



Income Tax (Earnings and Pensions) Act 2003

2003 CHAPTER 1

PART 7

EMPLOYMENT INCOME: SHARE-RELATED INCOME AND EXEMPTIONS

CHAPTER 2

CONDITIONAL INTERESTS IN SHARES

Introduction

422 Application of this Chapter

(1) This Chapter applies where—

- (a) a person (“the employee”) acquires a beneficial interest in shares in a company as a director or employee of that or another company, and
- (b) the interest is acquired on terms that make it only conditional.

(2) In this Chapter—

“the employee’s interest” means the beneficial interest in shares acquired by the employee as mentioned in subsection (1);

“the employer company” means the company as a director or employee of which the employee’s interest is acquired;

“the shares” means the shares mentioned in subsection (1)(a);

and “director” and “employee” have the extended meaning given by section 434(1).

423 Interests in shares acquired “as a director or employee”

- (1) For the purposes of this Chapter a person (“E”) acquires an interest in shares “as a director or employee” of a company if E acquires the interest in pursuance of—
- (a) a right conferred on, or opportunity offered to, E by reason of E’s office or employment as a director or employee of the company;
 - (b) a right or opportunity assigned to E, having been conferred on or offered to some other person by reason of E’s office or employment as a director or employee of the company; or
 - (c) an assignment, the interest having been acquired by some other person by reason of E’s office or employment as a director or employee of the company.
- (2) The references in subsection (1) to a right or opportunity conferred or offered by reason of E’s office or employment include—
- (a) one so conferred or offered after E has ceased to hold the office or employment, and
 - (b) one that arises from the fact that shares—
 - (i) which E acquired as a director or employee (or is treated as so acquiring by virtue of this paragraph), or
 - (ii) in which E so acquired an interest, were convertible shares.
- (3) A person who—
- (a) has acquired an interest in shares which is only conditional, convertible shares or an interest in convertible shares,
 - (b) acquired that interest or those shares as a director or employee of a company, or is treated by virtue of this subsection as having done so, and
 - (c) as a result of any two or more transactions—
 - (i) ceases to be entitled to that interest or those shares, and
 - (ii) becomes entitled to another interest in shares which is only conditional or to any convertible shares or to an interest in convertible shares,
 is to be treated for the purposes of this Chapter as if the interest or shares mentioned in paragraph (c)(ii) were also acquired as a director or employee of the company.
- (4) Subsection (3) also applies where the interest or shares mentioned in subsection (3) (c)(ii) were acquired by a person connected with the first-mentioned person.
- (5) Nothing in subsection (3) or (4) affects the rights or opportunities included by virtue of subsection (2)(b).
- (6) In this section “convertible shares” has the same meaning as in Chapter 3 of this Part (convertible shares) (see section 435(2) and the definition of shares in section 446(1)).

424 Meaning of interest being “only conditional”

- (1) For the purposes of this Chapter an interest in shares is “only conditional” for so long as the terms on which the person is entitled to it—
- (a) provide that if certain circumstances arise, or do not arise, there will be a transfer, reversion or forfeiture as a result of which that person will cease to be entitled to any beneficial interest in the shares, and

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- (b) are not such that, on the transfer, reversion or forfeiture, that person will be entitled to receive in respect of the interest an amount that is equal to or more than its market value at that time.
- (2) But a person is not to be regarded as having an interest in shares which is only conditional by reason only that one or more of the following is the case—
- (a) the shares are unpaid or partly paid and may be forfeited for non-payment of calls, in a case where there is no restriction on the meeting of calls by that person;
 - (b) the articles of association of the company require the shares to be offered for sale or transferred, if that person ceases to hold a relevant office or employment;
 - (c) that person may be required to offer the shares for sale or transfer them on ceasing, as a result of misconduct, to hold a relevant office or employment;
 - (d) in the case of an interest in a security, the security may be redeemed on payment of any amount.
- (3) In subsection (1)(a) the references, in relation to the terms of a person’s entitlement, to circumstances arising include references to—
- (a) the expiry of a period specified in or determined under those terms,
 - (b) the death of that or any other person, and
 - (c) the exercise by any person of a power conferred on that person by or under those terms.
- (4) For the purposes of subsection (1)(b) the market value of the interest is to be determined as if there were no provision for transfer, reversion or forfeiture.
- (5) In subsection (2)(b) “articles of association” includes, in the case of a company incorporated under the law of a country outside the United Kingdom, any equivalent document relating to the company.
- (6) The references in subsection (2)(b) and (c) to a person ceasing to hold a relevant office or employment are to that person ceasing to be an officer or employee of the company in question, or of one or more group companies or of any group company.
- (7) For the purposes of subsection (6)—
- (a) a company is a “group company” in relation to another company if they are members of the same group, and
 - (b) companies are taken to be members of the same group if, and only if, one is a 51% subsidiary of the other or both are 51% subsidiaries of a third company.

