

# Disguised Remuneration

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## Who is likely to be affected?

Employers, directors, and employees who use arrangements involving trusts and other vehicles to avoid, reduce, or defer liabilities to income tax on rewards of an employment or to avoid restrictions on pensions tax relief.

## General description of the measure

In many cases, these third party arrangements allow an employee to enjoy the full benefit of a sum of money paid or assets provided while arguing that, because of the structure of the arrangements, there is no legal right to the money or assets. This argument is used to support a proposition that income tax and national insurance contributions (NICs) are due (if at all) only on the use of the money or assets during the period of the employee's employment and not on their full value.

Legislation will be introduced in Finance Bill 2011 to ensure that where a third party makes provision for what is in substance a reward or recognition or loan in connection with the employee's employment, an income tax charge arises. This will be based on:

- a sum of money made available; or
- on the higher of the cost or market value where an asset is used to deliver the reward or recognition. For example, where the asset in question is transferred or otherwise made available for an employee's use and benefit as if the employee owned the asset.

The amount concerned will count as a payment of employment income and the employer will be required to account for PAYE accordingly.

## Policy objective

The measure supports the Government's objective of a fairer tax system by ensuring that:

- income tax and NICs on employment income are not avoided or deferred; and
- contributions to unregistered pension schemes do not benefit from tax advantages on pension savings beyond the annual and lifetime allowances available in registered pensions schemes.

## Background to this measure

- The June Budget announced that legislation would be introduced from April 2011 to tackle arrangements using trusts and other vehicles to reward employees which seek to avoid, defer or reduce tax liabilities.
- The Government also confirmed that the scope of the legislation would include Employer Financed Retirement Benefit Schemes (EFRBS), in order to protect revenues and in keeping with the restriction of pensions tax relief through the reduced annual and lifetime allowances announced on 14 October 2010.

## Detailed proposal

### Operative date

The legislation will have effect on and after 6 April 2011 and apply to rewards which are earmarked for an individual employee or otherwise made available on and after that date.

In addition, anti-forestalling provisions apply to the payment of sums and the provision of readily convertible assets for the purposes of securing the payment of sums (including loans) where the sum is paid or the asset is provided between 9 December 2010 and 5 April 2011 where, if paid or provided on or after 6 April 2011, they would be caught by the legislation.

The anti-forestalling charge will arise on 6 April 2012 if sums paid have not been repaid, or readily convertible assets used to secure the payment of a sum have not been returned before that date, or not otherwise charged to tax under section 62 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA). Any sum paid to which these anti-forestalling provisions apply, less a deduction for any amount which has been repaid, will count as employment income. The employer will be required to account for income tax under PAYE as if the amount concerned was a payment made on 6 April 2012. The value of any readily convertible asset provided (to which the anti-forestalling provisions apply) will also count as employment income. The employer will be required to operate PAYE, as if the amount concerned was a payment made on 6 April 2012.

### Current law

The measure is mostly concerned with Parts 2 to 7 of ITEPA. Part 11 of ITEPA, which provides for the operation of PAYE, is also affected. Section 6(1) of ITEPA provides that the charge to tax on employment income is a charge to tax on "general earnings" and "specific employment income". Specific employment income means any amount that counts as employment income, which is explained in section 7(4) and (6) of ITEPA.

#### *Existing casework and litigation*

Some of the types of transaction which will be chargeable to tax under this measure (including the earmarking of funds held in a discretionary trust) are not accepted by HM Revenue & Customs (HMRC) as effective in avoiding tax under the present law. HMRC will continue to challenge such transactions under the present law, including in litigation where necessary.

### Proposed revisions

Where trusts and other intermediate vehicles are used in arrangements aimed at providing value to an individual for what is in substance a reward or recognition in connection with the individual's employment, or loan in connection with the employee's employment, a new Part 7A of ITEPA will provide for a new employment income charge to apply in the following ways:

- sums or assets that are earmarked for employees by trusts or other intermediaries will be treated as though the amount of the sum or the value of the asset concerned is a payment of PAYE income provided by the employee's employer to the employee;
- loans provided to employees by trusts and other intermediaries will be treated as though the value of the loan provided is a payment of PAYE income provided by the employee's employer to the employee; and

- assets provided to employees by trusts and other intermediaries will be regarded for tax purposes as a payment of PAYE income by the employer where certain conditions specified in new Part 7A are met.

#### *National Insurance Contributions*

Regulations will be brought forward to apply NICs to amounts chargeable to tax to under this measure.

### Summary of impacts

<b>Exchequer impact (£m)</b>	This measure is expected to increase receipts by up to £500 million per year. The final costing will be subject to scrutiny by the Office for Budget Responsibility and will be set out at the Budget. This measure will also prevent the future use of such tax avoidance arrangements, protecting tax from the pensions allowance changes being introduced in April 2011.
<b>Economic impact</b>	The measure is not expected to have significant economic impacts.
<b>Impact on individuals and households</b>	<p>In relation to the arrangements known to HMRC, there are approximately 5,000 employers who are currently using these schemes, with an estimated 50,000 employees thought to be indirectly benefiting. The take up is likely to be wider than this as there has been extensive marketing and widening accessibility of these arrangements over the last few years. Given the nature and complexity of the arrangements that this measure seeks to address, it is expected that most employees affected will be higher rate or additional rate tax payers.</p> <p>This legislation will mean that employees benefiting from such schemes will have to pay more tax and NICs – in line with those employees for whom these arrangements have not been implemented. However, we do not expect there to be any significant administrative or compliance cost to individuals and households from this change because the income tax charge will be collected through PAYE via their employers.</p>
<b>Equalities impacts</b>	The measure targets tax avoidance behaviours rather than particular types of individual or business. The Government has no evidence to suggest that the measure will have any adverse equalities impacts.
<b>Impact on business including third sector</b>	<p>The objective of this legislation is to prevent the avoidance or deferral of income tax and NICs on employment income. It will impact on employers and intermediaries who use trusts or loans to reward employees with a view to avoiding or deferring paying tax and NICs.</p> <p>The data which HMRC has on known arrangements suggests that there is a broad range of employers who have implemented these arrangements – around 5,000. The type of businesses thought to be involved ranges from large employers in the financial services industry to single-employee limited companies. We believe that only a minority of employers have implemented these arrangements and although the legislation creates a new income tax charge it is not expected to have a material impact on the tax obligations of the vast majority of compliant businesses. The administrative burden of the measure is therefore thought to be negligible.</p> <p>Some small businesses will be affected by the proposal if they are using these remuneration arrangements to reward employees. To exclude small</p>

	<p>businesses from the legislation would create unfairness and further opportunities for tax avoidance.</p> <p>On the assumption that most businesses will discontinue the use of these arrangements, compliance costs to business overall are thought to be insignificant.</p> <p>There will be some compliance costs for those currently operating, and planning to operate, EFRBS pension arrangements. The cost will be in terms of the legal fees for the transfer of policies and the dissemination and familiarisation costs of the rule changes. These costs will of course vary across businesses, depending on the historical nature of the arrangement. It is estimated that there are only relatively small numbers of such schemes in operation. However, changes to pension tax relief being introduced in April 2011 would have been likely to trigger some increased take-up.</p> <p>There will be some further impacts on intermediaries and professional pension specialists who advise on these schemes, as with any rule change of this kind. This may cause further cost to businesses through consultation, seeking advice and reorganisation of their pension and remuneration arrangements under the new rules.</p>
<b>Impact on public sector</b>	<p>It is expected that over time the measure will reduce the cost of the resource HMRC currently uses to intervene in similar schemes. However, there will be resource implications in producing guidance for customers and for HMRC employees along with any necessary staff awareness or training in connection with the new measure.</p>
<b>Other impacts</b>	<p>No significant additional impacts to those discussed above have been identified.</p>

### **Monitoring and evaluation**

The impact of the policy will principally be monitored via the Disclosure of Tax Avoidance Schemes process, tax gap analysis, revenues from income tax and other forms of intelligence.

The policy will be reviewed on an ongoing basis. The Government is committed to focusing available resources into tackling tax avoidance.

### **Further advice**

If you have any questions about this change, please contact Peter Robinson on 020 7147 2423 (email: [peter.w.robinson@hmrc.gsi.gov.uk](mailto:peter.w.robinson@hmrc.gsi.gov.uk)) or David McDowell on 020 7147 0175 (email: [david.mcdowell@hmrc.gsi.gov.uk](mailto:david.mcdowell@hmrc.gsi.gov.uk)).

**1 Employment income through third parties**

Schedule 1 contains provision about employment income through third parties.

## SCHEDULES

### SCHEDULE 1

Section 1

#### EMPLOYMENT INCOME THROUGH THIRD PARTIES

*Main provision*

1 After Part 7 of ITEPA 2003 insert –

#### **“PART 7A**

#### EMPLOYMENT INCOME THROUGH THIRD PARTIES

#### **CHAPTER 1**

#### APPLICATION ETC

#### **554A Application of Chapter 2**

- (1) Chapter 2 applies if –
  - (a) a person (“A”) is an employee, or a former or prospective employee, of another person (“B”),
  - (b) there is an arrangement (“the relevant arrangement”) to which A is a party or which otherwise (wholly or partly) covers or relates to A,
  - (c) it is reasonable to suppose that, in essence –
    - (i) the relevant arrangement, or
    - (ii) the relevant arrangement so far as it covers or relates to A,
 is (wholly or partly) a means of providing, or is otherwise concerned (wholly or partly) with the provision of, rewards or recognition or loans in connection with A’s employment, or former or prospective employment, with B,
  - (d) a relevant step is taken by a relevant third person, and
  - (e) it is reasonable to suppose that, in essence –
    - (i) the relevant step is taken (wholly or partly) in pursuance of the relevant arrangement, or
    - (ii) there is some other connection (direct or indirect) between the relevant step and the relevant arrangement.
- (2) In this Part “relevant step” means a step within section 554B, 554C or 554D.
- (3) Subsection (1) is subject to subsection (4) and sections 554E to 554H.

- (4) Chapter 2 does not apply if –
  - (a) the relevant step does not involve a sum of money,
  - (b) the asset which is the subject of the relevant step is exactly the same asset as was the subject of an earlier relevant step, and
  - (c) Chapter 2 applied by reason of that earlier relevant step in respect of A’s employment with B.
- (5) In subsection (1)(b) and (c)(ii) references to A include references to any person linked with A.
- (6) For the purposes of subsection (1)(c) it does not matter if the relevant arrangement does not include details of the steps which will or may be taken in connection with providing, in essence, rewards or recognition or loans as mentioned (for example, details of any sums of money or assets which will or may be involved or details of how or when or by whom or in whose favour any step will or may be taken).
- (7) In subsection (1)(d) “relevant third person” means –
  - (a) A acting as a trustee of an arrangement,
  - (b) B acting as a trustee of an arrangement, or
  - (c) any person other than A and B.
- (8) In subsection (7) “trustee”, in the case of an arrangement in relation to which there would be no trustees apart from this subsection, means any person –
  - (a) who holds any sum of money or asset, or on whose behalf any sum of money or asset is held, under the arrangement, or
  - (b) who is responsible for the management of any sum of money or asset held under the arrangement.
- (9) For the purposes of subsection (1)(e) –
  - (a) the relevant step is connected with the relevant arrangement if (for example) the relevant step is taken (wholly or partly) in pursuance of an arrangement at one end of a series of arrangements with the relevant arrangement being at the other end, and
  - (b) it does not matter if the person taking the relevant step is unaware of the relevant arrangement.
- (10) For the purposes of subsection (1)(c) and (e) in particular, all relevant circumstances are to be taken into account in order to get to the essence of the matter.

