



Unapproved employee share schemes: Office of Tax Simplification recommendations

Who is likely to be affected?

Businesses that award employment-related securities (ERS) (such as shares) or ERS options to employees, and the employees who receive these awards.

Payroll and share plan administrators.

General description of the measure

The measure will give effect to a number of changes to the tax rules for ERS and ERS options recommended by the Office of Tax Simplification (OTS). These include:

- new taxation and National Insurance contributions (NICs) arrangements for ERS and ERS options awarded to internationally mobile employees (IMEs);
- removal of tax and NICs charges that currently apply on certain share for share exchanges; and
- an extension to circumstances in which corporation tax relief can be claimed when an employee acquires shares following takeover of a company.

In addition, as recommended by the OTS, the measure will change the circumstances in which taxable earnings can arise where an employer meets an employee's tax liability on certain payments of employment income, and will simplify the tax rules in relation to nil-paid and partly-paid ERS and the valuation of listed company shares.

Policy objective

This measure supports the Government's objective to simplify the tax system.

Background to the measure

In July 2011, the Government asked the OTS to identify potential simplifications of the tax rules for employee share schemes. The OTS published its recommendations on 'unapproved' employee share schemes on 16 January 2013.

On 24 May 2013, the Government launched a consultation on five of the recommendations made by the OTS.

A summary of responses to this consultation was published on 10 December 2013.

Detailed proposal

Operative date

Changes to section 222 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) will have effect from 6 April 2014.

The income tax, corporation tax and NICs changes in relation to ERS and ERS options awarded to IMEs will apply to grants and awards made on or after 1 September 2014.

Other changes will have effect from the date that Finance Bill 2014 receives Royal Assent.

Current law

Part 7 of ITEPA provides rules for the taxation of employment income relating to ERS and ERS options. Sections 421E and 474 include provisions relating to residence.

The acquisition of ERS is a payment of earnings liable for Class 1 NICs (section 3 of the Social Security Contributions and Benefits Act 1992 (SSCBA 1992)). Section 4(4)(a) of the SSCBA 1992 treats gains from the exercise, assignment or release of an ERS option as earnings. Regulation 22(7) of the Social Security (Contributions) Regulations 2001 (SSCR 2001) ensures that the NICs treatment of ERS is generally aligned with their income treatment under Chapters 2 to 4A of Part 7 ITEPA. However, UK NICs liability can be affected by relevant EU legislation and bilateral Reciprocal Agreements/Double Contribution Conventions on social security.

Section 483 of ITEPA provides the rules that apply where ERS options are assigned or released by an employee in exchange for new ERS options. There are no similar provisions in place for restricted shares or other types of ERS.

Chapter 3C to Part 7 of ITEPA provides rules that apply where ERS are acquired for less than market value (including nil-paid and partly-paid ERS).

Part 12 of the Corporation Tax Act 2009 (CTA 2009) provides corporation tax (CT) relief for employee share acquisitions, subject to certain conditions. These include (at sections 1008 and 1016) conditions relating to the shares acquired. Sections 1007 and 1015 of CTA 2009 set out basic requirements for relief. These requirements include a link between the acquisition of shares and a person's employment, and conditions concerning the business undertaken by the employing company.

Section 222 of ITEPA deals with cases in which an employer is required to make a payment on account of PAYE tax in relation to a notional payment of taxable income to an employee from which a deduction was not possible. It provides that the payment on account by the employer will be treated as earnings from the employment, and therefore taxable income of the employee, if this is not made good to the employer within 90 days of the event that causes the notional payment. For NICs, an amount which is treated as earnings by virtue of section 222 of ITEPA is treated as earnings liable for Class 1 NICs in accordance with regulation 22(4) of the SSCR 2001.

Section 272(3) of the Taxation of Chargeable Gains Act 1992 (TCGA) sets out the usual methods to be applied when determining for tax purposes the market value of shares or securities listed in The Stock Exchange Daily Official List.

Proposed revisions

Legislation in Finance Bill 2014 will introduce a new Chapter 5B of Part 2 of ITEPA, to more broadly align the tax rules for ERS and ERS options awarded to IMEs with those already in place for other types of employment income. This will involve the establishment of rules around the 'relevant periods' for each category of ERS, and provisions for apportionment within these relevant periods between amounts chargeable to tax in the UK and other income. The NICs position will be aligned as far as possible with the new income tax rules through secondary legislation.

Legislation in Finance Bill 2014 will apply a new income tax rollover relief in Part 7 of ITEPA for cases where restricted, nil-paid or partly-paid ERS are exchanged for new securities of the same type. Chapter 3C of Part 7 (concerning securities acquired for less than market value) will also be simplified more generally in relation to nil-paid and partly-paid ERS and the discharge of notional loans.

The CT relief for employee share acquisitions at Part 12 CTA 2009 will be extended by Finance Bill 2014. Subject to certain conditions, this relief will be available in relation to shares acquired within a 90 day period following the takeover of a company by an unlisted company, and shares acquired by an overseas individual seconded to work for a UK company.

Legislation in Finance Bill 2014 will also change the deadline at section 222 of ITEPA. This deadline concerns the period within which an employee must make good a PAYE amount paid by their employer on account of tax due on a payment received by that employee, if a charge is not to apply. This deadline will be changed from 90 days from the date of the event that causes the notional payment to 90 days after the end of the tax year in which that event occurred.

Section 272 of TCGA will also be amended to replace the current methods for calculating market value of listed shares or securities specified at (a) and (b) of subsection (3) with a single method based on the closing price of the shares or securities on the relevant trading day.

