



# Income Tax (Earnings and Pensions) Act 2003

## 2003 CHAPTER 1

### PART 7

[<sup>F1</sup>EMPLOYMENT INCOME: INCOME AND EXEMPTIONS RELATING TO SECURITIES]

### [<sup>F2</sup>CHAPTER 3

#### CONVERTIBLE SECURITIES

#### Textual Amendments

- F2** Pt. 7 Ch. 3 substituted (1.9.2003 with effect in accordance with Sch. 22 para. 4(2) of the amending Act) by [Finance Act 2003 \(c. 14\)](#), [Sch. 22 para. 4\(1\)](#); S.I. 2003/1997, art. 2

#### *Introduction*

#### **435 Application of this Chapter**

This Chapter applies to employment-related securities if they are—

- (a) convertible securities, or
  - (b) an interest in convertible securities,
- at the time of the acquisition.

#### **436 “Convertible securities”**

For the purposes of this Chapter securities are convertible securities if—

---

*Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)*

---

- (a) they confer on the holder an <sup>F3</sup>entitlement (whether immediate or deferred and whether conditional or unconditional) to convert them into securities of a different description,
- (b) a contract, agreement, arrangement or condition authorises or requires the grant of such an entitlement to the holder if certain circumstances arise, or do not arise, or
- (c) a contract, agreement, arrangement or condition makes provision for the conversion of the securities (otherwise than by the holder) into securities of a different description.

#### Textual Amendments

**F3** Words in s. 436(a) substituted (with effect in accordance with Sch. 2 para. 9(4) of the amending Act) by Finance (No. 2) Act 2005 (c. 22), **Sch. 2 para. 9(1)**

### *Tax relief on acquisition*

#### 437 Adjustment of charge

<sup>F4</sup>(1) For the purposes of—

- (a) any liability to tax under Chapter 1 of Part 3 (earnings), Chapter 10 of Part 3 (taxable benefits: residual liability to charge) <sup>F5</sup>, section 226A (employee shareholder shares: amount treated as earnings) or Chapter 5 of this Part (acquisition of securities pursuant to securities option) <sup>F6</sup> or Chapter 2 of Part 7A (employment income provided through third parties)], and
- (b) the operation of Chapter 3C of this Part (acquisition of securities for less than market value),

the market value of the employment-related securities is to be determined as if they were not convertible securities or an interest in convertible securities]

<sup>F7</sup>(2) Subsection (1) does not apply if the main purpose (or one of the main purposes) of the arrangements under which the right or opportunity to acquire the employment-related securities is made available is the avoidance of tax or national insurance contributions unless the market value of the employment-related securities determined under subsection (1) would be greater than that determined under subsection (3).

(3) Where subsection (1) does not apply by virtue of subsection (2) the market value of the employment-related securities is to be determined—

- (a) where the securities which are (or an interest in which is) the employment-related securities fall within paragraph (a) of section 436 and the entitlement to convert is not both immediate and unconditional, as if it were,
- (b) where they fall within paragraph (b) of that section, as if the circumstances are such that an entitlement to convert arises immediately, and
- (c) where they fall within paragraph (c) of that section, as if provision were made for their immediate conversion;

and in each case is to be determined as if they were immediately and fully convertible.

(4) In subsection (3) “immediately and fully convertible” means convertible immediately after the acquisition of the employment-related securities so as to obtain the maximum gain that would be possible on a conversion at that time (assuming, where the securities

*Changes to legislation:* There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)

into which the securities may be converted were not in existence at that time and it is appropriate to do so, that they were) without giving any consideration for the conversion or incurring any expenses in connection with it.]

#### Textual Amendments

- F4** S. 437(1): s. 437 renumbered as s. 437(1) (with effect in accordance with Sch. 2 para. 9(4) of the amending Act) by [Finance \(No. 2\) Act 2005 \(c. 22\)](#), [Sch. 2 para. 9\(2\)](#)
- F5** Words in s. 437(1)(a) inserted (1.9.2013) by [Finance Act 2013 \(c. 29\)](#), [Sch. 23 paras. 7, 38](#); [S.I. 2013/1755, art. 2](#)
- F6** Words in s. 437(1)(a) inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 17](#)
- F7** S. 437(2)-(4) inserted (with effect in accordance with Sch. 2 para. 9(4) of the amending Act) by [Finance \(No. 2\) Act 2005 \(c. 22\)](#), [Sch. 2 para. 9\(3\)](#)

