



Income Tax (Earnings and Pensions) Act 2003

2003 CHAPTER 1

PART 3

EMPLOYMENT INCOME: EARNINGS AND BENEFITS ETC. TREATED AS EARNINGS

CHAPTER 7

TAXABLE BENEFITS: LOANS

Introduction

173 Loans to which this Chapter applies

- (1) This Chapter applies to a loan if it is an employment-related loan.
- (2) In this Chapter—
 - (a) “loan” includes any form of credit, and
 - (b) references to making a loan (and related expressions) include arranging, guaranteeing or in any way facilitating a loan.
- (3) Sections 288 and 289 make provision for exemption and relief for certain bridging loans connected with employment moves.

174 Employment-related loans

- (1) For the purposes of this Chapter an employment-related loan is a loan—
 - (a) made to an employee or a relative of an employee, and
 - (b) of a class described in subsection (2).
- (2) For the purposes of this Chapter the classes of employment-related loan are—

Status: Point in time view as at 06/04/2005.

Changes to legislation: *There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 7. (See end of Document for details)*

A

A loan made by the employee's employer.

B

A loan made by a company or partnership over which the employee's employer had control.

C

A loan made by a company or partnership by which the employer (being a company or partnership) was controlled.

D

A loan made by a company or partnership which was controlled by a person by whom the employer (being a company or partnership) was controlled.

E

A loan made by a person having a material interest in—

- (a) a close company which was the employer, had control over the employer or was controlled by the employer, or
- (b) a company or partnership controlling that close company.

(3) In this section—

“employee” includes a prospective employee, and
 “employer” includes a prospective employer.

(4) References in this section to a loan being made by a person extend to a person who—

- (a) assumes the rights and liabilities of the person who originally made the loan, or
- (b) arranges, guarantees or in any way facilitates the continuation of a loan already in existence.

(5) A loan is not an employment-related loan if—

- (a) it is made by an individual in the normal course of the individual's domestic, family or personal relationships, or
- (b) it is made to a relative of the employee and the employee derives no benefit from it.

(6) For the purposes of this section a person (“X”) is a relative of another (“Y”) if X is—

- (a) Y's spouse,
- (b) a parent, child or remoter relation in the direct line either of Y or of Y's spouse,
- (c) a brother or sister of Y or of Y's spouse, or
- (d) the spouse of a person falling within paragraph (b) or (c).

Status: Point in time view as at 06/04/2005.

Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 7. (See end of Document for details)

Benefit of taxable cheap loan treated as earnings

175 Benefit of taxable cheap loan treated as earnings

- (1) The cash equivalent of the benefit of an employment-related loan is to be treated as earnings from the employee's employment for a tax year if the loan is a taxable cheap loan in relation to that year.
- (2) For the purposes of this Chapter an employment-related loan is a "taxable cheap loan" in relation to a particular tax year if—
 - (a) there is a period consisting of the whole or part of that year during which the loan is outstanding and the employee holds the employment,
 - (b) no interest is paid on it for that year, or the amount of interest paid on it for that year is less than the interest that would have been payable at the official rate, and
 - (c) none of the exceptions in sections 176 to 179 apply.
- (3) The cash equivalent of the benefit of an employment-related loan for a tax year is the difference between—
 - (a) the amount of interest that would have been payable on the loan for that year at the official rate, and
 - (b) the amount of interest (if any) actually paid on the loan for that year.
- (4) If there are two or more employment-related loans, this section applies to each separately.
- (5) This section is subject to—
 - section 180 (threshold for benefit of loan to be treated as earnings);
 - section 186 (replacement loans).