Summary of impacts

Exchequer impact (£m)	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
	-	+5	+5	+5	+20	+20
	These figures are set out in Table 2.1 of the Autumn Statement and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside the Autumn Statement.					
Economic impact	The measure is not expected to have any significant economic impacts.					
Impact on individuals and households	Changes to the rules on IMEs and valuation could increase or reduce the amount of tax chargeable on individuals, depending upon the circumstances. Changes to the tax treatment of ERS exchanges and nil-paid and partly-paid shares, and the change to the deadline at section 222 of ITEPA, will reduce tax costs in certain circumstances.					
Equalities impacts	Detailed information on the award of ERS or ERS options to or by individuals with protected characteristics is not available. However, it is not anticipated that any of the proposed changes will impact disproportionately on any individuals with protected characteristics.					
Impact on business including civil society organisations	<p>The measure simplifies the rules for the taxation of ERS and ERS options, and will provide greater clarity for businesses.</p> <p>The impact upon each individual business will depend upon the extent to which they carry out ERS transactions covered by this measure. Overall however, the changes are expected to have a negligible impact on businesses. There will be some savings for individual businesses (depending upon their particular circumstances) but the changes could impose one-off familiarisation and/ or compliance costs in some cases.</p> <p>Changes to the rules on IMEs could increase business costs by requiring updates to payroll and other record keeping processes - and may require additional monitoring or tracking of ERS awards in some cases. These costs will depend upon the particular circumstances of the business and the relevant IMEs. However, it is also anticipated that long-term savings for businesses could arise from the increased consistency, clarity and simplicity these changes will provide.</p>					

	Changes to the rules on ERS exchanges and corporation tax relief will reduce costs and complexity associated with businesses structuring arrangements around these rules.
Operational impact (£m) (HMRC or other)	The costs or savings for HM Revenue & Customs in implementing these changes are anticipated to be negligible.
Other impacts	<u>Small and micro business assessment</u> : no major issues specific to smaller businesses have been identified. Other impacts have been considered and none have been identified.

Monitoring and evaluation

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

Further advice

If you have any questions about this change, please contact Colin Strudwick on 03000 585275 (email: colin.strudwick@hmrc.gsi.gov.uk).

1 Payments made by employer on account of tax where deduction not possible

- (1) In section 222 of ITEPA 2003 (payments by employer on account of tax where deduction not possible), in subsection (1)(c), for “before the end of the period of 90 days beginning with the relevant date” substitute “within 90 days after the end of the tax year in which the relevant date falls”.
- (2) The amendment made by this section has effect in relation to payments of income treated as made on or after 6 April 2014.

2 Employment-related securities etc

Schedule 1 contains provision relating to employment-related securities.

SCHEDULES

SCHEDULE 1

Section 2

EMPLOYMENT-RELATED SECURITIES ETC

PART 1

INTERNATIONALLY MOBILE EMPLOYEES

- 1 ITEPA 2003 is amended as follows.
- 2 Part 2 (employment income: charge to tax) is amended as follows.
- 3 In section 6 (nature of charge to tax on employment income), in subsection (3A), for “Chapter 5A” substitute “Chapter 5B”.
- 4 In section 10 (meaning of “taxable earnings” and “taxable specific income”), in subsection (4), for the words from “Chapter 5A” to the end substitute “Chapter 5B (taxable specific income from employment-related securities etc: internationally mobile employees)”.
- 5 For Chapter 5A (taxable specific income: effect of remittance basis) substitute—

“CHAPTER 5B

TAXABLE SPECIFIC INCOME FROM EMPLOYMENT-RELATED SECURITIES ETC: INTERNATIONALLY MOBILE EMPLOYEES

41F Taxable specific income: internationally mobile employees etc

- (1) This section applies if—
 - (a) an amount counts under Chapters 2 to 5 of Part 7 (employment-related securities etc) as employment income of an individual for a tax year (“the securities income”) in respect of an employment (“the relevant employment”), and
 - (b) one or more of the international mobility conditions is met in relation to the individual (see subsection (2)).
- (2) The “international mobility conditions” are—
 - (a) that any part of the relevant period (see section 41G) is within a tax year for which section 809B, 809D or 809E of ITA 2007 (remittance basis) applies to the individual;
 - (b) that any part of the relevant period is within a tax year for which the individual is not UK resident;
 - (c) that any part of the relevant period is within the overseas part of a tax year that is a split year with respect to the individual.

- (3) An amount equal to—
SI – FSI
is an amount of “taxable specific income” from the relevant employment for the tax year mentioned in subsection (1)(a).
- (4) In subsection (3)—
(a) SI is the amount of the securities income, and
(b) FSI is the amount of the securities income that is “foreign”.
- (5) The amount of the securities income that is “foreign” is the sum of any chargeable foreign securities income and any unchargeable foreign securities income (see sections 41H to 41J).
- (6) The full amount of any chargeable foreign securities income which is remitted to the United Kingdom in a tax year is an amount of “taxable specific income” from the relevant employment for that year.
- (7) Subsection (6) applies whether or not the relevant employment is held when the chargeable foreign securities income is remitted.
- (8) For the purposes of Chapter A1 of Part 14 of ITA 2007 (remittance basis), treat the relevant securities or relevant securities option as deriving from the chargeable foreign securities income.
- (9) But where—
(a) the chargeable event is the disposal of the relevant securities or the assignment or release of the relevant securities option, and
(b) the individual receives consideration for the disposal, assignment or release of an amount equal to or exceeding the market value of the relevant securities or relevant securities option,
for the purposes of that Chapter treat the consideration (and not the relevant securities or relevant securities option) as deriving from the chargeable foreign securities income.
- (10) See Chapter A1 of Part 14 of ITA 2007 for the meaning of “remitted to the United Kingdom”.
- (11) In this section and section 41G—
“the chargeable event” means the event giving rise to the securities income, and
“the relevant securities” or “the relevant securities option” means the employment-related securities or employment-related securities option by virtue of which the amount mentioned in subsection (1)(a) counts as employment income.

