Inland Revenue
Te Tari Taake

Regulatory Impact Statement: Tax Deferred Employee Share Schemes

Decision sought	*Final Cabinet decisions*
Agency responsible	*Inland Revenue*
Proposing Ministers	*Revenue, Finance*
Date finalised	*3 April 2025*

The proposal is to allow unlisted companies to offer shares to employees where the recognition of income and payment of tax can be deferred to a time when the shares have been disposed of, can easily be sold, or pay a dividend.

Summary: Problem definition and options

What is the policy problem?

Some start-up companies remunerate their employees partly with shares in the company through an employee share scheme (ESS). Start-up companies are often cash constrained. An ESS can reduce the amount of cash salary they pay, while remaining competitive in terms of remuneration and motivating employees by providing a stake in the businesses' success.

Currently, the employee is taxed on the share once the employee is free of any employment related restrictions and holding the same interest as any other shareholder. There are two common concerns for businesses utilising ESS that arise in the context of the tax settings. The first is the valuation of the shares, and second is the liquidity on the employee's part to pay the tax on the income. These create barriers to use of ESS because the employee may not have the funds to service this tax liability as it arises, and it can be challenging to calculate the tax liability due to the difficulty valuing the shares issued.

Many start-up companies deal with this problem by issuing their employees long-dated options to acquire shares, which are a type of ESS. Long-dated share option plans give employees the option to buy shares at a certain price (the exercise price) on or after a future date or event. Tax on options is not calculated or payable until the options are exercised. The benefit of long-dated options is that they give employees more control over when their tax liability arises. However, until the option is exercised the employee is not a shareholder in the company and this may limit their sense of having a stake in its success.

What is the policy objective?

The overall objective is to minimise the tax barriers to start-ups using ESS as part of talent acquisition and retention in New Zealand. Specifically, the intended outcome is to minimise the barriers created by valuation and liquidity issues faced by start-up companies so that tax implications are less of a consideration for employers when deciding whether to offer ESS to employees. Any change should mean that issuing shares is as attractive from a tax perspective as long-dated options, while maintaining consistency of tax treatment between share schemes and other forms of remuneration (such as cash remuneration).

What policy options have been considered, including any alternatives to regulation?

Ministers' preferred option was option 3. Introducing this change will require changes to tax legislation. There are no non-regulatory options available. The following policy options were considered as part of this project:

Option 1 - Retain the status quo: Companies are currently able to give their employees control over when their tax liability arises by issuing options instead of shares. These options are usually long dated and give the employee the opportunity to purchase shares in the company for a fixed price. The tax liability for these shares will only arise when the option is exercised. Until the option is exercised, the employee holds no equity in the company, has no voting rights and no entitlement to dividends that shareholders may receive.

Option 2 - Defer tax on employee shares for start-up companies until a liquidity event occurs: This option would allow start-up companies to issue shares on the basis that the calculation of income and payment of tax is deferred until a liquidity event occurs. This would also defer the company's deduction. Deferring the payment of tax on ESS shares is not a tax concession so long as the calculation of income from the ESS is also deferred. There are challenges with this approach, including defining what a start-up company is.

Option 3 - Defer tax on employee shares for all unlisted companies until liquidity: This option would have some of the same benefits and challenges as option 2 but would avoid the need to define a start-up company. The proposal is limited to unlisted companies since a company becoming listed is itself a liquidity event. The tax would be deferred until the shares are sold, cancelled or paid a dividend.

What consultation has been undertaken?

The first consultation on this issue was an issues paper published in May 2017. The proposal did not progress further. In 2023 an Upstart Nation Report identified the tax treatment of ESS as a barrier to the success of start-up companies in New Zealand. In 2024 the Minister of Revenue asked officials to re-consult on the deferral proposal. Officials published an issues paper on 31st January 2025, which proposed option 2 as a solution.

Inland Revenue invited multiple firms and organisations for targeted consultation on the issues paper over a period of six weeks. We held videoconferences with Deloitte, PwC, EY, KPMG, New Zealand Law Society, CA ANZ, representatives from venture capitalist firms, and the Angel Association (start-up specialists). We also received 11 written submissions.