176 Exception for loans on ordinary commercial terms

- (1) A loan on ordinary commercial terms is not a taxable cheap loan.
- (2) In this section a "loan on ordinary commercial terms" means a loan—
 - (a) made by a person ("the lender") in the ordinary course of a business carried on by the lender which includes—
 - (i) the lending of money, or
 - (ii) the supplying of goods or services on credit, and
 - (b) in relation to which condition A, B or C is met.
- (3) Condition A is met if—
 - (a) at the time the loan was made comparable loans were available to all those who might be expected to avail themselves of the services provided by the lender in the course of the lender's business,
 - (b) a substantial proportion of the loans (consisting of the loan in question and the comparable loans) made by the lender at or about the time the loan in question was made were made to members of the public,
 - (c) the loan in question is held on the same terms as comparable loans generally made by the lender to members of the public at or about the time the loan in question was made, and

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- (d) where those terms differ from the terms applicable immediately after the loan in question was first made, they were imposed in the ordinary course of the lender's business.
- (4) For the purposes of condition A a loan is comparable to another loan if it is made for the same or similar purposes and on the same terms and conditions.
- (5) Condition B is met if—
- (a) the loan has been varied before 6th April 2000,
 - (b) a substantial proportion of the relevant loans were made to members of the public,
 - (c) the loan in question is held on the same terms as relevant loans generally made by the lender to members of the public at or about the relevant time, and
 - (d) where those terms differ from the terms applicable immediately after the relevant time, they were imposed in the ordinary course of the lender's business.
- (6) Condition C is met if—
- (a) the loan has been varied on or after 6th April 2000,
 - (b) a substantial proportion of the relevant loans were made to members of the public,
 - (c) at the relevant time members of the public who had loans from the lender for similar purposes had a right to vary their loans on the same terms and conditions as applied in relation to the variation of the loan in question,
 - (d) the loan in question as varied is held on the same terms as any existing loans so varied, and
 - (e) where those terms differ from the terms applicable immediately after the relevant time, they were imposed in the ordinary course of the lender's business.
- (7) For the purposes of condition B and C—
- (a) the "relevant time" is the time of the variation of the loan in question, and
 - (b) the "relevant loans" are—
 - (i) the loan in question,
 - (ii) any existing loans which were varied at or about the relevant time so as to be held on the same terms as the loan in question after it was varied, and
 - (iii) any new loans which were made by the lender at or about that time and are held on those terms.
- (8) No account is to be taken of amounts which are incurred on fees, commission or other incidental expenses by the person to whom a loan is made for the purpose of obtaining the loan—
- (a) in determining for the purposes of condition A whether loans made by a lender before 1st June 1994 are made or held on the same terms or conditions, or
 - (b) in determining for the purposes of condition B or C whether rights to vary loans are exercisable on the same terms and conditions or loans are held on the same terms.
- (9) No account is to be taken of amounts which are incurred on penalties, interest or similar amounts by the person to whom a loan is made as a result of varying the loan in

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determining for the purposes of condition B or C whether rights to vary loans are exercisable on the same terms and conditions or loans are held on the same terms.

- (10) For the purposes of this section a “member of the public” means a member of the public at large with whom the lender deals at arm’s length.

177 Exceptions for loans at fixed rate of interest

- (1) A fixed rate loan made on or after 6th April 1978 is not a taxable cheap loan by reason only of an increase in the official rate of interest since the year in which the loan was made if the condition in subsection (2) is met.
- (2) The condition in this subsection is met if the amount of interest paid on the loan for the tax year in which it was made was equal to or greater than the interest that would have been payable at the official rate for that year.
- (3) A fixed rate loan made before 6th April 1978 is not a taxable cheap loan if the condition in subsection (4) is met.
- (4) The condition in this subsection is met if the rate of interest for the loan is equal to or greater than the rate which could have been expected to apply to a loan made—
 - (a) at the same time as the loan in question,
 - (b) on the same terms (other than as to the rate of interest), and
 - (c) between persons not connected with each other dealing at arm’s length.
- (5) In this section a “fixed rate loan” means a loan—
 - (a) made for a fixed period which cannot be changed, and
 - (b) made at a fixed rate of interest which cannot be changed during that period.