41G Section 41F: the relevant period

- (1) “The relevant period” is to be determined as follows.
- (2) In the case of an amount that counts as employment income by virtue of Chapter 2 of Part 7 (restricted securities) (other than where subsection (4) applies) or Chapter 3 of that Part (convertible securities), the relevant period—

- (a) begins with the day of the acquisition, and
 - (b) ends with the day of the chargeable event.
- (3) In the case of an amount that counts as employment income by virtue of section 446B (securities with artificially depressed market value: charge on acquisition), the relevant period is the tax year in which the acquisition occurs.
- (4) In a case within subsection (1)(aa) or (b) of section 446E (securities with artificially depressed market value: charge on restricted securities) where an amount counts as employment income by virtue of that section, the relevant period –
- (a) begins at the beginning of the tax year in which the chargeable event is treated as occurring, and
 - (b) ends with the day on which the chargeable event is treated as occurring.
- (5) In the case of an amount that counts as employment income by virtue of section 446L (securities with artificially enhanced market value), the relevant period –
- (a) begins at the beginning of the tax year in which the valuation date (within the meaning of that section) falls, and
 - (b) ends with the valuation date.
- (6) In the case of an amount that counts as employment income by virtue of section 446U (securities acquired for less than market value: discharge of notional loan) or 446UA (avoidance cases in respect of such securities) –
- (a) if the relevant securities were acquired by virtue of the exercise of a securities option (“the option”), the relevant period –
 - (i) begins with the day of the acquisition of the option, and
 - (ii) ends with the day the option vests, and
 - (b) otherwise, the relevant period is –
 - (i) the tax year in which the notional loan (within the meaning of Chapter 3C of Part 7) is treated as made, or
 - (ii) if the chargeable event occurs in that year, the period beginning at the beginning of that year and ending with the day of that event.
- (7) In the case of an amount that counts as employment income by virtue of –
- (a) Chapter 3D of Part 7 (securities disposed of for more than market value), or
 - (b) Chapter 4 of that Part (post-acquisition benefits from securities),
- the relevant period is the tax year in which the chargeable event occurs.
- (8) In the case of an amount that counts as employment income by virtue of Chapter 5 of Part 7 (employment-related securities options), the relevant period –
- (a) begins with the day of the acquisition, and

- (b) ends with the day of the chargeable event or, if earlier, the day the relevant securities option vests.
- (9) If the relevant period determined in accordance with subsections (2) to (8) would not, in all the circumstances, be just and reasonable, the relevant period is to be such period as is just and reasonable.
- (10) In this section “the acquisition” has the same meaning as in Chapters 2 to 4 or Chapter 5 of Part 7 (see section 421B or 471).
- (11) For the purposes of this section an option “vests” –
 - (a) when it becomes exercisable, or
 - (b) if earlier, when it becomes exercisable subject only to a period of time expiring.
- (12) See section 41F(11) for the definitions of “the chargeable event”, “the relevant securities” and “the relevant securities option”.

41H Section 41F: chargeable and unchargeable foreign securities income

- (1) The extent to which the securities income is “chargeable foreign securities income” or “unchargeable foreign securities income” is to be determined as follows.
- (2) Treat an equal amount of the securities income as accruing on each day of the relevant period.
- (3) If any part of the relevant period is within a tax year to which subsection (4) applies, the securities income treated as accruing in that part of the relevant period is “chargeable foreign securities income”.

This is subject to section 41I (limit where duties of associated employment performed in UK).
- (4) This subsection applies to a tax year if –
 - (a) section 809B, 809D or 809E of ITA 2007 applies to the individual for the year,
 - (b) the individual does not meet the requirement of section 26A for the year (reading references there to the employee as references to the individual),
 - (c) the relevant employment is with a foreign employer, and
 - (d) the duties of the relevant employment are performed wholly outside the United Kingdom in the year.
- (5) If any part of the relevant period is within a tax year to which subsection (6) applies –
 - (a) if the duties of the relevant employment are performed wholly outside the United Kingdom, the securities income treated as accruing in that part of the relevant period is “chargeable foreign securities income”, and
 - (b) if some, but not all, of those duties are performed outside the United Kingdom –
 - (i) the securities income mentioned in paragraph (a) is to be apportioned (on a just and reasonable basis) between duties performed in the United Kingdom and duties performed outside the United Kingdom, and

- (ii) the income apportioned in respect of duties performed outside the United Kingdom is “chargeable foreign securities income”.
- (6) This subsection applies for a tax year if –
 - (a) section 809B, 809D or 809E of ITA 2007 applies to the individual for the year,
 - (b) the individual meets the requirement of section 26A for the year (reading references there to the employee as references to the individual), and
 - (c) some or all of the duties of the relevant employment are performed outside the United Kingdom in the year.
- (7) If any part of the relevant period is within a tax year for which the individual is not UK resident –
 - (a) if the duties of the relevant employment are performed wholly outside the United Kingdom in that year, the securities income treated as accruing in that part of the relevant period is “unchargeable foreign securities income”, or
 - (b) if some, but not all, of those duties are performed outside the United Kingdom in that year –
 - (i) the securities income mentioned in paragraph (a) is to be apportioned (on a just and reasonable basis) between duties performed in the United Kingdom and duties performed outside the United Kingdom, and
 - (ii) the income apportioned in respect of duties performed outside the United Kingdom is “unchargeable foreign securities income”.
- (8) If any part of the relevant period is within the overseas part of a tax year that is a split year with respect to the individual –
 - (a) if the duties of the relevant employment are performed wholly outside the United Kingdom in that overseas part, the securities income treated as accruing in that part of the relevant period is “unchargeable foreign securities income”, or
 - (b) if some, but not all, of those duties are performed outside the United Kingdom in that overseas part –
 - (i) the securities income mentioned in paragraph (a) is to be apportioned (on a just and reasonable basis) between duties performed in the United Kingdom and duties performed outside the United Kingdom, and
 - (ii) the income apportioned in respect of duties performed outside the United Kingdom is “unchargeable foreign securities income”.
- (9) This section is subject to section 41J (chargeable and unchargeable foreign securities income: just and reasonable apportionment).

41I Limit on “chargeable foreign securities income” where duties of associated employment performed in UK

- (1) This section imposes a limit on the extent to which section 41H(3) applies in relation to a period when –
 - (a) the individual holds associated employments as well as the relevant employment, and
 - (b) the duties of the associated employments are not performed wholly outside the United Kingdom.
- (2) The amount of the securities income for the period that is to be regarded as “chargeable foreign securities income” is limited to such amount as is just and reasonable, having regard to –
 - (a) the employment income for the period from all the employments mentioned in subsection (1)(a),
 - (b) the proportion of that income that is general earnings to which section 22 applies (chargeable overseas earnings),
 - (c) the nature of, and time devoted to, the duties performed outside the United Kingdom, and those performed in the United Kingdom, in the period, and
 - (d) all other relevant circumstances.
- (3) In this section “associated employments” means employments with the same employer or with associated employers.
- (4) Section 24(5) and (6) (meaning of “associated employer”) applies for the purposes of this section.

