for unquoted options, and for incentive rights, at the point of the offer. Further, while loans and contribution plans are permissible, the offer document is required to explain these terms in a clear, concise and effective manner. Because the loan arrangements will only have the benefit of relief where they are no recourse, or limited recourse; and need to be provided free of interest charges and fees, this means that aside from the risk of holding the financial product, the only other financial risk the employee faces where loans are provided relates to the value of the financial product itself. In the event that the financial product is worth less than the amount owing on the loan, the employee is not responsible for the debt, which is borne by the employer.

83 Australian-resident employees of a foreign employer with a small workforce in Australia will have a greater opportunity to participate, because the new class order will make it less costly for foreign employers to make their multinational employee incentive schemes available to their Australian-resident employees.

Impact, costs and benefits to other stakeholders

Trustees

84 We have removed from our class order the obligation to have the financial records of the trust audited. We have been told that this imposes an additional and unnecessary burden where the trust is not already required, under the Corporations Act, to undertake an audit.

85 Our new class orders will also permit underlying financial products to be held on a pooled basis, which was not permissible under [CO 03/184]. This will broaden the services that a professional trustee is able to provide their employer-clients.

ASIC

86 The broadening of relief under the new class orders and revised RG 49 will reduce the need for ASIC to utilise staff and resources in assessing employee incentive scheme applications, and will reduce the administration required to process the offer document and related employee incentive scheme documentation. This will enable ASIC to better utilise its resources on undertaking more surveillance, compliance and enforcement activities where there is a greater risk to investors and a greater potential benefit to the market.

87 The simplification of the notification requirements will reduce the administrative processes that ASIC has to undertake and will result in some savings to ASIC's registry functions.

What is the net impact?

88 Because our proposals are expanding the scope of employee incentive scheme relief from what is currently available under [CO 03/184], while maintaining protection for employees, we consider the net impact is positive.

Are there any competition considerations?

89 The only competition consideration is the different conditions of class order relief for listed bodies and unlisted bodies. While less conditions are imposed on offers to employees of listed companies under [CO 14/1000] than offers to employees of unlisted companies under [CO 14/1001], we consider that our concerns about the adequacy of information available to employees in relation to unlisted employers makes this necessary and unavoidable.

90 We note that, compared with [CO 03/184], [CO 14/1001] has substantially broadened the scope of relief available for unlisted bodies.

Option 2: Making substantive changes to broaden the scope of relief without imposing conditions

91 Under this proposal, we would broaden our relief (similar to Option 1)—however, we would not impose particular conditions on such relief. For example, this would mean that we would:

(a) leave it to employers to determine whether they had a sufficient relationship with the issuer to offer financial products of the issuer;

(b) leave it to employers to determine the categories of persons they would make offers to;

(c) not place any issue limits on the number of underlying financial products that could be issued under an employee incentive scheme; and

(d) leave it to commercial arrangements to determine the terms of any trusts, contribution plans and loans.

Impact on employers

92 The effect of providing employers with relief from the disclosure, licensing, managed investment scheme registration, advertising, hawking, and on-sale provisions to make offers of financial products under employee incentive schemes would reduce the cost to industry.

93 The cost savings of Option 2 are estimated roughly equivalent to Option 1. This is because, while the economic benefits will be greater under Option 2, the costs of complying with the conditions imposed under Option 1 are not considered to be significantly different to those under Option 2. Employers will generally need to seek advice on structuring their employee incentive schemes, and ASIC's conditions by themselves do not impose significant additional compliance issues for employers. We therefore estimate the cost savings associated with Option 2 to also be approximately $3.095 million per year.

94 However, responses to our public consultation acknowledged that this would not provide a level of protection to employees that employees are entitled to assume they will receive, notwithstanding they will not receive a regulated disclosure document.

Impact on employees

95 From the submissions we received, it is apparent that under Option 2 employers would be at liberty to offer employee incentive schemes without limitation. While this would mean that employee incentive schemes would be accessible to a much larger population of employees, it would also mean that a large number of employees may not understand the risks and terms of the offer.

96 We consider that a certain minimum level of information and disclosure is still required despite the existing employer–employee relationship.