178 Exception for loans where interest qualifies for tax relief

A loan is not a taxable cheap loan in relation to a particular tax year if, assuming interest is paid on the loan for that year (whether or not it is in fact paid), the whole of that interest—

- (a) is eligible for relief under section 353 of ICTA (general provision for relief for payments of interest, excluding MIRAS),
- (b) would be eligible for relief under that section but for the fact that it is a payment of relevant loan interest to which section 369 of ICTA applies (mortgage interest payable under deduction of tax),
- (c) is deductible in computing the amount of the profits to be charged [^{F1}to tax] in respect of a trade, profession or vocation carried on [^{F2}wholly or partly in the United Kingdom] by the person to whom the loan is made, or
- (d) is deductible in computing the amount of the profits to be charged [^{F3}to tax in respect of a UK property business, or a Schedule A business,] carried on by that person.

Textual Amendments

- F1** Words in s. 178(c) substituted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\)](#), s. 883(1), [Sch. 1 para. 587\(a\)\(i\)](#) (with [Sch. 2](#))
- F2** Words in s. 178(c) inserted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\)](#), s. 883(1), [Sch. 1 para. 587\(a\)\(ii\)](#) (with [Sch. 2](#))

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F3 Words in s. 178(d) substituted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), s. 883\(1\), Sch. 1 para. 587\(b\)](#) (with Sch. 2)

179 Exception for certain advances for necessary expenses

- (1) An advance by an employer to an employee for the purpose of paying for—
 - (a) necessary expenses, or
 - (b) incidental overnight expenses,
 is not a taxable cheap loan in relation to a particular tax year if the following conditions are met.
- (2) The conditions are—
 - (a) that at all times in the tax year in question the amount outstanding on such advances made by the employer to the employee does not exceed £1,000,
 - (b) that the advance is spent within 6 months after the date on which it is made, and
 - (c) that the employee accounts to the employer at regular intervals for the expenditure of the amount advanced.
- (3) If, on an application made by the employer, the Inland Revenue are satisfied that there is good reason to do so in the case of a particular advance, they may authorise that either or both of the following limits are increased in relation to that advance—
 - (a) the sum of money specified in subsection (2)(a);
 - (b) the time limit specified in subsection (2)(b).
- (4) An application under subsection (3)—
 - (a) must be in writing, and
 - (b) must contain such particulars and be supported by such evidence as the Inland Revenue may require.
- (5) In this section “necessary expenses” are expenses (including travel expenses) which—
 - (a) the employee is obliged to incur and pay as holder of the employment, and
 - (b) are necessarily incurred in the performance of the duties of the employment.
- (6) In this section “incidental overnight expenses” are expenses which—
 - (a) are incidental to the employee’s absence from the place where the employee normally lives,
 - (b) relate to a continuous period of such absence in relation to which the overnight stay conditions are met, and
 - (c) would not be deductible under Part 5 if the employee incurred and paid them and Chapter 2 of Part 4 (mileage allowances and passenger payments) did not apply.
- (7) In subsection (6)(b) “the overnight stay conditions” has the same meaning as in section 240 (exemption for incidental overnight expenses) (see section 240(4)).

180 Threshold for benefit of loan to be treated as earnings

- (1) The cash equivalent of the benefit of an employment-related loan is not to be treated as earnings of the employment for a tax year under section 175(1)—
 - (a) if the normal £5,000 threshold is not exceeded, or

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- (b) where the loan is a non-qualifying loan and that threshold is exceeded, if the £5,000 threshold for non-qualifying loans is not exceeded.
- (2) The normal £5,000 threshold is not exceeded if at all times in the year the amount outstanding on the loan (or, if two or more employment-related loans which are taxable cheap loans are outstanding in the year, the aggregate of the amount outstanding on them) does not exceed £5,000.
- (3) The £5,000 threshold for non-qualifying loans is not exceeded if at all times in the year the amount outstanding on the loan (or if two or more employment-related loans which are non-qualifying loans are outstanding in the year, the aggregate of the amounts outstanding on them) does not exceed £5,000.
- (4) In this section a “non-qualifying loan” means a taxable cheap loan which is not a qualifying loan.
- (5) For the purposes of this section a loan is a “qualifying loan” in relation to a particular tax year if, assuming interest is paid on the loan for that year (whether or not it is in fact paid), the whole or part of that interest—
- (a) is eligible for relief under section 353 of ICTA (general provision for relief for payments of interest, excluding MIRAS),
 - (b) would be eligible for relief under that section but for the fact that it is a payment of relevant loan interest to which section 369 of ICTA applies (mortgage interest payable under deduction of tax),
 - (c) is deductible in computing the amount of the profits to be charged [^{F4}to tax] in respect of a trade, profession or vocation carried on [^{F5}wholly or partly in the United Kingdom] by the person to whom the loan is made, or
 - (d) is deductible in computing the amount of the profits to be charged [^{F6}to tax in respect of a UK property business, or a Schedule A business,] carried on by that person.