41J Chargeable and unchargeable foreign securities income: just and reasonable apportionment

- (1) This section applies if the proportion of the securities income that would otherwise be regarded as “chargeable foreign securities income” or “unchargeable foreign securities income” is not, having regard to all the circumstances, just and reasonable.
- (2) The amounts of the securities income that are “chargeable foreign securities income” and “unchargeable foreign securities income” are such amounts as are just and reasonable (rather than the amounts calculated in accordance with section 41H).”

6 Part 7 (employment income: income and exemptions relating to securities) is amended as follows.

7 In section 418 (other related provisions), before subsection (1) insert –

“(A1) This Part needs to be read with Chapter 5B of Part 2 (taxable specific income from employment-related securities etc: internationally mobile employees).”

8 Omit section 421E (employment-related securities: exclusions, residence etc).

9 In section 425 (no charge in respect of acquisition in certain cases), after subsection (5) insert –

“(6) No election may be made under subsection (3) unless, at the time of the acquisition, the earnings from the employment are (or would be

- if there were any) general earnings to which any of the charging provisions of Chapters 4 and 5 of Part 2 applies.”
- 10 In section 430 (election for outstanding restrictions to be ignored), after subsection (3) insert –
- “(4) No election may be made under this section unless, at the time of the chargeable event, the earnings from the employment are (or would be if there were any) general earnings to which any of the charging provisions of Chapters 4 and 5 of Part 2 applies.”
- 11 In section 431 (election for full or partial disapplication of Chapter 2 of Part 7 of ITEPA 2003), after subsection (5) insert –
- “(6) No election may be made under this section unless, at the time of the acquisition, the earnings from the employment are (or would be if there were any) general earnings to which any of the charging provisions of Chapters 4 and 5 of Part 2 applies.”
- 12 Omit section 474 (cases where Chapter 5 of Part 7 of ITEPA 2003 (employment-related securities options) does not apply).
- 13 Part 7A (employment income provided through third parties) is amended as follows.
- 14 In section 554L (exclusions: earmarking for employee share schemes (3)), in subsection (10)(c)(i), for “section 474” substitute “Chapter 5B of Part 2”.
- 15 (1) Section 554M (exclusions: earmarking for employee share schemes (4)) is amended as follows.
- (2) In subsection (9)(b)(i), for “section 474” substitute “Chapter 5B of Part 2”.
- (3) In subsection (10)(b)(i), for “section 474” substitute “Chapter 5B of Part 2”.
- 16 (1) Section 554N (exclusions: other cases involving employment-related securities etc) is amended as follows.
- (2) In subsection (1)(b), omit “, or would apply apart from section 421E(1),”.
- (3) In subsection (2)(b), omit “, or would apply apart from section 474(1),”.
- (4) In subsection (6) –
- (a) omit “421E(1),” and
- (b) omit “, 474(1)”.
- (5) In subsection (10) –
- (a) in paragraph (b), omit “, but ignoring section 474(1)”, and
- (b) in paragraph (c), omit “or would be a chargeable event apart from section 474(1)”.
- (6) In subsection (13)(c)(i), for “section 474” substitute “Chapter 5B of Part 2”.
- 17 In Chapter 4 of Part 11 (PAYE: special types of income), in section 700A (employment-related securities etc: remittance basis), in subsection (3), for “41A” substitute “41F”.

PART 2

RESTRICTED SECURITIES AND SECURITIES ACQUIRED FOR LESS THAN MARKET VALUE:
REPLACEMENT AND ADDITIONAL SECURITIES AND ROLLOVER RELIEF ETC

- 18 ITEPA 2003 is amended as follows.
- 19 (1) In Chapter 1 of Part 7 (income and exemptions relating to securities: general), section 421D (replacement and additional securities and changes in interests) is amended as follows.
- (2) In subsection (3), insert at the end “and for the purposes of Chapter 3C as a payment made for their acquisition at or before the time of the acquisition”.
- (3) In subsection (4), insert at the end “or a payment was made for their acquisition at or before the time of the acquisition”.
- 20 In Chapter 2 of Part 7 (restricted securities), before section 431 (election for full or partial disapplication of Chapter 2) but after the heading before that section (supplementary) insert –

“430A Application of this Chapter where securities exchanged for further securities

- (1) This section applies if –
- (a) an associated person disposes of the employment-related securities (the “old securities”) for consideration, otherwise than to another associated person,
 - (b) the whole or part of the consideration consists of, or includes, other securities which are restricted securities (the “new securities”) being acquired by an associated person,
 - (c) the value of the consideration determined in accordance with subsection (2) is no more than what would have been the market value of the old securities immediately before the disposal but for any restrictions, and
 - (d) the avoidance of tax or national insurance contributions is not the main purpose (or one of the main purposes) of the disposal.
- (2) The value of the consideration is the sum of –
- (a) what would have been the market value of the new securities immediately before the disposal but for any restrictions, and
 - (b) the value of the rest of the consideration (if any).
- (3) If the consideration consists partly of the new securities and partly of other consideration, the disposal is to be treated for the purposes of this Chapter as being two separate disposals as follows –
- (a) a disposal, that is a chargeable event within section 427(3)(c), of the appropriate amount of the old securities (see subsection (4)) for such of the consideration as does not consist of the new securities, and
 - (b) a disposal, to which this section applies, of the remaining old securities for consideration consisting wholly of the new securities.

- (4) In subsection (3)(a) the appropriate amount of the old securities is –

$$OS \times \frac{OC}{TC}$$

where –

OS is the total number of the old securities,

OC is the value of such of the consideration as does not consist of the new securities, and

TC is value of the consideration determined in accordance with subsection (2).