**554B Relevant steps: earmarking of sum of money or asset**

- (1) A person (“P”) takes a step within this section if P earmarks (however informally) any sum of money or asset held by or on behalf of P with a view to a later relevant step being taken in relation to a relevant sum or asset by P or any other person (on the meeting of any condition or otherwise).
- (2) For the purposes of subsection (1) it does not matter –
  - (a) if details of the later relevant step have not been worked out (for example, details of the sum of money or asset which would be the subject of the step or details of how or when or

- by whom or in whose favour the step will or may be taken),  
or
- (b) if A, or any person linked with A, has no legal right to have a relevant step taken in relation to any relevant sum or asset.
- (3) In this section “relevant sum or asset” means –
- (a) the earmarked sum of money or asset, or
- (b) a sum of money or asset which may (directly or indirectly) arise or derive from the earmarked sum of money or asset.

#### **554C Relevant steps: payment of sum, transfer of asset etc**

- (1) A person (“P”) takes a step within this section if P –
- (a) pays a sum of money to a relevant person,
- (b) transfers the property in an asset to a relevant person,
- (c) takes a step by virtue of which a relevant person acquires an asset within subsection (4),
- (d) makes available a sum of money or asset for use –
- (i) as security for a loan made or to be made to a relevant person, or
- (ii) otherwise as security for the meeting of any liability, or the performance of any undertaking, which a relevant person has or will have, or
- (e) grants to a relevant person a lease of any premises the effective duration of which is likely to exceed 21 years.
- (2) In subsection (1) “relevant person” –
- (a) means A or a person chosen by A or within a class of person chosen by A, and
- (b) includes, if P is taking a step on A’s behalf or otherwise at A’s direction or request, any other person.
- (3) In subsection (2) references to A include references to any person linked with A.
- (4) The following assets are within this subsection –
- (a) securities,
- (b) interests in securities, and
- (c) securities options,
- as defined in section 420; and in subsection (1)(c) “acquires” is to be read in accordance with section 421B(2)(a).
- (5) For the purposes of subsection (1)(d) –
- (a) the reference to making a sum of money or asset available is a reference to making it available in any way, however informal,
- (b) it does not matter if the relevant person has no legal right to have the sum of money or asset used as mentioned, and
- (c) it does not matter if the sum of money or asset is not actually used as mentioned.
- (6) For the purposes of subsection (1)(e), if there are circumstances which make it likely that a lease (“the original lease”) will be extended for any period, the effective duration of the original lease is

to be determined on the assumption that the original lease will be so extended.

- (7) Further, if—
- (a) A is, or is likely to become, entitled to a later lease, or the grant of a later lease, of the same premises, or
  - (b) it is otherwise likely that A will be granted a later lease of the same premises,
- the term of the original lease is to be treated as continuing until the end of the term of the later lease.
- (8) In subsection (7) —
- (a) references to A include references to—
    - (i) any person linked with A, and
    - (ii) the person to whom the original lease was granted where the original lease was not granted to A or any person linked with A,
  - (b) references to the same premises include references to any premises which include the whole or part of the same premises, and
  - (c) in relation to Scotland, “term” means period.
- (9) In this section “lease” and “premises” have the same meaning as they have in Chapter 4 of Part 3 of ITTOIA 2005.

#### **554D Relevant steps: making asset available**

- (1) A person (“P”) takes a step within this section if, without transferring the property in an asset to a relevant person, P—
- (a) at any time, makes the asset available for the relevant person to benefit from in a way which is substantially similar to the way in which the relevant person would have been able to benefit from the asset had the property in the asset been transferred to the relevant person at that time, or
  - (b) at or after the end of the relevant period, makes the asset available for the relevant person to benefit from.
- (2) If—
- (a) before the end of the relevant period, P makes available an asset for a relevant person to benefit from, and
  - (b) at the end of the relevant period, P continues to make the asset available for the relevant person to benefit from,
- P is treated as taking a step within this section by virtue of subsection (1)(b) at the end of the relevant period.
- (3) For the purposes of subsections (1) and (2) —
- (a) references to making an asset available are references to making it available in any way, however informal,
  - (b) it does not matter if the relevant person has no legal right to benefit from the asset, and
  - (c) it does not matter if the relevant person does not actually benefit from the asset.

- (4) In subsections (1) and (2) “the relevant period” means the period of two years starting with the day on which A’s employment with B ceases.
- (5) In subsections (1) and (2) “relevant person” –
  - (a) means A or a person chosen by A or within a class of person chosen by A, and
  - (b) includes, if P is taking a step on A’s behalf or otherwise at A’s direction or request, any other person.
- (6) In subsection (5) references to A include references to any person linked with A.

**554E Exclusions: steps under certain schemes and arrangements**

- (1) Chapter 2 does not apply by reason of a relevant step if the step is taken under any of the following –
  - (a) an approved SIP (within the meaning of Chapter 6 of Part 7),
  - (b) an approved SAYE option scheme (within the meaning of Chapter 7 of Part 7),
  - (c) an approved CSOP scheme (within the meaning of Chapter 8 of Part 7),
  - (d) an arrangement the sole purpose of which is the issue of qualifying options (within the meaning of Chapter 9 of Part 7),
  - (e) an arrangement the sole purpose of which is the provision of excluded benefits (within the meaning of section 393B(3)),
  - (f) a registered pension scheme, or
  - (g) an arrangement the sole purpose of which is the making of payments which are authorised for the purposes of section 160(1) of FA 2004 (see section 164 of that Act).
- (2) In subsection (1)(g) “payments” is to be read in accordance with section 161 of FA 2004.
- (3) The Commissioners for Her Majesty’s Revenue and Customs may by regulations provide that, in the cases set out in the regulations, Chapter 2 is not to apply by reason of a relevant step taken under a relevant non-UK scheme (within the meaning of paragraph 1(5) of Schedule 34 to FA 2004).
- (4) Regulations under subsection (3) may have retrospective effect.

**554F Exclusions: commercial transactions**

- (1) Chapter 2 does not apply by reason of a relevant step which is the payment of a sum of money by way of a loan if the loan –
  - (a) is a loan on ordinary commercial terms for the purposes of section 176, ignoring conditions B and C in that section, and
  - (b) is not, and is not connected (directly or indirectly) with, an arrangement which has a tax avoidance purpose.
- (2) Chapter 2 does not apply by reason of a relevant step taken by a person (“P”), which is not the payment of a sum of money by way of a loan, if –

- (a) the step is taken for the purposes of a transaction which P has with A and which P entered into in the ordinary course of P's business,
  - (b) a substantial proportion of P's business involves similar transactions with members of the public,
  - (c) the terms on which P entered into the transaction with A are substantially the same as the terms on which P normally enters into similar transactions with members of the public, and
  - (d) the transaction is not, and is not connected (directly or indirectly) with, an arrangement which has a tax avoidance purpose.
- (3) For the purposes of subsections (1)(b) and (2)(d) an arrangement has a tax avoidance purpose if subsection (4) applies to a person who is a party to the arrangement.
- (4) This subsection applies to a person if the main purpose, or one of the main purposes, of the person in entering into the arrangement is the avoidance of tax or national insurance contributions.
- (5) For the purposes of subsection (2)(b) and (c) a transaction is "similar" if it is of the same or a similar type to the transaction which P has with A.
- (6) In subsection (2)(b) and (c) "members of the public" means members of the public at large with whom P deals at arm's length.
- (7) In this section references to A include references to any person linked with A.

#### **554G Exclusions: transactions under employee benefit packages**

- (1) Chapter 2 does not apply by reason of a relevant step taken by a person ("P") if –
- (a) the step is taken for the purposes of a transaction which P has with A and which P entered into in the ordinary course of P's business,
  - (b) where the step is the payment of a sum of money by way of a loan, a substantial proportion of P's business involves making similar loans to members of the public,
  - (c) the transaction with A is part of a package of benefits which is available to a substantial proportion of B's employees,
  - (d) the terms on which similar transactions are offered by P under the package are generous enough to enable substantially all of the employees of B to whom the package is available to take advantage of what is offered (if they want to),
  - (e) the terms on which P enters into the transaction with A are substantially the same as the terms on which P normally enters into similar transactions under the package with employees of B,
  - (f) a majority of B's employees to whom the package is available do not have a material interest (within the meaning of section 68) in B,

- (g) the transaction with A is not, and is not connected (directly or indirectly) with, an arrangement which has a tax avoidance purpose, and
  - (h) subsection (5) does not apply.
- (2) In subsection (1)(b) “members of the public” means members of the public at large with whom P deals at arm’s length.
  - (3) For the purposes of subsection (1)(g) an arrangement has a tax avoidance purpose if subsection (4) applies to a person who is a party to the arrangement.
  - (4) This subsection applies to a person if the main purpose, or one of the main purposes, of the person in entering into the arrangement is the avoidance of tax or national insurance contributions.
  - (5) This subsection applies if any feature of the package of benefits has or is likely to have the effect that, of the employees of B to whom the package is available, it is employees within subsection (6) on whom benefits under the package will be wholly or mainly conferred.
  - (6) The employees within this subsection are –
    - (a) directors,
    - (b) senior employees,
    - (c) employees who receive, or as a result of the package of benefits are likely to receive, the higher or highest levels of remuneration, and
    - (d) if B is a member of a group of companies, any employees not within paragraph (b) or (c) who –
      - (i) are senior employees in the group, or
      - (ii) receive, or as a result of the package of benefits are likely to receive, the higher or highest levels of remuneration in the group.
  - (7) In subsection (6)(d) “group of companies” means a company and any other companies of which it has control.
  - (8) For the purposes of subsection (1) –
    - (a) a loan is “similar” if it is made for the same or similar purposes as the loan made to A, and
    - (b) a transaction is “similar” if it is of the same or a similar type to the transaction which P has with A.
  - (9) In this section references to A include references to any person linked with A.

#### **554H Exclusions: employment-related securities etc**

- (1) Chapter 2 does not apply by reason of –
  - (a) an acquisition of any employment-related securities if section 425(2) applies to the acquisition, or
  - (b) an acquisition of an employment-related securities option if section 475(1) applies to the acquisition.
- (2) Terms used in subsection (1) have the same meanings as they have in Chapter 2 or 5 of Part 7 (as the case may be).