425 Cases where this Chapter does not apply

- (1) This Chapter does not apply where a person acquires a beneficial interest in shares as a director or employee of a company if the earnings from the office or employment in question were not (or would not have been if there had been any) general earnings to which section 15 or 21 applies (earnings for year when employee resident and ordinarily resident in the UK).
- (2) This Chapter does not apply by virtue of section 423(2)(a) (right or opportunity conferred or offered after person has ceased to hold office or employment) if it would not apply if the right or opportunity had been conferred or offered in the last tax year in which the office or employment was held.

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Tax exemption

426 No charge in respect of acquisition of employee’s interest in certain circumstances

- (1) Subsection (2) applies if the terms on which the employee acquires the employee’s interest are such that the interest will cease to be only conditional within 5 years after its acquisition.
- (2) No liability to income tax arises in respect of the acquisition of the employee’s interest, except as provided by—
 - (a) Chapter 8 of Part 3 (taxable benefits: notional loans in respect of acquisitions of shares), or
 - (b) section 476 (charge on exercise of share option by employee).

Tax charge

427 Charge on interest in shares ceasing to be only conditional or on disposal

- (1) This section applies if—
 - (a) the shares cease, without the employee ceasing to have a beneficial interest in them, to be shares in which the employee’s interest is only conditional, or
 - (b) in a case where the shares have not so ceased, the employee sells or otherwise disposes of the employee’s interest or any other beneficial interest in the shares.
- (2) The taxable amount determined under section 428 counts as employment income of the employee for the relevant tax year.
- (3) The “relevant tax year” is the tax year in which the shares cease to be shares in which the employee’s interest is only conditional, or in which the sale or other disposal takes place.
- (4) Subsection (2) is subject to section 494 (approved SIPs: no charge on removal of restrictions).

428 Amount of charge

- (1) The taxable amount for the purposes of section 427 (charge on interest in shares ceasing to be only conditional or on disposal) is—

MV DA

where—

MV is the market value of the employee’s interest immediately after it ceases to be only conditional or, as the case may be, at the time of the sale or other disposal, and

DA is the total of any deductible amounts.

- (2) For the purposes of subsection (1) each of the following is a “deductible amount”—
 - (a) the amount or value of any consideration given for the employee’s interest;

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- (b) any amount that constitutes earnings from the employee's employment under Chapter 1 of Part 3 (earnings) in respect of the acquisition of the employee's interest;
 - (c) any amount that is treated as earnings from the employee's employment under Chapter 8 of Part 3 (taxable benefits: notional loans in respect of acquisitions of shares) in respect of the acquisition; and
 - (d) if the employee's interest was acquired by the exercise of a share option, any amount that counts as employment income of the employee under section 476 (charge on employee on exercise etc. of option) in respect of the exercise.
- (3) If, not later than the event referred to in section 427(1)(a) or (b) occurred in relation to the employee's interest, a different event occurred in respect of the shares by virtue of which an amount counts as employment income of the employee under—
- (a) section 449 (charge on occurrence of chargeable event), or
 - (b) section 453 (charge on increase in value of shares of dependent subsidiary),
- that amount is a “deductible amount” for the purposes of subsection (1).
- (4) The references in subsection (3) to an event include the expiry of a period.
- (5) Section 541(2) (effects of the EMI code on other income tax charges) also provides that an amount is to be regarded as a “deductible amount” for the purposes of subsection (1).

Supplementary provisions

429 Amount or value of consideration given for employee's interest

- (1) This section applies for the purposes of section 428 (amount of charge) in determining the amount or value of the consideration given for the employee's interest.
- (2) Subject to the following provisions of this section, that consideration is any given in respect of the acquisition of an interest in the shares by—
 - (a) the employee, or
 - (b) if section 423(1)(c) applies, the person by whom the interest in the shares was acquired.
- (3) The amount or value of the consideration given by a person for an interest in the shares includes the amount or value of any consideration given—
 - (a) for a right to acquire the shares, and
 - (b) for anything by virtue of which the employee's interest in the shares ceases to be only conditional.
- (4) If any consideration is given partly in respect of one thing and partly in respect of another, the amount given in respect of the different things is to be determined on a just and reasonable apportionment.
- (5) The consideration which for the purposes of this section is taken to be given wholly or partly for anything does not include the performance of any duties of, or in connection with, the office or employment by reference to which the interest in the shares in question has been acquired by a person as a director or employee of a company.
- (6) No amount is to be counted more than once in calculating the amount or value of any consideration.

