

Notes for Guidance - Taxes Consolidation Act 1997

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Part 17 Profit Sharing Schemes and Employee Share Ownership Trusts

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Part 17 Profit Sharing Schemes and Employee Share Ownership Trusts

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PART 17

PROFIT SHARING SCHEMES AND EMPLOYEE SHARE OWNERSHIP TRUSTS

CHAPTER 1

Profit Sharing Schemes

Overview

Chapter 1 of *Part 17* provides for an exemption from income tax in respect of shares given by companies to their employees under Revenue approved profit sharing arrangements.

509 Interpretation (*Chapter 1*)

Summary

This section defines certain terms and references used throughout *Part 17*. In addition, it provides for the capital gains tax treatment of shares qualifying for relief under approved profit sharing schemes (APSS) as well as enabling the Revenue Commissioners to delegate their powers under these provisions.

Details

Definitions

“the appropriate percentage” is the percentage (that is, 100 per cent, 75 per cent or 50 (1) per cent, as appropriate) of the locked-in value of the shares where the participant disposes of his/her shares before the release date.

“approved scheme” is a Revenue approved scheme.

“the company concerned” is the company which establishes a profit sharing scheme.

“group scheme” is the company which establishes the profit sharing scheme and all other companies under that company’s control.

“participating company” is any company which is part of a group scheme, including the company controlling that group.

“initial market value” is the market value of any shares on the date of their allocation or on such earlier dates as are agreed between the Revenue and the trustees of the scheme.

“locked-in value” is the market value of any shares at the date of their allocation or, where shares are disposed of before the release date, the excess of the disposal proceeds over the initial market value.

“market value” is the price which any shares might reasonably be expected to fetch on a sale in the open market.

“participant” is an individual to whom the trustees of the scheme have allocated shares.

“the period of retention” is the period beginning on the date shares are allocated to a participant and ending 2 years later or, if earlier, the date the participant ceases employment with the company or reaches 66 years of age or the date of the participant’s death.

“shares” includes stock and specified securities.

“specified securities” are securities (within the meaning of *Schedule 12*), other than ordinary shares, which were transferred to the APSS trustees by the trustees of an Employee Share Ownership Trust (ESOT), which itself acquired those securities by way of an amalgamation to which *section 586* applies. It also includes securities which replaced these securities as a result of a company reorganisation under *section 584* as well as any further securities acquired using dividends on the securities previously acquired. This aligns the rule governing these securities with that which applies in the case of ordinary shares. The purpose of using the definition in *Schedule 12* of securities is to align insofar as is possible the definitions for both APSS and ESOT purposes and so ensure that securities acquired by the ESOT in these particular circumstances can be transferred to the APSS. There is no need to do this for ordinary shares because these can already be transferred.

The one overriding condition which must be satisfied relates only to the case of a company limited by shares. Before any securities acquired by the ESOT can qualify, the ESOT must also acquire the same percentage of the ordinary share capital of the takeover company as it had of the ordinary share capital of the company being taken over immediately before the takeover. Since the need to use securities other than ordinary shares only arises in circumstances where the aggregate share capital value of the takeover company is less than that of the company being taken over companies of equal size or greater cannot satisfy this condition. Whatever form these securities take they must at the very least have been issued by the takeover company under the provisions of *section 586*.

In the case of a company not limited by shares (i.e. a cooperative) no such *de minimis* rule applies because there are no ordinary shares available regardless of the size of the takeover company.

“the trust instrument” is the instrument referred to in *paragraph 3(3)(c)* of *Schedule 11*, and which complies with the provisions of such trusts as set out in *Part 5* of *Schedule 11*.

“the trustees” are the body of persons an approved scheme is obliged to establish by virtue of *paragraph 3(3)* of *Schedule 11*.

Disposal of shares

Any provision of this Chapter relating to the order in which a participant’s shares are treated as disposed of for the purposes of this Chapter is to apply irrespective of any direction in relation to those shares given by the participator to the trustees. This ensures that the first-in-first-out identification rule overrides any specific directions given to the trustees by the participant. It also has relevance in relation to *subsections (2)* and *(4)* of *section 515* which deal with the treatment of shares under a scheme which are in excess of the €12,700 limit or which are not authorised under the terms of the legislation. (2)

Capital gains tax

For capital gains tax purposes — (3)

- no deduction in respect of any amount chargeable to income tax under this Chapter is allowable against the consideration on the disposal of such shares,
- any charge to income tax (under *section 513*) in respect of capital receipts in respect of a participant is to be disregarded in determining whether a distribution (such as a distribution on winding up a company) is a capital distribution chargeable to capital gains tax,
- the ordinary capital gains tax rules apply in determining what constitutes a disposal and in calculating gains and losses in respect of approved profit sharing scheme shares. However, there are 2 specific exceptions to this treatment in

subsection (5) and (6) of section 510 which secure that the trustees are not liable to capital gains tax in certain circumstances.

Delegation of Revenue Powers

The Revenue Commissioners may delegate their functions under **Chapter 1 of Part 17 (4)** and **Schedule 11** to an officer of the Revenue Commissioners.

510 Approved profit sharing schemes: appropriated shares

Summary

Where the trustees of an approved scheme have acquired shares and allocated them to a participant a charge to income tax does not arise on the participant in respect of the right to receive the beneficial interest in those shares by virtue of such an allocation.

Details

Interpretation

The references to an approved scheme are references to a scheme approved in accordance with **Part 2 of Schedule 11**. A reference to a participant is taken as a reference to an individual to whom the trustees of an approved scheme have allocated shares. Subject to **section 514** (company reconstructions, amalgamations, etc), any reference to a participant's shares is construed as a reference to the shares which have been allocated to him/her by the trustees of an approved scheme. (1)

The initial market value of a share is the market value of the share at the date of allocation to a participant or at an earlier date or dates agreed with the Revenue Commissioners. That market value is determined in the same way as for capital gains tax, namely, the price the share might reasonably be expected to fetch on a sale in the open market without taking into account any of the contractual obligations imposed personally on a participant by **section 511(4)**. (2)

Application

This section applies where the trustees of an approved scheme allocate shares which they have previously acquired and which meet the conditions in **Part 3 of Schedule 11** to a participant in the scheme. (3)

Exemption from income tax

Where shares are allocated to a participant by the trustees under an approved scheme, a charge to income tax is not made on that participant in respect of the right to receive the beneficial interest passing to him/her by virtue of such allocation. (4)

Capital gains tax

For capital gains tax purposes, a participant is treated from the date of allocation as absolutely entitled to his/her shares as against the trustees. This means that, from the moment of allocation, any liability to capital gains tax is on the participant and the ending of the retention period does not constitute an occasion for a charge to capital gains tax on the trustees as would otherwise be the case. (5)

If shares are allocated to a participant by the trustees under an approved scheme — (5A)

- where those shares were previously transferred to such trustees by the trustees of an employee share ownership trust (ESOT) to which **section 519** applies, and
- where the shares were transferred at a date later than that on which the shares could have first been transferred in accordance with the terms of the employee

share ownership trust deed or any other document but, regardless of the reason, were not transferred on that earlier date,

then, for capital gains tax purposes, the allocation to the participant concerned shall be deemed to have taken place on the day following the day when those shares could have first been transferred out of the ESOT to the trustees of the approved scheme.