- (3) Chapter 2 does not apply by reason of an event within subsection (4) if by virtue of the event an amount counts as employment income of A in respect of A's employment with B.
- (4) The events within this subsection are –
  - (a) a chargeable event for the purposes of section 426, 438 or 476,
  - (b) an event which gives rise to the discharge of a notional loan for the purposes of section 446U, or
  - (c) a disposal to which Chapter 3D of Part 7 applies.

#### **554I Interpretation**

- (1) This section applies for the purposes of this Part.
- (2) “A” and “B” are defined in section 554A(1)(a).
- (3) “Arrangement” includes any agreement, scheme, settlement, transaction, trust or understanding (whether or not it is legally enforceable).
- (4) “Relevant step” is defined in section 554A(2).
- (5) References to a relevant step which involves a sum of money are references to –
  - (a) a step within section 554B where P earmarks a sum of money,
  - (b) a step within section 554C(1)(a), or
  - (c) a step within section 554C(1)(d) where P makes available a sum of money for use as security.
- (6) References to the asset which is the subject of a relevant step are, in the case of a step within section 554C(1)(e), references to the lease granted.
- (7) For this purpose, the lease granted is to be treated as including any extensions of the lease, or any later lease, which by virtue of section 554C(6) or (7) is taken into account in determining the effective duration of the lease for the purposes of 554C(1)(e).
- (8) References to the payment of a sum of money include (in particular) references to the payment of a sum of money by way of a loan.
- (9) References to any person linked with A are references to –
  - (a) any person who is or has been connected with A,
  - (b) a close company in which A or a person within any other paragraph of this subsection is or has been a participator,
  - (c) a company in which A or a person within any other paragraph of this subsection is or has been a participator and which would be a close company if it were a UK resident company, or
  - (d) a company which is a 51% subsidiary of a company within paragraph (b) or (c).
- (10) In applying section 993 of ITA 2007 for the purposes of subsection (9) –
  - (a) a man and woman living together as if they were spouses of each other are treated as if they were spouses of each other, and

- (b) two people of the same sex living together as if they were civil partners of each other are treated as if they were civil partners of each other.
- (11) In subsection (9) “participator” –
- (a) in relation to a close company, means a person who is a participator in relation to the company for the purposes of section 455 of CTA 2010 (see sections 454 and 455(5) of that Act), and
  - (b) in relation to a company which would be a close company if it were a UK resident company, means a person who would be such a participator if the company were a close company.

## CHAPTER 2

### TREATMENT OF RELEVANT STEP FOR INCOME TAX PURPOSES

#### *Employment income*

#### **554J 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 554K) 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
  - (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) Nothing in Part 4 of this Act affects a liability to income tax by virtue of subsection (1).

#### **554K 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) But 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.

- (4) In subsection (2)(a) “market value” has the same meaning as it has for the purposes of TCGA 1992 by virtue of Part 8 of that Act.  
But see sections 437 and 452 of this Act.
- (5) In subsection (2)(b) the reference to the cost of the relevant step is to the expenses incurred in or in connection with the taking of 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.
- (6) The Commissioners for Her Majesty’s Revenue and Customs may by regulations provide for the value of a relevant step taken under a relevant non-UK scheme (within the meaning of paragraph 1(5) of Schedule 34 to FA 2004) as determined under subsection (1) or (2) to be reduced so far as provided for by the regulations.
- (7) Regulations under subsection (6) may have retrospective effect.
- (8) This section is subject to sections 554L, 554M, 554N and 554O which, so far as applicable, are to be applied in that order.
- (9) Regulations under subsection (6) may make provision about how those sections are to be applied where the value of a relevant step as determined under subsection (1) or (2) is reduced under the regulations.
- (10) This section is also subject to paragraph 55A of Schedule 36 to FA 2004.

#### **554L Residence issues**

- (1) After the value of the relevant step is determined under section 554K, 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 554J(1).

#### **554M 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 554L) 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 554L or this section, but
  - (b) before any reductions made to it under section 554N or 554O.
- (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.

#### **554N 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, “for” a tax year in which A is UK resident, or
  - (b) which are, in accordance with section 29, “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 554L or 554M) 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 is not “relevant”.

#### **554O Transfer of assets: consideration given before relevant step taken**

- (1) This section applies if –
  - (a) the relevant step is a step within section 554C(1)(b) and does not also involve a sum of money,

- (b) the transfer of the property in the asset is for consideration given by A in the form of the payment of a sum of money to P, and
  - (c) the payment is made before the relevant step is taken.
- (2) The value of the relevant step (after any reductions under sections 554L to 554N) is reduced (but not below nil) by the amount of the consideration given.
- (3) In subsection (1)(b) the reference to A includes a reference to any person linked with A.

*Remittance basis*

**554P Remittance basis: A is ordinarily UK resident**

- (1) Subsection (2) applies if –
  - (a) the value of the relevant step, or a part of it, is “for” a tax year (“the relevant tax year”) as determined under section 554L,
  - (b) section 809B, 809D or 809E of ITA 2007 (remittance basis) applies to A for the relevant tax year,
  - (c) A is ordinarily UK resident in the relevant tax year,
  - (d) A’s employment with B in the relevant tax year is employment with a foreign employer, and
  - (e) the duties of A’s employment with B in the relevant tax year are performed wholly outside the United Kingdom.
- (2) A’s employment income by virtue of section 554J(1), or the relevant part of it, is “taxable specific income” in a tax year so far as it is remitted to the United Kingdom in that year.
- (3) For this purpose, any income which is remitted before A’s employment with B starts is treated as being remitted in the tax year in which the employment starts.
- (4) Subsection (5) applies if in the relevant tax year –
  - (a) A has associated employments, and
  - (b) the duties of the associated employments are not performed wholly outside the United Kingdom.
- (5) The amount of A’s employment income to which subsection (2) applies is limited to such amount as is just and reasonable, having regard to –
  - (a) A’s employment income for the relevant tax year from all associated employments, together with A’s employment with B,
  - (b) the proportion of that income which is general earnings to which section 22 applies or is employment income to which section 41A applies,
  - (c) the nature of and time devoted to the duties performed outside the United Kingdom, and those performed in the United Kingdom, in the relevant tax year, and
  - (d) all other relevant circumstances,and, if the amount of A’s employment income to which subsection (2) would otherwise apply exceeds that limit, the amount of A’s

employment income to which that subsection applies is instead to be such amount as is just and reasonable.

- (6) In this section “associated employments” means employments with B or with employers associated with B; and section 24(5) and (6) applies for the purposes of this subsection.

#### **554Q Remittance basis: A is not ordinarily resident**

- (1) Subsection (2) applies if—
  - (a) the value of the relevant step, or a part of it—
    - (i) is “for” a tax year (“the relevant tax year”) as determined under section 554L, and
    - (ii) is not in respect of duties performed in the United Kingdom,
  - (b) section 809B, 809D or 809E of ITA 2007 (remittance basis) applies to A for the relevant tax year, and
  - (c) A is not ordinarily UK resident in the relevant tax year.
- (2) A’s employment income by virtue of section 554J(1), or the relevant part of it, is “taxable specific income” in a tax year so far as it is remitted to the United Kingdom in that year.
- (3) For this purpose, any income which is remitted before A’s employment with B starts is treated as being remitted in the tax year in which the employment starts.
- (4) The question of the extent to which the value of the relevant step, or any part of it, is not in respect of duties performed in the United Kingdom is to be determined on a just and reasonable basis.

#### **554R Remittance basis: supplementary**

- (1) Subsection (2) applies if section 554P(1)(a) or 554Q(1)(a) applies to a part (“the relevant part”) of the value of the relevant step.
- (2) Any reduction to the value of the relevant step to be made under any of sections 554M to 554O is to be made so that X% of the reduction is made by way of reducing the relevant part.
- (3) In subsection (2) “X%” means the proportion of the value of the relevant step represented by the relevant part before any reductions under any of sections 554M to 554O.
- (4) For the purpose of applying section 554P(2) or 554Q(2), see Chapter A1 of Part 14 of ITA 2007 for the meaning of “remitted to the United Kingdom” etc.
- (5) If the relevant step involves a sum of money, for the purposes of that Chapter the sum of money is treated as deriving from A’s employment income (or the relevant part of it) to which section 554P(2) or 554Q(2) applies.
- (6) In any other case, for the purposes of that Chapter the asset which is the subject of the relevant step is treated as deriving from A’s employment income (or the relevant part of it) to which section 554P(2) or 554Q(2) applies.
- (7) Subsection (8) applies if—

- (a) after the relevant step is taken, there is another relevant step (“the later relevant step”) by reason of which this Chapter applies in respect of A’s employment with B, and
  - (b) within the meaning of section 554M, there is overlap between the sum of money or asset (“sum or asset R”) which is the subject of the relevant step and the sum of money or asset (“sum or asset S”) which is the subject of the later relevant step.
- (8) Except so far as, in any event –
- (a) sum or asset S and sum or asset R are the same sum of money or asset, or
  - (b) sum or asset S derives from sum or asset R,
- for the purposes of Chapter A1 of Part 14 of ITA 2007 sum or asset S is treated, to the extent of the overlap, as deriving from sum or asset R.

#### *Supplementary*

#### **554S Subsequent income tax liability**

- (1) This section applies if –
- (a) after the relevant step is taken, another event (“the later event”) occurs,
  - (b) other than by virtue of this Chapter or Chapters 2 to 5 of Part 7, the later event would (apart from this section) give rise to a liability for income tax of A or any other person on an amount (“the later amount”), and
  - (c) it is just and reasonable for this section to apply in order to avoid a double charge to income tax in respect of the sum of money or asset which is the subject of the relevant step.
- (2) So far as it is just and reasonable in order to avoid a double charge to income tax as mentioned in subsection (1)(c), there is to be no liability to income tax on the later amount by virtue of the later event.

#### **554T Location of employment duties**

The following provisions apply for the purposes of this Chapter –

- (a) section 38 (but as if references to general earnings were to the value of the relevant step or a part of it),
- (b) section 39(1) and (2),
- (c) section 40 (but as if in subsections (3) and (4) references to section 24(1)(b) were to section 554P(4)(b)), and
- (d) section 41 (but as if references to general earnings were to the value of the relevant step or a part of it).”

#### *Other amendments to ITEPA 2003*

- 2 ITEPA 2003 is amended as follows.
- 3 In section 1(1)(a) (overview of contents of Act) for “7” substitute “7A”.
- 4 (1) Amend section 3 (structure of employment income Parts) as follows.

