



Corporation Tax relief for employee share acquisitions etc

Draft legislation and Explanatory Note
20 March 2013

This draft legislation clarifies the rules that determine the availability of corporation tax deductions where companies grant share options or award shares to their employees. It will be published as part of the Finance Bill 2013.

The Explanatory Note gives details of how these provisions will apply. They will have effect for accounting periods ending on or after 20 March 2013.

DRAFT LEGISLATION

Corporation tax relief for employee share acquisitions etc

- (1) Chapter 6 of Part 12 of CTA 2009 (relief for employee share acquisitions: relationship between relief under Part 12 and other reliefs) is amended as follows.
- (2) For section 1038 substitute -

"1038 Exclusion of other deductions

- (1) Subsection (2) applies if relief is or, apart from condition 2 in section 1009(1), would be available under this Part.
For this purpose, it does not matter if the amount of the relief is or would be calculated as nil.
- (2) Except as provided for by this Part, for the purpose of calculating any company's profits for corporation tax purposes for any accounting period, no deduction is allowed -
 - (a) in relation to the provision of the shares or to any matter connected with the provision of the shares, or
 - (b) so far as not covered by paragraph (a) in a case in which the shares are acquired pursuant to an option, in relation to the option or to any matter connected with the option.
- (3) In a case in which section 1022 has applied, in subsection (2)(b) references to the option cover the new option and any relevant earlier qualifying option.
- (4) For the purposes of subsection (2) it does not matter if the accounting period in question falls wholly before or after the time at which the shares are acquired.
- (5) In a case in which the shares are acquired under an employee share scheme, the deductions disallowed by subsection (2) include (in particular) deductions for amounts paid or payable by the employing company in relation to the participation of the employee in the scheme.
- (6) But subsection (2) does not disallow deductions for -
 - (a) expenses incurred in setting up the scheme,
 - (b) expenses incurred in meeting, or contributing to, the costs of administering the scheme,
 - (c) the costs of borrowing for the purposes of the scheme, or
 - (d) fees, commission, stamp duty, stamp duty reserve tax, and similar incidental expenses of acquiring the shares.
- (7) "Employee share scheme" means a scheme or arrangement for enabling shares to be acquired because of persons' employment.
- (8) In a case in which relief is or, apart from condition 2 in section 1009(1), would be available under Chapter 5 by virtue of section 1030(2), subsection (2) does not disallow deductions in relation to the provision of the convertible securities."

(3) After section 1038 insert -

"1038A Exclusion of deductions for share options: shares not acquired

- (1) Subsection (2) applies if -
 - (a) a person obtains an option to acquire shares and the requirements of section 1015(1)(a) to (c) are met in relation to the obtaining of the option, or
 - (b) so far as not covered by paragraph (a), a person obtains an option to acquire shares and the obtaining of the option is connected with an option previously obtained in a case covered by paragraph (a) or this paragraph.
- (2) For the purpose of calculating any company's profits for corporation tax purposes for any accounting period, no deduction is allowed in relation to -
 - (a) the option, or
 - (b) any matter connected with the option,unless the shares are acquired pursuant to the option.
- (3) For the purposes of subsection (2) it does not matter if the accounting period in question falls wholly before or after the time at which the option is obtained.
- (4) In a case in which the shares would be acquired under an employee share scheme, the deductions disallowed by subsection (2) include (in particular) deductions for amounts paid or payable by the employing company in relation to the participation of the employee in the scheme.
- (5) But subsection (2) does not disallow deductions for -
 - (a) expenses incurred in setting up the scheme,
 - (b) expenses incurred in meeting, or contributing to, the costs of administering the scheme,
 - (c) the costs of borrowing for the purposes of the scheme, or
 - (d) fees, commission, stamp duty, stamp duty reserve tax, and similar incidental expenses of acquiring the shares.
- (6) "Employee share scheme" means a scheme or arrangement for enabling shares to be acquired because of persons' employment.
- (7) Subsection (2) does not disallow deductions for -
 - (a) amounts on which the employee is subject to a charge under ITEPA 2003,
 - (b) amounts on which the employee would have been subject to a charge under ITEPA 2003 had the employee been a UK employee at all material times, or
 - (c) if the employee has died, amounts on which the employee would have been subject to a charge under ITEPA 2003 had the employee been alive.
- (8) "UK employee" is to be read in accordance with section 1017(4)."