The trustees are exempt from capital gains tax on any gains arising at the time when shares are allocated to a participant provided the shares are allocated to the participants within 18 months of acquisition. **(6)(b)**

For the purpose of determining whether shares are allocated within the 18 months period, the “first-in-first-out” rule applies.

Surcharge on undistributed income of trust

Where the trustees of an approved scheme acquire shares and within a period of 18 months after their acquisition, the shares are allocated in accordance with the scheme, any dividends on the shares received by the trustees are not liable to the income tax surcharge of 20 per cent on the undistributed income of certain trusts provided for in **section 805**. It should be noted that the income referred to is income of the profit sharing trust received by the trust before the allocation of the shares to participants and not income received by the trust on behalf of participants. The latter income is to be charged to tax in the hands of participants in the ordinary way. **(6)(a)**

For the purpose of determining whether shares are allocated within the 18 months period, the “first-in-first-out” rule applies.

Information

The Revenue Commissioners may request information by notice in writing within such time as they may direct (but not being less than 30 days). The information may, in particular, relate to the giving or withdrawal of approval and the determination of any participant’s tax liabilities. The circumstances in which approval may be withdrawn are set out in **paragraph 5(1) of Schedule 11**. **(7)**

With effect from 2009 onwards the trustees of an approved profit sharing scheme are obliged to automatically furnish the same information referred to in the paragraph above to the Revenue Commissioners in respect of each calendar year. This return of information is required by 31 March in the year following the year in question. Failure to do so will result in penalties as set out in **sections 1052 and 1054**, as appropriate. **(8)**

511 The period of retention, release date and appropriate percentage

Summary

This section provides that a scheme to obtain the benefit of the tax treatment provided by this Chapter must be one approved by the Revenue Commissioners.

Details

Definitions

The “period of retention” is the period starting on the date on which shares are allocated to the participant and ending on the second anniversary of that date or, if it is earlier — **(1)**

- the date on which the participant ceases to be an employee of the company running the scheme (or of a participating company in the case of a group scheme) on account of injury, disability or redundancy;
- the date on which the participant reaches pensionable age for social welfare

- purposes (this is, 66 years); or
- the date of the participant’s death.

The “release date” (which is the date after which a participant in an approved scheme may dispose of shares acquired under the scheme without being liable for income tax) is — (2)

- as and from 10 May, 1997, the 3rd anniversary of the date the shares were allocated to the participant, and
- before 10, May, 1997, the 5th anniversary of the date the shares were allocated to the participant.

The “appropriate percentage” is a percentage of the locked-in value of shares disposed of after the period of retention and before the release date. The application of the appropriate percentage to the locked-in value of shares disposed of gives the amount on which income tax is charged under *section 512*. The appropriate percentages, tapered on an a time basis, may be summarised as follows — (3),(3)(b)(i), (3)(b)(ii), (3)(b)(iii)

Disposals before 10 May, 1997

Period held	Percentage of locked-in value (or sale proceeds if smaller)	
Before the 4th anniversary (after the date of allocation of the shares)	100 per cent	
On or after the 4th anniversary and before the 5th anniversary	75 per cent	
Before the 5th anniversary and the participant ceases to be an employee/director because of injury, disability, redundancy or reached pensionable age	50 per cent	
Disposals on or after 10 May, 1997		(3)(a)(i), (3)(a)(ii)
Before the 3rd anniversary (after the date of allocation of the shares)	100 per cent	
Before the 3rd anniversary and the participant ceases to be an employee/director because of injury, disability, redundancy or reaching pensionable age	50 per cent	

The appropriate percentage in relation to excess or unauthorised shares is 100 per cent of their market-value at the date of disposal.

Obligations of participant

No scheme is to be approved of by the Revenue Commissioners unless the Revenue Commissioners are satisfied there is a contractual agreement between the participant and the company which has established the scheme imposing certain obligations on the participant. (4)

These obligations require each participant under contract with the company —

- to permit his/her shares to remain in the hands of the trustees throughout the period of retention,
- not to assign, charge or otherwise dispose of his/her beneficial interest in his/her shares during that period,
- to pay to the trustees, before a transfer of ownership takes place, a sum equal to the amount of the locked-in value multiplied by the standard rate of income tax, if the participant directs the trustees to transfer ownership of the shares to him/her at any time before the release date,

- not to direct the trustees to dispose of his/her shares at any time before the release date other than for sale for the best consideration in money that can be obtained at the time of sale.

The obligation to pay a sum equal to income tax at the standard rate imposed on a person who directs the trustees to transfer ownership of the shares to him/ her before the release date is not to be construed as binding his/her personal representatives to pay any sum to the trustees. It should be noted that, if a participant dies while the trustees are holding scheme shares on his/her behalf, the period of retention comes to an end immediately even if the shares have been held for less than 3 years. The tax charge is confined to disposals made before the release date or, if it is earlier, before the date of the participant's death. Accordingly a participant's personal representatives can dispose of the shares immediately and no part of the sale proceeds will attract liability to income tax. (5)

Mitigation on restrictions on disposals of shares

The restrictions imposed on a participant's rights in respect of shares allocated to him/her are relaxed in certain circumstances. In particular, the obligation requiring the participant to accept that the shares are to remain in the hands of the trustees during the period of retention is relaxed so as to enable the participant to instruct the trustees to accept (for example, in a prospective takeover of the company running the scheme) either a share for share offer, or a cash offer, or an offer partly of shares and partly of cash, in respect of his/her scheme shares, even though this may result in the disposal of the shares during the period of retention. The tax consequences of offers of this kind are dealt with in **sections 513 and 514**. (6)

The obligations imposed on a participant are mitigated by —

- securing that any obligation imposed on a participant is not to prevent him/her from directing the trustees to accept an offer for any of his/her shares if this would result in a new holding (within the meaning of **section 594**) being equated with the original shares for the purposes of capital gains tax, (6)(a)
- enabling a participant to direct the trustees to agree to a transaction affecting his/her shares or such of them as are of a particular class if the transaction would be entered into pursuant to an arrangement or scheme affecting — (6)(b)
 - all the ordinary share capital of the company or all the shares of the class held by the participant, or
 - all the shares or class of shares in question which are held by a class of shareholders identified otherwise than by their employment or their participation in an approved scheme,
- enabling a participant to direct the trustees to accept a cash offer (with or without other assets) for shares if the offer is part of a general offer and the person making the offer, if it is taken up, would achieve control of the company (as defined in **section 11**), (6)(c)
- enabling a participant after the expiry of the retention period, to sell his/ her beneficial interest in shares to the trustees for the best consideration in money that can reasonably be obtained at that time for the shares. (6)(d)

Disposal of beneficial interest

Where a participant assigns, charges or otherwise disposes of any of his/her beneficial interest in any of his/her shares during the period of retention, he/she is treated as respect those shares, as if at the time they were allocated to him/ her, he/she were ineligible to participate in the scheme and **section 515** applies accordingly. (7)

511A Shares acquired from an employee share ownership trust

Summary

This section ensures that the three year retention period for which shares must be held to benefit from the tax relief will be satisfied by a combination of the time the shares are held in an Employee Share Ownership Trust (ESOT) and in an Approved Profit Sharing Scheme (APSS).