Stakeholders generally highlighted that in most cases, using long-dated options provides an adequate mechanism to defer an employee's ESS tax liability and that option 2 was too complicated and would not provide enough of a benefit. However, a simplified regime which does not define a 'start-up' (option 3) could benefit some. Stakeholders conveyed a strong interest in further consultation on options that would be concessionary in nature, however, these were not analysed given they would not meet policy objectives.

Is the preferred option in the Cabinet paper the same as the preferred option in the RIS?

The preferred option of officials is option 1 (retain the status quo). In the absence of concessions, long-dated options schemes appear to achieve the tax objectives sought by the relevant parties. Officials would also support option 3. This option does the best job of achieving the intended outcome, while making the policy non-concessional and as simple as possible for companies to interpret and follow. However, it would come at a cost.

Summary: Minister's preferred option in the Cabinet paper

Costs (Core information)

The Ministers' preferred option is option 3. This option will decrease immediate revenue collected by Inland Revenue from employees who already participate in ESS (that are not options) by $9.9 million over the forecast period. The introduction of a deferral regime is not expected to have any negative distribution or competitive consequence.

Broadly, this change may increase compliance costs as a result of any tax advice and system changes needed to navigate a new deferral regime. s 18(c)(i) [redacted] There will also be administration costs for Inland Revenue s 9(2)(g)(i) [redacted] s 18(c)(i) [redacted]

Benefits (Core information)

The key benefits of this policy are likely to be limited to unlisted companies that do not prefer the use of long-dated share options. However, potential take-up is unclear. It may assist the competitiveness of early-stage firms when compared to more mature firms. It may also have a marginal increase on start-up company talent acquisition and retention by giving employers viable alternatives to long-dated options. Employees who have shares in a company will have a vested interest in the company's success, which may lead to the company becoming more successful than if the employee had options.

Balance of benefits and costs (Core information)

Does the RIS indicate that the benefits of the Minister's preferred option are likely to outweigh the costs?

Many companies who already use long-dated options appear to be comfortable in doing so. As a result, the deferral regime may be underused. Despite this, new companies entering the start-up space who have no history of using long-dated options may be more likely to use ESS since share ownership can be more desirable than a long-dated option from the perspective of the employee. For some company's long-dated options will remain preferred from a commercial perspective. The benefit of the proposal would be the removal of tax implications as a key determinant of which type of scheme a company offers.

Over time compliance costs will decrease as companies become familiar with the regime and embed relevant systems. The revenue cost is also expected to steadily reduce to $0 by 2034 as employees' shares are sold, cancelled or paid a dividend and the deferred tax becomes payable. The benefits of the proposal may grow over time if the regime is utilised, while its costs should decrease, meaning the benefits may outweigh the costs in the future.

Implementation

How will the proposal be implemented, who will implement it, and what are the risks?

The proposal will be implemented legislatively by amendments to the Income Tax Act 2007 through the Annual Rates 2025-26 tax Bill and will take effect from 1 April 2026. No transitional arrangements will be required. The proposal will be implemented by employers who choose to use it. Inland Revenue will be responsible for producing guidance on the scheme and answering queries about it. There should be no need for material change to any of the mechanics for collection or auditing of returns.

There is a risk that it will be more difficult to effectively monitor when a taxing date arises following the end of the employment relationship between the employee and the company issuing shares. s 18(c)(i) [redacted]

Limitations and Constraints on Analysis

There were partial gaps in the evidence base. We do not hold data on what kind of ESS (options or shares) are used by start-up companies, nor what percentage of start-up companies use ESS. Our information is anecdotal, provided during consultation.

Consultation helped to mitigate information gaps. Through consultation officials were advised that tax is a factor in the lack of use of ESS, and the main difficulty is valuation as it relates to taxation. Officials were also advised that while long-dated options can be exercised at any time, most employees do not exercise until there is a liquidity event, which eliminates issues of liquidity and share valuation.

