Award schemes | Jersey income tax practice note

With effect from 1 January 2023

Absent specific law determining otherwise, the taxation of officer and employee share award schemes, including share option schemes, follows the principles laid out in UK tax cases such as *Abbott v Philbin 39 TC 82*.

In summary, this means a non-cash award is subject to Jersey income tax when an employee is given an award by an employer that creates an enforceable right that can be 'turned to pecuniary account' (in other words turned to cash). For many awards, the enforceable right occurs at the time the award is entered into by the employee i.e. at grant of the award.

Once the tax point of the award has been established, the employer must then determine the arms-length value of the award at that time. For vanilla awards where there is an established market for the underlying asset e.g. shares listed on FTSE250 or TISE, the arms-length value of the award is relatively easy to determine. In all other cases, Revenue Jersey will generally accept award valuations determined by suitably qualified specialists.

However, Revenue Jersey recognises that the terms of some awards include conditions that, whilst appropriate to support the commercial aims of the employer, add significant complexity to the valuation exercise. Recognising this challenge, when a request for a ruling is made in respect of an award scheme, Revenue Jersey will not generally challenge the tax point of an award in the following circumstances:

Scheme mechanism	**Revenue Jersey will accept without further enquiry the tax point of the award as being:**
Scheme is either cash-based, or some or all of the award can be converted to cash at any time from award up to and including vesting Example – employee is granted share options but the scheme allows the employee and/or employer to satisfy the award with cash equal to the value of those shares	Cash element – follow principles of Article 65A Income Tax (Jersey) Law 1961
Scheme creates a right to receive an asset and that right can only be altered or withdrawn if the employee does not behave in an expected/ reasonable way for the duration of the scheme Example - a share option scheme is created where the number of shares exercisable by the employee can be reduced or forfeited if the employee is a 'bad leaver', does not follow agreed risk management procedures and/or exceeds agreed proprietary trading limits. These conditions do not delay the tax point to vesting since, by acting in a reasonable manner, it is within the employee's power to meet those conditions	When the parties enter into the scheme agreement

Scheme creates a right to receive an asset when conditions are met that are outside the direct/immediate sphere of influence of the employee Example - employer will give an employee 100 shares in a year's time if the employer's overall and/or employee's divisional Earnings Before Interest, Taxes, Depreciation and Amortisation ('EBITDA') growth in that period exceeds 10%. Although the employee can help to influence EBITDA, he/ she cannot influence that performance measure on their own	When conditions are met

For the avoidance of doubt, this note does not dispense with the requirement for the employer to value an award at the time of the tax point.

Sundry points

What is the 'right' referred to

This is a clause or series of clauses in any agreement/contract between employer and employee under which the employee could sue the employer for non-performance of the award by the employer. Subject to the table above, this is not generally when the employee has an indefeasible right in respect of the underlying asset.

Vesting

Arises when the employee is eligible to take beneficial ownership of the award asset. This is not necessarily the same time as when the employee takes actual beneficial ownership (e.g. on exercise of share options).

Payment made to enter into the award and/or payment on vesting

Payments that must be made by the employee as part of their entitlement to the award are deductible costs in arriving at the benefit in kind amount.

For example, with a share option agreement, to arrive at the taxable benefit in kind value, the employee can deduct from the pecuniary value of the award any payment the employee makes on grant of the option plus any amount payable on exercise of the option.

Valuations

Revenue Jersey does not confirm valuations provided by taxpayers. We assume valuations provided to us are honest and fair having regard to the Customers' Charter.

Should Revenue Jersey receive information that calls into question a valuation provided by a taxpayer, we may instruct a specialist valuer to confirm that valuation and, if considered appropriate, revisit the quantum of benefit in kind disclosed to us (within normal statutory time limits). Please also see Revenue Jersey Code of Practice on Interventions in the event that an intervention leads to an increase in the taxable benefit in kind arising.

'Flowering' rights

Some assets have rights attaching to them that increase over time (i.e. they 'flower'). For example, at the time of grant of a share option, the underlying shares might have no rights to dividends or to vote in general meetings but these rights are engaged by the time the option vests. Ordinarily, shares with no rights to dividends or votes will be worth less than shares with those rights attaching. Any valuation of an award where the tax point is different to the time that the award vests should value that award based on the assumption that all of the *expected* rights at the time of vesting will materialise e.g. if a share option uses 'flowering shares' as per the above example and the additional rights accrue through the simple passage of time, the valuation should be based on shares with full dividend and voting rights, not the value at grant where no rights attached to the shares.

Discounts

The valuation of the award should not take account of the time between grant of award and vesting or exercise. Therefore, 'time value' discounts will not generally be allowed.