



Faculty of Taxation

## **TAXREP 8/03**

### **Comments on the Pre-Budget Report (November 2002) and Provisions for Corporation Tax Relief for Employee Share Acquisitions**

*Memorandum submitted in March 2003 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales to the Inland Revenue in response to the November 2002 Pre-Budget Report and draft clauses published in December 2002 on Corporation Tax Relief for Employee Share Acquisitions*

#### **CONTENTS**

	<b>Paragraph</b>
<b>INTRODUCTION</b>	<b>1</b>
<b>WHO WE ARE</b>	<b>2-4</b>
<b>PRE-BUDGET REPORT</b>	<b>5-10</b>
<b>CORPORATION TAX RELIEF FOR EMPLOYEE SHARE ACQUISITIONS</b>	<b>11-14</b>

# Tax Representation

## **Comments on the Pre-Budget Report (November 2002) and Provisions for Corporation Tax Relief for Employee Share Acquisitions**

### **INTRODUCTION**

1. We have set out below our comments on the draft clauses issued at the time of the Pre-Budget Report in November 2002 and on the draft clauses issued in December 2002 dealing with Corporation Tax relief for Employee Share Acquisitions.

### **WHO WE ARE**

2. The Institute is the largest accountancy body in Europe, with more than 123,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.
3. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry (DTI) through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy (which includes taxation).
4. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter "TAXline" to more than 11,000 members of the ICAEW who pay an additional subscription.

### **PRE-BUDGET REPORT**

#### **Employee Benefit Trusts (EBT)**

5. We note the Government's intention is to allow a tax deduction only to the extent that, and at the time when, the employees themselves are taxable. However many legitimate payments to genuine EBTs will not now rank for relief, for instance payments to be used for charitable purposes by EBTs which have charitable objects and make payments to charities relevant to employees, without directly benefiting known employees. . In addition some benefits received by employees via EBTs, but which are specifically exempted from tax under the benefit in kind legislation, will result in no deduction being available to the company for the expense incurred via the EBT. If a similar benefit is provided direct to the

# Tax Representation

employee it will continue to rank for tax relief in the hands of the company. For instance benefits exempt under section 155 ICTA 1988.

6. In paragraph 2 of the draft Schedule a deduction is also disallowed if the benefit is provided by a UK-based employer to a foreign-based employee who would be exempt from tax on UK duties under a treaty. A deduction should be allowed in these circumstances.
7. The drafting of paragraph 2(3) also appears defective. We presume that the intention is that sub-paragraph (a) of paragraph 2(3) will apply solely to decide whether the payment would be liable to income tax, and sub-paragraph (b) will apply solely to decide whether it would be subject to NIC. As currently drafted it appears that, in strictness, both tests must be applied for both purposes.
8. It is also unclear what happens if the benefit is taxable but the measure of the tax charge is completely unrelated to the cost of providing it, e.g. the provision of cars for disabled employees.

## **Taxation of UK branches of Foreign Companies**

9. We are concerned that while the legislative changes are effective from 27 November 2002 the legislation will not be finalised and on the Statute Book before Summer 2003 when the Finance Act 2003 receives the Royal Assent.
10. We are also concerned that this represents a further instance where legislation is introduced for companies while the existing legislation is retained for unincorporated bodies in equivalent circumstances. The maintenance of parallel (corporation and income tax) legislation adds to the complexity of the overall legislation and causes potential confusion for both advisers and taxpayers. We believe that there should be only one set of rules and these should apply for all tax purposes.

## **Capital Allowances – avoidance affecting proceeds of balancing events**

11. If the provisions, in draft section 570A CAA 2001, apply then the vendor is denied an allowance which is a penal provision. We believe that it is more appropriate to reduce the allowance from the excessive amount to one that is just and reasonable or what the allowance would have been if the transaction had taken place at arm's length or prices that would have prevailed if the parties to the transaction had been unconnected.

## **CORPORATION TAX RELIEF FOR EMPLOYEE SHARE ACQUISITIONS**

12. We welcome these provisions which are in general terms relieving and which provide statutory relief in respect of costs incurred in allowing employees to acquire shares in the company for which they work. We note that this will bring the UK treatment into line with the position in the United States.
13. In relation to the detailed provisions we have the following comments.

# Tax Representation

14. In paragraph 21(3), where an employee dies the basis of valuation is not clear. We would suggest that more detailed provisions should be included. A suitable model can be found in section 140A(8), ICTA 1988.
15. In paragraph 32, we believe the definition of 'relevant expenses' is too wide and would apparently deny relief, for example, if a deduction has been claimed in the last pre 1 January 2003 accounting period for incidental costs associated with the administration of a share issue actually made in the following accounting period. It would appear that what is needed is an exclusion from the definition of 'relevant expenses' for the same classes of expense as are listed in paragraph 24(3). In any event relief should be restricted under the Schedule only to the extent that a deduction is available for the pre 1 January 2003 'relevant expenses', not 'if or to the extent' that one is available.

IKY

1 April 2003