

Vermilion:

Where are the grey areas on whether share options are granted ‘by reason of employment’?

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Legislation

- ITEPA03, section 421B:

‘(1) Subject as follows (and to any provision contained in Chapters 2 to 4A) those Chapters apply to securities, or an interest in securities, acquired by a person where the right or opportunity to acquire the securities or interest is available **by reason of an employment of that person** or any other person.’

NB: ‘any other person’ – statutory anti-re-direction provision.

Legislation (2)

- Section 421B(3):

- ‘(3) A right or opportunity to acquire securities or an interest in securities ***made available by a person’s employer***, or by a person connected with a person’s employer, is to be regarded for the purposes of subsection (1) as available by reason of an employment of that person unless—
- (a) the person by whom the right or opportunity is made available is an individual, and
 - (b) the right or opportunity is made available in the normal course of the domestic, family or personal relationships of that person.’

NB: an individual > not by employer.

Vermilion Holdings Limited v. HMRC

- First-tier Tribunal [2019] S.F.T.D. 815 – win for taxpayer
- Upper Tribunal [2020] S.T.C. 1366 – win for HMRC
- Court of Session (Inner House) [2021] S.T.C. 1874 – win for taxpayer
- Supreme Court [2023] UKSC 37 – win for HMRC

Facts

- Mr Noble advised Vermilion re obtaining investment
- Paid partly in cash and partly in share options – same for solicitors who advised on investment
- More investment required
- Various conditions, including reduction in share options and appointment as chairman, at specified salary
- Solicitors also required to reduce options by same amount
- New Finance Director got no options – same salary as Mr Noble
- Reduction achieved not by amending / waiving existing options – instead, existing options cancelled and new ones on essentially identical terms issued
- Per Supreme Court – different class of shares? But no difference economically
- Also for ten years > extended period

Issues

- Section 471 ITEPA03 – same wording as section 421B
- Subsection (1) – right or opportunity to acquire options available ‘by reason of employment’ of Mr Noble?
- Subsection (3) – right or opportunity to acquire options ‘made available by’ Mr Noble’s employer?
- FTT – HMRC relied only on ‘made available by’ test
- UT – HMRC sought to add in case on ‘by reason of employment’ test – allowed to do so – won on that test
- Court of Session – HMRC relied on both – taxpayer won on both
- Supreme Court – HMRC relied on both – won on ‘made available by’ – ‘by reason of employment’ test not considered

Decision

- Purpose of ‘made available by’ rule > avoid having to determine issues of causation arising within ‘by reason of employment’ test
- NB – very narrow view of purpose of the provision – overlooking overall purpose of provisions of which it is a part, which is to tax remuneration from employment as employment income, but not tax other gains that may be related to employment as employment income
- Decision (para 24):
- ‘In this case the correct question was: did Vermilion confer the 2007 option on Mr Noble’s nominee while Mr Noble was its employee? The answer is that it did.’
- Not ‘absurd, unjust or anomalous’
- *Price v. HMRC* [2013] UKFTT 297 (TC) > focus on specific transaction by which individual acquired right or opportunity

‘By reason of’

- Previous case-law:
 - *Wicks v. Firth* [1982] Ch. 355 - what is it that enables the person concerned to enjoy the benefit?
 - *Mairs v. Haughey* [1992] S.T.C. 495 – payment for loss of redundancy rights on transfer of employment
 - *Wilcock v. Eve* [1995] S.T.C. 18 – *ex gratia* payment to compensate for loss of opportunity to buy shares when employer sold out of group
 - *Charman v. HMRC* [2022] 1 W.L.R. 2277 – share for share exchange on re-organisation of group

Consequences

- If share option / other security issued by employer directly to employee, within ERS provisions – why it was issued / background to issue seems to make no difference
- Per Supreme Court – this is because intention is to relieve HMRC / courts of having to consider questions of causation
- Replacement options / securities?
- Rights issues?
- Bonus issues?
- What if listed plc and shares originally bought in open market?
- Exception for domestic / family / personal relationships?
- Founder shares?

Where is left for ‘by reason of’?

- Still important in other areas
- Phrase appears 230 times in ITEPA03
- Important examples >
 - expenses payments (s. 70) – but paid by employer enough (s. 71)
 - cash vouchers (s. 73(1)) – but enough if provided by employer (s.73(2))
 - same for non-cash vouchers (s. 82), credit-tokens (s. 90), living accommodation (s. 97), and residual benefits (s. 201), including scholarships (s. 212)
 - cars and vans (s. 114) – but enough if made available by employer (s. 117)