- (5) If the consideration consists wholly of the new securities –
- (a) neither the disposal of the old securities, nor the acquisition of the new securities, gives rise to any liability to income tax,
 - (b) the disposal is not a chargeable event within section 427(3)(c), and
 - (c) this Chapter applies to the new securities as it applies to the old securities, subject to subsections (6) to (17).
- (6) No election may be made under section 425 or 431 in relation to the new securities.
- (7) If, at the time of the disposal, sections 426 to 429 do not apply to the old securities by virtue of –
- (a) an election made under section 430(1) or 431(1) in relation to the old securities, or
 - (b) this subsection,
- sections 426 to 430 do not apply to the new securities.
- (8) If there is a chargeable event for the purposes of section 426 in relation to any of the new securities, for the purposes of section 428 (amount of charge) –
- (a) IUP (see subsection (3) of that section) is to be determined in accordance with subsection (9), and
 - (b) PCP (see subsection (4) of that section) is to be determined in accordance with subsection (10).
- (9) IUP is equal to what IUP was, for the purposes of determining the taxable amount for the purposes of section 426, in relation to chargeable events relating to the old securities that occurred before the disposal (or what it would have been had there been any such chargeable events).
- (10) PCP is the aggregate of –
- (a) PCP determined in accordance with section 428(4), and
 - (b) what PCP would have been, for the purposes of determining the taxable amount for the purposes of section 426, if a chargeable event relating to the old securities had occurred immediately before the disposal but after any chargeable events relating to the old securities that actually did occur before the disposal.
- (11) Subsections (12) to (14) apply if –

- (a) section 425(2) (no liability to income tax on acquisition of certain securities subject to forfeiture etc) applied in relation to the old securities, and
 - (b) at the time of the disposal, there is still a restriction relating to those securities such that they are restricted securities by virtue of section 423(2) (provision for forfeiture etc).
 - (12) This Chapter has effect in relation to any of the new securities that are not restricted securities by virtue of section 423(2) as if –
 - (a) there were a restriction relating to them (“the deemed restriction”) corresponding to the restriction relating to the old securities mentioned in subsection (11)(b), and
 - (b) immediately after their acquisition, the deemed restriction were removed.
 - (13) Subsection (14) applies if –
 - (a) there is a restriction by virtue of which some or all of the new securities are, at the time of the disposal, restricted securities, by virtue of subsection (2) of section 423, and
 - (b) within 5 years after the acquisition of the old securities, the restriction is not removed or varied such that the new securities to which it relates cease to be restricted securities by virtue of that subsection.
 - (14) For the purposes of this Chapter the restriction mentioned in subsection (13) is to be treated as being removed 5 years after the acquisition of the old securities.
 - (15) Subsection (16) applies if, at the time of the disposal –
 - (a) there is a restriction relating to the old securities such that they are restricted securities by virtue of section 423(2), and
 - (b) subsections (13) and (14) apply in relation to the old securities (including by virtue of subsection (16)).
 - (16) Subsections (12) to (14) apply in relation to the new securities, but the references in subsections (13)(b) and (14) to the acquisition of the old securities are to be read as references to the acquisition of the original forfeitable securities.
 - (17) In subsection (16) “original forfeitable securities” means the restricted securities by virtue of the application to which of section 425(2) subsections (13) and (14) apply to the old securities.
 - (18) In this section references to restricted securities include a restricted interest in securities.”
- 21 (1) In Chapter 3C of Part 7 (securities acquired for less than market value), section 446U (discharge of notional loan) is amended as follows.
- (2) In subsection (1), omit the “or” at the end of paragraph (a) and for paragraph (b) substitute –
- “(b) if there is an outstanding or contingent liability to pay for the employment-related securities, that liability is released, extinguished, transferred or adjusted so as no longer to bind any associated person (except in circumstances in which subsection (4)(aa) applies), or”.

- (3) After that subsection insert –
- “(1A) Subsection (1)(a) does not apply if, at the time of the acquisition, there was an actual or contingent liability to make one or more further payments equal to the amount initially outstanding for the employment-related securities.”
- (4) In subsection (4), omit the “or” at the end of paragraph (a) and after that paragraph insert –
- “(aa) the employment-related securities are disposed of otherwise than to an associated person together with the liability to make such further payment or payments for consideration of an amount that reflects the transfer of the liability, or”.
- 22 In section 554N (exclusions from Chapter 2 of Part 7A: other cases involving employment related securities etc), in subsection (6), after “429,” insert “430A(5)(b),”.

PART 3

CT RELIEF FOR EMPLOYEE SHARE ACQUISITIONS

- 23 Part 12 of CTA 2009 (other relief for employee share acquisitions) is amended as follows.
- 24 In Chapter 1 (introduction), in section 1002 (“employment”), after subsection (4) insert –
- “(5) See also sections 1007A and 1015A (application of Chapters 2 and 3 in relation to employees of overseas companies who work for companies in the UK).”
- 25 In Chapter 2 (CT relief if shares are acquired by employee or other person), after section 1007 insert –

“1007A Application of Chapter in relation to employees of overseas companies who work for companies in the UK

- (1) This section applies if –
- (a) a person has an employment (“the actual employment”) with a non-UK resident company that is not within the charge to corporation tax (“the overseas employer”),
 - (b) in performing any of the duties of the actual employment, the person works in the United Kingdom for, but is not employed by, another company (“the host employer”), and
 - (c) the host employer is –
 - (i) a UK resident company, or
 - (ii) a non-UK resident company that is within the charge to corporation tax.
- (2) For the purposes of this Chapter, the person is to be treated as having an employment with the host employer, the duties of which consist of the work the person does for the host employer.
- (3) In section 1008 (conditions relating to the shares acquired) references to the employing company are to be read as including references to the overseas employer.

- (4) If the amount of relief would otherwise be more than the amount of employment income of the person charged to tax under ITEPA 2003 in relation to the acquisition of the shares, the amount of relief is (notwithstanding any other provision of this Chapter) limited to the amount of that income so charged.
- (5) If relief is available to more than one host employer in respect of the same acquisition of shares, relief may only be given to one of them in respect of that acquisition.
- (6) For the purposes of this section a person works for another person if the person provides, and is obliged to provide, personal service to the other person.”