- (4) For the purposes of the following subsections -
"pre-20 March 2013 relevant accounting period" means an accounting period which begins before 20 March 2013 but ends on or after that date, and
"relevant accounting period" means an accounting period which ends on or after 20 March 2013.
- (5) The amendment made by subsection (2) above has effect for the purpose of disallowing deductions for relevant accounting periods.
For this purpose, it does not matter if the acquisition of shares which gives rise, or would give rise, to the relief under Part 12 of CTA 2009 occurs before a company's first relevant accounting period.
- (6) But the amendment made by subsection (2) above has no effect for the purpose of disallowing a deduction for a pre-20 March 2013 relevant accounting period where the acquisition of shares which gives rise, or would give rise, to the relief under Part 12 of CTA 2009 occurs before 20 March 2013.
- (7) The amendment made by subsection (3) above has effect for the purpose of disallowing deductions for relevant accounting periods.
For this purpose, it does not matter if the option is obtained before a company's first relevant accounting period.
- (8) But the amendment made by subsection (3) above has no effect for the purpose of disallowing a deduction for a pre-20 March 2013 relevant accounting period where -
(a) the option is obtained before 20 March 2013, and
(b) before that date, an event (for example, the lapse or cancellation of the option) occurs in consequence of which the shares cannot be acquired pursuant to the option.

EXPLANATORY NOTE

CORPORATION TAX RELIEF FOR EMPLOYEE SHARE ACQUISITIONS ETC

SUMMARY

1. This clause clarifies the rules on availability of corporation tax (CT) deductions where companies award shares or grant share options to their employees. It makes clear that, other than in specified circumstances, no CT deduction is available in relation to an employee share option unless shares are acquired pursuant to that option. It also makes clear that, except in specified circumstances, no other CT deductions should be made in cases where statutory CT relief is available. This legislation will have effect in relation to accounting periods ending on or after 20 March 2013.

DETAILS OF THE CLAUSE

2. Subsection (2) introduces a new section 1038 Corporation Tax Act 2009 (CTA 2009) in place of the current section 1038. The existing legislation excludes other CT deductions where relief for employee share acquisitions is available under Part 12 CTA 2009, and this remains the purpose of the revised section 1038.
3. New subsections 1038(1) and 1038(2) set out the rule that where relief is, or would be, available under Part 12, no other CT deduction is allowed in relation to the provision of shares or share options; or for any connected matter. By virtue of subsection 1038(4) these provisions apply for any accounting period, whether before or after the employee acquires the shares in question.
4. New subsection 1038(3) provides that in cases where section 1022 CTA 2009 (concerning the takeover of a company whose shares are subject to a share option) applies, the exclusion at subsection 1038(2) in relation to share options has effect for any new options granted on the takeover of the company as well as any relevant earlier qualifying option.
5. New subsections 1038(5), 1038(6) and 1038(7) broadly reproduce provisions in the current section 1038, setting out the expenses for which CT deduction is excluded under subsection 1038(2) and providing exceptions to this exclusion in specified circumstances.
6. New subsection 1038(8) disregards deductions relating to the provision of convertible securities that are not shares from the exclusion at subsection 1038(2) in certain cases.
7. Subsection (3) introduces new section 1038A CTA 2009, which clarifies the exclusion of CT deductions in respect of share options pursuant to which shares are not acquired by employees.

8. New subsection 1038A(1) sets out rules applying in the case of share options obtained by employees because of their employment. Subsection 1038A(1)(b) also applies this new section to other share options connected with an option covered by subsection 1038A(1)(a), for example new options issued on a takeover of a company. By virtue of new subsection 1038A(3) these provisions apply for any accounting period, whether before or after the employee obtains the option in question.
9. New subsection 1038A(2) provides that no CT deduction is allowable for any accounting period in relation to a share option or matters connected with it, unless shares are acquired pursuant to the option.
10. New subsection 1038A(4), 1038A(5) and 1038A(6) broadly reproduce provisions in the current section 1038, setting out the expenses for which CT deduction is excluded under new subsection 1038A(2) and providing exceptions to this exclusion in specified circumstances.
11. New subsections 1038A(7) and 1038A(8) provide that subsection 1038A(2) does not disallow a deduction for amounts on which an employee is subject to an income tax charge, or would have been subject to certain circumstances.
12. Subsections (5) and (6) provide that the new section 1038 applies for company accounting periods ending on or after 20 March 2013, regardless of when the acquisition of shares took place. However, the provision will not operate to deny a CT deduction in a company accounting period spanning 20 March 2013 where the shares were acquired before that date.
13. Subsections (7) and (8) provide that the new section 1038A applies for company accounting periods ending on or after 20 March 2013, regardless of when the share option was obtained. However, the provision will not operate to deny a CT deduction in an accounting period spanning 20 March 2013 where an option to acquire shares lapsed or otherwise ceased to be exercisable before that date.