- (2) At the end of subsection (1) insert –  
“Part 7A deals with employment income through third parties.”
- (3) In subsection (2) for “7” substitute “7A”.
- 5 For the “or” after section 7(6)(b) (meaning of “specific employment income”) substitute –  
“(ba) Part 7A (employment income through third parties), or”.
- 6 (1) Amend section 10 (provision relating to “taxable specific income”) as follows.
- (2) In subsection (3) for “or 7” substitute “, 7 or 7A”.
- (3) After subsection (4) insert –  
“(5) Subsection (3) is also subject to sections 554P to 554R (employment income under Part 7A: remittance basis).”
- 7 (1) Amend section 13 (person liable for tax) as follows.
- (2) In subsection (3) for “or 7” substitute “, 7 or 7A”.
- (3) After subsection (4A) insert –  
“(4B) If –  
(a) the tax is on specific employment income under Chapter 2 of Part 7A, and  
(b) the relevant step is taken, or (if relevant) the income is remitted to the United Kingdom, after the death of A,  
A’s personal representatives are liable for the tax.  
(4C) Terms used in subsection (4B) have the same meaning as in Part 7A.”
- (4) In subsection (5) for “or (4A)” substitute “, (4A) or (4B)”.
- 8 After section 63(4) (the benefits code) insert –  
“(5) The benefits code has effect subject to section 554J(2).”
- 9 Under Step 1 in section 218(1) (exclusion of lower-paid employments from benefits code: calculation of earnings rate for tax year) –  
(a) omit the “and” after paragraphs (c) and (d), and  
(b) after paragraph (e) insert “, and  
(f) the total amount which counts as employment income in respect of the employment for the year under Chapter 2 of Part 7A.”
- 10 In section 222(1)(a) and (3) (payments treated as earnings: payments by employer on account of tax where deduction not possible) after “687,” insert “687A,”.
- 11 In section 227(3) (scope of exemptions to income tax under Part 4) after “all” insert “(subject to section 554J(3))”.
- 12 After section 228(2) (scope of exemptions to income tax under Part 4) insert –  
“(3) Subsections (1) and (2) are subject to section 554J(3).”

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- 13 (1) Amend section 394 (employer-financed retirement benefits: charge on benefit received) as follows.
- (2) After subsection (4) insert –
- “(4A) Subsection (4B) applies if the receipt of a benefit to which this Chapter applies gives rise to other relevant income.
- (4B) Subsection (1) or (2) (as the case may be) applies to the amount of the benefit only so far as that amount exceeds the other relevant income.
- (4C) In subsections (4A) and (4B) “other relevant income” means –
- (a) earnings within Chapter 1 of Part 3 which are charged to income tax, or
- (b) employment income under Chapter 2 of Part 7A.
- (4D) But anything which is exempt income is not “other relevant income”.”
- (3) In subsection (5) after “Act” insert “(apart from Chapter 1 of Part 3 or Chapter 2 of Part 7A)”.
- 14 In section 428(7) (restricted employment-related securities: amount of charge) –
- (a) omit the “and” after paragraph (d), and
- (b) after paragraph (e) insert “, and
- (f) any amount that has counted as employment income of the employee in respect of the employment under Chapter 2 of Part 7A in relation to the employment-related securities where the relevant step for the purposes of that Part was taken prior to the acquisition or was the step by virtue of which the acquisition occurred.”
- 15 In section 437(1)(a) (convertible employment-related securities: market value) after “option)” insert “or Chapter 2 of Part 7A (employment income through third parties)”.
- 16 After section 441(9) (convertible employment-related securities: amount of gain realised) insert –
- “(10) Subsection (11) applies for the purposes of subsection (2) or (3) if –
- (a) prior to the acquisition, the employment-related securities were the subject of a relevant step for the purposes 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.”

- 17 In section 446B(4) (employment-related securities with artificially depressed market value: charge on acquisition) –
- (a) omit the “or” after paragraph (d), and
  - (b) after paragraph (e) insert “, or
  - (f) Chapter 2 of Part 7A (employment income through third parties)”.
- 18 After section 446C(4) (employment-related securities with artificially depressed market value: amount of charge) insert –
- “(4A) Subsection (4B) applies if, prior to the acquisition, the employment-related securities were the subject of a relevant step for the purposes of Part 7A by reason of which Chapter 2 of that Part applied in respect of the employment.
- (4B) If what would be MV in accordance with subsection (3) or (4) (as the case may be) is less than the amount that counted as employment income of the employee in respect of the employment under Chapter 2 of Part 7A, MV is the amount of that employment income instead of the amount determined in accordance with subsection (3) or (4).”
- 19 After section 446S(3) (employment-related securities acquired for less than market value: notional loan) insert –
- “(4) This section is not affected by section 554J(2).”
- 20 In section 446T(3) (employment-related securities acquired for less than market value: amount of notional loan) –
- (a) omit the “and” after paragraph (d), and
  - (b) after paragraph (e) insert “, and
  - (f) any amount that has counted as employment income of the employee in respect of the employment under Chapter 2 of Part 7A in relation to the employment-related securities.”
- 21 In section 446V (employment-related securities acquired for less than market value: charges under Chapter 3C of Part 4 to be additional to other charges) –
- (a) omit the “or” after paragraph (d), and
  - (b) after paragraph (e) insert “, or
  - (f) Chapter 2 of Part 7A (employment income through third parties)”.
- 22 In section 452(2) (shares in research institution spin-out companies: market value on acquisition) –
- (a) omit the “and” after paragraph (c), and
  - (b) after paragraph (d) insert “, and
  - (e) determining any amount that counts as employment income of the employee in respect of the employment under Chapter 2 of Part 7A (employment income through third parties)”.
- 23 In section 480(5) (employment-related securities options: deductible amounts) –
- (a) omit the “and” after paragraph (b), and

- (b) after paragraph (c) insert “, and
- (d) any amount that has counted as employment income of the employee in respect of the employment under Chapter 2 of Part 7A in relation to the employment-related securities option.”

24 After section 687(4) (PAYE: payments by intermediary) insert –

- “(5) This section does not apply in relation to a payment so far as the sum paid is employment income under Chapter 2 of Part 7A.”

25 After section 687 insert –

**“687A Payment of employment income under Part 7A**

- (1) This section applies if –
  - (a) the value of a relevant step counts as employment income under Chapter 2 of Part 7A, and
  - (b) the relevant step is the payment of a sum of money, and references to A and B are to be read accordingly.
- (2) For the purposes of PAYE regulations B is treated as making a payment of PAYE income of A of an amount which, on the basis of the best estimate which can reasonably be made, is the amount of the employment income.
- (3) The payment is treated as made on the latest of the following days –
  - (a) the day on which the relevant step is taken,
  - (b) the day on which A’s employment with B starts, and
  - (c) the day which is 30 days after the day on which FA 2011 is passed.
- (4) Subsection (2) does not apply if the person who takes the relevant step (whether or not a person to whom PAYE regulations apply) deducts income tax from the payment, and accounts for it, in accordance with PAYE regulations.”

26 (1) Amend section 689 (PAYE: employee of non-UK employer) as follows.

(2) After subsection (1) insert –

- “(1A) Subject to subsection (4), subsection (1)(b) does not apply in relation to a payment so far as the sum paid is employment income under Chapter 2 of Part 7A.”

(3) In subsection (4) after “sections” insert “687A and”.

27 Before section 696 insert –

**“695A Employment income under Part 7A**

- (1) This section applies if –
  - (a) the value of a relevant step counts as employment income under Chapter 2 of Part 7A, and
  - (b) the relevant step is not the payment of a sum of money, and references to A and B are to be read accordingly.

- (2) For the purposes of PAYE regulations B is treated as making a payment of PAYE income of A of an amount which, on the basis of the best estimate which can reasonably be made, is –
- (a) the amount of the employment income, less
  - (b) so much of that amount (if any) to which section 554P(2) or 554Q(2) applies.
- (3) The payment is treated as made on the latest of the following days –
- (a) the day on which the relevant step is taken,
  - (b) the day on which A’s employment with B starts, and
  - (c) the day which is 30 days after the day on which FA 2011 is passed.
- (4) Subsection (2) does not apply if the person who takes the relevant step (whether or not a person to whom PAYE regulations apply) accounts for income tax on the relevant step in accordance with PAYE regulations.”
- 28 After section 696(2) (PAYE: readily convertible assets) insert –
- “(3) This section does not apply to any PAYE income so far as it is employment income under Chapter 2 of Part 7A.”
- 29 In section 710(2)(a) (PAYE: accounting for tax on notional payments) after “687,” insert “687A,”.
- 30 (1) Amend section 716A (priority rule in relation to certain dividend income) as follows.
- (2) Make the existing text subsection (1).
- (3) After subsection (1) insert –
- “(2) Subsection (1) is subject to section 554J(2).”

*Amendments to FA 2004*

- 31 FA 2004 is amended as follows.
- 32 After paragraph 3(6) of Schedule 34 (non-UK pension schemes) insert –
- “(7) The provision which may be made under sub-paragraph (6) includes (in particular) provision in consequence of Part 7A of ITEPA 2003.”
- 33 After paragraph 55 of Schedule 36 (pension schemes: transitional provisions) insert –
- “55A(1) This paragraph applies if –
- (a) Chapter 2 of Part 7A of ITEPA 2003 applies by reason of a relevant step within section 554C of that Act,
  - (b) the step is the provision of a lump sum under an employer-financed retirement benefits scheme within the meaning of Chapter 2 of Part 6 of that Act, and
  - (c) before 6 April 2006 an employer has paid any sum or sums, with a view to the provision of benefits under the scheme, in respect of which an employee is taxed.

- (2) Paragraph 53(3) applies for the purposes of sub-paragraph (1)(c) as it applies for the purposes of paragraph 53(1)(b).
- (3) There is to be a limit on the amount which counts as employment income under Chapter 2 of Part 7A of ITEPA 2003.
- (4) To determine this limit, apply paragraph 54 or 55 as if –
  - (a) references to section 394 of ITEPA 2003 were to Chapter 2 of Part 7A of ITEPA 2003,
  - (b) paragraph 54(3)(b) or 55(3) were omitted, and
  - (c) in paragraph 55(2) the reference to paragraph 53(1)(b) were to sub-paragraph (1)(c) of this paragraph.
- (5) The limit is the amount of the lump sum less any part of that lump sum to which Chapter 2 of Part 7A of ITEPA 2003 does not apply by virtue of paragraph 54 or 55 as applied under sub-paragraph (4) of this paragraph.
- (6) It is to be assumed in any case, unless the contrary is shown, that this paragraph does not apply.”

*Amendments to ITTOIA 2005*

- 34 ITTOIA 2005 is amended as follows.
- 35 (1) Amend section 39 (employee benefit contributions: meaning of “employee benefit scheme” etc) as follows.
- (2) In subsection (2) after “employer” insert “or persons linked with present or former employees of the employer”.
  - (3) After subsection (2) insert –
    - “(3) Section 554I(9) to (11) of ITEPA 2003 applies for the purposes of subsection (2) but as if references to A were to a present or former employee of the employer.
    - (4) So far as it is not covered by subsection (2), “employee benefit scheme” also means –
      - (a) an arrangement (“the relevant arrangement”) within subsection (1)(b) of section 554A of ITEPA 2003 to which subsection (1)(c) of that section applies, or
      - (b) any other arrangement connected (directly or indirectly) with the relevant arrangement.”
- 36 (1) Amend section 40 (employee benefit contributions: provision of qualifying benefits) as follows.
- (2) In subsection (5) after “scheme” insert “and the payment or transfer –
    - (a) gives rise to an employment income tax charge under Chapter 2 of Part 6 of ITEPA 2003 or under Part 9 of that Act, or
    - (b) is an excluded benefit as defined in section 393B(3) of that Act.”