26 In Chapter 3 (CT relief if employee or other person obtains option to acquire shares), after section 1015 insert –

“1015A Application of Chapter in relation to employees of overseas companies who work for companies in the UK

- (1) This section applies if –
 - (a) a person has an employment (“the actual employment”) with a non-UK resident company that is not within the charge to corporation tax (“the overseas employer”),
 - (b) in performing any of the duties of the actual employment, the person works in the United Kingdom for, but is not employed by, another company (“the host employer”), and
 - (c) the host employer is –
 - (i) a UK resident company, or
 - (ii) a non-UK resident company that is within the charge to corporation tax.
- (2) For the purposes of this Chapter, the person is to be treated as having an employment with the host employer, the duties of which consist of the work the person does for the host employer.
- (3) In section 1016 (conditions relating to the shares acquired) references to the employing company are to be read as including references to the overseas employer.
- (4) If the amount of relief would otherwise be more than the amount of employment income of the person charged to tax under ITEPA 2003 in relation to the acquisition of the shares pursuant to the option, the amount of relief is (notwithstanding any other provision of this Chapter) limited to the amount of that income so charged.
- (5) If relief is available to more than one host employer in respect of the same acquisition of shares pursuant to an option, relief may only be given to one of them in respect of that acquisition.
- (6) For the purposes of this section a person works for another person if the person provides, and is obliged to provide, personal service to the other person.”

27 (1) Section 1016 (conditions relating to shares acquired) is amended as follows.

(2) In subsection (1), omit the “or” at the end of paragraph (b) of Condition 2 and

after paragraph (c) of that Condition insert “, or
 (d) shares within subsection (1A)”.

(3) After subsection (1) insert –

“(1A) Shares are within this subsection if –

- (a) after the option is obtained, the company in which the shares are to be acquired (“the relevant company”) comes to be controlled by another company (“the takeover”),
- (b) immediately before the takeover, the shares were within any of paragraphs (a) to (c) of Condition 2,
- (c) as a result of the takeover, the shares cease to be within any of those paragraphs,
- (d) the shares are acquired pursuant to the option within the period of 90 days beginning with the day of the takeover, and
- (e) the avoidance of tax is not the main purpose (or one of the main purposes) of the takeover.”

28 In Chapter 4 (additional CT relief in cases involving restricted shares), after section 1025 insert –

“1025A Application of Chapter in relation to employees of overseas companies who work for companies in the UK

- (1) This section applies if the original relief is available under –
 - (a) Chapter 2 as a consequence of section 1007A, or
 - (b) Chapter 3 as a consequence of section 1015A.
- (2) If the amount of relief available as a result of a chargeable event would otherwise be more than the amount of employment income of the employee charged to tax under ITEPA 2003 in relation to the event, the amount of relief is (notwithstanding any other provision of this Chapter) limited to the amount of that income so charged.
- (3) If relief is available to more than one company as a result of the same chargeable event, relief may only be given to one of them in respect of that event.
- (4) No relief is available as a result of the employee’s death.”

29 In Chapter 5 (additional CT relief in cases involving convertible shares), after section 1030 insert –

“1030A Application of Chapter in relation to employees of overseas companies who work for companies in the UK

- (1) This section applies if the original relief is, or (in the case of convertible securities that are not shares) would have been, available under –
 - (a) Chapter 2 as a consequence of section 1007A, or
 - (b) Chapter 3 as a consequence of section 1015A.
- (2) If the amount of relief available as a result of a chargeable event would otherwise be more than the amount of employment income of the employee charged to tax under ITEPA 2003 in relation to the event, the amount of relief is (notwithstanding any other provision of this Chapter) limited to the amount of that income so charged.

- (3) If relief is available to more than one company as a result of the same chargeable event, relief may only be given to one of them in respect of that event.
- (4) No relief is available as a result of the employee’s death.”

PART 4

COMMENCEMENT

- 30 The amendments made by Part 1 of this Schedule have effect in relation to employment-related securities and employment-related securities options where the date of the acquisition is on or after 1 September 2014 (except employment-related securities acquired pursuant to an option acquired before that date).
- 31 In Part 3 of this Schedule, paragraphs 24 to 26, 28 and 29 come into force on 1 September 2014.

EXPLANATORY NOTE

PAYMENTS MADE BY EMPLOYER ON ACCOUNT OF TAX WHERE DEDUCTION NOT POSSIBLE

EMPLOYMENT-RELATED SECURITIES ETC

SUMMARY

1. Clauses [X & Y] and Schedule [Z] implement a number of recommendations made by the Office of Tax Simplification (OTS) to simplify the tax rules in relation to employment-related securities (ERS) - such as employee shares - or ERS options awarded to employees. It changes the tax treatment of ERS and ERS options awarded to internationally mobile employees, introduces a new relief for certain ERS exchanges, simplifies the rules around nil-paid and partly-paid ERS and extends the corporation tax relief available to companies in relation to employee share acquisitions. It also changes the deadline for employees to make good to their employer amounts the employer has paid to HM Revenue and Customs in respect of the tax due on notional (non-cash) payments received by the employee, before that employee is liable to a tax charge on the relevant amount.

DETAILS OF CLAUSE [X]

2. Subsection (1) of Clause 1 amends section 222 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) concerning payments made by an employer on account of tax, in cases where the deduction of tax amounts on notional (non-cash) payments to an employee (such as ERS income) is not possible. The amendment changes the deadline for an employee to make good the relevant amount to their employer before this outstanding amount is treated as earnings of that employee (and is therefore subject to a tax charge). This deadline is currently 90 days after the notional payment is made by the employer, and will be changed to 90 days after the end of the relevant tax year.

DETAILS OF THE SCHEDULE

Part 1 Internationally mobile employees

3. Paragraphs 1 to 5 amend Part 2 of ITEPA by substituting a new Chapter 5B (taxable specific income from employment-related securities: internationally mobile employees etc) for the current Chapter 5A (taxable specific income: effect of the remittance basis) and making consequential amendments to sections 6 and 10 of ITEPA. The new Chapter 5B comprises sections 41F to 41J, which set out new rules for the taxation of ERS and ERS options received by internationally mobile employees, and also contain provisions on the effect of the remittance basis on ERS income that are currently in Chapter 5A.

