



Income Tax (Earnings and Pensions) Act 2003

2003 CHAPTER 1

PART 7

EMPLOYMENT INCOME: SHARE-RELATED INCOME AND EXEMPTIONS

CHAPTER 5

SHARE OPTIONS

Introduction

471 Share options to which this Chapter applies

- (1) This Chapter applies to a share option granted by reason of a person's office or employment as a director or employee of a company.
- (2) The person may be a director or employee of the company whose shares are the subject of the share option, or of another company.
- (3) The share option may be granted to the director or employee or to another person.
- (4) In this Chapter, a "share option" means a right to acquire shares in a company and (unless the context indicates a different meaning)—
 - "the employee", in relation to a share option, means the person mentioned in subsection (1); and
 - "the share option" means the right to acquire shares mentioned there;and "director" and "employee" have the extended meaning given by section 487(1).

472 Introduction to taxation of share options

- (1) The starting-point is that liability to tax may arise by virtue of Chapter 1 of Part 3 (earnings) or Chapter 10 of that Part (taxable benefits: residual liability to charge) when the share option is received, but not when it is exercised.
- (2) But section 474 (no charge in respect of receipt of shorter-term option) contains an exemption from this liability.
- (3) Liability to tax may arise when the share option is exercised by virtue of—
 - (a) Chapter 8 of Part 3 (taxable benefits: notional loans in respect of acquisitions of shares), or
 - (b) section 476 or 477 (charge on exercise etc. of option).
- (4) Liability to tax may also arise when the share option is assigned or released by virtue of section 476 or 477.
- (5) There are special rules relating to share options received under—
 - (a) approved SAYE option schemes (see Chapter 7 of this Part),
 - (b) approved CSOP schemes (see Chapter 8 of this Part), or
 - (c) enterprise management incentives (see Chapter 9 of this Part).

473 Share options to which this Chapter does not apply

- (1) This Chapter (apart from sections 472 and 485) does not apply to a share option granted by reason of a person's office or employment if the earnings from the office or employment 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 (apart from sections 472 and 485) does not apply to a share option so granted after the person has ceased to hold the office or employment, if it would not apply in the event of the option being granted in the last tax year in which the office or employment was held.

Receipt of share option

474 No charge in respect of receipt of shorter-term option

- (1) Subsection (2) applies if the share option cannot be exercised after the tenth anniversary of the date on which it was obtained.
- (2) No liability to income tax arises in respect of the receipt of the share option, except as provided by section 526 (approved CSOP scheme: charge where option granted at a discount).

475 Value of longer-term option for purposes of liability to tax in respect of receipt

- (1) This section applies if the share option can be exercised after the tenth anniversary of the date on which it was obtained.
- (2) For the purposes of any liability to tax by virtue of Chapter 1 of Part 3 (earnings) in respect of the receipt of the share option, the value of the option is taken to be—

MV – C

where—

MV is the higher of—

- (a) the market value at the time the share option is obtained of the shares that are the subject of the share option, and
- (b) the market value at that time of any shares for which those shares may be exchanged, and

C is—

- (a) the amount or value of the consideration for which the shares that are the subject of the share option may be acquired, or
- (b) if that consideration is variable, the least amount or value of the consideration for which they may be acquired.

- (3) In this section “market value” has the same meaning as it has for the purposes of TCGA 1992 by virtue of Part 8 of that Act.

Tax charge on exercise, assignment or release of share option

476 Charge on exercise, assignment or release of option by employee

- (1) This section applies if the employee realises a gain by exercising, assigning or releasing the share option.
- (2) The taxable amount determined under section 478 counts as employment income of the employee for the relevant tax year.
- (3) The “relevant tax year” is the tax year in which the option is exercised, assigned or released.
- (4) Subsection (2) is subject to—
 - section 519 (approved SAYE option schemes: no charge in respect of exercise of option),
 - section 524 (approved CSOP schemes: no charge in respect of exercise of option), and
 - section 530 (enterprise management incentives: no charge on exercise of option to acquire shares at market value).

477 Charge on employee where option exercised, assigned or released by another person

- (1) This section applies if a person other than the employee realises a gain by exercising, assigning or releasing the share option and any of the following is the case—
 - (a) the option was granted to that other person, or
 - (b) the other person acquired the share option otherwise than by or under an assignment made by way of a bargain at arm’s length, or
 - (c) the employee and the other person are connected persons at the time when the gain is realised.
- (2) The taxable amount determined under section 478 counts as employment income of the employee for the relevant tax year.

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- (3) The “relevant tax year” is the tax year in which the option is exercised, assigned or released.
- (4) This section does not apply if the share option is exercised, assigned or released after the death of the person to whom it was granted by—
 - (a) that person’s personal representatives, or
 - (b) the person on whom the option devolved under a testamentary disposition or on an intestacy or partial intestacy, whether beneficially or as trustee.
- (5) This section does not apply by virtue of subsection (1)(b) or (c) if the employee was divested of the share option by operation of law.
- (6) In that case the person who realises the gain is chargeable to tax under Case VI of Schedule D on an amount equal to the amount of the gain in a case within subsection (1)(b) or (c) (see section 479 or 480).

