FACT SHEET | PUKA MEKA

Employer obligations for employee share scheme benefits paid in cash

Issued | Tukuna: 31 March 2025

IS 25/06 FS

This fact sheet accompanies Interpretation Statement **IS 25/06: Employer obligations for employee share scheme benefits paid in cash**, which explains an employer's PAYE, student loan and KiwiSaver obligations when an employee receives a benefit under an employee share scheme that is paid in cash.

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

START DATE | RĀ TĪMATA

This fact sheet accompanies IS 25/06 which applies to an employee share scheme benefit paid in cash on or after 1 November 2024.

REPLACES | WHAKAKAPIA

- This fact sheet updates and replaces **IS 24/05 FS: Employer obligations for employee share scheme benefits paid in cash** for the amendments to s 11(1)(cb) of the Accident Compensation Act 2001 by the Taxation (Annual Rates for 2024-25, Emergency Response, and Remedial Measures) Act 2025.

Introduction

1. This fact sheet sets out the main points from Interpretation Statement **IS 25/06: Employer obligations for employee share scheme benefits paid in cash**.

2. An employee share scheme (ESS) benefit is usually provided in **shares**. However, in some circumstances, an employee may receive **cash** instead of shares under an ESS (a **cash-settled ESS benefit**). This fact sheet sets out:

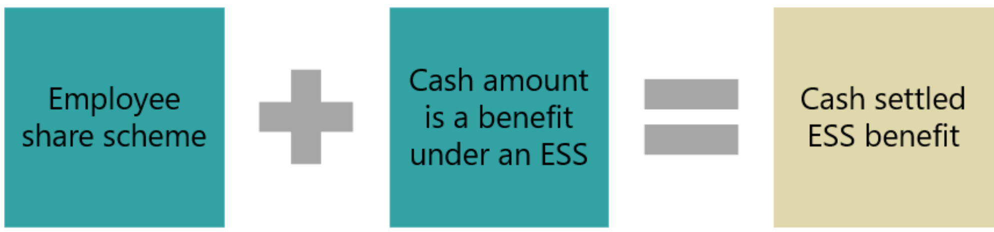
   - what a cash-settled ESS benefit is; and
   - an employer's PAYE, student loan and KiwiSaver obligations.

3. It also provides a flowchart which sets out the key questions to determine an employer's obligations for awards provided to an employee under a share scheme.

What is a cash-settled employee share scheme benefit?

4. If the cash is a "benefit" under an ESS, some tax rules apply differently compared to other cash payments. Accordingly, the first step in determining the employer's obligations is to clarify whether the cash that an employee receives under a share scheme is truly a cash-settled ESS benefit. This involves considering two questions:

   - Is the scheme an "employee share scheme"?
   - Does the cash amount give rise to a "benefit" under an ESS?



Is the scheme an "employee share scheme"?

5. Broadly, a scheme will be an "employee share scheme" if it is an arrangement with a purpose or effect of issuing or transferring shares in a company to an employee. This requirement is assessed when the scheme is entered into. Transferring shares does not have to be the sole or even principal purpose or effect of the arrangement. For example, where an arrangement provides for an award to be paid partly in shares and partly in cash, a purpose or effect of the arrangement is to transfer shares to the

employee. The arrangement must be connected to the employee's employment or service.

6. Not every share scheme is an "employee share scheme" for tax purposes. Under some schemes, the benefits are linked to shares but under the terms of the scheme, the employee never becomes a shareholder in the company. The benefits are always paid out in cash. In this case, the amount will generally be an ordinary cash bonus and subject to the usual PAYE rules.

Does the amount give rise to a "benefit" under an employee share scheme?

7. The next question is whether the cash amount gives rise to a "benefit" under an ESS. A cash amount will give rise to a "benefit" under an ESS if the share scheme taxing date is triggered by the transfer or cancellation of shares or related rights (eg options) and cash is paid or payable to the employee in relation to that transfer or cancellation under the ESS.

8. For example, an employee may be granted rights to acquire shares and the terms of the ESS may allow for the employer to cancel the rights and provide a cash equivalent in certain circumstances (eg on the sale of the company or retirement of the employee). Here, the cash amount received will give rise to a benefit under an ESS. This is because the share scheme taxing date is triggered by the cancellation of the rights and cash is paid for the cancellation of the rights under the ESS.

9. An example of an ESS where the cash amount will not generally give rise to a "benefit" under the scheme is where the terms of the scheme provide that the incentive is provided partly in cash and partly in shares. The part that is paid in cash is likely to be paid in satisfaction of the rights to cash granted under the scheme (ie there is no transfer or cancellation of rights to shares). In this situation, the cash amount will generally be an ordinary cash bonus and subject to the usual PAYE rules. The part of the incentive scheme that is settled in shares would give rise to a benefit under an ESS (even if cash is provided instead of shares).

What are an employer's PAYE, student loan and KiwiSaver obligations on ESS benefits?

10. If an ESS benefit is provided in **shares**, there is no requirement for the employer to withhold tax. However, the employer can elect to withhold and pay tax on the share benefit if they choose to. In this situation, the benefit is an "extra pay" and the relevant

"extra pay" tax rate applies. If the employer elects to withhold tax they must also deduct student loan repayments (if applicable) but Accident Compensation Corporation (ACC) earners' levy and KiwiSaver do not apply.

11. If the employee receives a **cash-settled ESS benefit**, the employer **must** withhold tax at the applicable "extra pay" rate. The employer must also deduct student loan repayments (if applicable). This is because a cash-settled ESS benefit:

- is an "extra pay" under the general definition of "extra pay" in s RD 7(1)(a) and a PAYE income payment; and
- is included in the definition of "salary and wages" under the Student Loan Scheme Act 2011.