Details

This section, comprising 2 subsections, applies where on or after the passing of the Finance Act 1998— (1)

- (a) shares are appropriated by an APSS to a participant,
- (b) those shares had been transferred by an ESOT to that APSS, and
- (c) the person was a beneficiary of the ESOT at all times during a “holding period”, which is defined as a period beginning on the later of the day the shares were acquired or the person became a beneficiary and ending on the day the shares were appropriated. The reference to “at all times” excludes the 30 day period which is allowed during which a person may remain a participant in an APSS after ceasing to be a beneficiary of the ESOT.

For the purposes of *section 511* — (2)

- (a) the period of retention ends —
 - (i) where the holding period is 2 years or more on the day following the end of the holding period, and
 - (ii) where the holding period is less than 2 years, 2 years after the beginning of the holding period, or earlier if the person retires, is made redundant or dies, and
- (b) the release date means —
 - (i) where the holding period is 3 years or more, on the day following the end of the holding period, and
 - (ii) where the holding period is less than 3 years, 3 years after the beginning of the holding period.

512 Disposals of scheme shares

Summary

If the trustees dispose of a participant’s share before the release date or, if earlier, before the date of the participant’s death, the participant is charged to income tax under Schedule E on the appropriate percentage of the lesser of —

- the locked-in value of the share, and
- the proceeds of disposal.

If shares are disposed of otherwise than at arm’s length, the market value of the shares disposed of is substituted for the amount of the sale proceeds for the purpose of calculating the charge to tax. Where the disposal of shares is made from a holding which was allocated to the participant at different times the “first-in-first-out” identification rule applies for the purpose of determining the initial market value and the locked-in value of those shares and the appropriate percentage to be applied in relation to each of those shares.

If a participant dies while the trustees are holding shares on his/her behalf, his/her personal representatives can dispose of the shares immediately and no part of the sale proceeds will attract liability to income tax under the section.

Details

Locked-in value

Subject to *sections 514* (which provides, in the case of a company reconstruction or amalgamation, that the locked-in value is determined by apportioning the locked-in value of the old shares among the new shares) and *515(6)* (which provides that the locked-in value of unauthorised or excess shares is their market value at that time), the locked-in value of a participant's shares at any time is (if there has been a capital receipt in respect of the shares) the amount by which their initial market value exceeds the amount or value of that capital receipt or the aggregate of such receipts. If there have been no capital receipts in respect of the shares, the locked-in value of the shares is their initial market value. Examples of the case where there has been a capital receipt are given in the note on *section 513*. (1)

Disposal of shares before release date

If the trustees dispose of a participant's share before the release date or, if it is earlier, before the date of the participant's death, the participant is liable to income tax under Schedule E for the year of assessment in which the disposal takes place on the lesser of the appropriate percentage of — (2) & (3)

- the locked-in value of the shares, and
- the proceeds of the disposal.

It should be noted that no liability to tax is imposed in relation to disposals made before the release date but after the date of the death of the participant.

Example 1

1 January, 2005: 100 shares allocated to an employee.

The shares are valued at €3 each as at this date.

31 July, 2007: The shares are disposed of for €2 each.

The disposal proceeds, €200 are less than the locked-in value, €300, therefore income tax is charged on €200 (100% of €200).

Example 2

The facts are as stated in Example 1 but in this disposal proceeds are €5 per share.

The locked-in value, €300, is less than the disposal proceeds, €500, therefore income tax is charged on €300.

Rights issues

The references in this note to the rights arising under a rights issue is to be taken as references to rights conferred in respect of a participant's shares, being rights to be allotted other shares in the same company which are to be paid for. (5)(b)

If at any time before the disposal of any of a participant's shares the participant has made a payment or payments to the trustees to enable them to exercise rights arising on a rights issue on his/her behalf, the proceeds of any disposal of shares following the rights issue are to be reduced (in order to calculate whether the proceeds are less than the acquisition cost) by that proportion of the amount or amounts provided by the participant to enable the trustees to exercise rights on his/her behalf which the market value of the shares disposed of bears to the market value of the participant's total (4)

holding of scheme shares at the time of the disposal.

Shares acquired under a rights issue must be held by trustees in the same way as the original shares.

Example

On 1 January, 2005, 100 shares, valued at €5 each, are allocated to an employee.

On 1 July, 2007, there is a rights issue, 1 for 2 at €2 each. Participant pays €100 to take up rights shares. On 1 October, 2007, he/she disposes of 80 shares at €6 each.

Date	Number of shares	Locked-in value (LIV)	Payment for rights
1 January, 2005	100	€500	—
1 July, 2007	100+50=150	€500	€100
1 October, 2007	80	€266 *	

*266= $500 \times \frac{80}{150}$

Adjustment to disposal proceeds

Consideration for rights	€100	
Market value of 80 shares sold	€480	
Market value of remaining shares	€420	(70 x €6)
Reduction in disposal proceeds		
	$100 \times \frac{480}{480 + 420}$	€54
Reduced disposal proceeds	€480 – €54 =	€426

The LIV of the shares (€266) is less than the reduced disposal proceeds (€426), accordingly income tax is charged on €266 (100% of €266).

The term “shares” (which includes stock by virtue of *section 509(4)*), in relation to a new holding arising on a rights issue, is extended to include securities and rights of any description. In other words, if as a result of a company reconstruction, the shares originally allocated are replaced by shares or stock which do not satisfy the conditions required for the approval of a scheme as set out in *Part 2 of Schedule 11* that does not mean that the scheme automatically ceases to be “approved”. (5)(a)

Any payment to trustees, to the extent that it consists of the proceeds from the sale of some of the rights arising under a rights issue, which are used by the trustees, at the direction of the participant, to take up the balance of the rights are not to be taken into account for the purpose of reducing the proceeds of a disposal of shares following a rights issue. The proceeds so used do not come from the participant’s own resources but are essentially derived from the shares and accordingly cannot be taken into account for the purposes of that reduction. (5)(b)

If there is more than one disposal following a rights issue, the amount of the payment or payments to be taken into account in calculating the reduction in the disposal proceeds following a rights issue is itself to be reduced by the amount of any reductions which have already been made on earlier disposals.

Example

The facts are as in the previous example, except that on 1 December, 2007 the remaining 70 shares are disposed of at €5 each.

The locked-in value of the 70 shares sold is €234 (€500 – €266). The disposal proceeds are €350.

Adjustment to disposal proceeds

Consideration for rights €100.

Deemed reduction from consideration by virtue of reduction in sale proceeds on previous occasion €54.

For the purposes of the second disposal the consideration for the rights is taken as €46 (€100 – €54).

The reduction in disposal proceeds is —

$$€46 \times \frac{350}{350} = €46$$

Reduced disposal proceeds €350 – €46 = €304.

The LIV (€234) of the shares sold is less than the reduced disposal proceeds, accordingly income tax is charged on €234 (100% of €234).