Public consultation did not specifically occur on option 3, although it was discussed during some targeted consultation meetings and the outcome of general consultation fed into the option analysis. A number of other options for improving ESS tax treatment were raised during consultation. Largely due to time constraints, and not meeting the stated objectives, these have not been analysed further. There were also constraints, particularly for option 3, created by time frames. After the consultation phased closed there was a short amount of time to consider consultation outcomes and present advice to Ministers.

On balance, despite some information gaps, officials believe that the analysis undertaken, and the information and insights provided by consultation provided adequate information for Cabinet to consider options and make an informed decision.

Summary: Official's preferred option

Summary of Option, Costs, Benefits and Implementation

Official's preferred option is to maintain the status quo. Broadly, officials believe that current share schemes, particularly long-dated options, provide start-ups with the ability to provide employees with shares whilst minimising valuation and liquidity issues. Maintaining the status quo would not result in additional benefits, but it also would not result in changes to Government revenue, compliance or administrative costs.

On balance, officials do not believe that any other option provides enough of a benefit to either start-ups, non-listed companies, or the New Zealand economy as a whole to outweigh the costs that would be associated. Officials would also support option 3 as this option appears to achieve the intended outcome, however, it would come at a cost.

I have read the Regulatory Impact Statement and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the preferred option.

s 9(2)(a)

Responsible Manager(s) signature: ______________________

Claire McLellan
Acting Policy Lead
3 April 2025

Quality Assurance Statement	
Reviewing Agency: Inland Revenue	**QA rating:** Partially meets
Panel Comment: Inland Revenue's RIA QA Panel has reviewed the *Regulatory Impact Statement: Tax Deferred ESS* and considers that the information and analysis summarised in the RIA partially meets the quality criteria of the Regulatory Impact Analysis framework. The analysis has been prepared under time constraints, and while there has been consultation with the industry on option 2, there was only limited consultation on option 3. However, subject to these limitations, the analysis is otherwise complete, clear and convincing.	

Section 1: Diagnosing the policy problem

What is the context behind the policy problem and how is the status quo expected to develop?

1. In 2022, there were over 2,400 start-up companies in New Zealand valued at $9 billion.[1] Many New Zealand start-ups go on to reach success; in the last 5 years, founders of six start-ups have sold their stake through IPO or acquisitions at over $100 million each.[2]

2. Start-ups are supported by policies and initiatives that are in place to help engage and assist with growing the sector. This includes access to grants and funding from Government departments and local government, as well as providing advice and practical assistance with tasks such as digital support and obtaining permits and licenses. There are multiple cross agency efforts and initiatives to support business growth and start-ups in New Zealand.[3] Due to the cash restrained nature of start-ups, they are heavily reliant on external funding from venture capital investors.

3. It is common for start-up companies to remunerate their employees partly with shares in the company through an employee share scheme (ESS). Start-up companies are often cash constrained, and all available cash is allocated to developing the business. ESS can reduce the amount of cash salary they pay, while remaining competitive in terms of remuneration. ESS may also motivate employees by providing a stake in the businesses' success. The employee is taxed on the share once the employee is free of any employment related restrictions, and holding the same interest as any other shareholder. The employee may not have the funds to service this tax liability at this stage and it is challenging to calculate the tax liability due to the difficulty valuing the shares issued. In 2024, 624 companies returned ESS tax information, and 16,321 individuals had an ESS tax obligation.

4. The issue of tax on employee share schemes was raised recently by the Startup Advisors Council in its 2023 Upstart Nation Report.[4] The National Party's 100-point economic plan committed to investigating changes to the treatment of ESS issued by start-ups to their employees. Inland Revenue has responded by releasing an issues paper on 31 January 2025 which received some interest from stakeholders.

5. Feedback has highlighted that the majority of start-ups use long-dated options as a self-help solution to delay the taxation of ESS. These long-dated options allow employees to exercise an option when they are in a position to fund tax on the shares. It also lowers the risk that an employee will owe tax on shares that have decreased in value since the share scheme taxing date, and therefore cannot cover the tax by selling the shares.

