INCOME TAX (EARNINGS AND PENSIONS) ACT 2003

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Example 3

Ne = £5,000; Da = 183; De = 183; Smg = 0

Part 7: Employment income: share-related income and exemptions

PAYE implications

Chapter 7: Approved SAYE option schemes

Overview

2089. This Chapter tells an employee receiving or exercising a share option whether or not the option is within the Save-as-You-Earn ("SAYE") rules and what the tax consequences are. A SAYE option scheme is defined in section 516. This label has not been used in the statute up to now. The name in the source legislation is "savings-related share option scheme" and these schemes are commonly referred to as SAYE share option schemes or simply SAYE schemes in practice.

2090. The label SAYE denotes a SAYE option scheme in these notes.

2091. Unlike in sections 185 and 187 of and Schedule 9 to ICTA, in this Act SAYE has been separated from the CSOP schemes in an attempt to make these rules easier to read and understand.

2092. The rules for APS schemes (profit sharing schemes approved under Schedule 9 to ICTA) are not rewritten in this Act. These rules will therefore still be found in sections 186 and 187 of and Schedules 9 and 10 to ICTA. There is reference to this in section 418(2) and in Part 8 of Schedule 7 to this Act.

2093. The redrafting of the SAYE and CSOP schemes has been influenced by the way the newer schemes, Enterprise Management Incentives ("EMI") and Share Incentive Plans ("SIP"), were drafted in FA 2000. This is a matter of style and also part of an attempt to achieve consistency across the share schemes where possible. Codes have been introduced for each scheme or plan as explained in the notes on the introduction to this Part.

2094. Each section of this Chapter and each paragraph of Schedule 3 has a heading to help explain its contents and there are several examples of both sections and paragraphs containing introductory material.

2095. The requirements for the initial and continuing approval of the scheme are now contained in paragraphs 40 to 44 of Schedule 3. There are transitional provisions in

Schedule 7 to ensure that a scheme approved under Schedule 9 to ICTA is treated as a SAYE option scheme approved under this Act.

Section 516: Approved SAYE option schemes

2096. This section sets out what is contained in this Chapter and in Schedule 3. It sets the scene: SAYE is a scheme which requires prior approval by the Inland Revenue and which enables the option-holder to benefit from income tax relief.

2097. There are references in the SAYE code in several places to the Inland Revenue, where in ICTA these refer to the Board. This reflects practice and is in line with the approach in FA 2000 to the EMI and SIP codes. The Inland Revenue is defined in section 720 as "any officer of the Board of Inland Revenue". See *Change 158* in Annex 1.

2098. In *subsection (3)(c)* there is a cross-reference to Part 2 of Schedule 7D to TCGA 1992 which covers the capital gains tax angle (see Schedule 6 to this Act).

2099. Share options are described as being granted rather than obtained in most contexts and especially where the timing of the grant is significant. This ties in with the terminology in EMI and perhaps gives a clearer indication of the exact date of the occasion.

2100. The definitions derive from section 187 of ICTA. There are minor definitions and a new index of defined expressions, at the end of Schedule 3 to this Act. This is based on the approach in the tax-relieved share schemes, introduced by FA 2000. The definition of "share option" matches the one used for EMI in FA 2000 (and in the EMI code). In section 516 there is also a fuller definition of the SAYE option scheme itself than in ICTA.

Section 517: Share options to which this Chapter applies

2101. This is an introductory section, which derives from section 185(1) of ICTA. This Chapter applies to an individual who obtains an option in accordance with the provisions of an approved scheme by reason of his or her employment. This phrase in section 185(1) matches the expression in the benefits code. The rules in paragraph 10 of Schedule 3 to this Act govern the particular employment.

2102. The reference to a commencement date in section 185(1) of ICTA is spent and is not rewritten.

Section 518: No charge in respect of receipt of option

2103. This derives from section 185(2) of ICTA. Here, as elsewhere, the phrase "no liability to income tax arises" expresses this type of exemption.

Section 519: No charge in respect of exercise of option

2104. This and the following section derive from section 185(3) and (4) of ICTA and explain the conditions for relief from income tax on the exercise of an option and on post-acquisition benefits.

2105. The relief and the exceptions are set out in a more straightforward way and in a positive framework. No liability to income tax arises in the circumstances set out in this section (subject to the two conditions in *subsections (2) and (3)*) on the exercise of an option in accordance with the approved provisions of the scheme. Under condition A, the option is exercised after three years from the date on which it is granted. This period between grant and exercise is the norm for a SAYE scheme.

2106. There are a number of circumstances however for an early (pre-three year) exercise which are catered for in SAYE schemes. Rules about these appear in Schedule 3 to this Act. Following on from section 185(4) of ICTA, this section identifies those circumstances for which tax relief is provided. But under condition B the position is expressed positively, although the formulation makes reference to the circumstances where tax relief is not available on the early exercise of an option.

2107. There is a clarification of the time limit in section 185(4) of ICTA, which refers to the exercise of an option within three years of its being obtained in subsections (2) and (3)(a). This section confirms that the period is inclusive of the date of the grant. So, if granted an option on 1 January 2002, an employee can be confident that it can be exercised on the same date three years later and the exercise will qualify for income tax relief. See *Change 129* in Annex 1.

2108. There are similar clarifications in the CSOP code and there are references to time limits elsewhere in the notes on the approved schemes. These are instances where, to a greater or lesser extent, doubt may exist as to whether or not the "trigger date", from which a period is measured, is to be included in the period. As the law ignores fractions of a day when computing periods of this nature, the start date for the various periods has been identified.

2109. The Inland Revenue practice under which the charge on the exercise, assignment and release of unapproved share options is lifted after the death of an option holder has now been given statutory effect in section 477(4). There is a cross-reference to this section in *subsection (4)*. Also, to make it clear that the operation of section 477 acts in conjunction with the approved share scheme rules, which concern the time when a share option lapses after death, there is also a signpost to paragraph 32 of Schedule 3 to this Act in *subsection (5)(a).*

2110. In *subsection (5)(b)* there is a direct signpost to paragraph 42(3) of Schedule 3 to this Act, under which, for SAYE, the option holder is protected against the possibility of approval being withdrawn from an approved scheme.

Section 520: No charge in respect of post-acquisition benefits

2111. This section mirrors the previous section and gives relief in the same circumstances from income tax on specified charges on an increase in the value of shares acquired by way of a tax-relieved exercise.

2112. There is a signpost in *subsection (3)* to paragraph 42(3) of Schedule 3 to this Act under which, for SAYE, the option holder is protected against the possibility of approval being withdrawn from an approved scheme.