Textual Amendments

- F4** Words in s. 180(5)(c) substituted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), s. 883\(1\), Sch. 1 para. 588\(a\)\(i\)](#) (with Sch. 2)
- F5** Words in s. 180(5)(c) inserted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), s. 883\(1\), Sch. 1 para. 588\(a\)\(ii\)](#) (with Sch. 2)
- F6** Words in s. 180(5)(d) substituted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), s. 883\(1\), Sch. 1 para. 588\(b\)](#) (with Sch. 2)

Calculation of amount of interest at official rate

181 The official rate of interest

- (1) “The official rate of interest” for the purposes of this Chapter means the rate applicable under section 178 of FA 1989 (general power of Treasury to specify rates of interest).
- (2) Regulations under that section may make different provision in relation to a loan if—
- (a) it was made in the currency of a country or territory outside the United Kingdom, and
 - (b) the employee normally lives in that country or territory, and has actually lived there at some time in the period of 6 years ending with the tax year in question.

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- (3) Subsection (2) does not affect the general power under section 178(3) of FA 1989 to make different provision for different purposes.

182 Normal method of calculation: averaging

The normal method of calculating for the purposes of this Chapter the amount of interest that would be payable on a loan for a tax year at the official rate is as follows.

Step 1

Calculate the average amount of the loan outstanding during the tax year—

1. Find the maximum amount of the loan outstanding on 5th April preceding the tax year or, if the loan was made in the tax year, on the date it was made.
2. Find the maximum amount outstanding on 5th April of the tax year or, if the loan was discharged in the tax year, on the date of discharge.
3. Add these amounts together and divide the result by 2.

Step 2

If the official rate of interest changed during the period in the tax year when the loan was outstanding, calculate the average official rate of interest for that period as follows—

1. Multiply each official rate of interest in force during the period by the number of days when it is in force.
2. Add these products together.
3. Divide the result by the number of days in the period.

Step 3

Calculate the amount of interest that would be payable on the loan for the tax year at the official rate as follows—

$$A \times I \times \frac{M}{12}$$

where—

A is the average amount of the loan outstanding during the tax year obtained from step 1,

I is the official rate of interest in force during the period in the tax year when the loan was outstanding or, if the official rate changed, the average official rate of interest obtained from step 2, and

M is the number of whole months during which the loan was outstanding in the year.

For this purpose a month begins on the sixth day of the calendar month.

183 Alternative method of calculation

- (1) The alternative method of calculating for the purposes of this Chapter the amount of interest that would be payable on a loan for a tax year at the official rate applies for a tax year—

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- (a) if the Inland Revenue so require, by notice to the employee, or
 - (b) if the employee so elects, by notice to the Inland Revenue.
- (2) Notice may be given on or before the first anniversary of the normal self-assessment filing date for the tax year in relation to which the question arises whether the loan is a taxable cheap loan.
- (3) The alternative method is as follows—
 - Step 1*

Find for each day in the tax year in question the maximum amount of the loan outstanding on that day and multiply it by the official rate of interest in force on that day.
 - Step 2*

Add together each of the amounts obtained under step 1.
 - Step 3*

Divide the result by the number of days in the tax year.
- (4) Where in any tax year the cash equivalent of the benefit of the same taxable cheap loan is to be treated as earnings of two or more employees then, for the purposes of determining the cash equivalent of the benefit of the loan, the alternative method applies if—
 - (a) the notice under subsection (1)(a) is given to all those employees, or
 - (b) the notice under subsection (1)(b) is given by all those employees.