478 Amount of charges

- (1) The taxable amount for the purposes of sections 476 and 477 (charges on exercise, assignment or release of option) is—

$$AG - DA$$

where—

AG is the amount of the gain (see section 479 or 480), 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) subject to subsection (3), any amount that constitutes earnings from the employee’s employment under Chapter 1 of Part 3 (earnings) in respect of the receipt of the share option,
 - (b) subject to subsection (3), any amount that is treated as earnings from the employee’s employment under Chapter 10 of Part 3 (taxable benefits: residual liability to charge) in respect of the receipt of the share option, and
 - (c) any amount that is a deductible amount by virtue of section 481 or 482 (deductible amounts in respect of secondary Class 1 contributions or special contribution met by the employee).
- (3) If—
 - (a) the taxable amount is being determined for the purposes of section 477, and
 - (b) section 476 or that section has already applied to the share option by virtue of an earlier event,
 so much of the amounts in subsection (2)(a) or (b) as was deducted in calculating the taxable amount on that occasion is not a deductible amount.

479 Amount of gain realised by exercising option

- (1) The amount of the gain realised by exercising the share option is—

$$MV - DC$$

where—

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MV is the amount that a person might reasonably expect to obtain from a sale of the shares acquired in the open market at the time the option is exercised, and DC is the total of any deductible costs.

- (2) For the purposes of subsection (1) each of the following is a “deductible cost”—
- (a) subject to subsection (3), the amount or value of any consideration given for the grant of the share option;
 - (b) the amount or value of any consideration given for the shares acquired;
 - (c) in a case within section 477(1)(b) or (c), the amount of any gain realised by a previous holder on an assignment of the option; and
 - (d) if an amount counts as employment income of the employee under section 526 (approved CSOP schemes: charge where option granted at a discount) in respect of the share option, so much of that amount as is attributable to the shares in question.
- (3) If section 476 or 477 has already applied to the share option by virtue of an earlier event, so much of the consideration given for the grant of the share option as was deducted in calculating the amount of the gain on that occasion is not a deductible cost.
- (4) The amount of the gain is calculated in accordance with section 531 (enterprise management incentives: limitation of charge on exercise of option to acquire shares below market value) or 532 (enterprise management incentives: modified tax consequences following disqualifying events) if—
- (a) it is being calculated for the purposes of section 476 (charge on exercise etc. of option by employee), and
 - (b) section 531 or 532, as the case may be, applies.

480 Amount of gain realised by assigning or releasing option

- (1) The amount of the gain realised by assigning or releasing the share option is—

$$C - DC$$

where—

C is the amount or value of the consideration for the assignment or release, and DC is the total of any deductible costs.

- (2) For the purposes of subsection (1) each of the following is a “deductible cost”—
- (a) subject to subsection (3), the amount or value of any consideration given for the grant of the share option;
 - (b) in a case within section 477(1)(b) or (c), the amount of any gain realised by a previous holder on an assignment of the share option; and
 - (c) if an amount counts as employment income of the employee under section 526 (approved CSOP schemes: charge where option granted at a discount) in respect of the share option, so much of that amount as is attributable to the shares in question.
- (3) If section 476 or 477 has already applied to the share option by virtue of an earlier event, so much of the consideration given for the grant of the share option as was deducted in calculating the amount of the gain on that occasion is not a deductible cost.

481 Deductible amount in respect of secondary Class 1 contributions met by employee

- (1) The amount calculated under subsection (2) is a deductible amount for the purposes of section 478(1) 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 contributions in respect of the gain, or
 - (b) an election having effect under paragraph 3B of Schedule 1 to that Act 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 the gain.
- (2) The amount is the sum of—
 - (a) any amount that under the agreement referred to in subsection (1)(a) is recovered in respect of the gain by the secondary contributor before 5th June in the tax year following that in which the exercise, assignment or release of the share option occurred, and
 - (b) the amount of any liability in respect of the gain 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 any liability in respect of the gain for the purposes of subsection (2)(b) is limited to the amount of the liability met before 5th June in the tax year following that in which the exercise, assignment or release of the share option occurred.
- (4) Subsection (1) does not apply in respect of a liability to pay Class 1 contributions which is prevented from arising by virtue of section 2(1)(a) of the Social Security Contributions (Share Options) Act 2001 (c. 20) (liability to pay Class 1 contributions in respect of gain replaced by liability to pay special contribution).
- (5) In this section—

“approval”, in relation to an election, means approval by the Board of Inland Revenue 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).