### *Tax charge on post-acquisition chargeable events*

#### **438 Charge on occurrence of chargeable event**

- <sup>F8</sup>(1) If a chargeable event occurs in relation to the employment-related securities, the taxable amount counts as employment income of the employee for the relevant tax year.
- (2) For this purpose—
- “chargeable event” has the meaning given by section 439,
  - “the taxable amount” is the amount determined under section 440, and
  - “the relevant tax year” is the tax year in which the chargeable event occurs.
- (3) Relief may be available under section 442A (relief for secondary Class 1 contributions met by employee) against an amount counting as employment income under this section.]
- (5) This section is subject to section 443 (case outside charge under this section).

#### Textual Amendments

- F8** S. 438(1)-(3) substituted for s. 438(1)-(4) (1.9.2004) by [Finance Act 2004 \(c. 12\)](#), [s. 85\(2\)](#), [Sch. 16 para. 2\(2\)](#); [S.I. 2004/1945, art. 2](#)

#### **439 Chargeable events**

- (1) This section applies for the purposes of section 438 (charge on occurrence of chargeable event).
- (2) Any of the events mentioned in subsection (3) is a “chargeable event” in relation to the employment-related securities.
- (3) The events are—
- the conversion of the employment-related securities (or the securities in which they are an interest) into securities of a different description in circumstances

---

*Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)*

---

- in which an associated person is beneficially entitled to the securities into which the employment-related securities are converted,
- (b) the disposal for consideration of the employment-related securities, or any interest in them, by an associated person otherwise than to another associated person (at a time when they are still convertible securities or an interest in convertible securities),
  - (c) the release for consideration of the entitlement to convert the employment-related securities (or the securities in which they are an interest) into securities of a different description, and
  - (d) the receipt by an associated person of a benefit in money or money's worth in connection with the entitlement to convert (other than securities acquired on the conversion of the employment-related securities or consideration such as is mentioned in paragraph (b) or (c)).
- (4) A benefit received on account of any disability (within the meaning of [<sup>F9</sup>the Equality Act 2010 in England and Wales and Scotland, or] the Disability Discrimination Act 1995) of the employee is to be disregarded for the purposes of subsection (3)(d).

#### Textual Amendments

- F9** Words in s. 439(4) inserted by [Equality Act 2010 \(c. 15\)](#), [Sch. 26 para. 51](#) (as inserted (1.10.2010) by [S.I. 2010/2279](#), [art. 1\(2\)](#), [Sch. 1 para. 5](#)) (with [S.I. 2010/2317](#), [art. 2](#))

#### 440 Amount of charge

- (1) The taxable amount for the purposes of section 438 (charge on occurrence of chargeable event) is—

### AG - CE

- (2) AG is the amount of any gain realised on the occurrence of the chargeable event.
  - (3) CE is the amount of any consideration given for the entitlement to convert the employment-related securities or the securities in which they are an interest together with the amount of any expenses incurred by the holder of the employment-related securities in connection with the conversion, disposal, release or receipt.
- [<sup>F10</sup>(3A) If (because of subsection (2) of section 437) subsection (1) of that section did not apply in relation to the employment-related securities, the taxable amount is to be reduced by the amount by which—
- (a) the market value of the employment-related securities for the purposes specified in that subsection, exceeded
  - (b) what it would have been had that subsection applied,
- (less the aggregate of any amount by which the taxable amount on any previous chargeable event relating to the employment-related securities has been reduced under this subsection).]
- (4) Section 441 explains what is the amount of any gain realised on the occurrence of a chargeable event.

*Changes to legislation:* There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)

- (5) Section 442 explains whether consideration is given for the entitlement to convert the employment-related securities or the securities in which they are an interest and, if it is, what is its amount.