- (3) After subsection (6) insert –
- “(6A) For the purposes of section 38 qualifying benefits are also provided if –
- (a) a relevant step for the purposes of Part 7A of ITEPA 2003 is taken, and
  - (b) Chapter 2 of that Part applies by reason of the step.”
- 37 (1) Amend section 41 (employee benefit contributions: timing of qualifying benefits etc) as follows.
- (2) For subsection (1) substitute –
- “(1) If the provision of a qualifying benefit takes the form of a payment of money which is not a chargeable relevant step, the benefit is provided for the purposes of section 38 when the money is treated as received for the purposes of Chapter 4 of Part 2 of ITEPA 2003 in accordance with section 18 of that Act, so far as section 18 is applicable to the payment.
- (1A) If the provision of a qualifying benefit is a chargeable relevant step, for the purposes of section 38 –
- (a) the benefit is provided when A’s employment with B starts if the chargeable relevant step is taken before then, or
  - (b) otherwise, the benefit is provided when the chargeable relevant step is taken.”
- (3) In subsection (2) after “benefit” insert “which is not a chargeable relevant step”.
- (4) After subsection (3) insert –
- “(4) If the provision of a qualifying benefit which is a chargeable relevant step does not involve a sum of money for the purposes of Part 7A of ITEPA 2003, the amount provided for the purposes of section 38 is the cost of the relevant step as defined in section 554K(5) of that Act.
- (5) But if the amount given by subsection (4) is more than the amount that is charged to tax under ITEPA 2003 in relation to the relevant step, the deduction allowable under section 38(2) or (3) is limited to that lower amount.
- (6) In this section –
- (a) “chargeable relevant step” means a relevant step for the purposes of Part 7A of ITEPA 2003 by reason of which Chapter 2 of that Part applies (whether or not it also gives rise to any liability for income tax by virtue of any other enactment), and
  - (b) in subsection (1A) the reference to A’s employment with B is to be read accordingly.”
- 38 In section 44(1) (employee benefit contributions: interpretation) –
- (a) in the definition of “employee benefit scheme” for “39(2)” substitute “39(2) to (4)”, and
  - (b) in the definition of “employer-financed retirement benefits scheme” after “Act)” insert “but ignoring section 393B(2)(a) and (c) of that Act”.

*Amendments to ITA 2007*

- 39 ITA 2007 is amended as follows.
- 40 After section 809F(5) (remittance basis: effect) insert –
- “(5A) For the effect on amounts which count as employment income under Chapter 2 of Part 7A of ITEPA 2003, see sections 554P to 554R of that Act.”
- 41 For section 809Z7(4) (remittance basis: meaning of “foreign specific employment income”) substitute –
- “(4) An individual’s “foreign specific employment income” for a tax year (“the relevant tax year”) consists of the income (if any) within subsections (4A) and (4B).
- (4A) The income within this subsection is the individual’s specific employment income for the relevant tax year so far as it consists of foreign securities income for the purposes of section 41A of ITEPA 2003.
- (4B) The income within this subsection is any income, or any part of any income, of the individual –
- (a) to which section 554P(2) or 554Q(2) of ITEPA 2003 applies, and
- (b) which consists of the value of a relevant step, or a part of the value of a relevant step, which is “for” the relevant tax year as determined under section 554L of ITEPA 2003.”

*Amendments to CTA 2009*

- 42 CTA 2009 is amended as follows.
- 43 (1) Amend section 1291 (employee benefit contributions: meaning of “employee benefit scheme” etc) as follows.
- (2) In subsection (2) after “employer” insert “or persons linked with present or former employees of the employer”.
- (3) After subsection (2) insert –
- “(3) Section 554I(9) to (11) of ITEPA 2003 applies for the purposes of subsection (2) but as if references to A were to a present or former employee of the employer.
- (4) So far as it is not covered by subsection (2), “employee benefit scheme” also means –
- (a) an arrangement (“the relevant arrangement”) within subsection (1)(b) of section 554A of ITEPA 2003 to which subsection (1)(c) of that section applies, or
- (b) any other arrangement connected (directly or indirectly) with the relevant arrangement.”
- 44 (1) Amend section 1292 (employee benefit contributions: provision of qualifying benefits) as follows.

- (2) In subsection (5) after “scheme” insert “and the payment or transfer –
- (a) gives rise to an employment income tax charge under Chapter 2 of Part 6 of ITEPA 2003 or under Part 9 of that Act, or
  - (b) is an excluded benefit as defined in section 393B(3) of that Act.”
- (3) After subsection (6) insert –
- “(6A) For the purposes of section 1290 qualifying benefits are also provided if –
- (a) a relevant step for the purposes of Part 7A of ITEPA 2003 is taken, and
  - (b) Chapter 2 of that Part applies by reason of the step.”
- 45 (1) Amend section 1293 (employee benefit contributions: timing of qualifying benefits etc) as follows.
- (2) For subsection (1) substitute –
- “(1) If the provision of a qualifying benefit takes the form of a payment of money which is not a chargeable relevant step, the benefit is provided for the purposes of section 1290 when the money is treated as received for the purposes of Chapter 4 of Part 2 of ITEPA 2003 in accordance with section 18 of that Act, so far as section 18 is applicable to the payment.
- (1A) If the provision of a qualifying benefit is a chargeable relevant step, for the purposes of section 1290 –
- (a) the benefit is provided when A’s employment with B starts if the chargeable relevant step is taken before then, or
  - (b) otherwise, the benefit is provided when the chargeable relevant step is taken.”
- (3) In subsection (2) after “benefit” insert “which is not a chargeable relevant step”.
- (4) After subsection (3) insert –
- “(4) If the provision of a qualifying benefit which is a chargeable relevant step does not involve a sum of money for the purposes of Part 7A of ITEPA 2003, the amount provided for the purposes of section 1290 is the cost of the relevant step as defined in section 554K(5) of that Act.
- (5) But if the amount given by subsection (4) is more than the amount that is charged to tax under ITEPA 2003 in relation to the relevant step, the deduction allowable under section 1290(2) or (3) is limited to that lower amount.
- (6) In this section –
- (a) “chargeable relevant step” means a relevant step for the purposes of Part 7A of ITEPA 2003 by reason of which Chapter 2 of that Part applies (whether or not it also gives rise to any liability for income tax by virtue of any other enactment), and
  - (b) in subsection (1A) the reference to A’s employment with B is to be read accordingly.”

- 46 In section 1296(1) (employee benefit contributions: interpretation) –
- (a) in the definition of “employee benefit scheme” for “1291(2)” substitute “1291(2) to (4)”, and
  - (b) in the definition of “employer-financed retirement benefits scheme” after “Act)” insert “but ignoring section 393B(2)(a) and (c) of that Act”.

#### *Commencement*

- 47 (1) Part 7A of ITEPA 2003 (as inserted by paragraph 1 of this Schedule) has effect in relation to relevant steps taken on or after 6 April 2011; and the other amendments made by this Schedule have effect accordingly.
- (2) Sub-paragraph (1) is subject to the following paragraphs.
- 48 (1) This paragraph applies if –
- (a) on or after 9 December 2010 but before 6 April 2011 a relevant step (“the early step”) within section 554C(1)(a) of ITEPA 2003 is taken,
  - (b) Chapter 2 of Part 7A of ITEPA 2003 would have applied by reason of the early step had the reference in paragraph 47(1) of this Schedule to 6 April 2011 been a reference to 9 December 2010, and
  - (c) the early step is not chargeable to income tax by virtue of Schedule 34 to FA 2004 in whole or in part.
- (2) Subject to what follows, Chapter 2 of Part 7A of ITEPA 2003 is to apply by reason of the early step; and the amendments made by this Schedule have effect accordingly.
- (3) In determining the tax year for which the employment income of A counts for the purposes of section 554J(1) of ITEPA 2003, the early step is treated as having been taken on 6 April 2012; but otherwise Chapter 2 of Part 7A of that Act applies by reference to when the early step was actually taken.
- (4) The amount which (apart from this sub-paragraph) would count as employment income of A is to be reduced by an amount to reflect so much of the sum paid as has been repaid to P before 6 April 2012 by the person to whom the payment was made; and any adjustments that need to be made to any assessment to tax may be made accordingly.
- (5) The amount of the reduction (if any) under sub-paragraph (4) –
- (a) is to be determined on a just and reasonable basis, and
  - (b) may be the full amount of the employment income or nil or an amount in between (depending on the circumstances).
- (6) Section 554M of ITEPA 2003 does not apply in relation to the early step and, in the application of that section in relation to any other relevant step (whenever taken), the early step is to be ignored.
- (7) For the purposes of section 687A(3)(a) of ITEPA 2003 (as inserted by paragraph 25 of this Schedule), the early step is treated as having been taken on 6 April 2012.
- 49 (1) This paragraph applies if –
- (a) on or after 9 December 2010 but before 6 April 2011 a relevant step (“the early step”) within section 554C(1)(d) of ITEPA 2003 is taken,
  - (b) the relevant step does not involve a sum of money within the meaning of section 554I(5) of ITEPA 2003,

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- (c) the asset which is the subject of the early step is a readily convertible asset which P makes available to secure the payment of a sum of money,
  - (d) ignoring section 554A(4) of ITEPA 2003, Chapter 2 of Part 7A of ITEPA 2003 would have applied by reason of the early step had the reference in paragraph 47(1) of this Schedule to 6 April 2011 been a reference to 9 December 2010, and
  - (e) the early step is not chargeable to income tax by virtue of Schedule 34 to FA 2004 in whole or in part.
- (2) “Readily convertible asset” means anything mentioned in section 702(1)(a) to (c) of ITEPA 2003 (ignoring section 702(3)).
- (3) Subject to what follows, Chapter 2 of Part 7A of ITEPA 2003 is to apply by reason of the early step; and the amendments made by this Schedule have effect accordingly.
- (4) In determining the tax year for which the employment income of A counts for the purposes of section 554J(1) of ITEPA 2003, the early step is treated as having been taken on 6 April 2012; but otherwise Chapter 2 of Part 7A of that Act applies by reference to when the early step was actually taken.
- (5) The amount which (apart from this sub-paragraph) would count as employment income of A is to be reduced to nil if –
- (a) before 6 April 2012 the readily convertible asset has been returned to P, and
  - (b) as at that date the asset is not being used to secure the payment of the sum of money (or any part of it),
- and any adjustments that need to be made to any assessment to tax may be made accordingly.
- (6) Section 554M of ITEPA 2003 does not apply in relation to the early step and, in the application of that section in relation to any other relevant step (whenever taken), the early step is to be ignored.
- (7) The early step is to be ignored in the application of 554A(4) of ITEPA 2003 in relation to any other relevant step (whenever taken).
- (8) For the purposes of section 695A(3)(a) of ITEPA 2003 (as inserted by paragraph 27 of this Schedule), the early step is treated as having been taken on 6 April 2012.
- 50 The amendments made by paragraph 13 of this Schedule, so far as relating to Chapter 1 of Part 3 of ITEPA 2003, have effect in relation to benefits to which Chapter 2 of Part 6 of that Act applies received on or after 6 April 2011.
- 51 Paragraphs 34 to 38 of this Schedule come into force on 6 April 2011.
- 52 Paragraphs 42 to 46 of this Schedule come into force on 6 April 2011.