482 Deductible amount in respect of special contribution met by employee

- (1) The amount of the liability referred to in subsection (4) is a deductible amount for the purposes of section 478(1), if conditions A to D are met.
- (2) Condition A is that a notice in respect of the share option was given to the Board of Inland Revenue in accordance with section 1 of the Social Security Contributions (Share Options) Act 2001 (c. 20) before 11th August 2001.
- (3) Condition B is that the person or one of the persons who gave that notice is a person who (apart from that Act) was liable, or would have become liable, by virtue of an election under paragraph 3B(1) of Schedule 1 to the Contributions and Benefits Act, to pay secondary Class 1 contributions in respect of a gain arising on the exercise, assignment or release of the share option.

- (4) Condition C is that that person became liable to pay a special contribution under section 2 of the Social Security Contributions (Share Options) Act 2001 in respect of the share option.
- (5) Condition D is that that person met that liability before 11th August 2001 or before the end of such further period as the Board of Inland Revenue directed under section 2(5) of that Act.

Supplementary provisions

483 Extended meaning of “assign” and “release”

- (1) For the purposes of this Chapter, a person who receives a benefit in money or money’s worth in consideration for, or otherwise in connection with—
 - (a) failing or undertaking not to exercise a share option, or
 - (b) granting or undertaking to grant to another person a right to acquire shares which are subject to a share option or any interest in them,is to be treated as realising a gain by assigning or releasing the share option for a consideration equal to the amount or value of the benefit.
- (2) References in this Chapter to the release of a share option include agreeing to the restriction of the exercise of the option.

484 Amount or value of consideration given for grant of share option

- (1) This section applies for the purposes of sections 479 and 480 (amount of gain) in determining the amount or value of any consideration given for the grant of the share option.
- (2) If any consideration is given partly in respect of the grant and partly in respect of something else, the amount given in respect of the different things is to be determined on a just and reasonable apportionment.
- (3) The consideration given wholly or partly for the grant does not include the performance of any duties of, or in connection with, the office or employment by reason of which the share option was granted.

485 Application of this Chapter where share option exchanged for another

- (1) This section applies if—
 - (a) a share option (“the old option”) is assigned or released, and
 - (b) the whole or part of the consideration for the assignment or release consists of or includes another share option (“the new option”).
- (2) For the purposes of section 480 (amount of gain realised by assigning or releasing option) the new option is not to be treated as consideration for the assignment or release of the old option.
- (3) This Chapter applies to the new option as it applies to the old option.
- (4) For the purposes of sections 479 and 480 (amount of gain) the amount or value of the consideration for the grant of the new option is to be treated as being the sum of—

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- (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.
- (5) Two or more transactions are to be treated for the purposes of subsection (1) as a single transaction by which one share option is assigned for a consideration which consists of or includes another share option if—
- (a) the transactions result in—
 - (i) a person ceasing to hold a share option, and
 - (ii) that person or a connected person coming to hold another share option, and
 - (b) one or more of the transactions is effected under arrangements to which two or more persons holding share options, in respect of which there may be liability to tax under this Chapter, are parties.
- (6) Subsection (5) applies regardless of the order in which the assignment and the acquisition occur.

486 Duty to notify matters relating to share options

- (1) Subsection (2) applies if in a tax year a company—
- (a) grants a share option,
 - (b) allots or transfers shares on the exercise of a share option,
 - (c) receives notice of the assignment of a share option, or
 - (d) provides a benefit in money or money's worth—
 - (i) for the assignment of a share option,
 - (ii) for the release in whole or in part of a share option,
 - (iii) for or in connection with a failure, or undertaking not, to exercise a share option, or
 - (iv) for or in connection with the grant of, or an undertaking to grant, a right to acquire shares or an interest in shares to which a share option relates.
- (2) The company must provide the Inland Revenue with particulars in writing of the matter.
- (3) The particulars must be provided before 7th July in the tax year following that in which the matter occurred.
- (4) The particulars of any matter must include particulars of any secondary Class 1 contributions payable in connection with the matter which are—
- (a) recovered as mentioned in section 481(2)(a) (agreement for secondary contributor to recover secondary Class 1 contributions in respect of gain from the employee), or
 - (b) met as mentioned in section 481(3) (liability for secondary Class 1 contributions in respect of gain transferred to the employee).
- (5) A company need not deliver particulars under subsection (1) if it has already given them in a notice under paragraph 44 of Schedule 5 (enterprise management incentives: notice of option to be given to Inland Revenue).

In other respects the obligations imposed by subsection (1) and by that paragraph are independent of each other.

487 Minor definitions

(1) In this Chapter—

“company” means a body corporate;

“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 a 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;

“secondary Class 1 contributions” has the same meaning as in the Contributions and Benefits Act (see section 1);

“shares” includes—

- (a) stock, and
 - (b) any securities as defined in section 254(1) of ICTA issued by a company;
- “the Contributions and Benefits Act” means SSCBA 1992 or SSCB(NI)A 1992.

(2) In this Chapter—

“share option”,

“the employee”, and

“the share option”,

have the meaning indicated in section 471(4).