4. These new sections of ITEPA set out what income from ERS and ERS options (securities income) is to be subject to UK income tax, either on the normal ‘arising’ basis or the remittance basis where this applies. The effect of the remittance basis is that, broadly, for those to whom the remittance basis applies, income or gains in respect of foreign duties are only taxable in the UK to the extent that they are remitted to (brought into, used in, or enjoyed in) the UK.

5. New section 41F of ITEPA includes subsection (1) and (2), which set out the scope of the new rules. They apply when an amount counts as employment income under Chapters 2 to 5 of Part 7 of ITEPA (which provides rules for the taxation of ERS and ERS options) and at least one of the ‘international mobility conditions’ specified in subsection (2) are met. The rules at subsections (3) and (4) identify the amount of securities income from the relevant employment for the tax year that will be subject to income tax on the arising basis. These subsections provide that this amount should be established by deducting securities income that is ‘foreign’ from total securities income. Subsection (5) specifies that the amount of securities income that is foreign is the total of any ‘chargeable foreign securities income’ and any ‘unchargeable foreign securities income’, with reference to new sections 41H to 41J of ITEPA. Subsection (6) identifies any chargeable foreign securities income that will be subject to income tax on the remittance basis. Subsections (7) to (9) make provision in relation to amounts remitted to the UK in a tax year; set out rules that apply on the disposal, assignment or release of ERS or options for consideration; and broadly reproduce certain provisions currently found in section 41A of ITEPA, concerning the effect of the remittance basis on taxable specific income from ERS.

6. New section 41G of ITEPA (at subsections (2) – (8)) defines the ‘relevant period’ for each type of ERS for the purposes of the international mobility conditions at new section 41F, which determine whether these new rules apply in relation to an individual’s ERS income. This is also the period over which securities income is to be apportioned between that which is subject to income tax in the UK, and that which is not. Where appropriate, the relevant periods broadly replicate those already in operation for the remittance basis of taxation at the current section 41B of ITEPA. The rules at subsection (2) to (8) are subject to an override (at subsection (9)) where the relevant period they provide is not just and reasonable.

7. New sections 41H to 41J of ITEPA determine how ‘unchargeable’ and ‘chargeable’ foreign securities income are to be calculated, for the purposes of establishing how much of the total securities income is not to be subject to UK income tax or which may be subject to UK income tax on the remittance basis where this applies. Where appropriate, these sections broadly replicate rules currently in sections 41C to 41E of ITEPA, which establish the amount of foreign securities income for the purposes of the remittance basis of taxation.

8. New section 41H of ITEPA sets out rules to determine whether ERS income is ‘chargeable or ‘unchargeable’ foreign securities income. Chargeable foreign securities income will be subject to UK income tax on the remittance basis. Subsection (2) provides that ERS income is regarded as accruing equally on each day within the relevant period, as set out in new section 41G of ITEPA. Subsections (3) to (7) provide rules that apply for the calculation of chargeable and unchargeable foreign securities income in various cases. These include tax years within the relevant period during which: the remittance basis applies, an

individual satisfies or does not satisfy the requirement for a 3-year period of non-residence in the UK at section 26A of ITEPA, and the relevant employment is with a foreign employer, or the duties are performed wholly or partly outside the UK. Subsection (8) sets out the rules that apply where any part of the relevant period is within the overseas part of a tax year that is a split year (where an individual either leaves the UK to live or work abroad or comes from abroad to live or work in the UK). Subsection (9) provides that the rules in this new section are subject to provisions on just and reasonable apportionment at new section 41J of ITEPA.

9. New section 41I of ITEPA limits the amount of securities income that is chargeable foreign securities income in various cases where an individual has associated employment (in addition to their relevant employment), which involves UK duties. Subsection (2) provides that the amount of chargeable foreign securities income for the period is limited to the amount that is just and reasonable with reference to factors specified in this subsection.

10. New section 41J of ITEPA provides an override where the proportion of securities income that is chargeable or unchargeable foreign securities income, as determined under new section 41H, is not just and reasonable in the circumstances.

11. Paragraph 7 of the Schedule inserts a new subsection (A1) into section 418 of ITEPA. This requires Part 7 of ITEPA (concerning income from ERS and ERS options) to be read alongside the new Chapter 5B of Part 2 of ITEPA.

12. Paragraph 8 repeals section 421E of ITEPA which sets out the current residence provisions for the taxation of certain ERS.

13. Paragraphs 9 to 11 amend sections 425, 430 and 431 of ITEPA to limit the availability of the elections available under these sections (which allow for the disapplication of certain provisions within Part 7 of ITEPA). They provide that these elections can only be made where at the time of the acquisition of the ERS (or in the case of section 430 at the time of a chargeable event in relation to the ERS), the charging provisions of Chapter 4 and 5 of Part 2 of ITEPA apply in relation to earnings from the relevant employment (or in cases where there are no earnings from that employment, would apply if there were any earnings). These charging provisions apply where an employee is UK resident, or performs duties in the UK.

14. Paragraph 12 repeals section 474 of ITEPA which provides the current residence provisions for the taxation of ERS options.

15. Paragraphs 13 to 16 amend various sections of ITEPA, in consequence of the omission of Chapter 5A and sections 421E and 474 of ITEPA and the insertion of new Chapter 5B of Part 2.

Part 2 Restricted securities and securities acquired for less than market value: replacement and additional securities and rollover relief etc

16. Part 2 of the Schedule provides rollover relief from income tax for certain cases in which restricted securities held by an employee are exchanged for other restricted securities. It also amends the rules at Chapter 3C of Part 7 of ITEPA concerning notional loans, under which tax may be chargeable in relation to nil-paid or partly-paid ERS.