**DRAFT EXPLANATORY NOTE**

**EMPLOYMENT INCOME THROUGH THIRD PARTIES**

**SUMMARY**

1. This clause and Schedule insert a new Part 7A into the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) and make necessary amendments to legislation as a result of that insertion. The Schedule introduces rules that will apply in certain circumstances where employees and their employers enter into arrangements which result in a payment of money or the provision of an asset by a third party rather than the employer. The new rules create a tax charge which will apply to certain loans of money or assets by third parties to the employee; the earmarking of money or assets for the employee by a third party; and to the outright payments of money or transfers of assets to the employee by a third party where these are not otherwise charged to tax as earnings from the employment.
2. The Schedule also includes anti-forestalling rules which will mean that certain events occurring on or after 9 December 2010 (the date on which the Schedule was published in draft form) but before 6 April 2011 will fall to be taxed on 6 April 2012 under the new rules. These rules are explained in paragraphs (94 to 107) below.

**DETAILS OF THE SCHEDULE**

3. Paragraph 1 inserts new Part 7A into ITEPA.

**CHAPTER 1 – APPLICATION ETC**

4. New section 554A sets out the circumstances in which chapter 2 of Part 7A applies. It introduces the concept of “relevant steps” (taken in pursuance of, or connected to, “relevant arrangements”) which, under chapter 2, will count as employment income of the employee, or prospective or former employee (“A”). References to the “employee” throughout the rest of this Explanatory Note include references to a prospective or former employee unless otherwise stated.
5. New section 554A(1)(b) defines “relevant arrangement” and new section 554A(1)(c) applies a condition that, in so far as the arrangement relates to A, it must be reasonable to suppose that, in essence, the arrangement is (wholly or partly) a means of providing rewards or recognition, or loans, in connection with A’s employment with the employer. Under new section 554A(6), it does not matter if

at the time it is made the arrangement does not include certain details, such as the sum of money to be provided.

6. New section 554A(1)(d) requires that for a tax charge under chapter 2 of new Part 7A to apply, a relevant step must be taken by a “relevant third person” as defined in new section 554A(7) and (8). Relevant steps are defined in new section 554A(2) as steps taken under new sections 554B, 554C and 554D.
7. New section 554A(1)(e) contains a requirement that it must be reasonable to suppose that in essence either the “relevant step” is taken (wholly or partly) in pursuance of the relevant arrangement or that it and the relevant arrangement are connected in some other way either directly or indirectly. New section 554A(9) sets out further details on when such a connection exists. New section 554A(10) provides that in getting to the essence of the matter for the purposes of determining if the conditions in new sections 554A(1)(c) and 554A(1)(e) in particular are met, all relevant circumstances must be taken into account.
8. New section 554A(4) sets out an exclusion from the charge under chapter 2 of Part 7A, which will apply in cases where an asset is provided to an employee under relevant arrangements but exactly the same asset has previously been the subject of a charge under that chapter (for example, at the point at which it was earmarked) in respect of A’s employment with the employer.
9. New section 554A(5) provides that references to A in new sections 554A(1)(b) and 554A(1)(c)(ii) include references to any person linked with A.
10. New section 554B provides that a relevant step occurs when a relevant third person (“P”) (as defined in new section 554A(7)) earmarks a sum of money or asset held by or on behalf of P, however informally, with a view to a later relevant step being taken in relation to that sum or asset or a sum or asset arising or deriving from it, by P or any other person, conditionally or otherwise.
11. New section 554B(2) provides that for the purposes of new section 554B(1) it does not matter whether the details of the later relevant step have been worked out, or whether the employee (“A”) or a person linked with A has a legal right to have a relevant step taken in connection with the sum or asset (or a sum or asset arising or deriving from it).
12. New section 554C(1) provides that a relevant third person (as defined in new section 554A(7)) (“P”) takes a relevant step if P pays a sum of money; transfers an asset; or grants a lease which is likely to have an effective duration exceeding 21 years to a relevant person in each

case. New section 554C(2) defines “relevant person” and new section 554C(3) provides that references to the employee (“A”) in that definition include references to any person linked with A.

13. P also takes a relevant step under new section 554C(1) if P takes a step whereby a relevant person acquires an asset in securities, securities options or an interest in securities or makes available a sum of money or asset for use as security to obtain a loan to a relevant person or otherwise to secure the meeting of any liability or the performance of any undertaking in respect of a relevant person. Under new section 554C(5), it does not matter whether this is done in an informal way or if the relevant person has a legal right to use the sum of money or asset as security or actually does so.
14. New section 554C(6) to (8) set out conditions for determining the effective duration of a lease for the purposes of new section 554C(1).
15. New section 554D provides that a relevant third person (as defined in new section 554A(7)) takes a relevant step if that person (“P”) makes available an asset to a relevant person in the circumstances set out in new section 554D(1) or (2). “Relevant person” is defined in new section 554D(5) and (6).
16. New section 554D(1)(a) applies if the asset is made available (as defined in new section 554D(3)) for a relevant person to benefit from in a way which is substantially similar to that which would be the case were the asset transferred. If new section 554D(1)(a) does not apply new section 554D(1)(b) applies where an asset is made available to a relevant person to benefit from at or after the end of the period of two years starting on the day the employee’s employment with their employer ceases. New section 554D(2) provides that where an asset is made available before the end of that period and P continues to make it available after the end of that period, a relevant step is taken at the end of that period.
17. New section 554E provides that chapter 2 does not apply by reason of a relevant step under tax-advantaged employee share schemes under chapters 6, 7, 8 and 9 of Part 7 of ITEPA, under registered pension schemes or under arrangements for the provision of excluded benefits as defined by section 393B(3) of ITEPA.
18. New section 554E(3) provides a power for further provision disapplying chapter 2 to be made in regulations in relation to relevant steps taken under a relevant non-UK pension scheme. New section 554E(4) provides that any regulations made under this power may have retrospective effect.

19. New section 554F provides an exclusion from a charge under new Part 7A where the relevant step is an ordinary commercial transaction.
20. New section 554F(1) provides that Chapter 2 does not apply by reason of a relevant step which is a payment of a sum of money by way of a loan if the loan is a loan on ordinary commercial terms, as defined in section 176(2) and (3) of ITEPA and the loan is not connected with an arrangement which has a tax avoidance purpose. New section 554F(3) and (4) defines when an arrangement has a tax avoidance purpose.
21. New section 554F(2) provides that Chapter 2 does not apply by reason of any other relevant step if the person taking the step does so in the course of a normal commercial transaction with the employee (“A”) which meets the conditions in new section 544F(2)(a) to (d). New section 554F(7) provides that references to A in the section include references to any person linked with A.
22. New section 554G provides that Chapter 2 does not apply by reason of a relevant step if the step taken is a transaction with the employee (“A”) under certain employee benefits packages, described in new section 554G(1)(a) to (f) and is not connected with an arrangement which has a tax avoidance purpose. New section 554G(3) and (4) defines when an arrangement has a tax avoidance purpose and new section 554G(9) provides that references to an employee (“A”) in the section include references to any person linked with A.
23. The exclusion in new section 554G does not apply if, under new section 554G(1)(h), (5) and (6), a package of employee benefits will be wholly or mainly conferred on directors or senior employees in receipt of higher levels or the highest levels of remuneration, and where the employer is part of a group, senior employees or those receiving the highest levels of remuneration in the group.
24. New section 554H provides that Chapter 2 does not apply to employment-related securities in some circumstances.
25. New section 554H(1) provides that Chapter 2 does not apply to an acquisition of employment-related securities if that acquisition falls within section 425(2) of ITEPA, nor to an acquisition of employment-related securities options which falls within section 475(1) of that Act.
26. New section 554H(2) provides that terms used in new section 554H(1) have the same meanings as in Chapter 2 or 5 of Part 7 of ITEPA.

27. New sections 554H(3) and (4) provide that Chapter 2 does not apply on the occurrence of certain events to which provisions in Part 7 of ITEPA apply. Those events take place when an amount counts as employment income under sections 426, 438 or 476, or by virtue of discharge of a notional loan for the purposes of section 446U or a disposal to which Chapter 3D of Part 7 applies.
28. New section 554I contains definitions for the purposes of Part 7A.
29. New section 554I(5) relates to references to “a relevant step which involves a sum of money” and new sections 554I(6) and (7) qualify references to “the asset which is the subject of a relevant step” where the relevant step is the granting of a lease.
30. New section 554I(8) provides that references to “the payment of sum of money” include references to the payment of a sum of money by way of a loan.
31. New section 554I(9) to (11) defines who is a person linked to the employee.

## **CHAPTER 2 – TREATMENT OF RELEVANT STEP FOR INCOME TAX PURPOSES**

### *Employment income*

32. New section 554J provides for the value of a relevant step under new sections 554B to 554D to count as employment income of the employee (“A”). New section 554J(1)(a) provides that the relevant step counts as employment income for the tax year in which A’s employment starts if the relevant step is taken before that time. New section 554J(1)(b) provides that in all other cases the relevant step counts as employment income for the tax year in which the relevant step is taken.
33. New section 554J(2) provides for a priority rule where a relevant step otherwise gives rise to an amount which is treated as earnings under the benefits code, or any income from UK dividends to which Chapter 3 of Part 4 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA) applies. In both cases new section 554J(1) applies instead of the provision in the benefits code or Chapter 3 of Part 4 of ITTOIA.
34. New section 554J(3) provides that none of the employment income exemptions in Part 4 of ITEPA affects a liability to income tax by virtue of new section 554J(1).
35. New section 554K determines the value of a relevant step under new sections 554B to 554D, which, by virtue of new section 554K(8), are

subject to the rules in new sections 554L to 554O, which apply in that order.