97 The cost to employees is that, without an appropriate framework created by the imposition of certain conditions of relief, employees may be taken advantage of—both in terms of the employee incentive scheme, given their

poor negotiating position compared with that of an employer, and also in the level of disclosure about the arrangements that would apply under the relevant schemes. Because the terms of the scheme would be the subject of individual contractual arrangements between each employee and their employer, employees would incur the cost of seeking advice about the arrangement, rather than being able to rely on uniform requirements. Further, without appropriate conditions, employers may seek to offer high-risk financial products which may compound the financial exposure that an employee faces in circumstances where they are already reliant on the employer for their main or significant source of income.

Impact on ASIC

98 The impact of Option 2 would mean that ASIC would not have to consider applications for case-by-case relief. However, without conditions, the number of complaints that ASIC may receive could increase substantially as uninformed employees suffer financial losses as a result of not understanding the offers they have accepted under an employee incentive scheme made without any minimum conditions of disclosure or conduct.

Option 3: Making changes of a minor or mechanical nature

99 Under this option, we would retain our existing relief in [CO 03/184] and RG 49—however, we would make the following minor or mechanical changes to the conditions:

(a) reducing the quotation requirement;

(b) relaxing the trust requirements for listed bodies;

(c) clarifying the inclusion of non-executive directors in the class order; and

(d) reducing the issue limit calculation from five to three years.

Impact on employers

100 While this would address a small number of instances where individual relief has been sought, it would not address the more substantive shortcomings of our existing class order relief. This would mean that employers would have to continue to seek individual relief in a large number of instances. This alternative was not supported in the responses we received to CP 218.

101 Option 3 would not reduce or remove the bulk of the compliance costs discussed as those that would be saved under Option 1. That is, the majority of individual relief applications would still need to be made (at a cost of over $1 million (see paragraph 69(a))); and the trust arrangements would not

accommodate pooled arrangements, and would not remove the audit requirement (at a cost of over $1 million (see paragraph 69(c))). If we were to change the lodgement obligation to accord with the lodgement obligation in Option 1, this would result in an estimated saving of approximately $650,000.

Impact on employees

102 Where employers are unable to rely on [CO 03/184] or the other exemptions in the Corporations Act, consumers (employees) would continue to miss out on the opportunity to participate in employee incentive arrangements.

Impact on ASIC

103 Under this option, ASIC would continue to receive a significant number of individual applications for relief, which would not best utilise ASIC's limited resources.

D Consultation

CP 218 *Employee incentive schemes*

104 We undertook informal roundtable discussions in Melbourne, Perth and Sydney. We then published CP 218 and allowed 10 weeks for stakeholders to respond. This consultation canvassed the various options and focused in detail on Option 1. This was because our review and consultation indicated that this option would provide the most benefit to industry (employers) and consumers (employees), while continuing to address our objective of ensuring that employees receive adequate information about, and safeguards around, the financial products they are being offered.

105 We received 21 written responses, including from large ASX-listed employers, law and accountancy firms, remuneration consultants and advisers, employee share scheme trustee and administration service providers, and a number of industry associations and governance bodies. We also reviewed public newsletters commenting on CP 218 and took questions from a number of other stakeholders who contacted us but did not make written submissions.

106 Eight submissions expressly commented on the proposed options and all eight supported Option 1 (which was Option 2 in CP 218) over the other options. While all supported Option 1, these submissions suggested a number of the requirements we proposed in CP 218 should be changed.

107 One respondent submitted that ASIC should not seek to regulate employee incentive scheme offers where there is no investment decision, but is merely a remuneration-related payment with no risks of financial loss. We did not agree. Our view is that employee incentive schemes that involve offers of financial products almost always involve an investment decision that warrants class order relief with appropriate conditions.

108 In summary, the substantive issues raised include:

(a) the relief for unlisted bodies being too onerous;

(b) the definition of ‘incentive right’ being too narrow;

(c) the objective requirement we proposed for demonstrating interdependence being too restrictive;

(d) requiring a narrower form of relief for non-executive directors being unnecessary and out of step with market practice; and

(e) the trust requirements being burdensome and unnecessary.

109 In light of the submissions, a number of the class order conditions proposed under Option 1 have been significantly broadened and refined. Table 2 sets

out the changes that we proposed in CP 218 and what we ended up deciding was the appropriate balance between providing class order relief that was deregulatory and requiring the imposition of new conditions within the scope of that deregulatory relief.