Identification of shares

Where the trustees dispose of a participant’s shares before the release date or, if earlier, before the date of the participant’s death and the disposal is made from a holding of shares which were allocated to the participant at different times, then, for the purposes of determining the initial market value and the locked-in value of each of those shares and the appropriate percentage in relation to each of those shares, the first-in-first-out identification rule is to be observed (that is, each is to be treated as being of shares which were allocated earlier before those which were allocated later). (6)

Example

1 January, 2005: 100 shares, valued at €5 each, are allocated to employee.

1 January, 2007: 200 shares, valued at €2 each, are allocated to the same employee.

1 October, 2007: 150 shares are disposed of at €2.50 each.

Under the identification rule the calculations are to be made as if the 150 shares sold comprised the 100 shares which were allocated on 1 January, 2005, and 50 of the shares which were allocated on 1 January, 2007.

First allocation

Disposal proceeds of 100 shares, treated as if they were those allocated on 1 January, 2005 – €250. Locked-in value of 100 shares allocated on 1 January, 2005 – €500. Income tax is charged on €250 (100% of €250).

Second allocation

Disposal proceeds of 50 shares treated as allocated on 1 January, 2007 – €125. Locked-in value of 50 shares allocated on 1 January, 2007 —

$$€400 \times \frac{50}{200} = €100$$

Income tax is charged therefore on €100 (100% of €100).

Disposal of beneficial interest

If at any time a participant disposes of his/her beneficial interest in his/her shares, but no formal transfer of the shares is executed, the disposal is to be treated as if it were a disposal of the shares themselves for the like consideration) as was obtained for the disposal of the beneficial interest. There is no disposal of the participant’s beneficial interest if that interest becomes vested in any person on the insolvency of the participant (7)

(for example, if it vests in the Official Assignee, etc under the Bankruptcy laws) or otherwise by operation of law.

[The consequences of the assignment of a beneficial interest during the period of retention are dealt with in the notes on *section 511(7)* and in the next paragraph.]

Substitution of market value for sale proceeds in certain circumstances

Where — (8)

- a transfer of shares to trustees occurs before the release date,
- any other disposal occurs in relation to which the Revenue Commissioners are of the opinion that the disposal is not at arm's length, and
- a disposal of shares occurs in consequence of the disposal of the participant's beneficial interest during the period of retention,

then, the market value of the shares disposed of is to be substituted for the amount of the sale proceeds for the purpose of calculating the charge to income tax.

513 Capital receipts in respect of scheme shares

Summary

This section ensures that capital receipts in relation to scheme shares which arise at a time when a participant's shares are held by trustees are subject to a charge to income tax on the participant.

Any capital receipt the entitlement to which arises after a participant's death is not to be charged to income tax under this section.

Details

If the trustees (or a participant) become entitled before the release date to receive any money or money's worth (referred to in the section and this note as a "capital receipt") in respect of, or by reference to, a participant's shares, the participant is to be charged to income tax under Schedule E for the year of assessment in which the entitlement arises on the appropriate percentage (determined at the time when the entitlement arises) of the amount or value of the receipt. (1)

Money or money's worth is not a capital receipt to the extent that it — (2)

- already constitutes income in the hands of a recipient for income tax purposes, (for example, a dividend on scheme shares),
- consists of the proceeds of a disposal of scheme shares,
- consists of "new shares" (that is, shares issued under a company reconstruction or amalgamation and which were issued in respect of, or otherwise represent, the original shares).

The term "capital receipt" does not include the proceeds of the disposal of part of the rights arising under a rights issue, provided those proceeds are used to exercise other such rights. Accordingly, there is no charge to income tax on such proceeds. (3)

If the amount or value of a capital receipt would exceed the sum which, immediately before the entitlement to the receipt arose, was the locked-in value of the shares in respect of which the capital receipt arose, the charge to tax is to be restricted to the appropriate percentage of the locked-in value of the shares immediately before the entitlement. (4)

There is no charge to tax on a capital receipt where the entitlement arose after the death of the participant to whose shares the receipt is referable. (5)

Excluded from the charge to tax is any receipt the amount or value of which does not exceed €13. (6)

Example

1 January 2005: 500 shares, valued at €1 each, allocated to participant.

1 July 2006: Capital receipt of 10c per share (that is, €50 received).

1 January 2007: Capital receipt of €1 per share (that is, €500 received).

1 October 2007: The shares are sold for €3 each.

The locked-in value of the shares immediately before the first capital receipt is €500.

First capital receipt

There is an income tax charge for 2006 on the first receipt.

Income tax is charged on €50 (100% of €50).

The locked-in value of the shares immediately after the receipt is €500 – €50 = €450.

Second capital receipt

There is an income tax charge for 2007 on the second receipt.

As the value of the receipt (€500) exceeds the locked-in value of the shares before the receipt (€450) the income tax charge is on the appropriate percentage of the locked-in value i.e. €450 (100% of €450).

Immediately after the second receipt the locked-in value of the shares is NIL (€450 – €450) and so there is no income tax charge on the disposal of the shares on 1 October, 2007.

514 Company reconstructions, amalgamations, etc

Summary

This section contains technical provisions to cater for the situation where, in consequence of company reconstructions or reorganisations, the shares originally allocated to participants are replaced by new shares or securities. Broadly, the section is designed to ensure that the new shares or securities stand in the place of the original shares and are dealt with by the trustees in the same way as the original shares.

Details

“new shares” are shares comprised in a new holding which were issued in respect of, or otherwise represent, shares comprised in the original holding. (1)

“the corresponding shares” are shares in the holding before the reconstruction in respect of which the new shares were issued or which the new shares otherwise represent.

This section applies where there is a transaction in relation to any of a participant’s shares (referred to as “the original holding”) which, for capital gains tax purposes, would result in a new holding being equated with an original holding. The scope of these transactions includes bonus issues, rights issues, alterations of rights attaching to a share class, conversion of securities, including exchanges and company amalgamations, reconstructions and takeovers. (2)

Shares issued as part of a company reconstruction, which trigger a distribution charge in accordance with **section 131(2)**, are not to be treated as standing in the place of the original shares in respect of which they were issued. Since the shares in question are, therefore, chargeable directly to tax in the hands of the participants under Schedule F, they should, accordingly, be passed direct to the participants by the trustees. (3)(a)

[**Section 131(2)** treats as a distribution an amount paid by a company where that company repays share capital after 27 November, 1975, and after the repayment, issues

fully paid up, other than for full consideration, share capital.]

The existing charge to tax provided for in *sections 130(2)* and *132(2)* are preserved in relation to “redemption moneys” or “capital repayments”. In this instance, as the charge to tax is not on the shares themselves but on the proceeds of redemption or repayment the shares involved should be retained by the trustees and allocated to the participants holding the original shares. These bonus shares, broadly, are subject to the normal provisions of approved profit sharing schemes. (3)(b)

The rules needed to ensure that new shares issued on a reconstruction stand in the place of the original shares are that — (4)

- a company reconstruction is not to be treated as involving a disposal of shares comprised in the original holding (so that there will not be an income tax charge under *section 512*) at the time of the reconstruction,
- the new shares are to be treated as having been allocated to the participant on the date the corresponding shares were allocated (so that the period for the purpose of calculating the appropriate percentage (under *section 511(3)*) will run from the original date of allocation,
- the conditions which have to be satisfied in respect of scheme shares (see *Part 3* of *Schedule 11*) are treated as fulfilled in respect of the new shares if they were fulfilled, in respect of the corresponding shares.