36. New section 554K(1) provides that the value of a relevant step is the amount of the sum if the relevant step involves a sum of money.
37. New section 554K(2) provides that in any other case the value of a relevant step is the market value of the asset which is the subject of the relevant step at the time when the relevant step is taken, or if higher, the cost of the relevant step.
38. But new section 554K(2)(b) is ignored by virtue of new section 554K(3) if the relevant step is within new section 554C(1)(c) (which relates to securities) and any of Chapters 2 to 4A of Part 7 apply by virtue of the acquisition which is the subject of the relevant step.
39. New section 554K(4) defines “market value” for the purposes of new section 554K(2)(a), subject to rules applying in the case of certain employment-related securities at sections 437 and 452 of ITEPA.
40. New section 554K(5) qualifies the reference to “the cost of the relevant step” in new section 554K(2)(b).
41. New section 554K(6) provides that where a relevant step includes a step under a relevant non-UK pension scheme, regulations may provide for the value of the relevant step to be reduced. New section 554K(7) provides that such regulations may have retrospective effect and new section 554K(9) provides a power for regulations to make further provision about how new sections 554L to 554O apply where the value of a relevant step is so reduced.
42. New section 554L deals with residence issues. Once the value of a relevant step has been determined, it requires that the tax year or years that value is “for” is determined. For the purposes of new section 554L(1), new section 554L(2) applies the rules in sections 16(1) to (4) and 17(1) to (3) of ITEPA to determine the year the relevant step is for as though the value of the relevant step was general earnings covered by sections 16(1) to (4) and 17(1) to (3) of ITEPA.
43. In a case where the value of a relevant step, or part of it, is “for” a tax year in which A is non-resident, new section 554L(3) applies new section 554L(4) so that the part of value of a relevant step derived from duties performed outside the UK is to be deducted from the value of a relevant step, and for that deduction to be determined on a just and reasonable basis under new section 554L(5).

44. New section 554L(6) provides that the tax year for which the value of the relevant step counts as employment income under new section 554J is not affected by this section.
45. New section 554M provides for the value of a relevant step to be reduced by the value of an earlier relevant step if there is an overlap between the sum of money or asset which is the subject of the relevant steps, each of which relate to the employee's employment with the employer ("B"). By virtue of new section 554M(4) there is an overlap for the purposes of this section if the sum of money subject to the relevant steps is the same sum of money or asset, or if the sum or asset subject to a relevant step defined as ("sum or asset P") in new section 554M(1)(a) essentially replaces the sum or asset of an earlier relevant step (defined as "sum or asset Q") in new section 554M(1)(b).
46. If there is an overlap which covers the whole of sum or asset Q, new section 554M(2)(a) provides for the value of the relevant step (after taking into account of any reductions under new section 554L) to be reduced by the value of the earlier relevant step. But if the overlap covers only part of sum or asset Q, new section 554M(2)(b) provides that the value of the relevant step (after taking into account of any reductions under new section 554L) is reduced by the part of the value of the earlier relevant step which corresponds to the part of sum or asset Q which overlaps sum or asset P, as determined on a just and reasonable basis.
47. New section 554M(3) applies a priority order so that references to the value of the earlier relevant step in new section 554M(2) mean the value after taking account of any reductions under new section 554L but before taking account of any reductions under new sections 554N or 554O.
48. New section 554M(5) makes provisions for cases where there has already been overlap between earlier relevant steps.
49. New section 554N provides for priority to be given over a new Part 7A charge to certain ITEPA charging provisions which also apply to a relevant step. New section 554N(2) provides that the value of a relevant step after taking account of any reductions under new sections 554L or 554M is to be reduced by the value of earnings subject to those charging provisions, but not below nil.
50. New section 554O provides for the value of a relevant step within new section 554C(1)(b) (which relates to the transfer of assets), which does not involve a sum of money, to be reduced (but not below nil) by an amount of consideration in the form of money paid by the employee or any person linked to the employee to the person taking

the relevant step in return for the asset which is subject to the relevant step, so long as the payment is made before the relevant step is taken.

*Remittance basis*

51. New section 554P provides for the application of the remittance basis at sections 809B, 809D, or 809E of the Income Tax Act 2007 (ITA) to the value of a relevant step determined under new section 554L if the employee (“A”) is ordinarily resident in the UK in the relevant tax year and A’s employment with the employer (“B”) is with a foreign employer and the duties of that employment are performed wholly outside the UK.
52. New section 554P(1) sets out the conditions for new section 554P(2) to apply and new section 554P(1)(a) defines “the relevant tax year” for that purpose as the tax year which the relevant step, or part of it, is “for” as determined under new section 554L.
53. New section 554P(2) provides that A’s employment income by virtue of new section 554J, or the relevant part of it, is “taxable specific employment income” in a tax year if it is remitted to the UK in that year, and for this purpose new section 554P(3) provides that any income which is remitted before the start of A’s employment with B is treated as being remitted in the tax year in which the employment starts.
54. New sections 554P(4) and (5) limit the amount of employment income to which new section 554P(2) applies where A has associated employments for which the duties are not performed wholly outside the UK to such an amount that is just and reasonable having regard to the factors listed in new sections 554P(5)(a) to (5)(d). New section 554P(6) defines “associated employments” for this purpose.
55. New section 554Q provides for the application of the remittance basis at sections 809B, 809D, or 809E of ITA to the value of a relevant step determined under new section 554L if the employee (“A”) is not ordinarily resident in the UK and the value of the relevant step, or a part of it, is not in respect of duties performed in the UK (to be determined on a just and reasonable basis by virtue of new section 554Q(4)).
56. New section 554Q(1) sets out the conditions for new section 554Q(2) to apply and new section 554Q(1)(a)(i) defines “the relevant tax year” for the purposes of the section as the tax year which the relevant step, or part of it, is “for” as determined under new section 554L.
57. New section 554Q(2) provides that A’s employment income under section 554J, or the relevant part of it, is “taxable specific

employment income” in a tax year if it is remitted to the UK in that year, and for this purpose new section 554Q(3) provides that any income which is remitted before the start of A’s employment with B is treated as being remitted in the tax year in which the employment starts.

58. New section 554R makes supplementary provision to the remittance basis provisions in new sections 554P and 554Q.
59. In particular, new section 554R(1) applies new section 554R(2) where new sections 554P(1)(a) and 554Q(1)(a) apply to only part of the value of a relevant step\_(defined in here as “the relevant part”). New section 554R(2) provides for a corresponding proportionate reduction of the relevant part where the value of the relevant step is reduced under new sections 554M to 554O. New section 554R(5) to (8) make further provision about the application of the remittance basis provisions in ITA in cases where Part 7A of ITEPA applies.

*Supplementary*

60. New section 554S prevents the possibility of a double tax charge where an event takes place after a relevant step and the later event would give rise to an income tax liability (other than under Chapter 2 of new Part 7A or Chapters 2 to 5 of Part 7) of the employee (“A”) or any other person and it is just and reasonable for new section 554S to apply in order to prevent such a double tax charge.
61. New section 554T applies provisions relevant to the location of employment duties in sections 38, 39(1) and (2), 40 and 41 of ITEPA with modifications to sections 38, 40 and 41.
62. Paragraphs 2 to 46 of the Schedule make other amendments to legislation required to give full effect to the provisions of Part 7A.
63. Paragraphs 2 to 30 are concerned with ITEPA.
64. Paragraphs 3 to 7 make consequential amendments to sections 1, 3, 7, 10 and 13 to reflect the insertion of new Part 7A into the Act, including, to bring amounts chargeable under new Part 7A within the definition of “employment income” and “taxable specific income”.
65. Paragraph 8 amends section 63 to reflect the fact that a tax charge under new Part 7A applies instead of a charge under the benefits code (by virtue of new section 554J) in cases where a charge under both would accrue.
66. Paragraph 9 amends section 218. Section 218 is in chapter 11 of Part 3 of ITEPA, which provides that the certain tax charges under the benefits code do not apply in relation to lower-paid employments

if certain conditions are met. Section 217 defines “lower-paid employment” and is reliant on section 218, under which the earnings rate for an employment is calculated. The amendment made by paragraph 9 provides that amounts which count as employment income for a year under new Part 7A are to be taken account of in determining the earnings rate for the employment.

67. Paragraph 10 amends section 222 to reflect amendments made by paragraphs 24 to 29.
68. Paragraphs 11 and 12 amend sections 227 and 228 respectively to add references to section 554J(3) (which provides that the exemptions in Part 4 do not apply in relation to new Part 7A).
69. Paragraph 13 amends section 394, which establishes the tax charge on relevant benefits provided under an employer-financed retirement benefits scheme, to provide that such a charge arises only to the extent that the benefit exceeds employment income which has been charged to tax under Part 7A. In addition, the amendment makes the same provision for cases where employment income the benefit relates to has been charged to tax under chapter 1 of Part 3 and amends subsection (5) to make clear that a tax charge can arise under both chapter 1 of Part 3 and new Part 7A in relation to a relevant benefit.
70. Paragraph 14 inserts a new paragraph (f) into section 428(7) providing that for the purposes of section 426 an amount that has counted as employment income of the employee under Chapter 2 of new Part 7A in relation to employment-related securities is a deductible amount, provided that it arose as the result of a relevant step prior to acquisition or was the step giving rise to the acquisition..
71. Paragraph 15 inserts new wording into section 437(1)(a) to add Chapter 2 of new Part 7A to the list of purposes for which the value of employment-related convertible securities is to be determined as if they were not convertible securities.
72. Paragraph 16 inserts new subsections (10) and (11) into section 441(9). New section 441(10) provides that new section 441(11) applies where prior to their acquisition, employment-related securities were the subject of a relevant step for the purposes of new Part 7A by reason of which Chapter 2 of that Part applied, and where the amount mentioned in paragraph 11(a) is higher than the amount mentioned in paragraph 11(b). New section 441(11) allows a deduction from the gain calculated under section 441 equal to the difference between the amount that counted as employment income of the employee in respect of the employment under Chapter 2 of new Part 7A, and the market value of the employment-related securities without conversion rights, at the time of the relevant step. New

section 441(11) also applies that the gain shall not be reduced below nil.

73. Paragraph 17 inserts a new paragraph (f) into section 446B(4). That subsection adds Chapter 2 of new Part 7A to the list of tax liabilities which is not affected by section 446B.
74. Paragraph 18 inserts new subsections (4A) and (4B) into section 446C. New section 446C(4A) provides that new section 446C(4B) will apply if the employment-related securities were the subject of a relevant step before acquisition, and Chapter 2 applied by reason of that step. New section 446C(4B) provides that if what would be the market value in accordance with subsection (3) or (4) of section 446C is lower than the amount that counted as employment income of the employee under Chapter 2 of new Part 7A, then market value should be used as the latter amount for section 446C.
75. Paragraph 19 inserts a new subsection (4) into section 446S(3), providing that that section is not affected by new section 554(2).
76. Paragraph 20 inserts a new paragraph (f) into section 446T(3). That subsection provides that an amount that has counted as employment income of the employee under Chapter 2 of new Part 7A in relation to employment-related securities is a deductible amount in calculating the notional loan for the purposes of that section.
77. Paragraph 21 inserts a new subsection (f) into section 446V. That subsection adds Chapter 2 of new Part 7A to the list of tax liabilities which is not affected by a charge calculated under Chapter 3C.
78. Paragraph 22 inserts a new subsection (e) into section 452(2). That subsection adds determining any amount that counts as employment income under Chapter 2 of new Part 7A to the list of relevant tax purposes for which the market value of the shares is to be calculated disregarding the effect on that market value of the intellectual property agreement.
79. Paragraph 23 inserts a new subsection (d) into section 480(5). That subsection provides that an amount that has counted as employment income of the employee under Chapter 2 of Part 7A in relation to the employment-related securities option is a deductible amount for the purposes of section 478.
80. Paragraph 24 inserts a new subsection (5) into section 687. New section 687(5) provides that the section does not apply to a payment which is employment income under Chapter 2 of new Part 7A.