Supplementary provisions relating to taxable cheap loans

184 Interest treated as paid

- (1) This section applies where the cash equivalent of the benefit of a taxable cheap loan is treated as earnings from an employee's employment for a tax year under section 175(1).
- (2) The employee is to be treated for the purposes of the Tax Acts as having paid interest on the loan in that year equal to the cash equivalent.
- (3) But the employee is not to be treated as having paid that interest for the purposes of this Chapter or of any of the other Chapters of this Part listed in section 216(4) (provisions of the benefits code which do not apply to lower-paid employment).
- (4) The interest is to be treated—
 - (a) as accruing during the period in the tax year during which the employee holds the employment and the loan is outstanding, and
 - (b) as paid by the employee at the end of the period.
- (5) The interest is not to be treated—
 - (a) as income of the person making the loan, or
 - (b) as relevant loan interest to which section 369 of ICTA applies (mortgage interest payable under deduction of tax).

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185 Apportionment of cash equivalent in case of joint loan etc.

Where in any tax year the cash equivalent of the benefit of the same taxable cheap loan is to be treated as earnings of two or more employees—

- (a) the cash equivalent of the benefit of the loan (determined in accordance with the provisions of this Chapter) is to be apportioned between them in a just and reasonable manner, and
- (b) the portion allocated to each employee is to be treated as the cash equivalent of the benefit of the loan so far as that employee is concerned.

186 Replacement loans

- (1) This section applies where an employment-related loan (“the original loan”) is replaced, directly or indirectly, by—
 - (a) a further employment-related loan, or
 - (b) a loan which is not an employment-related loan but which in turn is, in the same tax year or within 40 days after the end of the tax year, replaced, directly or indirectly, by a further employment-related loan.
- (2) In such a case, for the purposes of calculating the cash equivalent of the benefit of the original loan under section 175(3), section 182 (normal method of calculating interest at the official rate) applies as if the replacement loan, or each of the replacement loans, were the same loan as the original loan.
- (3) Where section 182 is applied as modified by subsection (2) then for the purposes of section 175(3)(b) the amount of interest actually paid on the loan for the tax year in question is the total of—
 - (a) the amount of interest actually paid on the original loan for that year, and
 - (b) the amount of interest actually paid on the replacement loan or on each of the replacement loans for that year.
- (4) In this section a “further employment-related loan” means a loan which is an employment-related loan made in relation to—
 - (a) the same or other employment with the person who is the employer in relation to the original loan, or
 - (b) employment with a person who is connected with that employer.

187 Aggregation of loans by close company to director

- (1) This section applies where, in relation to any tax year, there are employment-related loans between the same lender and borrower which are aggregable with each other.
- (2) The lender may elect for aggregation to apply for that tax year in the case of the borrower.
- (3) The effect of the election is that all the aggregable loans are to be treated as a single loan for the purposes of—
 - section 175 (benefit of taxable cheap loan treated as earnings),
 - the provisions of this Chapter relating to the calculation of the cash equivalent of the benefit of a taxable cheap loan, and
 - section 184 (interest treated as paid).

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- (4) For this purpose loans are aggregable for any tax year if they are made in the same currency and all the following conditions are met in relation to each of them—
- (a) there is a time in the tax year when—
 - (i) the loan is outstanding,
 - (ii) the lender is a close company, and
 - (iii) the borrower is a director of that company;
 - (b) at all times in the tax year the rate of interest on the loan is less than the official rate applying at that time;
 - (c) the loan is not a qualifying loan within the meaning of section 180 (see section 180(5)).
- (5) An election under this section must be made by the lender in a notice given—
- (a) to the Inland Revenue, and
 - (b) before 7th July after the end of the tax year to which the election relates.