6. The key issue with using long-dated options is that the employee is not a shareholder in the company until the share is exercised. This means they do not have the same rights as a

[1] New Zealand: Ecosystem by the Numbers (startupgenome.com)
[2] Assessing New Zealand's Startup Ecosystem (mbie.govt.nz)
[3] Support for business | Ministry of Business, Innovation & Employment
[4] UpStart Nation 2023

shareholder, such as voting rights or the payment of a dividend. Holding a share can be seen as beneficial in aligning the interests of the company and employee.

What is the policy problem or opportunity?

7. This project is seeking to address the issue that companies with illiquid shares find it difficult to reward their employees through the use of ESS. This is because the shares become taxable income of the employees once they are owned by the employee free of employment related restrictions. Employees often do not want to, or cannot, pay this tax, especially if there is no market for the shares. These issues are exacerbated by the valuation difficulties faced by start-ups. Valuation issues increase compliance costs as employers have to expend resource establishing a value for the shares for which there may be no market value information easily obtained. These liquidity and valuation issues can be a barrier to the use of ESS by start-ups as a way of attracting and retaining talent.

8. Under the status quo, such companies can instead reward their employees with long-dated options. Long-dated options, instead of granting shares directly, give employees the right to buy shares at a certain price (the exercise price) on or after a future date or event. Taxable income does not arise until and unless they are exercised. Anecdotal evidence from consultation suggests that long-dated options are commonly utilised by the start-up sector and are considered to provide a sufficient workaround to delay the point of taxation until there is a liquidity event.

9. However, some stakeholders regard options as inferior to shares (others think that at least for the employer they are superior, because they give the employee rights that are governed by contract, rather than by company law). Share ownership not restricted by employment conditions can be more desirable than a long-dated option from the perspective of the employee. There is an opportunity to equalise the tax treatment of shares and the tax treatment of options. This will allow companies to offer shares rather than options to their employees, without their decision being influenced by taxation.

What objectives are sought in relation to the policy problem?

10. The overall objective is to reduce the tax barriers to start-ups using ESS as part of talent acquisition and retention in New Zealand.

11. Specifically, the intended outcome is to minimise the barriers created by valuation and liquidity issues faced by start-up companies so that tax implications are less of a consideration for employers when deciding whether to offer ESS to employees. Any change should mean that issuing shares is as attractive from a tax perspective as long-dated options, while maintaining consistency of tax treatment between share schemes and other forms of remuneration (such as cash remuneration).

What consultation has been undertaken?

12. An issues paper was published on 31st January 2025, and eight targeted consultations were held with firms and organisations who are associated with the financing and accounting of start-up companies. This issues paper detailed the current taxation of ESS and proposed option 2 as a solution. Targeted consultation meetings were held from 24th February until

12th March. Public consultation was open for six weeks between 31 January and 14th March 2025 and 11 submissions were received.

13. Stakeholders who participated in targeted consultation calls were PwC, KPMG, EY, Deloitte, CA ANZ, NZ Law Society, Angel Association and representatives from venture capital firms who heavily contribute to start-up funding in New Zealand.

14. We received written submissions in response to the issues paper from 11 individuals and organisations. Those who submitted were Catalist Markets, NZ Law Society, CA ANZ, Sharesies, Corporate Taxpayers Group, Olivershaw Ltd, Taxpayers' Union, Deloitte, EY, PwC with Angel Association, and a member of the public.

15. The general feedback from both the targeted consultation meetings and the written submissions was that start-ups using long-dated options is far more common than share schemes. Stakeholders and submitters advised that the regime proposed in the issues paper was complex and the scope was narrow. Submitters and stakeholders also advised that long-dated options function well for start-ups and it is unlikely that this policy would make an impactful difference. However, many submitters and stakeholders urged officials to explore tax concession options, which they believed would make a much more material impact on the start-up space. These were not analysed given they would not meet policy objective of maintaining consistency of tax treatment between share schemes and other forms of remuneration (such as cash remuneration).

