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# Income Tax (Earnings and Pensions) Act 2003

## 2003 CHAPTER 1

### [<sup>F1</sup>PART 7A

EMPLOYMENT INCOME PROVIDED THROUGH THIRD PARTIES

### CHAPTER 2

TREATMENT OF RELEVANT STEP FOR INCOME TAX PURPOSES

*[<sup>F1</sup>Employment income*

#### Textual Amendments

**F1** Pt. 7A inserted (with effect in accordance with Sch. 2 paras. 52-59 of the amending Act) by [Finance Act 2011 \(c. 11\)](#), [Sch. 2 para. 1](#)

#### **554Z2** Value of relevant step to count as employment income

- (1) If this Chapter applies by reason of a relevant step, the value of the relevant step (see section 554Z3) counts as employment income of A in respect of A's employment with B—
  - (a) if the relevant step is taken before A's employment with B starts, for the tax year in which the employment starts, or
  - (b) otherwise, for the tax year in which the relevant step is taken.
- (2) If the relevant step gives rise to—
  - (a) an amount which (apart from this subsection) would be treated as earnings of A under a provision of the benefits code, or

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- (b) any income of A which (apart from this subsection) would be dealt with under Chapter 3 of Part 4 of ITTOIA 2005,  
 subsection (1) applies instead of that provision of the benefits code or Chapter 3 of Part 4 of ITTOIA 2005 (as the case may be).
- (3) In particular, in a case in which the relevant step is the making of an employment-related loan (within the meaning of Chapter 7 of Part 3), the effect of subsection (2) (a) is that the loan is not to be treated for any tax year as a taxable cheap loan for the purposes of that Chapter.

### **554Z3 Value of relevant step**

- (1) If the relevant step involves a sum of money, its value is the amount of the sum.
- (2) In any other case, the value of the relevant step is—
  - (a) the market value when the relevant step is taken of the asset which is the subject of the step, or
  - (b) if higher, the cost of the relevant step.
- (3) Subsection (2)(a) is subject to sections 437 and 452.
- (4) Subsection (2)(b) is to be ignored if—
  - (a) the relevant step is within section 554C(1)(c), and
  - (b) any of Chapters 2 to 4A of Part 7 apply by virtue of the acquisition.
- (5) Subsection (2)(b) is also to be ignored if section 554Z7 applies.
- (6) In subsection (2)(b) the reference to the cost of the relevant step is to the expense incurred in connection with the relevant step (including a proper proportion of any expense relating partly to the relevant step and partly to other matters) by the person or persons at whose cost the relevant step is taken.
- (7) Subsections (1) and (2) are subject to sections 554Z4, 554Z5, 554Z6, 554Z7 and 554Z8, which, so far as applicable, are to be applied in that order.

### **554Z4 Residence issues**

- (1) After the value of the relevant step is determined under section 554Z3, the particular tax year or years which the value of the relevant step is “for” are to be determined.
- (2) For this purpose, apply sections 16(1) to (4) and 17(1) to (3) as if the value of the relevant step were general earnings.
- (3) Subsection (4) applies if the value of the relevant step, or a part of it, is “for” a tax year in which A is non-UK resident.
- (4) The value, or the part of it, is to be reduced so far as it is not in respect of duties performed in the United Kingdom.
- (5) The question of the extent to which the value, or the part of it, is not in respect of duties performed in the United Kingdom is to be determined on a just and reasonable basis.
- (6) This section does not change the tax year for which the value of the relevant step counts as employment income under section 554Z2(1).