Loan released or written off

188 Loan released or written off: amount treated as earnings

- (1) If—
- (a) the whole or part of an employment-related loan is released or written off in a tax year, and
 - (b) at the time when it is released or written off the employee holds the employment in relation to which the loan is an employment-related loan (“employment E”),
- the amount released or written off is to be treated as earnings from the employment for that year.
- (2) But if the employment has terminated or become an excluded employment and there was a time when—
- (a) the whole or part of the loan was outstanding,
 - (b) the employee held the employment, and
 - (c) it was not an excluded employment,
- subsection (1) applies as if the employment had not terminated or become an excluded employment.
- (3) Where subsection (2) applies, any loan which replaces directly or indirectly the employment-related loan is to be treated as an employment-related loan in relation to employment E if—
- (a) it would, if employment E had not terminated or become excluded employment, have been an employment-related loan in relation to employment E, and
 - (b) it is not an employment-related loan in relation to other employment.
- (4) This section is subject to section 189 (exception where double charge).

Status: Point in time view as at 06/04/2005.

Changes to legislation: There are currently no known outstanding effects for the Income Tax (Earnings and Pensions) Act 2003, Chapter 7. (See end of Document for details)

189 Exception where double charge

(1) Section 188 (loan released or written off: amount treated as earnings) does not apply if, by virtue of any other provision of the Income Tax Acts, the amount released or written off—

- (a) is employment income of the employee, or
- (b) is or is treated as income of the employee (or of the employee as a borrower) which is not employment income and upon which that person is liable to pay income tax.

This is subject to subsections (2) and (3).

(2) If, as a result of subsection (1), Chapter 3 of Part 6 (payments and benefits on termination of employment etc.) would be the only provision by virtue of which the amount released or written off would be income of the employee—

- (a) section 188 does apply, and
- (b) accordingly Chapter 3 of Part 6 does not apply.

(3) If—

- (a) an amount is treated as the employee's income under [^{F7}section 633 of ITTOIA 2005 (capital sums paid to settlor by trustees of settlement)] in respect of a capital sum paid in relation to the release or writing-off of the loan, and
- (b) the amount released or written off exceeds the amount so treated as income, section 188 does apply but only the amount of the excess is to be treated as earnings from the employment for the tax year in question under that section.

Textual Amendments

F7 Words in s. 189(3)(a) substituted (6.4.2005) by [Income Tax \(Trading and Other Income\) Act 2005 \(c. 5\), s. 883\(1\), Sch. 1 para. 589](#) (with Sch. 2)

General supplementary provisions

190 Exclusion of charge after death of employee

(1) On the employee's death a taxable cheap loan is to be treated—

- (a) for the purposes of this Chapter as ceasing to be outstanding, and
- (b) for the purposes of section 182 (normal method of calculating interest at the official rate) as being discharged on the date of death.

(2) Section 188 (loan released or written off: amount treated as earnings) does not apply in relation to a release or writing off which takes effect on or after the death of the employee.

191 Claim for relief to take account of event after assessment

(1) A claim may be made for relief in the following cases.

(2) The first case is where—

- (a) the tax payable by an employee for a tax year in respect of a loan has been decided on the basis that, for the purposes of section 175 (benefit of taxable

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- cheap loan treated as earnings), the whole or part of the interest payable on the loan for that year was not paid, and
- (b) it is subsequently paid.
- (3) The second case is where—
- (a) the tax payable by an employee for a tax year in respect of a loan has been decided on that basis that, for the purposes of section 188 (loan released or written off: amount treated as earnings), the loan has been released or written off in that year, and
 - (b) the whole or part of the loan is subsequently repaid.
- (4) The third case is where—
- (a) the tax payable by an employee for a tax year in respect of a loan has been decided on the basis that—
 - (i) section 288 (limited exemption of certain bridging loans connected with employment moves), and
 - (ii) section 289 (relief for certain bridging loans not qualifying for exemption under section 288),will not apply because the condition in section 288(1)(b) (which requires that the limit on the exemption under section 287(1) has not been reached) will not be met, and
 - (b) that condition is met.
- (5) Where a claim is made under this section the tax payable is to be adjusted accordingly.

Status:

Point in time view as at 06/04/2005.

Changes to legislation:

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