16. Each stakeholder added valuable input. While each had their own take and suggestions around the proposal, the common themes from their feedback were:

Option 2 is too complicated, it needs to be simplified

17. Option 2, which took a narrow approach in defining the eligibility criteria and provided a number of taxing events, some of which did not coincide with liquidity, was seen as far too complicated. While some submitters said that employers would prefer to issue shares, long-dated options do achieve a tax liability deferral, are commonly used already, have lower compliance costs and required less tax knowledge to operate than option 2 would. To create a deferred tax scheme that makes issuing shares more or equally attractive to issuing long-dated options, the regime needs to be simple and easy to understand. Particularly because start-ups who are experiencing low liquidity and cash flow may have limited access to professional tax advice.

The definition of start-up in option 2 is too narrow

18. Many of the stakeholders who have regular involvement and interaction with start-ups, advised that there are plenty of start-ups who fall outside our proposed criteria. The initial $15 million annual turnover cap was far too low. This is because many start-ups are operating in a global market as opposed to the domestic New Zealand market. Stakeholders proposed at least a $50 million annual turnover cap to align closer with the equivalent Australian legislation. Many start-ups will still be operating in the start-up space despite being over 15 years old. This is due to the extended research and development phase involved with some industries, including scientific innovation. Stakeholders proposed that this be widened to include a much broader scope. A broader scope would ensure our target is not excluded.

Other key comments

19. One of the key points that arose through consultation is that there will be no benefit from a scheme which is more complex, or has an earlier taxing point, than a long-dated option. This feedback was key when option 2 was revised and reconsidered post-consultation. Option 3 responds to this point by removing the start-up criteria and narrowing the taxing events to those resulting in increased liquidity in order to pay the tax. There was limited opportunity to complete targeted consultation on option 3, but those that were consulted suggested that this version could be of use to the start-up sector.

20. Submitters and stakeholders were also of the view that in order to achieve meaningful change, amendments would need to offer some concession. For example, allowing the tax to be paid later than the time that the shares are valued. These concessionary options were not progressed as they did not meet the objectives of the policy and so have not been analysed.

21. Notably, although such an approach would allow start-up companies to offer more attractive remuneration packages to their employees in a way that minimises valuation and liquidity issues, such options would reduce the long-term tax take and would reduce horizontal or vertical equity in taxation. This is because concessions come at a fiscal cost and would likely create discrepancies in outcomes between the taxation of concessionary share scheme, non-concessionary share schemes and other forms of remuneration.

Section 2: Assessing options to address the policy problem

What criteria will be used to compare options to the status quo?

22. The below criteria have been used to compare any proposed changes with the status quo.

23. The first criterion is whether any proposal will minimise a barrier to using ESS, which is the imposition of a cash tax liability on a person who has only illiquid shares that are challenging to value.

24. The second criterion is whether a deferral regime means that the issuing of shares to employees is at least as attractive from a tax perspective as long-dated options and as similar as possible to the tax treatment of cash remuneration.

25. Proposals were also considered through other criteria including the cost of implementing the proposal and ongoing administrative costs for Inland Revenue s 18(c)(i) [redacted], and the compliance cost on business.

What scope will options be considered within?

26. The original scope for this project was informed by multiple avenues. Inland Revenue's 2017 issues paper shaped a lot of the thinking in relation to the deferral regime for ESS, which flowed through to this project. The lack of progression with the 2017 issues paper meant that the scope, particularly the problem definition, was not shaped by consultation that occurred in 2017. Instead, the 2017 issues paper combined with the 2023 Upstart Nation Report and The National Party's 100-point economic plan shaped the broad scope of the problem any proposals would seek to address. The Upstart Nation Report identified the tax treatment of ESS as a barrier to the success of start-up companies in New Zealand and the National Party's 100-point economic plan commitment to investigating changes to the treatment of options issued by start-ups to their employees.

27. Broadly, any proposals will be considered through the criteria above, which were developed through the scope of the problem definition and the desired objectives relative to it.