17. Paragraph 19 amends section 421D of ITEPA concerning replacement and additional securities and changes in interests. Sub-paragraph (2) addresses cases in which the value of nil-paid and partly-paid ERS has been reduced by the issue of certain additional or replacement securities. The provision makes clear that, in such cases, the value of that reduction should be treated as a payment for the acquisition of these new securities for the purposes of Chapter 3C of Part 7 of ITEPA. Chapter 3C provides tax rules for ERS acquired for less than market value, including nil-paid and partly-paid ERS, and taxes certain amounts in relation to these ERS as notional loans. Sub-paragraph (3) amends subsection (4) of section 421D of ITEPA to reflect this change.

18. Paragraph 20 inserts new section 430A of ITEPA, which introduces relief from income tax in certain cases where restricted ERS held by an individual ('old securities') are exchanged for other restricted ERS ('new securities'). Restricted ERS are those which contain provision for transfer, reversion or forfeiture which reduces their market value. Subsections (3) and (4) of new section 430A concern circumstances in which old securities are exchanged for new securities as well as other consideration, and provide that the new rollover relief will only be available on that part of the consideration that is new securities. That part of the consideration which is not new securities will give rise to a chargeable event on the disposal of the matching proportion of the old securities. Subsection (5) concerns cases in which the only consideration for the old securities is new securities, and provides that neither the disposal of the old securities nor the acquisition of the new securities will give rise to a tax liability and that Chapter 2 of Part 7 of ITEPA applies to the new securities as it applies to the old securities, subject to subsections (6) to (17).

19. Subsections (6) to (17) of new section 430A set out how the new securities are to be treated under Chapter 2 (concerning the taxation of restricted ERS). The tax arrangements for the old securities will, in certain respects, be transferred to the new securities. This includes (at subsection (7)) any elections to disregard certain provisions of ITEPA made in respect of the old securities under sections 430(1) or 431(1), and (at subsection (8) to (10)) the proportions used to calculate the amount of charge under section 428 of ITEPA, in the case of a subsequent chargeable event in relation to the new ERS.

20. Subsections (11) to (14) of new section 430A apply where no tax was chargeable on acquisition of the old securities by virtue of section 425(2) of ITEPA, because the ERS were 'forfeitable' within 5 years, and a forfeiture restriction still remains on the old securities at the time of the exchange. Broadly, on the occurrence of a chargeable event, income tax will apply in relation to these new securities in the same way as would have been the case for the old securities. Subsection (12) creates a chargeable event immediately after the acquisition of the new securities where the restriction on them is not a forfeiture restriction. Subsections (13) and (14) provide that where the new securities remain forfeitable more than 5 years after

the acquisition of the old securities, the forfeiture restriction is treated as having been removed five years after the acquisition of the old securities, so that a chargeable event occurs at that time. Subsections (15) to (17) ensure that these rules apply as intended in relation to subsequent exchanges of these new securities.

21. Paragraph 21 amends the rules at current section 446U of ITEPA concerning the discharge of notional loans, which apply for nil-paid and partly-paid ERS. Sub-paragraphs (2) and (3) remove certain disposals of these ERS from provisions that would otherwise treat the outstanding notional loans in respect of these ERS as employment income subject to tax at that time. Sub-paragraph (4) provides that the notional loan in relation to these ERS is discharged without this giving rise to an amount of employment income where these ERS are disposed of in certain circumstances.

Part 3 CT relief for employee share acquisitions

22. Part 3 of the Schedule extends the circumstances in which corporation tax relief is available under Part 12 of the Corporation Tax Act 2009 (CTA 2009) in relation to employee share acquisitions.

23. Paragraphs 25, 26, 28 and 29 introduce new sections 1007A, 1015A, 1025A and 1030A of CTA 2009, which modify certain requirements for relief under Part 12 CTA 2009. These new sections concern cases where an individual who is employed by an overseas company works for, but does not have employment with, a UK host company (for example during a period of secondment). The new sections provide that where certain conditions are met, that individual can be treated as having employment with the UK host for the purposes of the relief. This means that relief may be available to the UK host in relation to shares acquired by the individual – even though that host is not the employing company. A limit on the amount of relief available to the UK host is specified as the amount which is chargeable to income tax under ITEPA in relation to the acquisition of the shares, or a chargeable event in relation to the shares (whichever is appropriate). These new sections also make provision for cases in which there is more than one UK host company and circumstances in which the employee has died - as well as providing that relief may be available in relation to shares of the overseas employer or the UK host.

24. Paragraph 27 extends the availability of corporation tax relief under Part 12 of CTA 2009 in relation to shares acquired by exercise of a share option following the takeover of a company. It introduces new subsection (1A) to section 1016 CTA 2009. Section 1016 sets out conditions concerning shares that must be met for relief under Part 12 to be available in relation to share options. The change provides that where, immediately prior to a company takeover, the shares under option satisfied the current requirements at paragraphs (a) to (c) of Condition 2 at section 1016(1), but no longer do so as a result of the takeover, those shares will satisfy the relevant requirements of section 1016(1). This is subject to the shares being acquired by the employee within 90 days of the takeover.

Part 4 Commencement etc

25. Part 4 sets out the relevant dates of commencement for these changes.

BACKGROUND NOTE

26. Income tax is generally due where an employer awards share options, shares or other ERS to employees, and tax may also be due on certain disposals of ERS. The tax rules in this area are designed to ensure that the employment income paid in the form of ERS or options is subject to income tax as appropriate. In certain circumstances, corporation tax relief is available to companies in respect of employee share acquisitions.

27. The OTS published a report and recommendations on unapproved employee share schemes in January 2013. This identified a number of areas in which the current tax rules created undue complexity, and included recommendations for how these might be simplified.

28. The Government consulted on the recommendations being taken forward in this measure during summer 2013. A summary of responses to this consultation was published on 10 December 2013.

29. This measure supports the Government's objective to simplify the tax system. The changes mainly concern the tax treatment of ERS or ERS options, but the change to the rules in section 222 of ITEPA applies to notional (non-cash) payments more generally.

30. This measure will be implemented alongside other simplification changes recommended by the OTS in relation to the Government's four tax advantaged employee share schemes.

31. If you have any questions about these changes, or comments on the legislation, please contact Colin Strudwick on 03000 585275 (email: shareschemes@hmrc.gsi.gov.uk).