12. The election to withhold tax from an ESS benefit applies only to share-settled benefits (ie non-cash benefits). An employer cannot make an election to withhold tax (or choose not to withhold tax) where withholding is already required.

13. An employer is not required to deduct ACC earners' levy from either cash- or share-settled ESS benefits. This is because ESS benefits are excluded from the definition of "earnings as an employee" for the purposes of the Accident Compensation Act 2001.

14. An employer is not required to make KiwiSaver deductions or employer contributions for either cash- or share-settled ESS benefits. This is because KiwiSaver deductions and contributions are based on an employee's gross "salary or wages" and an ESS benefit is excluded from the definition of "salary or wages" for the purposes of the KiwiSaver Act 2006.

15. Generally, a child support deduction notice will not apply to an ESS benefit. However, if an employer has any questions about whether to make a child support deduction, they should contact Inland Revenue.

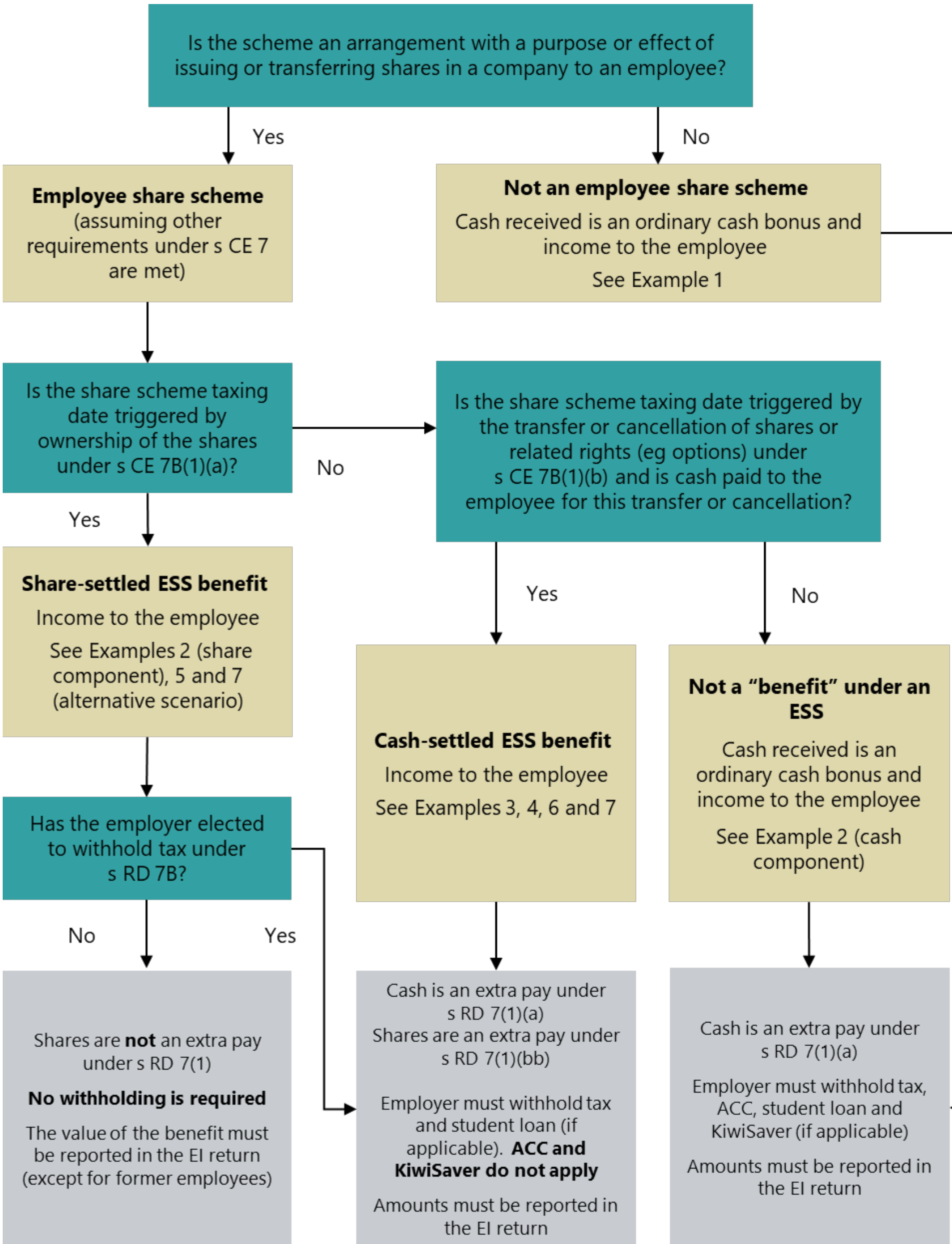
What are an employer's reporting obligations?

16. An employer is required to report the value of an ESS benefit to Inland Revenue in its employment income information (EI) (unless the person is a former employee receiving a share-settled benefit and the employer has not chosen to withhold tax).

17. If the employer has chosen to withhold tax (for a share-settled ESS benefit) or is required to withhold tax (for a cash-settled ESS benefit), then it must also report the amount of tax withheld from the ESS benefit in its EI.

Summary flowchart

Figure | Hoahoa 1: Key questions to determine employer obligations for awards provided to an employee under a share scheme[1]



[1] The examples referred to are in IS 25/06 at pages 33 to 39.

About this document | Mō tēnei tuhinga

Some of the Tax Counsel Office's longer or more complex items are accompanied by a fact sheet that summarises and explains an item's main points. While it summarises the Commissioner's considered views, a fact sheet should be read alongside the full item to completely understand the guidance. Fact sheets are not binding on the Commissioner. See further Status of Commissioner's advice (Commissioner's Statement, Inland Revenue, December 2012*)*.