BACKGROUND

14. Where an employee obtains a share option or is awarded shares, CT legislation generally allows the employing company a CT deduction at the point when the employee acquires the shares and, where applicable, is charged to income tax on them.
15. These rules broadly aim to achieve symmetry between the availability of CT relief to the employing company and a charge to income tax on the employee (where applicable).
16. In addition there are more general provisions in CT legislation that a company's taxable trading profits should be calculated by reference to generally accepted accounting practice (GAAP), except where this is specifically overridden in tax legislation.
17. A statutory relief for employee share acquisitions was introduced in 2003 and was designed, where appropriate, to override GAAP. Accounting standards were subsequently introduced to require companies to recognise an accounting expense, measured at fair value, in respect of shares and share options they provide to employees.
18. The argument is sometimes made that companies can deduct accounting expenses recognised for share-based payments against CT, even if the option or award lapses and the employee does not acquire shares; or alternatively that both the accounting expenses and the statutory deduction can be deducted in cases where the employee acquires shares.
19. In the Government's view it is wrong for companies to claim CT deductions for accounting expenses relating to share-based payments where shares are not acquired by the employee, other than where this is specifically provided for in legislation; or to claim what are, in effect, two deductions in respect of an acquisition of shares by an employee. The law has been applied on that basis by HM Revenue & Customs (HMRC) since the current rules were introduced in 2003.
20. HMRC will continue to resist claims of this type, on the basis that they are inadmissible under the terms of existing legislation.
21. The present clause is being introduced to clarify and confirm the position, and remove any uncertainty there may be among taxpayers and advisers about how the rules apply.

Corporation tax deductions for employee share acquisitions

Who is likely to be affected?

Companies granting share options or awarding shares to their employees.

General description of the measure

This measure clarifies legislation that determines the availability of corporation tax (CT) deductions where companies grant share options or award shares to their employees.

Policy objective

The policy objective is to remove any uncertainty as to what CT deductions companies are entitled to claim when they grant share options or award shares to their employees.

Background to the measure

This measure was announced at Budget 2013. It has not been the subject of consultation.

Detailed proposal

Operative date

The measure has effect in relation to accounting periods ending on or after 20 March 2013, irrespective of when shares were awarded or an option was granted. However, the measure will not operate to deny CT deduction in an accounting period spanning 20 March 2013 where the shares are acquired prior to that date or an option to acquire shares lapsed prior to that date.

Current law

Part 12 Corporation Tax Act 2009 (CTA 2009) provides the main statutory rules governing the CT relief available when companies grant share options or award shares to their employees. The general effect of Part 12 CTA 2009 is to link the CT relief available to the amount that is chargeable to income tax when the shares are acquired by the employee; or the amount that would be chargeable to income tax if the employee was a UK resident or if any relevant tax advantages did not apply.

Section 1038 CTA 2009 provides that no other CT deduction is available for expenses directly related to the provision of shares if relief is given under Part 12 CTA 2009, subject to specified exceptions.

Proposed revisions

Legislation will be introduced in Finance Bill 2013 to clarify the rules that govern the CT deductions available where companies grant share options or award shares to their employees.

The legislation clarifies that if relief is given under Part 12 CTA 2009, companies may not claim any other CT deduction in relation to the provision of the employee shares or share options, or in relation to any connected matter, other than where specified.

It also clarifies that, other than in specified circumstances, no CT deductions are available to a company in relation to employee share options, or any matter connected with such an option, unless shares are acquired pursuant to that option.

Summary of impacts

| Exchequer impact (£m) | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 |
|---|---|---------|---------|---------|---------|
| | nil | nil | nil | nil | nil |
| This measure is not expected to have an Exchequer impact. | | | | | |
| Economic impact | The measure is not expected to have any significant economic impacts. | | | | |
| Impact on individuals and households | The measure does not impact upon individuals and households, as it only applies to companies. | | | | |
| Equalities impacts | It is not anticipated that the legislation would impact disproportionately on any individuals with protected characteristics. | | | | |
| Impact on business including civil society organisations | The measure is designed to clarify the rules in relation to CT deductions for employee share awards and options on the same basis as these rules have been applied by HM Revenue & Customs (HMRC) since statutory CT relief for employee share acquisitions was introduced in 2003. It is therefore expected to have no impact on businesses or civil society organisations acting in accordance with HMRC guidance. | | | | |
| Operational impact (£m) (HMRC or other) | It is not expected that implementing this change will incur any additional costs for HMRC. | | | | |
| Other impacts | <p><u>Small firms impact test</u>: the measure concerns general rules governing the availability of CT deductions and therefore applies to all businesses that grant options or award shares to employees. This is primarily a clarifying measure, and is expected to have no impact on small firms currently acting in accordance with HMRC guidance.</p> <p>Other impacts have been considered and none have been identified.</p> | | | | |

Monitoring and evaluation

The measure will be kept under review through regular communication with affected taxpayer groups.

Further advice

If you have any questions about this change, please contact Andrew Ellis on 020 7147 2658 (email: andrew.ellis1@hmrc.gsi.gov.uk).