

# Employment-Related Securities

**(Lecture P1160 – 10.32 minutes)**

*What is an ERS?*

A security (i.e. shares, debt, derivatives and interests in investment partnerships) where the right or opportunity to acquire the securities (or interest in securities) is:

- available by reason of an employment of the person acquiring the securities (or interest) or any other person; or
- (under the “deeming provision” in s471(3) in ITEPA) made available by a person's employer (or a person connected with a person's employer), unless such right or opportunity is made available:
  - by an individual; and
  - in the normal course of the domestic, family or personal relationships of that individual.

“Employment” includes a former, current and prospective employment.

*General earnings charge on acquisition*

The employee or director will generally be treated as receiving employment income equal to the difference between:

- market value of the shares at the time of acquisition; and
- the amount (if any) paid (or required to be paid) for them
  - This is called the “Weight v Salmon” charge.

There are some exceptions, e.g. where founder shareholders, who also become directors, receive shares in their capacity as investors in the company rather than directors or employees.

Special rules apply to restricted securities and convertible securities. (The latter are not covered in this seminar.)

*Restricted securities*

Special rules apply upon the acquisition of ERS that are subject to restrictions. The latter may affect:

- an employee's ability to retain the securities
  - e.g. the articles of association may oblige an employee to transfer securities to 'permitted transferees' on the occurrence of certain events such as resignation, or

- the general rights attaching to the securities  
e.g. restrictions on transfer, dividend rights or voting rights.

Restrictions typically have the effect of reducing the market value of ERS and hence any income tax and NIC charges upon acquisition. However, where the ERS rules apply, income tax and NIC charges can arise on subsequent chargeable events, including the:

- lifting, variation or expiry of the restrictions; or
- disposal of the restricted securities.

#### *Election under s.431 ITEPA 03*

- Can elect to be taxed initially on the unrestricted MV (UMV)
  - Subsequent chargeable events then produce a CGT charge, rather than income tax and NIC charges
- A good idea except where share price falls after issue!
  - Election has to be made within 14 days of share issue as part of the reporting on an ERS annual return.

#### *Example*

On issue (with no s.431 election):

- Edwina pays MV of £2 per share for 1,000 restricted shares in Major Ltd
  - Shares worth £5 each with restrictions lifted.
  - Difference between restricted and unrestricted values is 60% of UMV

On sale (£140/share), the gain is £138,000:

- Edwina is chargeable to:
  - CGT on 40% of the gain (£55,200), but
  - income tax on 60% of the gain (£82,800)

The shares will be readily convertible assets, so also Class 1 NIC to pay on the part taxed as income.

On issue, she signs a s.431 election:

- Income tax is due on the uplift from £2 to £5 ("dry" tax charge) of £3,000

On sale (£140/share):

- Edwina is charged to CGT on the whole gain of £135,000 (the cost is the unrestricted MV on which tax already paid, i.e. £5).

*Contributed by Kevin Reed*