When scheme shares are disposed of the participant is generally liable to income tax on a percentage of the locked-in value (the initial market value of the shares less any capital receipts which have been charged to tax under *section 513*). When there has been a company reconstruction it is necessary to apportion the locked-in value of the old corresponding shares among the new shares. The steps to be taken are — (5)

- ascertain the locked-in value, before the reconstruction, of the old corresponding shares which have the same locked-in value of each other, and
- distribute that locked-in value among any of the old shares which survive into the new holding, and the new shares, pro rata, according to their market value immediately after the reconstruction.

It is also provided that *section 512(1)(a)* (which is concerned with the determination of locked-in value) is to apply only to capital receipts after the date of the reconstruction. This is to ensure that the locked-in values of the new shares which have been determined by reference to capital receipts received before that date will not be further reduced on account of the same receipts.

Any subsequent income tax charged in respect of the shares in the new holding will be by reference to their locked-in value immediately after the reconstruction, calculated as set out earlier.

Example

1 January 2005: 500 shares, valued at €1 each, allocated to participant.

1 July 2006: 200 shares, valued at €2 each, allocated to participant.

1 October 2006: 1 for 2 bonus issue.

Following the bonus issue the new holding comprises.

700 corresponding shares (that is, 500 + 200)

350 new shares (that is, 250 + 100)

The locked-in values (LIV) of the corresponding shares immediately before the bonus issue are —

- 500 with LIV €500
- 200 with LIV €400

The locked-in values of the new shares immediately after the bonus issue are—

- $500 + 250 = 750$ shares with LIV €500
- $200 + 100 = 300$ shares with LIV €400.

When, as part of a company reconstruction, the trustees become entitled to a capital receipt in addition to new shares, the necessary adjustment to the locked-in value of the corresponding shares in respect of the capital receipt must be made before the locked-in value of the new shares is calculated. In other words, because the income tax charge on the capital receipt will reduce the value of the corresponding shares, the locked-in value of the new shares will be determined by that reduced amount. (6)

Example

1 January 2004: 500 shares in company A, valued at €1 each, allocated to participant.

1 July 2005: 400 shares in company A, valued at €1 each, allocated to participant.

1 October 2005: Company A taken over by company B: one share in company B and cash of 40c given for every 2 shares in company A.

1 August 2007: 300 shares in company B disposed of for €2.

The capital receipt of 20c per share is treated as arising immediately before the takeover and the income tax charge for 2005 is as follows —

- 500 “A” shares allocated on 1 January 2004 gives rise to a capital receipt of €100
- 400 “A” shares allocated on 1 July 2005 gives rise to a capital receipt of €80

As the sum is received before the third anniversary of each allocation the appropriate percentage is 100 and the income tax charge is on —

• 500 shares €100 @ 100% =	€100
• 400 shares €80 @ 100% =	<u>€80</u>
	€180

Immediately after the capital receipt the revised locked-in values are —

- 500 “A” shares with LIV €500, less capital receipt €100 = €400
- 400 “A” shares with LIV €400, less capital receipt €80 = €320

Following the takeover the new holding is —

- 250 “B” shares, LIV €400
- 200 “B” shares, LIV €320

Using the “first-in-first-out” identification rule the 300 shares disposed of comprise —

- 250 “B” shares LIV €400 – Disposal proceeds @ €2 each = €500
- 50 “B” shares LIV €80 ($€320 \times 50/200$) – Disposal proceeds @ €2 each = €100.

The LIV in both cases is less than the disposal proceeds. As the 250 “B” shares are disposed of after the third anniversary no income tax charge arises. However an income tax charge (100% of €80) arises for the year 2005 on the disposal of the 50 “B” shares.

The remaining 150 “B” shares with a locked-in value of €240 ($€320 - €80$) are deemed to have been allocated on 1 July 2005.

For the purposes of the provisions relating to company reconstructions “shares” (which (7) by virtue of *section 509(1)* includes stock and specified securities), in relation to a new holding, includes securities and rights of any description which form part of the new holding for the purposes of *section 584* (reorganisation or reduction in share capital).

515 Excess or unauthorised shares

Summary

This section is concerned with the situation where the total of the initial market values of all shares allocated to an individual in any one year of assessment (whether under a single approved scheme or under 2 or more such schemes) exceeds the €12,700 limit or

the €38,100 limit, whichever is applicable, or where shares are allocated to an individual at a time when he/she is ineligible to participate in the scheme. Those shares which cause the limit to be exceeded are described as “excess shares”. Shares allocated to an ineligible person are described as “unauthorised shares”.

Excess or unauthorised shares receive special tax treatment. First, the locked-in value of such shares at any time (for example, when they are disposed of) is their market value at that time. The initial market value and the effect of any capital receipts which are normally deductible under *section 512(1)* in computing locked-in value are disregarded. Secondly, the appropriate percentage is always 100 per cent. The effect of this is that when excess or unauthorised shares are sold, the whole of the proceeds of sale or the market values of the shares (if it is not arm’s length sale) are chargeable to income tax at the time of the disposal. Excess or unauthorised shares still held by the trustees at the earlier of the release date or the date of the participant’s death, are treated as having been disposed of, immediately before that date, at their market value at that time.

Details

Excess shares

This section applies where the total market values of all the shares allocated to a participant in any one year of assessment (whether under a single approved scheme or under 2 or more such schemes) exceeds €12,700 or €38,100 where the conditions in *subsection (2A)* are satisfied. (1)

The conditions referred to in *subsection (1)* are as follows: (2A)

- shares allocated to an individual have been transferred to the trustees of the approved scheme by the trustees of an employee share ownership trust (ESOT) to which *section 519* applies,
- at the time of transfer a period of at least 10 years, or such lesser period as the Revenue Commissioners may allow (not being less than the period referred to in the following condition) commencing with the date the ESOT was established and ending at the time when all pledged shares became unpledged (“the encumbered period”) has elapsed,
- at all times in the 5 years since the ESOT was established or such shorter period as the Minister may allow, 50 per cent of the securities, or such lesser amount as the Minister may allow, held by the trustees at the time were pledged as security for borrowings,
- none of the shares pledged at any time since the ESOT was established have been transferred from the trustees of the ESOT to the trustees of the approved scheme because they have been pledged for the period of 10 years (or such lesser period allowed by the Revenue Commissioners) or more referred to above.

The €38,100 limit may only be applied in the first year of assessment during which “the encumbered period” has elapsed and then only in respect of shares allocated after the encumbered period has elapsed. (2B)

Where for any year of assessment a participant in a scheme is allocated shares in 2 or more schemes, at the same time, and the €12,700 limit or the €38,100 limit, whichever is applicable, is exceeded, then, the same proportion of shares allocated under each scheme is to be regarded as excess. For capital reorganisations, the rule is that a “new share” is to be treated as excess or unauthorised if the “corresponding” share was so treated. (2)

Unauthorised shares (3)

Unauthorised shares are shares allocated to an individual at a time when he/she was ineligible to participate in an approved scheme by virtue of *Part 4 of Schedule 11*

(which sets out the individuals ineligible to participate).

Treatment of excess and unauthorised shares (4)

In the case of excess or unauthorised shares the appropriate percentage for the purpose of charging an individual to income tax under Schedule E is always 100 per cent. In addition, when a person who has been allocated excess or unauthorised shares disposes of shares, he/she is treated as disposing of shares which are not excess or unauthorised shares before shares which are. This is subject to the first-in-first-out identification rule in *section 512(6)* and, by virtue of *section 509(2)*, overrides any direction given to the trustees by a participant.