Key changes made as a result of our CP 218 consultation

110 The following is a summary of our consultation and how we propose to respond in our new class order relief.

111 We note that, while we started out with having one class order to provide relief for employee incentive schemes, we decided to split it into two separate class orders—[CO 14/1000] for listed bodies and [CO 14/1001] for unlisted bodies)—given that the employers will generally be mutually exclusive.

Listed bodies

Who can make offers?

112 Responses were generally supportive of the proposed updates to our relief and guidance in relation to which listed bodies and their related parties can make offers under an employee incentive scheme.

113 We received feedback suggesting that we should broaden the scope of our class order relief to include bodies listed on other foreign markets, and leave it to the bodies to determine whether there is a sufficient connection between the participant and the listed body.

114 Given the scope of relief covered by our class order, we did not consider it appropriate to leave it to the listed body to decide whether relief should apply. We have retained our proposal that our class order relief should cover the listed body and its associated bodies corporate.

Who can participate in offers?

115 There was widespread support from respondents to expand the categories of eligible participants to whom offers may be made under our class order to include contractors, casual employees and prospective employees.

116 Some submissions suggested that some of our proposed parameters were still too narrow.

117 We have retained the categories of participants that we proposed in CP 218 but reduced the requirements in relation to contractors and casual employees, and we have removed the restrictions applying to non-executive directors.

What financial products can be offered?

118 There was strong support for our proposal to expand the scope of our relief to cover offers by listed bodies of equity-based securities, including stapled securities, certain quoted depositary interests, and options over, and incentive rights in relation to, these quoted financial products.

119 Some respondents submitted that we had not gone far enough in covering the types of financial products to which relief should apply, and that the conditions proposed for our definition of 'performance rights' would exclude a large number of derivatives currently being offered under employee incentive schemes.

120 We decided to expand our class order relief to cover offers by listed bodies of units in managed investment schemes quoted on ASX; and to offers of stapled securities quoted on ASX, without the need to be stapled to a share. We have also modified the definition of 'performance right' (referred to in our new class orders and updated RG 49 as an 'incentive right') so that it does not exclude a large number of derivatives that are being offered in relation to listed bodies.

What structures can be used?

121 Respondents supported our proposal to recognise the use of trusts for holding allocated products and unallocated products.

122 Some submissions did not agree with our proposed conditions, including:

(a) requiring the auditing of financial records;

(b) preventing claims for fees and charges; and

(c) requiring that participants have substantially the same rights as if they were the legal owner including an entitlement to dividends and voting.

123 There was broad agreement with our proposal to permit the use of both contribution plans and loans in an employee incentive scheme.

124 While we retained a number of conditions for trusts, loans and contribution plans, we decided to remove the audit obligation on trusts, to permit the use of dividends to pay down loans, to permit claims for reasonable disbursements, and not to prevent professional trustees who are not associates of the body from voting under their duties as trustees if it is in the best interest of beneficiaries for the trustee to vote.

What general conditions apply?

125 All respondents supported a relaxation of the quotation requirements, and most respondents agreed that offers of options and incentive rights be offered for 'no more than nominal monetary consideration'.

126 Some respondents did not agree with our formulation for calculating the 5% offer limit and many did not support our proposal to establish interdependence by imposing a 12-month restriction (where no more than 75% of an employee incentive scheme could vest absolutely within a 12-month period).

127 We have simplified the formula for calculating the 5% offer limit and are not proceeding with a quantitative interdependence test. We have also significantly reduced the content of the notification of reliance on our class order and are not prescribing the disclosure of material risks.

Unlisted bodies

What relief is available?

128 Given that listed and unlisted bodies are mutually exclusive categories, we decided to create a separate class order [CO 14/1001] for unlisted bodies.

129 The majority of the restrictions we proposed in order to protect participants in the less regulated and less transparent environment of unlisted bodies were generally not supported by respondents. We were told that they were too onerous and would render the relief to be of little use.

130 Unlisted bodies, particularly smaller enterprises (e.g. start-up companies), are very interested in offering employee incentive schemes. The experience overseas, particularly in the United States, is that start-up enterprises have used employee incentive schemes to attract talented employees in circumstances where the enterprises are cash poor and unable to remunerate staff sufficiently based on cash salaries alone.

