

17 March 2004

NATIONAL INSURANCE CONTRIBUTIONS AND STATUTORY PAYMENTS BILL – CONSEQUENTIAL TAX CHANGES

Who is likely to be affected?

1. Employees who agree to bear the employers' (secondary) Class 1 National Insurance liability due on earnings arising after the acquisition of employment-related restricted or convertible securities (usually shares).
2. Any employer who chooses to award restricted or convertible securities to their employees.

General description of the measures

3. The earnings in question result from what are referred to as 'post acquisition chargeable events', for example the lifting of a restriction applying to the securities or the conversion of securities into another form of security. Changes will be made to provide employees with income tax relief by way of a deduction from their taxable income, equal to the amount of any Secondary Class 1 National Insurance contributions (NICs) paid by them.
4. The changes will also ensure that the provision of the income tax relief to the employee will not affect:
 - the Capital Gains Tax (CGT) liability on any subsequent disposal of the securities; or
 - the Finance Act 2003 Schedule 23 Corporation Tax relief for employee share acquisition.

Operative date

5. These changes will be brought into effect to coincide with the commencement of changes to be made to the Social Security Contributions and Benefits Act 1992, by the National Insurance Contributions and Statutory Payments Bill 2004 ("NICs Bill"). The relevant NICs Bill clauses will come into force at a time to be provided for by way of a Treasury Order following Royal Assent of the Bill.

Current Law and Proposed Revisions

6. Employers are currently able to ask employees receiving share options to agree to pay the employer's (secondary) Class 1 NICs liability arising on gains made from those options. Employees who agree to pay their employer's NICs liability under these limited circumstances benefit from a reduction in their taxable income equivalent to the amount of the employer's liability they pay. Changes to tax legislation are necessary to provide the same income tax relief to employees who bear the employer's NICs liability due on post-acquisition earnings derived from restricted and convertible securities.

7. When securities acquired by way of a securities option are eventually disposed of, CGT may be due on their growth in value. Existing legislation ensures that the calculation of the CGT liability is unaffected by the income tax relief the employee benefited from when they paid their employer's NIC liability. This legislation needs to be amended to ensure that when employees pay employer's NICs on earnings from restricted and convertible securities, any CGT liability arising on disposal of those securities is not affected by the earlier income tax relief.

8. Minor changes will also be made to Schedule 23 in Finance Act 2003, to ensure the amount of the Corporation Tax relief which the employer obtains when employees acquire employment-related shares is not affected if the employee pays the secondary NICs.

Further information and advice

9. More details and further information about the NICs Bill can be found on the Inland Revenue website at www.inlandrevenue.gov.uk/nic/nic_bill.htm

10. If you have any questions about these changes, please contact the Share Schemes team on 020 7438 7659/7504/4339

www.inlandrevenue.gov.uk