#### Textual Amendments

- F10** S. 440(3A) inserted (with effect in accordance with Sch. 2 para. 10(2) of the amending Act) by Finance (No. 2) Act 2005 (c. 22), **Sch. 2 para. 10(1)**

#### 441 Amount of gain realised on occurrence of chargeable event

- (1) This section applies for the purposes of section 440 (amount of charge on occurrence of chargeable event).
- (2) The amount of the gain realised on the occurrence of an event that is a chargeable event by virtue of section 439(3)(a) (conversion) is—

$$\text{CMVCS} - (\text{CMVERS} + \text{CC})$$

- (3) The amount of the gain realised on the occurrence of an event that is a chargeable event by virtue of section 439(3)(b) (disposal) is—

$$\text{DC} - \text{CMVERS}$$

- (4) The amount of the gain realised on the occurrence of an event that is a chargeable event by virtue of section 439(3)(c) (release of entitlement to convert) is the amount of the consideration received by an associated person in respect of the release.
- (5) The amount of the gain realised on the occurrence of an event that is a chargeable event by virtue of section 439(3)(d) (receipt of benefit) is the amount or market value of the benefit.
- (6) CMVCS—
- (a) if the employment-related securities are securities, is the market value at the time of the chargeable event of the securities into which they are converted (determined, where those securities are themselves convertible securities, as if they were not), or
  - (b) if the employment-related securities are an interest in securities, is the same proportion of that market value as the market value of the interest in the securities in which the employment-related securities are an interest bears to the market value of those securities.
- (7) CMVERS is the market value of the employment-related securities at the time of the chargeable event determined as if they were not convertible securities or an interest in convertible securities.
- (8) CC is the amount of any consideration given for the conversion of the employment-related securities.
- (9) DC is the amount of the consideration given on the disposal.

[<sup>F11</sup>(10) Subsection (11) applies for the purposes of subsection (2) or (3) if—

---

*Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)*

---

- (a) prior to the acquisition, the employment-related securities were the subject of a relevant step within the meaning of Part 7A by reason of which Chapter 2 of that Part applied in respect of the employment, and
  - (b) the amount mentioned in subsection (11)(a) is higher than the amount mentioned in subsection (11)(b).
- (11) The amount of the gain realised is reduced (but not below nil) by the amount equal to—
- (a) the amount that counted as employment income of the employee in respect of the employment under Chapter 2 of Part 7A, less
  - (b) the market value of the employment-related securities when the relevant step was taken determined as if they were not convertible securities or an interest in convertible securities.]

#### **Textual Amendments**

**F11** S. 441(10)(11) inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 18](#)

#### **442 Amount of consideration given for entitlement to convert**

- (1) This section applies for the purposes of section 440 (amount of charge on occurrence of chargeable event).
- (2) Consideration is to be regarded as given for the entitlement to convert the employment-related securities (or the securities in which they are an interest) if (and only if) ACS exceeds NCMV.
- (3) The amount of the consideration to be regarded as so given is the amount of the excess.
- (4) ACS is the amount of the consideration given for the acquisition of the employment-related securities.
- (5) NCMV is the market value of the employment-related securities at the time of the acquisition, determined as if they were not convertible securities or an interest in convertible securities.

#### **[<sup>F12</sup>442A] Relief for secondary Class 1 contributions met by employee**

- (1) Relief is available under this section against an amount counting as employment income under section 438 (“the employment income amount”) if—
  - (a) an agreement having effect under paragraph 3A of Schedule 1 to the Contributions and Benefits Act has been entered into allowing the secondary contributor to recover from the employee the whole or part of any secondary Class 1 contribution in respect of that amount, or
  - (b) an election having effect under paragraph 3B of that Schedule is in force which has the effect of transferring to the employee the whole or part of the liability to pay secondary Class 1 contributions in respect of that amount.
- (2) The amount of the relief is the total of—
  - (a) any amount that under the agreement referred to in subsection (1)(a) is recovered in respect of the employment income amount by the secondary

*Changes to legislation:* There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)

- contributor before 5th June in the tax year following that in which the chargeable event occurs, and
- (b) the amount of any liability in respect of the employment income amount that, by virtue of the election referred to in subsection (1)(b), has become the employee's liability.
- (3) If notice of withdrawal of approval of the election is given, the amount of the liability referred to in subsection (2)(b) is limited to the amount met before 5th June in the tax year following that in which the gain is realised.
- (4) Relief under this section is given by way of deduction from the amount otherwise counting as employment income.
- (5) Relief under this section does not affect the amount to be taken into account—
- (a) as employment income in determining contributions payable under the Contributions and Benefits Act, or
- (b) as relevant employment income for the purposes of paragraph 3A or 3B of Schedule 1 to that Act.
- (6) In this section—
- “approval”, in relation to an election, means approval by [<sup>F13</sup>an officer of Revenue and Customs] under paragraph 3B of Schedule 1 to the Contributions and Benefits Act, and
- “secondary contributor” has the same meaning as in that Act (see section 7).]