Example

1 January 2005: 100 shares at €5 each allocated to employee.

1 January 2006: 50 shares at €6 each allocated to employee at a time when he is ineligible within the terms of *Part 4 of Schedule 11*.

1 January 2007: 120 shares disposed of at €10 each.

The 120 shares disposed of comprise 100 allocated on 1 January 2005 and 20 unauthorised shares allocated on 1 January 2006 (first-in-first-out rule).

“Normal scheme shares”

LIV	€500
Disposal proceeds	€1,000
Income tax is charged for 2007 on €500 (100% of €500).	
Unauthorised shares	
LIV = disposal proceeds	= €200

The income tax is charged for 2007 on €200 (100% of €200).

The total tax charge for 2007 is on €700 (€500 + €200).

If the remaining 30 unauthorised shares are retained by the employee until the release date they will be treated as having been sold immediately before that date and an income tax assessment under Schedule E will be made on the market value of the shares at that time.

Excess or unauthorised shares still held by trustees at the earlier of the release date or the date of the participant’s death are treated as having been disposed of, immediately before that date, at their market value at that time. (5)

Locked-in value

The locked-in value at any time of excess or unauthorised shares is to be their market value at that time. (6)

Company reconstruction (7)

Where there has been a company reconstruction to which *section 584* applies, a “new share” is to be treated as excess or unauthorised if the “corresponding” share was so treated.

Example

A participant’s holding in an approved scheme comprises 1,000 “A” shares, 200 of which are excess shares.

The company concerned is taken over and the trustees receive 3 “B” shares for every 2 “A” shares.

Corresponding shares	800 “A” non excess
	200 “A” excess
The new shares total	1,000 x 3/2 = 1,500 shares comprising
	800 x 3/2 = 1,200 non excess
	200 x 3/2 = 300 excess

Any order made by the Minister to reduce the time period or percentage referred to in *subsection (2A)* requires a prior resolution to that effect to be passed by Dáil Éireann. (8)

516 Assessment of trustees in respect of sums received

Where a participant directs the trustees to transfer his/her shares in cash at any time before the release date and the trustees have received a sum equal to tax at the standard rate on an amount representing the appropriate percentage of the locked-in value of the shares, the trustees are charged to tax under Case IV of Schedule D on that amount. The section also gives the participant credit for the tax paid by the trustees.

517 Payments to trustees of approved profit sharing scheme

Summary

A payment by a company to the trustees of an approved scheme may be deducted in computing the company's profits for corporation tax purposes if one of two conditions is satisfied. The conditions are either —

- that the payment is applied by the trustees in the acquisition of shares for allocation to participants within 9 months after the end of the period of account in which it is charge as an expense of the company incurring the expenditure or such longer period as the Revenue Commissioners may allow, or
- that the payment is required to meet reasonable expenses of the trustees in running the scheme.

A deduction is not allowed under the section to the extent that the deduction or the aggregate of such deductions exceeds the trading income of a company carrying on a trade after certain deductions and additions such as losses, capital allowances and balancing charges are taken into account.

Details

Any sum expended by a company which has established an approved profit sharing scheme, or a company participating in a group scheme, in making payments to the trustees of such a scheme is allowed, in the accounting period in which the payment is made, as a deduction in computing the profits or gains for that accounting period of a trade carried on by that company, or in the case of an investment company or an assurance company any sums paid to the trustees of an approved scheme may be added to its expenses of management for the purpose of providing relief to such a company in respect of the sums in question. (1)

This deduction is subject to two conditions either one of which must be complied with if any sum paid to trustees is to qualify for relief in the hands of the company. (2)

The first condition is that before the end of the “relevant period” (being the period of 9 months from the end of the period of account in which a sum paid to the trustees is charged as an expense of the company or such longer period as the Revenue Commissioners may allow) the sum in question must be applied by the trustees in the acquisition of shares for allocation to individuals who are eligible to participate in the scheme by virtue of their being, or having been, employees or directors of the company making the payment.

The second condition is that the sum must be one which is necessary to cover the reasonable expenses of the trustees in administering the scheme. (3)(a)

“trading income” is the income from the trade computed in accordance with Case I of Schedule D before any deduction under this Chapter and after any deduction for

ordinary trading losses (*section 396*), terminal losses (*section 394*), capital allowances and after any addition for balancing charges (*section 308*) and stock relief (*section 666*).

No deduction is allowed in respect of sums expended in making payments to trustees, if, in the accounting period they exceed the company's trading income or in the case of an investment company, if after taking into account deductions allowable for management expenses, other than deductions allowable under this section, they exceed the management company's income for the accounting period. (3)(b)

No deduction is allowed in respect of the sum expended in making payments to trustee, if the amount expended exceeds an amount, which, in the opinion of the Revenue Commissioners is reasonable, having regard to the number of employees or directors of the company making the payment who have agreed to participate in the scheme, the services rendered by them to that company, the levels of their remuneration, the length of their services or other similar factors. (4)

Payments to trustees are identified on a first-in-first-out basis for the purposes of the section. (5)

518 Costs of establishing profit sharing schemes

Summary

The cost of establishing an approved profit sharing scheme is allowable as a deduction for corporation tax purposes.

Details

The cost incurred on or after 10 May, 1997, in establishing a profit sharing scheme approved of by the Revenue Commissioners in accordance with *Part 2 of Schedule 11* is an allowable deduction in computing the profits or gains of a trade carried on by that company. (1) & (2)

In the case of an investment company or an assurance company, any sums expended on or after 10 May, 1997, in establishing an approved profit sharing scheme, may be added to its expenses of management for the purpose of providing relief to such a company in respect of the sums in question.

This applies provided the trustees have not acquired any shares before the approval is given. If the approval of the scheme is given later than 9 months after the end of the accounting period in which the sum is expended, then the costs are treated as incurred in the accounting period in which the approval is given and not in the accounting period in which the costs are actually incurred. (3)

CHAPTER 2

Employee share ownership trusts

519 Employee share ownership trusts

Summary

This section provides a number of tax reliefs for employee share ownership trusts (ESOTs) which have been approved of by the Revenue Commissioners and in respect of which such approval has not been withdrawn.

The reliefs are —

- the company establishing an ESOT may claim a corporation tax deduction for —

- the costs (legal, etc) of setting up an approved ESOT, and
- contributions to the trustees of an approved ESOT,
- dividend income accruing to the trustees of an approved ESOT is exempt from the income tax surcharge in respect of the undistributed income of discretionary trusts, and
- the trustees of an approved ESOT are exempt from capital gains tax on any gain arising on the disposal of securities where those securities are transferred to the trustees of an Approved Profit Sharing Scheme (APSS).

Details

Application

This section applies to an employee share ownership trust (ESOT) which the Revenue Commissioners have approved as a qualifying employee share ownership trust and in respect of which such approval has not been withdrawn. The Revenue approval is made in accordance with **Schedule 12**. **Schedule 12** contains the rules governing the approval process, the appointment of trustees, the eligibility of beneficiaries and the functions of trustees. (1)

Deduction for cost of establishing an ESOT

A corporation tax deduction may be claimed by a company in an accounting period for the cost of — (2)

- setting up an approved ESOT,
- contributions to the trustees of the approved ESOT where the company or a company it controls has employees who are beneficiaries under the ESOT and those contributions are expended by the trustees during the expenditure period on one or more of the qualifying purposes.