131 While the experience both in Australia and overseas is that employee incentive schemes are popular for either end of the corporate landscape (i.e. from billion dollar listed companies down to small start-up enterprises), it would appear that class order relief would benefit unlisted bodies to a larger degree than it would benefit listed bodies, given that the outlay for having to otherwise comply with the Corporations Act is generally equivalent. Therefore, based on the figures discussed at paragraph 68(d), even 10% to 15% of the 20,000 unlisted bodies registered with ASIC would mean that 2,000 to 3,000 unlisted bodies, a portion of which would be start-up enterprises, could avail themselves of the proposed class order relief under [CO 14/1001].

132 To maintain participant protections in the unlisted environment, we have retained the condition in our class order that offers of all eligible products must be for no more than nominal monetary consideration, and must not involve contribution plans or loans.

133 We have omitted or amended a number of class order conditions because, in light of submissions we have received, we consider that, on balance, the risks associated with relief can be reasonably managed by the other proposed restrictions, and the benefits of changing these conditions (i.e. to provide workable relief) outweigh the risks. We made the following changes to the conditions:

(a) We were told that the offer limit of up to $1,000 was too low to be workable, but that increasing it to up to $5,000 would make it useable. By retaining the condition that the offer, of up to $5,000, must be for no more than nominal monetary consideration, we have limited the risk for employees in that employees are not required to outlay additional funds to receive the benefit.

(b) We have removed the requirement that the offer must be accompanied by audited accounts or an independent expert's report, on the grounds that it would be commercially unattractive for many unlisted bodies. Instead of this, we have devised conditions that require special purpose financial statements and representations regarding the basis of valuation and solvency to safeguard employees. We also require a directors' solvency resolution as additional disclosure regarding the financial position of the unlisted body. This must be approved by the directors no earlier than one month before the making of the offer. This is further reinforced with a new condition requiring a prominent front page warning that makes it clear that the financial return may not eventuate, to remove any suggestion that it provides a substitute for a cash salary.

(c) Submissions indicated that it was not commercially attractive to prevent unlisted bodies from having different classes of shares with different rights outside of the employee incentive scheme arrangement, and we agreed with this position. We decided that, on balance, most of the safeguards we were intending to provide could be achieved by limiting the restriction to apply only to offers made in reliance on ASIC relief. That is, unlisted bodies can only offer fully paid voting ordinary shares to participants under an employee incentive scheme in reliance on ASIC relief, but are otherwise able to issue other classes of shares.

(d) We also originally omitted the use of trusts to keep the structural arrangements simple. However, we were told that trust arrangements are commonplace and assist with the costs and administration of the employee incentive scheme. Because trusts are there to recognise the interest of the employee-participant, we accepted that permitting relief to cover trusts would provide additional safeguards for the interests of employees, even though they do introduce an additional degree of complexity.

E Conclusion and recommended option

134 In arriving at our conclusion and recommended option, we have considered the counterfactual—that is, the likelihood that ASIC would and should permit its class order relief to lapse and require employers to undertake full compliance with regulated disclosure and financial services activities without relief. We would estimate the cost to employers, employees and the economy more generally to be in the order of tens of millions of dollars due to lost productivity, innovation and tax revenue. Given the research and evidence supporting the benefits of employee incentive schemes both in Australia and for some of our most significant trading partners, and the fact that ASIC has not received complaints about providing disclosure and licensing relief for employee incentive schemes, there seems to be no realistic possibility of this occurring.

135 With the change in market practices and the mechanisms employers are utilising to provide employee incentive schemes, our current RG 49 and [CO 03/184] have become outdated and no longer reflect the diverse range of offers relevant to the employer–employee relationship. Further, as the implementation of employee incentive schemes expands globally, more employers would prefer to implement these schemes without the burden of having to either comply with the Corporations Act, or to offer these schemes under the limited relief available under [CO 03/184]. These issues were evident during our review process of applications for relief, commentary on employee incentive schemes and industry feedback.