28. This project did not consider non-regulatory changes in scope. This is because addressing the barrier to using ESS, which is the imposition of a cash tax liability on a person who has only illiquid shares requires legislative change. Non-regulatory options would, therefore, not adequately address the issues.

29. The consideration of proposals was shaped by Ministers, who in 2024 asked officials to re-consult on the deferral proposal. Officials published an issues paper on 31st January 2025 focused on a deferral regime as a result.

30. The scope of the original options was not limited by stakeholder engagement. Because stakeholders were engaged on the problem definition and potential solutions at the same time, the outcome of consultation informed how officials shaped the detail of options 2 and 3, rather than scope of what types of options were considered.

What options are being considered?

Option One – *Status Quo*

31. Option One is to retain the status quo. Companies are currently able to give their employees control over when their tax liability arises by issuing options instead of shares. These options are usually long dated and give the employee the opportunity to purchase shares in the company for a fixed price. The tax liability for these shares will only arise when the option is exercised. Until the option is exercised, the employee holds no equity in the company, has no voting rights and no entitlement to dividends that shareholders may receive.
32. This is officials' preferred option. Officials prefer this option as stakeholder consultation indicated that start-ups are well-versed and content using long-dated options as remuneration for their employees. Some companies may not want an extensive and ever-growing list of shareholders, or the hassle of cancelling or buying back shares if an employee leaves.
33. It is less of an administrative burden to have long-dated options, some of which may never be exercised and no shares issued. Consulted stakeholders generally advised that the tax deferral regime is unlikely to make an impactful difference in the start-up sector and may be seldom used.
34. Stakeholders have also advised that there are alternative tax policies such as concessions that would make a material difference to the New Zealand start-up sector and urged officials to explore potential tax concessions as a future proposal.
35. Tax advisors are comfortable advising clients on the use of long-dated options in this context. However, for companies and employees without tax advisors, long-dated options may be challenging to explain.

Option Two – *Defer tax on employee shares for start-up companies until a liquidity event (option included in officials' issues paper)*

36. Option Two allows start-up companies to issue tax deferred shares to employees. Deferring the payment of tax on ESS shares is not a tax concession so long as the calculation of income from the ESS is also deferred. This is because the expected growth in share price compensates for the revenue implications of a deferral.
37. Start-up companies could be allowed to issue shares on the basis that the calculation of income and payment of tax is deferred until a liquidity event occurs. This would also defer the company's deduction.
38. Option two was the option that was consulted on as part of the 2025 issues paper.
39. Under this option, eligible start-up companies were proposed as:

    39.1. Unlisted companies,
    39.2. Under 10 years old, and
    39.3. With a turnover of less than $15 million

40. Taxing events would include an employee:

    40.1. ceasing to be an employee;
    40.2. ceasing to be a New Zealand tax resident;
    40.3. listing of the company
    40.4. sale or cancellation of shares; or
    40.5. the expiry of seven years since issue of the shares.

41. Officials and submissions identified key challenges with this approach, including;
    - Defining what a start-up company is;
    - Specifying what the liquidity events are; and
    - Clearly distinguishing between ordinary shares and deferral shares so that employers, employees and IRD (all of whom have a role in compliance) can clearly identify when tax should be collected and paid on particular shares.

42. In terms of the first challenge, there is an Australian precedent which defines a start up in terms of gross revenue and period since commencement of business. Under the Australian definition, companies are eligible as start-ups if they are unlisted, younger than 10 years old and with an annual turnover of less than $50 million. It's difficult to comment on the success of the Australian parameters due to lack of commentary on the subject, but Australia has continued to refine the taxing points and start-up eligibility criteria (changed in 2015 and then again in 2022).