Where such expenditure is incurred by a company carrying on a trade the deduction is given in computing the profits or gains of the trade carried on by that company.

Where such expenditure is incurred by a management or an assurance company, it is added to the company's management expenses.

If an approved ESOT is established later than 9 months after the end of the accounting period in which the establishment costs are incurred, then such costs are treated as having been incurred in the accounting period in which the ESOT is established and not in the accounting period in which the establishment costs are actually incurred. (3)

A company controls another company if the company can — (4)

- control the other company's affairs,
- acquire the greater part of the other company's share capital or voting power,
- acquire such part of the issued share capital of the other company that would entitle it to the greater part of the distributable income of the company, or
- acquire such rights as would, in the event of a winding up entitle the company to the greater part of the assets on a winding up.

Qualifying purposes in relation to expenditure of contributions by trustees of an ESOT are — (5)(a)

- acquiring shares in the company which established the trust,
- repaying borrowings,
- paying —
 - interest on borrowings

- a sum to a beneficiary of the ESOT,
- sums or transferring securities to the personal representatives of a deceased beneficiary,
- expenses.

The expenditure period in relation to expenditure of contributions by trustees of an ESOT on qualifying activities is the 9 months period starting from the end of the accounting period in which the sum is expended or such longer period as agreed by the Revenue Commissioners. (5)(b)

First-in-first-out basis

For the purposes of this section, the trustee of an ESOT are treated as applying the sums, paid to them by the company, on a first-in-first-out basis, irrespective of the number of companies making the payments. (6)

Exemption from income tax on dividends

The trustees of an approved ESOT are exempt from income tax on dividends received in respect of securities held in the trust if and to the extent that the income is spent by the trustees in an expenditure period on one or more qualifying purposes. (Both the “expenditure period” and “qualifying purposes” are defined in **paragraph 13** of **Schedule 12**). (7)

Exemption from capital gains tax on sale of securities

The trustees of an ESOT are exempt from capital gains tax on any gains arising from the sale of securities on the open market or the redemption of securities if and to the extent that such proceeds are used— (7A)

- to repay monies borrowed by those trustees,
- to pay interest on such borrowings, or
- to pay a sum to the personal representatives of a deceased beneficiary.

Exemption from capital gains tax on transfer of shares

A chargeable gain does not arise on the transfer of securities by the trustees of an approved ESOT to the trustees of an APSS. (8)

No chargeable gain shall accrue to the trustees of an approved ESOT on the transfer of any securities to the personal representatives of a deceased beneficiary. (8A)

The receipt of any sum of money or securities by the personal representatives of a deceased beneficiary from the trustees of an approved ESOT shall be exempt from income tax. (8B)

Withdrawal of reliefs

Where the Revenue Commissioners withdraw approval of an ESOT, the reliefs provided by the section cease to apply in relation to that ESOT from the effective date of the withdrawal. (9)

Definitions

For the purposes of **section 519**, a “deceased beneficiary” means a person who at the time of his/her death was— (10)

- (a) eligible to be a participant in an APSS had securities been available to distribute, and
- (b) was a beneficiary of the ESOT, the trust deed of which provided for the transfer of

securities to the APSS referred to in (a).

CHAPTER 3

Approved savings-related share option schemes

519A Approved savings-related share option schemes

Summary

This section provides an individual with an exemption from income tax on the receipt of the granting of the right and the exercise of the right to obtain shares in his or her employing company under an approved savings-related share option scheme. The shares must be paid for out of proceeds of a certified contractual savings scheme.

Details

Application

The section applies where an individual, being an employee or director by reason of his office or employment in a company, obtains a right to acquire shares in that company or another company and the right is obtained in accordance with the provisions of a savings-related share option scheme approved by the Revenue Commissioners on or after the 6 April, 1999 under ***Schedule 12A*** and in respect of which approval has not been withdrawn. (1)

No tax will be charged on receipt of the right referred to in ***subsection (1)***. (2)

Subject to exceptions outlined in ***subsection (4)***, income tax that would otherwise be due under the Tax Acts will not be chargeable on any gain realised by exercising the right. (3)

Where a “relevant body” is used to acquire scheme shares which will ultimately be passed on to the employee the following provisions apply: (3A)

(a) when shares are disposed of to an individual who is a member of the share scheme by a “relevant body”, no chargeable gain or allowable loss shall accrue to the “relevant body” (the trust or subsidiary company established to acquire the shares) in respect of that disposal, and the individual will be regarded as having acquired the shares at the price paid, and

(b) for this purpose and ***section 519B*** —

“relevant body” means a trust or company which exists to acquire and hold scheme shares.

“scheme shares” has the same meaning as in ***paragraph 10 of Schedule 12A***.

The effect of these provisions is that the employee is in exactly the same tax position as would arise if the company operating the scheme transferred newly issued shares directly to the employee without using a “relevant body” as an intermediary.

The tax relief outlined in ***subsection (3)*** does not apply where the right being exercised is exercised within 3 years of the right being granted and has become exercisable for one of the following reasons: (4)

- a person gaining control of the company (a take over) following a general offer to acquire the whole of one or more classes of the company’s shares,
- the amalgamation or reconstruction of the company under a scheme sanctioned by the court under section 201 of the Companies Act, 1963,
- a person becoming bound or entitled to acquire shares in the company under section 204 of the Companies Act, 1963,
- a resolution being passed for the winding up of the company,

- the sale out of the group of the company for which the option holder worked, or
- the sale out of the group of the business or part of a business in which the option holder worked.

The term “savings-related share option scheme” takes its meaning from *Schedule 12A*. (5)

519B Costs of establishing savings-related share option schemes

Summary

The cost of setting up a savings-related share option scheme is allowable as a deduction for corporation tax purposes. However, the cost to a company of enabling a “relevant body” to acquire scheme shares is not deductible.

Details

Subject to *subsection (2A)*, the cost incurred, on or after the 6 April, 1999, in establishing a savings-related share option scheme approved by the Revenue Commissioners in accordance with *Schedule 12A* and under which no employee or director has obtained rights prior to such approval is an allowable deduction in computing the profits or gains of a trade carried on by that company. (1)

Where such expenditure is incurred by a management or an assurance company, it may be added to its management expenses for the purpose of providing relief to such a company in respect of the sums in question. (2)

A corporation tax deduction is not, however, available for expenses incurred by a company in enabling a “relevant body” to acquire scheme shares. (2A)

If approval for the savings-related share option scheme is given later than 9 months after the end of the accounting period in which the sum is expended, then the sum is treated as expended in the accounting period in which the approval is given and not in the accounting period in which the sum is expended. (3)

519C Interest, etc under certified contractual savings schemes

Summary

This section provides relief from income tax on an individual’s savings under a certified contractual savings scheme used only in conjunction with a savings-related share option scheme approved by the Revenue Commissioners in accordance with *Schedule 12A*. It also exempts a relevant deposit taker (within the meaning of *section 256*) from having to deduct DIRT at source from that individual’s savings.