#### Textual Amendments

- F12** S. 442A inserted (1.9.2004) by Finance Act 2004 (c. 12), s. 85(2), Sch. 16 para. 2(3); S.I. 2004/1945, art. 2
- F13** Words in Act substituted (18.4.2005) by Commissioners for Revenue and Customs Act 2005 (c. 11), s. 53(1), Sch. 4 para. 102(1); S.I. 2005/1126, art. 2(2)(h)

#### 443 Case outside charge under section 438

- (1) Section 438 (charge on occurrence of chargeable event) does not apply if—
- (a) the employment-related securities are shares (or an interest in shares) in a company of a class,
- (b) all the company's shares of the class are convertible securities,
- [<sup>F14</sup>(ba) subsection (1A) is satisfied,]
- (c) all the company's shares of the class (other than the employment-related securities) are affected by an event similar to that which is a chargeable event in relation to the employment-related securities, and
- (d) subsection (3) or (4) is satisfied.

[<sup>F15</sup>(1A) This subsection is satisfied unless something which affects the employment-related securities has been done (at or before the time when section 438 would apply) as part of a scheme or arrangement the main purpose (or one of the main purposes) of which is the avoidance of tax or national insurance contributions.]

- (2) For the purposes of subsection (1)(c) shares are affected by an event similar to that which is a chargeable event in relation to the employment-related securities—

---

*Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)*

---

- (a) in the case of a chargeable event within section 439(3)(a) (conversion), if they are converted into securities of a different description,
  - (b) in the case of a chargeable event within section 439(3)(b) (disposal), if they are disposed of,
  - (c) in the case of a chargeable event within section 439(3)(c) (release of entitlement to convert), if the entitlement to convert them into securities of a different description is released, or
  - (d) in the case of a chargeable event within section 439(3)(d) (receipt of benefit), if a similar benefit is received in respect of the entitlement to convert them.
- (3) This subsection is satisfied if, immediately before the event that would be a chargeable event, the company is employee-controlled by virtue of holdings of shares of the class.
- (4) This subsection is satisfied if, immediately before that event, the majority of the company's shares of the class are not [<sup>F16</sup>employment-related securities.]

<sup>F17</sup>(5) .....

#### Textual Amendments

- F14** S. 443(1)(ba) inserted (retrospective to 7.5.2004) by [Finance Act 2004 \(c. 12\)](#), ss. 86(2)(b)(3)(8), 86(1)
- F15** S. 443(1A) substituted (with effect in accordance with Sch. 2 para. 11(2) of the amending Act) by [Finance \(No. 2\) Act 2005 \(c. 22\)](#), [Sch. 2 para. 11\(1\)](#)
- F16** Words in s. 443(4) substituted (retrospective to 7.5.2004) by [Finance Act 2004 \(c. 12\)](#), ss. 86(2)(b)(5)(8), 86(1)
- F17** S. 443(5) repealed (with effect in accordance with s. 86(8) of the amending Act) by [Finance Act 2004 \(c. 12\)](#), [Sch. 42 Pt. 2\(11\)](#)

### *Supplementary*

#### 444 Definitions

- (1) In this Chapter—  
“interest”, in relation to securities,  
“securities”, and  
“shares”,  
have the meaning indicated in section 420.
- (2) In this Chapter “market value” has the meaning indicated in section 421(1).
- (3) For the purposes of this Chapter sections 421(2) and 421A apply for determining the amount of the consideration given for anything and section 421I applies for determining the amount of the consideration given for the acquisition of employment-related securities.
- (4) In this Chapter—  
“the acquisition”,  
“the employee” (except in section 443), and  
“employment-related securities”,  
have the meaning indicated in section 421B(8).
- (5) In this Chapter “associated person” has the meaning indicated in section 421C.



**Changes to legislation:** *There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3. (See end of Document for details)*

---

- (6) In this Chapter—  
    “associated company”, and  
    “employee-controlled”,  
    have the meaning indicated in section 421H.
- (7) In this Chapter “convertible securities” has the meaning indicated in section 436.]

**Changes to legislation:**

There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 3.