136 To address the issues identified, we recommend implementing Option 1—that is, to make substantive changes to our existing policy by issuing revised guidance and new class order relief. Option 1 achieves our policy objectives of facilitating offers of employee incentive schemes where the benefits to employers, employees and ASIC are balanced against the risks to employees of being offered financial products without disclosure under a regulated disclosure document, or in limited circumstances under [CO 03/184].

137 We recommend Option 1 because it achieves our policy objectives without imposing an unreasonable burden on employers, employees and industry stakeholders. Option 1 achieves a net benefit for those involved in employee incentive schemes by providing certainty about our existing policy, expanding the scope of our relief and addressing key emerging issues in the market for employee incentive schemes.

F Implementation and review

Implementation

138 Our recommendations in Section E would be implemented by publishing the following documents:

(a) a revised Regulatory Guide 49 *Employee incentive schemes*;

(b) new class orders:

(i) [CO 14/1000] *Employee incentive schemes: Listed bodies*;

(ii) [CO 14/1001] *Employee incentive schemes: Unlisted bodies*; and

(iii) [CO 14/978] *Employee incentive schemes: Personal offers*;

(c) a report on submissions received on CP 218 (Report 417 *Response to submissions on CP 218 Employee incentive schemes* (REP 417)).

139 We expect to publish these documents in October 2014.

140 We will provide a transition period. Employers and employees will be entitled to continue to rely on [CO 03/184] after the date that the new class orders and updated RG 49 come into operation, provided that the employee share scheme arrangements have been approved, or are already in use before this date.

141 Because the intention is that our new class orders will broaden the scope of relief, we do not envisage that employers will have difficulty in transitioning to the new arrangements. To the extent that employers have difficulties, we will consider case-by-case relief. We will apply the requirements in our new class orders and our policy under the revised RG 49 from October 2014 when assessing any applications for individual employee incentive scheme relief.

Review

142 To rely on the relief under our new class orders [CO 14/1000] and [CO 14/1001], a body must notify ASIC and disclose some basic information about their employee incentive scheme. Because employee incentive schemes are generally private arrangements with little public promotion, ASIC would not have a means of monitoring these schemes without a notification requirement. This will enable us to monitor reliance on our class order relief and to make determinations preventing employers from relying on it in the event that they are substantively failing to comply with the conditions of our relief, or where ASIC has other substantive concerns about the activities or governance of a particular employer.

G Regulatory burden and cost offset (RBCO) estimate tables

Table 2: Option 1: Average annual compliance costs (from business as usual)

Costs ($m)	Business	Community organisations	Individuals	Total cost
Total by sector	(–$3.095m)	$nil	$nil	(–$3.095m)
Cost offset ($m)	**Business**	**Community organisations**	**Individuals**	**Total by source**
Agency	NA	NA	NA	NA
Within portfolio	NA	NA	NA	NA
Outside portfolio	NA	NA	NA	NA
Total by sector	NA	NA	NA	NA
Proposal is cost neutral?	No			
Proposal is deregulatory?	Yes			
Balance of cost offsets	$3.095m			

Note: NA = not applicable.

Table 3: Option 2: Average annual compliance costs (from business as usual)

Costs ($m)	Business	Community organisations	Individuals	Total cost
Total by sector	(–$3.095m)	$nil	$nil	(–$3.095m)
Cost offset ($m)	**Business**	**Community organisations**	**Individuals**	**Total by source**
Agency	NA	NA	NA	NA
Within portfolio	NA	NA	NA	NA
Outside portfolio	NA	NA	NA	NA
Total by sector	NA	NA	NA	NA
Proposal is cost neutral?	No			
Proposal is deregulatory?	Yes			
Balance of cost offsets	$3.095m			

Note: NA = not applicable.

Table 4: Option 3: Average annual compliance costs (from business as usual)

Costs ($m)	Business	Community organisations	Individuals	Total cost
Total by sector	(–$650,000)	$nil	$nil	(–$650,000)
Cost offset ($m)	**Business**	**Community organisations**	**Individuals**	**Total by source**
Agency	NA	NA	NA	NA
Within portfolio	NA	NA	NA	NA
Outside portfolio	NA	NA	NA	NA
Total by sector	NA	NA	NA	NA
Proposal is cost neutral?	No			
Proposal is deregulatory?	Yes			
Balance of cost offsets	$650,000			

Note: NA = not applicable.