43. In terms of the latter two challenges, the employee would need to "opt in" to the deferral regime at the initial issue of the shares. The "deferred tax employee share" would not give rise to income for the employee until a defined liquidity event occurs. These liquidity events would be:

    43.1. **Ceasing to be an employee:** When an employee ceases employment with a group, they may be entitled to retain shares or options that are yet to reach a taxing point. Implementing a rule that triggers the taxing point for shares when an individual leaves a company would provide a tax incentive for an individual to stay with the same company and would prevent issues around the difficulty in employers identifying taxing points for the shares of ex-employees. This is consistent with the rules in Australia.
    43.2. **Ceasing to be a New Zealand Tax resident:** Requiring tax to be paid at the time the individual has left New Zealand would prevent the possibility of tax obligations being ignored due to leaving New Zealand. This is also consistent with other sections of the Income Tax Act 2007 when a liability is crystallised at the point the person ceases to be a New Zealand tax resident, though it is not consistent with the treatment of unexercised ESS options.
    43.3. **Listing of the company:** Once the company hosts an Initial Public Offering (IPO), the complications with valuation are no longer a concern; the value of the share is the market price. At this point, the employee is generally able to sell their shares, or a portion of their shares, and will have the funds to cover their tax liability.

43.4. **Sale of shares by employee:** If the employee sells their shares, they will have the funds to cover their tax liability.

43.5. **Cancellation of shares:** If the employee leaves their company, they may be required to return their shares, or alternatively if the company is acquired or merged, the shares will be cancelled. This will trigger a tax liability.

44. Officials do not recommend this option. Through consultation, officials were repeatedly advised that the criteria for start-ups were too constrained and would not capture the full range of true start-ups. Further, the extensive taxing events mean it would still be easier to delay taxation through the use of long-dated options.

Option Three – *Defer tax on employee shares for all unlisted companies until liquidity (simplified proposal*)

45. Option Three is a simplified version of the issues paper proposal (option 2). It would open the deferral scheme to any New Zealand company that is not part of a listed group. The simplified regime also removes most of the above taxing points referred to in option 2.

46. Under the simplified regime, taxation would occur after the following events:
    - Sale or cancelation of shares
    - Listing of the company; or
    - Payment of a dividend to the deferred shares (payment to other share classes is not a taxing event)

47. The proposal is limited to unlisted companies since a company becoming listed is an indicator that there is a market for the shares of the company, where they can be sold. The tax would be deferred until the shares are sold, cancelled or paid a dividend.

48. On balance, the preferred option of officials is option 1 (retain the status quo). However, officials would also support option 3. The benefits of the Option 3 may grow overtime if the regime is utilised, while its costs should decrease, meaning the benefits may outweigh the costs in the future. If utilised, this option does the best job of achieving the intended outcome, while making the policy non-concessional and as simple as possible for companies to interpret and follow. However, the fiscal and administrative costs associated and the uncertainty of its benefits mean officials do not recommend this option over the status quo.

How do the options compare to the status quo/counterfactual?

	Option One – [*Status Quo / Counterfactual*]	Option Two – Defer tax on employee shares for start-up companies until a liquidity event	Option Three - Defer tax on employee shares for all unlisted companies until liquidity
Addresses tax barrier to ESS	0	0	+
Equity with treatment of cash remuneration	0	0	+
Equity with treatment of long-dated options	0	0/+	+
Administrative cost	0	- -	-
Compliance cost	0	- -	-
Fiscal Cost	0	-	-
Overall assessment	0	- -	0

Example key for qualitative judgements:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

49. Official's preferred option is to maintain the status quo. Broadly, officials believe that current share schemes, particularly long-dated options, provide start-ups with the ability to provide employees with the option to own shares whilst minimising valuation and liquidity issues.

50. Maintaining the status quo would not result in additional benefits, but it also would not result in changes to Government revenue or compliance and administrative costs. On balance, officials do not believe that any other option provides enough of a benefit to either start-ups, non-listed companies, or the New Zealand economy as a whole to outweigh the costs that would be associated. As a result, officials prefer maintaining the status quo.

51. However, provided it can be kept very simple, the deferred employee share option (option 3) can address the problem and meet the policy objectives. Therefore, option 3, is official's second preferred option. The simplified deferral regime is not expected to have material distributional impacts. It may increase the competitiveness of New Zealand start-up companies, by allowing them to offer a wider range of equity remuneration that is not tax disadvantaged.