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### **554Z5 Overlap with earlier relevant step**

- (1) This section applies if there is overlap between—
  - (a) the sum of money or asset (“sum or asset P”) which is the subject of the relevant step, and
  - (b) the sum of money or asset (“sum or asset Q”) which was the subject of an earlier relevant step (“the earlier relevant step”) by reason of which this Chapter applied in respect of A's employment with B.
- (2) The value of the relevant step (after any reductions under section 554Z4) is reduced (but not below nil)—
  - (a) if the overlap covers the whole of sum or asset Q, by the value of the earlier relevant step, or
  - (b) if the overlap covers only part of sum or asset Q, by the part of the value of the earlier relevant step which corresponds to the part of sum or asset Q covered by the overlap as determined on a just and reasonable basis.
- (3) In subsection (2) references to the value of the earlier relevant step are to that value—
  - (a) after any reductions made to it under section 554Z4 or this section or section 554Z7, but
  - (b) before any reductions made to it under section 554Z6 or 554Z8.
- (4) For the purposes of this section there is overlap between sum or asset P and sum or asset Q so far as—
  - (a) they are the same sum of money or asset, or
  - (b) sum or asset P, essentially, replaces sum or asset Q.
- (5) Further, if any reductions were made under this section to the value of the earlier relevant step, sum or asset P is treated as overlapping with any other sum of money or asset so far as the other sum of money or asset was treated as overlapping with sum or asset Q for the purposes of this section.

### **554Z6 Overlap with certain earnings**

- (1) This section applies if the relevant step gives rise to relevant earnings of A from A's employment with B—
  - (a) which are, in accordance with section 16 and (if applicable) section 17, “for” a tax year in which A is UK resident, or
  - (b) which are, in accordance with section 29 and (if applicable) section 30, “for” a tax year in which A is non-UK resident but which are in respect of duties performed in the United Kingdom for the purposes of section 27(1)(a).
- (2) The value of the relevant step (after any reductions under section 554Z4 or 554Z5) is reduced (but not below nil) by the amount of the relevant earnings.
- (3) For the purposes of this section the following are “relevant” earnings—
  - (a) earnings within Chapter 1 of Part 3,
  - (b) amounts treated as earnings under Chapter 12 of Part 3, and
  - (c) a deemed employment payment under section 50 or any part of such a payment.
- (4) But anything which is exempt income, or which falls within Chapter 3 of Part 4 of ITTOIA 2005, is not “relevant”.

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## **554Z7 Exercise price of share options**

(1) Subsection (3) applies if—

- (a) the relevant step is a step within section 554B (other than one treated as being taken by section 554L(5), (7) or (9) or 554M(4), (6) or (8)),
- (b) B is a company,
- (c) there is an arrangement (“B’s employee share scheme”) under which, in respect of A’s employment with B, a right (“a relevant share option”) may be granted to A—
  - (i) to acquire relevant shares, or
  - (ii) to receive a sum of money the amount of which is to be determined by reference to the market value of any relevant shares at the time the sum is to be paid,
- (d) in order to exercise the relevant share option so as—
  - (i) to acquire the relevant shares, or
  - (ii) to receive the sum of money,

A would, under the terms of the option, have to pay a sum of money the amount of which can be determined at the time of the grant of the option,

- (e) the subject of the relevant step is relevant shares (“earmarked shares”) which are earmarked, or otherwise start being held, solely with a view to providing shares, or paying a sum of money, pursuant to—
  - (i) a relevant share option granted to A under B’s employee share scheme as mentioned in paragraph (c) in relation to which the requirements of paragraph (d) are met, or
  - (ii) a relevant share option which is expected to be granted to A under B’s employee share scheme as mentioned in paragraph (c) and in relation to which the requirements of paragraph (d) would be met,
- (f) the number of relevant shares of any type which are earmarked shares does not exceed the maximum number of relevant shares of that type which might reasonably be expected to be needed for providing shares, or paying a sum of money, pursuant to the relevant share option which is granted or expected to be granted, and
- (g) there is no connection (direct or indirect) between the relevant step and a tax avoidance arrangement.

(2) Subsection (3) also applies if—

- (a) the relevant step is a step treated as being taken by section 554L(9) or 554M(8), and
- (b) in order to exercise the relevant share option to which the step relates so as—
  - (i) to acquire the shares which are the subject of the relevant step, or
  - (ii) to receive the sum of money determined by reference to the market value of those shares,

A would, under the terms of the option, have to pay a sum of money the amount of which can be determined at the time the option is granted.