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430 Amount or value of consideration given for right to acquire shares

- (1) This section applies for the purposes of section 429(3)(a) in determining the amount or value of any consideration given for a right to acquire shares.
- (2) Subsection (3) applies if the right to acquire shares (“the new option”) is the whole or part of the consideration for the assignment or release of another right to acquire shares (“the old option”).
- (3) The amount or value of the consideration given for the new option is to be treated as being the sum of—
 - (a) the amount by which the amount or value of the consideration given for the grant of the old option exceeds the amount or value of any consideration for the assignment or release of the old option, apart from the new option, and
 - (b) any valuable consideration given for the grant of the new option, apart from the old option.
- (4) Two or more transactions are to be treated for the purposes of subsection (2) as a single transaction by which a right to acquire shares is assigned for a consideration which consists of or includes another right to acquire shares if—
 - (a) the transactions result in—
 - (i) a person ceasing to hold a right to acquire shares, and
 - (ii) that person or a connected person coming to hold another right to acquire shares, and
 - (b) one or more of the transactions is effected under arrangements to which two or more persons who hold rights to acquire shares, in respect of which there may be a liability to tax under Chapter 5 of this Part (share options), are parties.
- (5) Subsection (4) applies regardless of the order in which the assignment and the acquisition occur.
- (6) In this section “release” includes agreeing to the restriction of the exercise of the right.

431 Application of this Chapter where employee dies

- (1) If the employee dies holding the employee’s interest, this Chapter applies as if the employee had disposed of the interest immediately before dying.
- (2) The market value of the interest at the time of that disposal is to be determined for the purposes of section 428 (amount of charge) on the basis—
 - (a) that it is known that the disposal is being made immediately before the employee’s death, and
 - (b) that any restriction on disposal is to be disregarded in so far as it is a restriction terminating on the employee’s death.

432 Duty to notify provision of conditional interests in shares

- (1) Subsection (2) applies if—
 - (a) a person provides an individual with an interest in shares which is only conditional, and
 - (b) the circumstances are such that subsequent events may result in an amount counting as employment income of that individual under section 427 (charge on interest in shares ceasing to be only conditional or on disposal).

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- (2) Each of the following persons—
- (a) the person providing the interest in shares, and
 - (b) the employer company,
- must provide the Inland Revenue with particulars in writing of the interest and its provision.
- (3) The particulars must be provided before 7th July in the tax year following that in which the interest is provided.

433 Duty to notify events resulting in charges under section 427

- (1) Subsection (2) applies if—
- (a) a person has an interest in shares which is only conditional,
 - (b) either—
 - (i) the shares cease to be shares in which that person’s interest is only conditional,
 - (ii) the shares are disposed of, or
 - (iii) that person dies, and
 - (c) by virtue of that event an amount counts as employment income under section 427 (charge on interest in shares ceasing to be only conditional or on disposal).
- (2) Each of the following persons—
- (a) the person who provided the interest in shares, and
 - (b) the employer company,
- must provide the Inland Revenue with particulars in writing of the interest and the event.
- (3) The particulars must be provided before 7th July in the tax year following that in which the event occurs.

434 Minor definitions

- (1) In this Chapter—
- “director”—
- (a) in the case of a company whose affairs are managed by a board of directors or similar body, means a member of that board or similar body,
 - (b) in the case of a company whose affairs are managed by a single director or similar person, means that director or person,
 - (c) in the case of a company whose affairs are managed by its members, means a member,
- and includes any person who is to be or has been a director;
- “employee” includes—
- (a) in relation to a company, a person taking part in the management of the affairs of the company who is not a director, and
 - (b) a person who is to be or has been an employee;
- “market value”, in relation to an interest in shares, means the amount that might reasonably be expected to be obtained from a sale of the interest in the open market;

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“shares” (except in section 423 in the expression “convertible shares”) includes—

- (a) stock,
- (b) securities issued by a company, and
- (c) any other interest of a member of a company;

“terms” on which a person is entitled to an interest in shares means terms imposed by contract or arrangement or in any other way.

(2) In this Chapter—

- “the employee”,
- “the employee’s interest”,
- “the employer company”, and
- “the shares”,

have the meaning indicated in section 422(1) and (2).