52. There is uncertainty to whether the deferral regime would be used, in preference to long-dated options. This is one of officials' key concerns with this approach, and is one of the reasons why, on balance, officials recommended the status quo over it. Based on the consultation feedback, a large proportion of companies have already structured options to smooth or defer their ESS tax liability. Therefore, it is hard to know how great the benefit of a deferral regime would be, as there may be few businesses who find it advantageous enough to transfer their already existing long-dated options to a deferral regime. It may provide a greater benefit to new companies or companies that have not yet offered an options scheme to employees.

53. The cost of introducing a deferred employee share scheme is the existence of an additional choice. This will require guidance from Inland Revenue and advice to clients from advisors
s 9(2)(g)(i)
s 18(c)(i)

Is the Minister's preferred option in the Cabinet paper the same as the agency's preferred option in the RIS?

54. Minister's preferred option is to progress with option 3, the simplified deferral regime. This differs from the officials' preferred approach, which is to retain the status quo.

What are the marginal costs and benefits of the preferred option in the Cabinet paper?

Affected groups	**Comment.** *nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks.*	**Impact** *$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts.*	**Evidence Certainty.** *High, medium, or low, and explain reasoning in comment column*
Additional costs of the preferred option compared to taking no action			
Inland Revenue	Inland Revenue will need to publish guidance, maintain an additional piece of legislation, and monitor and enforce compliance	Unknown s 9(2)(g)(i) [redacted]	Medium s 18(c)(i) [redacted]
Early-stage New Zealand companies, their owners and employees	On-going benefit from being able to offer a wider range of equity remuneration schemes on a tax effective basis	Unable to estimate	Low. Although the scheme would result in increased compliance costs initially, there is not much evidence on the likely take up of a simple scheme.
The Government	Reduction in revenue over the forecast period	$9.9 million over forecast	Medium. Costing completed using Inland Revenue data.
Total monetised costs		s 9(2)(g)(i) [redacted]	Medium given the evidence gaps, and our uncertainty as to the increase in compliance costs given the

			extent to which the changes would be taken up by relevant groups is uncertain.
Non-monetised costs		*Low*	
Additional benefits of the preferred option compared to taking no action			
Inland Revenue	N/A	N/A	N/A
Early-stage New Zealand companies, their owners and employees	On-going benefit from being able to offer a wider range of equity remuneration schemes on a tax effective basis	Unable to estimate	Low. There is not much evidence on the likely take up of a simple scheme but consultation feedback suggests take-up is likely to be low.
The Government	N/A	N/A	N/A
Total monetised benefits		Difficult to determine. On balance, there will be a low.	Low-to-Medium given the evidence gaps, and our uncertainty as to the extent to which the changes would be taken up by relevant groups.
Non-monetised benefits		Difficult to determine. On balance, there will be a low to no benefit.	Low

Section 3: Delivering an option

How will the proposal be implemented?

55. The new arrangements will be implemented legislatively by amendments to the Income Tax Act 2007 through the Annual Rates 2025-26 tax Bill as required. The legislative changes will take effect from 1 April 2026.

56. Inland Revenue would be responsible for the implementation and administration of the new rules. Inland Revenue will issue guidance in the Act Commentary and Inland Revenue website to support understanding of the new rules and taxpayer compliance. Internal guidance will also be issued to support operational departments.

57. s 18(c)(i)

How will the proposal be monitored, evaluated, and reviewed?

58. Inland Revenue would monitor the effectiveness of the policy through normal compliance processes. Private sector stakeholders would be able to correspond with officials about the operation of the new rules at any time. If any problems emerge, they will feed into evaluation of the policy.

59. We expect to get feedback over time from industry bodies and advisors as to the level of take up of the deferred employee share scheme. If there are uncertainties or difficulties in applying the law, we expect to receive requests for guidance or law change, and these will be considered through usual processes.