(3) The value of the relevant step (after any reductions under sections 554Z4 to 554Z6) is to be reduced (but not below nil) by—

- (a) the amount of the sum of money which A would have to pay as mentioned in subsection (1)(d) or (2)(b), or

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- (b) if the value of the relevant step was reduced under section 554Z4, X% of the amount of that sum of money.
- (4) In subsection (3)(b) “X%” means the proportion of the value of the relevant step (as determined under section 554Z3) left after the reduction under section 554Z4.
- (5) If subsection (3) applies by virtue of subsection (1) and the relevant step is taken in relation to an expected grant of a relevant share option as mentioned in subsection (1)(e)(ii), subsection (7) applies if—
  - (a) the grant is not made before the end of the date (“the final grant date”) falling immediately after the period of three months starting with the date on which the relevant step is taken, and
  - (b) as at the end of the final grant date, any of the earmarked shares continue to be held by or on behalf of P solely on the basis mentioned in subsection (1)(e).
- (6) If subsection (3) applies by virtue of subsection (1), subsection (7) also applies if at any time after the taking of the relevant step—
  - (a) any of the earmarked shares cease to be held by or on behalf of P solely on the basis mentioned in subsection (1)(e), but
  - (b) the shares continue to be held by or on behalf of P on the basis mentioned in section 554B(1)(a) or (b).
- (7) This Part has effect as if a relevant step within section 554B were taken at the end of the final grant date or when the shares cease to be held as mentioned in subsection (6)—
  - (a) the subject of which is the earmarked shares mentioned in subsection (5)(b) or (6), and
  - (b) by reason of which this Chapter is to apply (subject only to section 554A(4)).
- (8) In this section “relevant shares” has the meaning given by section 554I(4).

### **554Z8 Cases where consideration given for relevant step**

- (1) Subsection (2) applies if—
  - (a) the relevant step is a step within section 554C(1)(a) to (c),
  - (b) the relevant step is for consideration given by A in the form of the transfer of an asset to P from A,
  - (c) the transfer by A of the asset is made before, or at or about, the time the relevant step is taken and is not by way of a loan, and
  - (d) there is no connection (direct or indirect) between the transfer by A of the asset and a tax avoidance arrangement.
- (2) The value of the relevant step (after any reductions under sections 554Z4 to 554Z6) is reduced (but not below nil) by—
  - (a) the market value of the asset transferred by A at the time of its transfer, or
  - (b) if the value of the relevant step was reduced under section 554Z4, X% of that market value.
- (3) For the purposes of subsection (1)(d) it is (in particular) to be assumed that the transfer by A of the asset is connected with a tax avoidance arrangement if—
  - (a) before the transfer, the asset was transferred to A by another person by way of a loan, or

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- (b) the asset is, or carries with it, any rights or interests under the relevant arrangement or any arrangement which is connected (directly or indirectly) with the relevant arrangement.
- (4) In subsection (3)(b) “the relevant arrangement” has the meaning given by section 554A(1)(b).
- (5) Subsection (6) applies if—
- (a) the relevant step is a step within section 554C(1)(b) or (c) or (e) or 554D and does not also involve a sum of money,
  - (b) the relevant step is for consideration given by A in the form of the payment of a sum of money to P by A, and
  - (c) the payment is made before, or at or about, the time the relevant step is taken.
- (6) The value of the relevant step (after any reductions under sections 554Z4 to 554Z6) is reduced (but not below nil) by—
- (a) the amount of the consideration given, or
  - (b) if the value of the relevant step was reduced under section 554Z4, X% of the amount of that consideration.
- (7) In subsections (2)(b) and (6)(b) “X%” means the proportion of the value of the relevant step (as determined under section 554Z3) left after the reduction under section 554Z4.
- (8) In this section references to A include references to any person linked with A.]

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