Details

Definitions

“qualifying savings institution” specifies the financial institutions with whom individuals may save under certified contractual savings schemes. It includes branches in the State of all licensed banks and certain other institutions excluded from the requirement to hold a licence from the Central Bank, such as building societies, trustee savings banks, the Post Office Savings Bank and credit unions. It also includes branches in the State of financial institutions who hold a licence or other similar authorisation under the law of another Member State of the EEA which corresponds to a licence from the Central Bank. Qualifying savings institutions also includes credit institutions authorised outside the EEA who are authorised to operate a branch in the State. Other financial institutions may be added by an order of the Minister for Finance. (1)

“EEA Agreement” means the Agreement on the European Economic Area signed at Opporto on 2 May 1992, as adjusted by all subsequent amendments to that Agreement.

“EEA state” means a state which is a contracting party to the EEA Agreement.

Any terminal bonus or interest paid by a qualifying savings institution to an individual on or after 6 April 1999 under a certified contractual savings scheme is exempt from income tax and is not to be included in computing an individual’s total income for the purposes of the Income Tax Acts. (2) & (6)

Any terminal bonus or interest paid by a qualifying savings institution under a certified contractual savings scheme is not, where the qualifying savings institution is a relevant deposit taker within the meaning of *section 256*, treated as relevant interest and therefore is not subject to a deduction of tax at source under *section 257*. (3)

A certified contractual savings scheme is a scheme — (4)

- providing for periodical contributions to be made by individuals for a specified period to a qualifying savings institution,
- where those individuals are eligible to participate, that is to obtain and exercise rights under an approved savings-related share option scheme and whose contributions under the scheme are to be used in accordance with the provisions of *paragraph 17 of Schedule 12A*, and
- which is certified by the Revenue Commissioners as qualifying for exemption under the section according to requirements specified by the Minister for Finance in accordance with the provisions of *Schedule 12B*.

Schedule 12B contains supplementary provisions in relation to the section. (5)

CHAPTER 4

Approved Share Option Schemes

Overview

Chapter 4 of *Part 17* relates to Revenue approved share option schemes under which employees are given options to purchase shares in their employer company at a pre-determined price and can make a gain where they purchase shares that have increased in value since the option was granted.

519D Approved share option schemes

Summary

Up to 24 November 2010 (date of publication of National Recovery Plan), this section provided for tax relief in respect of share options granted to employees under schemes approved by the Revenue Commissioners. The approval of such schemes and the conditions which must have been satisfied before such approval could be given are set out in *Schedule 12C*. Under an approved share option scheme the normal charge to income tax at the date of exercise of the option did not apply and, instead, the employee was chargeable to capital gains tax on the full gain (i.e. the difference between the amount paid for the shares and the amount received) on a disposal of the shares. To qualify for this favourable treatment a period of at least 3 years must have elapsed between the date of the grant of the option and the date of any subsequent sale of the shares. All gains arising, or options to acquire shares received, on or after 24 November 2010 are chargeable to income tax regardless of whether a scheme received Revenue approval, or that options to acquire shares were received, before that date.

Options that had been granted before the scheme was approved by the Revenue

Commissioners also qualified for the relief provided the scheme was approved before 31 December 2001 and that at the time of the grant and exercise (if prior to approval) the scheme would have been capable of being approved had the legislation been in force at those dates.

Details

The provisions of this section will apply where an individual obtains an option to acquire shares in a company— (1)

- (a) by virtue of an employment or directorship in that company, or another company, and
- (b) the individual obtains the option to acquire shares under a share option scheme approved under *Schedule 12C* and which approval has not been withdrawn.

Tax will not be chargeable, under any provision of the Tax Acts, in respect of the receipt of an option referred to in *subsection (1)*. Previously, such a charge could have arisen in certain circumstances i.e. where the option received is not exercisable for at least 7 years. This is subject to *subsection (8)* which disapplies this tax exemption in respect of options that are received on or after 24 November 2010. (2)

Subject to *subsection (4)*, where an individual exercises the option granted under the terms of an approved scheme at a time when the scheme is approved, tax will not be chargeable under the provisions of the Tax Acts in respect of any gain realised on the exercise of the option. In these circumstances, the base cost for capital gains tax will be the acquisition cost rather than the market value at date of acquisition. This is subject to *subsection (9)* which disapplies this tax exemption in respect of any gain realised on or after 24 November 2010. (3)

A condition is imposed that the exemption granted on the exercise of the option, as set out in *subsection (3)*, does not apply in the case where shares, acquired by the exercise of an option, or shares which are exchanged for those shares in a take-over, are disposed of by the individual within a period of 3 years of the date of the grant of the option. (4)

Where a company uses “a relevant body” (i.e. a dedicated trust or subsidiary company) to acquire and hold the “scheme shares” (for example, existing shares which the company cannot legally buy itself) that trust or company will not be liable to capital gains tax on any disposal of such shares to the employees under the terms of the scheme. Arising from this, the “base cost” to the employees for capital gains tax purposes of the scheme shares is set at the price actually paid for them – the same as would be the case if the employee acquired the shares directly from the company. Without this provision, the insertion of trust/subsidiary company between the employer company and the employee would result in the employee being able to use the possibly higher market value as his or her base cost. In addition, the company is not entitled to a corporation tax deduction in respect of any expenses (e.g. discounts on shares) incurred by it in enabling the trust/subsidiary company to acquire scheme shares. Both these conditions are to ensure that both the employee and the company are in exactly the same position as they would have been had the trust / subsidiary company not been used. (5)(a)

The terms “relevant body” and “scheme shares” are defined for the purposes of *subsections (5) and (6)*. (5)(b)

Where a company incurs costs in establishing a share option scheme approved by the Revenue Commissioners in accordance with *Schedule 12C* and, subject to *subsection (7)*, under which no employee or director has obtained options prior to such approval, such costs are allowable as a deduction in computing the profits or gains of a trade carried on by a company, or where incurred by a management or assurance company, may be added to its management expenses for the purposes of computing the company’s (6)(a)& (b)

profits for corporation tax purposes.

No deduction is available under any provision of the Tax Acts (including this provision) for expenses incurred in enabling a relevant body to acquire scheme shares. (6)(c)

If approval is given for the share option scheme later than 9 months after the end of the accounting period in which the sum was expended, then the sum is treated as being expended in the accounting period in which the approval is given and not in the period in which it is expended. (6)(d)

Where a share option scheme is approved and, prior to such approval, an individual obtained an option under the scheme which meets the conditions of *paragraph (b)* of this subsection then that option will be treated as an option obtained under an approved scheme. (7)(a)

The conditions referred to are that: (7)(b)

- (i) the option was exercised on or after 15 February 2001, and
- (ii) the scheme was approved on or before 31 December 2001, and at the time the option was obtained or exercised (if exercise occurred before the date of approval), that the scheme would have been approved under *Schedule 12C* if that Schedule had been in place at the time the option was obtained.

The tax exemption given by *subsection (2)* does not apply in respect of rights to acquire shares where such rights are received on or after 24 November 2010. (8)

The tax exemption given by *subsection (3)* does not apply in respect of any gain realised by the exercise of an option on or after 24 November 2010. (9)