81. Paragraph 25 inserts new section 687A. New section 687A is in Part 11, which deals with the operation of PAYE, and provides that where the subject of a relevant step which counts as employment income under new Part 7A is a sum of money, the employer of the employee is treated as making a payment of PAYE income for the purposes of the PAYE Regulations. As a result the employer is therefore responsible for operating PAYE rather than the third party who took the relevant step. This will not apply, however, where the third party does in fact operate PAYE (new section 687A(4)). New section 687A(3) contains rules on when a payment is treated as made under new Part 7A for the purposes of PAYE and provides in particular that where a relevant step is taken in relation to a prospective employee, the payment is to be treated as made on the first day of the employee's employment.
82. Paragraph 26 amends section 689, which makes provision for the operation of PAYE where an employee of a non-UK employer works for another person in the UK ("the relevant person") but is paid by someone other than the relevant person, such as their employer or an intermediary of their employer, and that person is not under an obligation to operate PAYE. In these cases, the obligation to operate PAYE falls on the relevant person. Paragraph 26 amends section 689 so that it applies to payments chargeable to tax under new Part 7A.
83. Paragraph 27 inserts new section 695A. This deals with the value and timing for PAYE purposes of relevant steps that are not the payment of a sum of money and, similarly to new section 687A, requires the employer to operate PAYE unless the third party who took the relevant step does so.
84. Paragraph 28 amends section 696, which deals with the operation of PAYE where PAYE income is in the form of a readily convertible asset, to provide that the section does not apply where the readily convertible asset is the subject of a relevant step (in which case new section 695A applies).
85. Paragraph 29 amends section 710, which provides that certain payments dealt with by Part 11 are "notional payments". Section 710 requires employers to deduct PAYE in respect of notional payments from any payments that the employer actually makes. If the employer does not make actual payments which are sufficiently large to deduct PAYE from, the employer must account to HM Revenue & Customs for the tax which they are required, but unable, to deduct. Paragraph 29 adds payments dealt with by new section 687A to the list of payments which are notional payments. The amendment made by paragraph 10 is consequential to this. Section 222 provides that any amount accounted for by an employer under section 710 is to be treated as earnings from the employee's employment for the purposes of income tax unless the employee makes good to the employer the

amount accounted for. Paragraph 10 amends section 222 to reflect the addition of payments dealt with by section 687A to the list of notional payments.

86. Paragraph 30 amends section 716A to add a reference to new section 554J(2) (which provides that Part 7A applies instead of chapter 3 of Part 4 of ITTOIA in cases where a tax charge would accrue under both provisions).

*Amendments to the Finance Act (FA) 2004*

87. Paragraph 32 amends Schedule 34 to FA 2004 to extend the powers already contained there for the Commissioners for Her Majesty's Revenue and Customs to make regulations about whether certain payments by non-UK pension schemes are referable to a scheme member's UK tax-relieved fund for the purposes of determining the application of UK tax rules to the scheme. The amendment will allow such regulations to make provision in consequence of new Part 7A of ITEPA.
88. Paragraphs 52 to 55 of Schedule 36 contain transitional provisions which deal with the replacement of non-approved retirement benefits schemes with employer financed retirement benefits schemes by FA 2004. Paragraph 33 inserts paragraph 55A into Schedule 36, which deals with the interaction between new Part 7A of ITEPA and those transitional provisions.

*Amendments to ITTOIA*

89. Paragraphs 34 to 38 are concerned with chapter 4 of Part 2 of ITTOIA, which contains rules restricting deductions from trade profits for the purposes of income tax. Sections 38 to 44 deal with employee benefit contributions. Paragraphs 34 to 38 amend those rules to deal with the interactions with new Part 7A of ITEPA. In particular, paragraph 35 inserts new section 39(4) to provide that a relevant arrangement (or an arrangement connected to a relevant arrangement) under new Part 7A of ITEPA is an employee benefit scheme for the purposes of determining whether something is an employee benefit contribution; and paragraph 36(3) inserts new section 40(6A) to provide that qualifying benefits are provided by an employee benefit scheme if a relevant step giving rise to a tax charge under chapter 2 of new Part 7A of ITEPA is taken.
90. Paragraph 36(2) makes an additional amendment to section 40(5) to make clear that a payment or transfer under an employer-financed retirement benefits scheme only amounts to the provision of qualifying benefits if the payment or transfer gives rise to a tax charge under chapter 2 of Part 6, or Part 9, of ITEPA, or is an excluded benefit under section 393B(3) of that Act.

*Amendments to ITA*

91. Paragraphs 39 to 41 are consequential on sections 554P to 554R. They make amendments to chapter A1 of Part 14 of ITA, which provides for the remittance basis of the charge to income tax, to add necessary cross references to new Part 7A of ITEPA.

*Amendments to the Corporation Tax Act (CTA) 2009*

92. Paragraphs 42 to 46 are concerned with chapter 1 of Part 20 of CTA 2009, which contains rules restricting deductions from income for the purposes of corporation tax. The amendments are equivalent to those made to ITTOIA by paragraphs 34 to 38 in relation to deductions from trade profits for income tax purposes.

*Commencement*

93. Paragraph 47 provides that new Part 7A of ITEPA (as inserted by paragraph 1) has effect in relation to relevant steps which are taken on or after 6 April 2011; and the other amendments made by the Schedule have effect accordingly. Paragraph 47(2) makes paragraph 47(1) subject to paragraphs 48 and 49.
94. Paragraphs 48 and 49 contain anti-forestalling provisions which apply to certain relevant steps (“early steps”) which occur on or after 9 December 2010 but before 6 April 2011
95. Paragraph 48 applies if a relevant step within new section 554C(1)(a) (which relates to the payment of sums of money) is taken on or after 9 December 2010 but before 6 April 2011 and which would have been subject to the provisions in Chapter 2 of new Part 7A of ITEPA had the reference to 6 April 2011 in paragraph 47 been a reference to 9 December 2010, and the early step is not chargeable to tax by virtue of Schedule 34 to FA 2004 (in whole or in part). The term “early step” is defined in paragraph 48(1)(b).
96. Paragraph 48(2) applies Chapter 2 of new Part 7A of ITEPA by reason of the early step and provides that the amendments made by the Schedule have effect accordingly.
97. Paragraph 48(3) provides for the early step to be treated as having been taken on 6 April 2012 in determining the tax year for which the relevant step counts as employment income of the employee (“A”) for the purposes of new section 554J(1) of ITEPA. Paragraph 48(7) contains equivalent provision for the purposes of PAYE. Paragraph 48(3) also provides that for all other purposes, the early step is treated as taken when it is actually taken.

98. Paragraph 48(4) provides for the amount counting as employment income of A by virtue of paragraph 48 to be reduced by any amount of the sum (which is the subject of the early step) that is repaid to the person taking the step (“P”) by the person to whom the payment was made. The effect of paragraph 48(4) is such that a tax charge will not arise under Chapter 2 of new Part 7A of ITEPA in relation to an early step if the sum which is the subject of the early step is repaid in full before 6 April 2012 by the person to whom the sum was paid. Paragraph 48(4) also provides for the making of any adjustments that need to be made to any assessment to tax as a consequence of a repayment before 6 April 2012 resulting in a reduction in the amount that counts as employment income in respect of an early step.
99. Paragraph 48(5) makes further provision for the amount of any reduction under paragraph 48(4).
100. Paragraph 48(6) provides that that the overlap provisions in new section 554M of ITEPA do not apply in relation to the early step and that in applying that section to any other relevant step (whenever taken) the early step is to be ignored.
101. Paragraph 49(1) provides that paragraph 49 applies where the subject of the early step is a readily convertible asset which is made available on or after 9 December 2010 but before 6 April 2011 to be used to secure a payment of a sum of money. Further requirements for the application of paragraph 49(1) are set out in paragraph 49(1)(d) and (e).
102. Paragraph 49(2) defines the term “readily convertible asset” for the purposes of paragraph 49.
103. Paragraph 49(3) applies Chapter 2 of new Part 7A of ITEPA by reason of the early step and provides that the amendments made by this Schedule have effect accordingly.
104. Paragraph 49(4) provides for the early step to be treated as having been taken on 6 April 2012 in determining the tax year for which the relevant step counts as employment income of the employee (“A”) for the purposes of new section 554J(1) of ITEPA. Paragraph 49(8) contains equivalent provision for the purposes of PAYE. Paragraph 49(3) also provides that for all other purposes, the early step is treated as taken when it is actually taken.
105. Paragraph 49(5) provides for the amount which would otherwise count as employment income of the employee to be reduced to nil if the asset which is the subject of the early step is returned to the person who took the step before 6 April 2012 and the asset is no longer being used as security on that date.

## FINANCE (No.3) BILL

106. Paragraph 49(6) provides that that the overlap provisions in new section 554M do not apply in relation to the early step and that in applying that section to any other relevant step (whenever taken) the early step is to be ignored.
107. Paragraph 49(7) provides that the early step is to be ignored when applying new section 554A(4) of ITEPA in relation to any other relevant step.
108. Paragraph 50 provides for the amendments made by paragraph 13 of this Schedule to section 394 of ITEPA which relate to chapter 1 of Part 3 of that Act to have effect in relation to benefits under Chapter 2 of Part 6 of ITEPA received on or after 6 April 2011.
109. Paragraphs 51 and 52 provide for the amendments made by paragraphs 34 to 38 and 42 to 46 of this Schedule to come into force on 6 April 2011.

### BACKGROUND NOTE

110. The June Budget announced that legislation would be introduced from April 2011 to tackle arrangements using trusts and other vehicles to reward employees which seek to avoid, defer or reduce tax liabilities.
111. The Government also confirmed that the scope of the legislation would include Employer Financed Retirement Benefit Schemes (EFRBS), in order to protect revenues and in keeping with the restriction of pensions tax relief through the reduced annual and lifetime allowances announced on 14 October 2010.
112. If you have any questions about this change or comments on the legislation, please contact Peter Robinson on 020 7147 2423 (email: peter.w.robinson@hmrc.gsi.gov.uk) or David McDowell on 020 7147 0175 (email: david.mcdowell@hmrc.gsi.gov.uk).