

Foskett Panel Awards

HMRC's view on the tax treatment of your compensation received from Lloyds Banking Group

Introduction

We're sending this paper with your Final Decision. It explains HMRC's view on how to treat your compensation award, for tax purposes. You may have to pay tax on any amounts you've received. This will depend on:

- the type of compensation you've been awarded; and
- your personal circumstances.

The Foskett Panel was set up to reassess the direct and consequential losses suffered by victims of the fraud committed at the HBOS Impaired Assets unit based at Reading and Bishopsgate.

HMRC has discussed this paper with the Foskett Panel but this paper does not constitute advice from them, or HMRC.

This paper lists all 19 types of compensation awards and gives HMRC's view of the tax treatment for each one.

If you have any questions about this paper after speaking to your advisor, please contact your customer compliance manager (if you have one) or email aneesah.aziz@hmrc.gov.uk.

If you have any health or personal circumstances that may make it difficult for you to deal with us, we may be able to offer further help. For more information, go to www.gov.uk/get-help-hmrc-extra-support/ or GOV.UK and search 'HMRC extra support'.

Tax treatment

Below, HMRC has set out its view of the tax treatment for the different types of award. The tax treatment covers how the amount of tax is calculated. In some cases, it also covers how tax is to be collected. For some taxes, Lloyds Banking Group (“the Bank”) has a duty to collect some amounts by deducting those amounts from the relevant part of your award.

In setting out our view below, we refer to parts of the Income Tax (Earnings and Pensions) Act 2003 (abbreviated as “ITEPA”), the Income Tax (Trading and Other Income) Act 2005 (abbreviated as ITTOIA), the Taxation of Chargeable Gains Act 1992 (“TCGA92”) and Extra-Statutory Concession D33 (“ESC D33”).

1. Type of award: Compensation for the loss, or reduction, of salary and/or other remuneration, if you were employed in a damaged business (or hypothetical business) or prevented from being employed in another business as a result of the fraud.

HMRC’s view: Compensation you’ve received for loss of income, may have to be taxed as Employment Income if you were an employee or director of the business to which your award relates. The Foskett Panel may have described this loss as “loss of salary” in your award decision.

Such an award will still be taxed as Employment Income even if the compensation was paid by a third party and/or you were no longer employed by the damaged business when you received it.

Your award may be considered as Employment Income if it constitutes:

- earnings, within section 62 of the ITEPA (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim00515>) or
- a termination payment, within section 401 of the ITEPA (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim12800>).

The Bank may have deducted Income Tax and National Insurance contributions from the part of your award that constitutes Employment Income, under Pay As You Earn (PAYE).

For Employment Income purposes, compensation should derive its character from the nature of the payment it replaces (see, for example, the case of “Mairs v Haughey” (1993 BTC 339)). In other words, if the original payment would have

been taxable as earnings, so is the compensation (and vice versa). This is known as ‘the replacement principle’.

As a result, if any part of your award replaces any earnings you should have received from the employment but did not, because of the fraud, it must be taxed as earnings from that employment, under section 62 of the ITEPA. This includes:

- earnings that you’d already earned but were not paid, as a result of the fraud; and
- if you remained an employee of the same business after the fraud, but your earnings were lower than they would otherwise have been.

‘Earnings’ includes all wages, salary, and bonuses (as well as any other “benefits” that are in the form of money, or have monetary value to the recipient).

If part of your award replaces earnings that you lost as a result of the termination of your employment (for any reason, including the cessation of the business), then that part will be taxable as a ‘termination payment’ within section 401 of the ITEPA. This applies to amounts which you would have earned had you continued in the employment, rather than amounts that relate to periods where you were actually an employee (which would instead be taxable as earnings).

However, as explained below, section 401 of the ITEPA will not apply to the extent that the award relates to amounts that you could have received from a hypothetical employment which you might have held if not for the fraud.

Section 401 of the ITEPA will apply if your award is directly or indirectly connected to the termination of the employment. This is a phrase of very wide scope (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim13012>). However, if your award is earnings within the definition at section 62 of the ITEPA, then it will not be subject to section 401 of the ITEPA, as section 62 has priority (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim12810>).

If part of your award is taxable under section 401 of the ITEPA (and does not fall within section 62) then that part will only be taxed to the extent that it exceeds £30,000 (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim13505>). Please note: You must add your award amount to any other termination payments you’ve received for the same employment, if applying the £30,000 ‘threshold’ (see <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim13530>).

If your award has been determined on the assumption that you would have remained in employment to a particular date, if not for the fraud, the compensation you receive should be apportioned on a just and reasonable basis between the period during which you were actually employed and the period during which you were not employed (but would have been, if not for the fraud). You'll find an example on how to carry out this apportionment below.

Any amounts which constitute earnings for Income Tax purposes will also be subject to Class 1 National Insurance contributions. Amounts that are termination payments will not be subject to National Insurance contributions.

The Foskett Panel may have considered a number of counter-factual scenarios to determine your award. You may have to pay Income Tax as Employment Income if, and to the extent that, your award relates to a specific employment which you held in the past. If, however, part of your award relates to amounts that could have been derived from a hypothetical employment that you never actually held (for example, if the Panel considers that you may have launched a separate successful business, if not for the fraud) then that part won't be considered as Employment Income.

However, amounts which relate to a hypothetical scenario, will be subject to Income Tax as Miscellaneous Income. Miscellaneous income, also referred to as the "sweep up provision", taxes amounts which are income but are not specifically within the scope of another part of the income tax rules. Amounts which are taxed as miscellaneous income are taxed under Part 5 of the ITTOIA (as to which see page 6 below).

If your award has been determined in relation to both an actual historic employment and a hypothetical alternative employment, your award should be apportioned (on a just and reasonable basis) between:

- amounts that relate to your historical employment (which will be taxable as Employment Income); and
- amounts that relate to the hypothetical employment (which will be taxable as Miscellaneous Income).

Similarly, if you were a shareholder as well as an employee of the company to which your award relates, you should apportion the award between:

- the part which relates to lost Employment Income (which may be taxable as earnings or a termination payment, as described above); and
- the part which relates to the value of those shares or any dividends (as to which see pages 7 and 8 below).

HMRC would expect any apportionments you carry out for tax purposes to be consistent with any workings the Foskett Panel have done to determine the amount of your award.

Example 1 – Employment Income

From November 2006 to April 2007, you were employed as manager of a business that was affected by the fraud. Your employment was terminated in May 2007 as a result of the fraud.

Compensation is assessed from the period November 2006 to November 2018. You receive £900,000 as compensation for ‘net loss of salary income’.

This is described by the Foskett Panel as the “adjusted loss after chance applied.” It reflects the Panel’s assessed probability of the loss arising. It’s the net loss, after deducting the salary you actually received over the period.

The £900,000 consists of:

- First Amount - £480,000 salary for the period November 2006 to November 2018, from the damaged business (comprising both the periods:
 - November 2006 to April 2007 (6 months) during which you were an employee; and
 - May 2007 to November 2018 (138 months) during which the Foskett Panel considers you may have been an employee, if not for the fraud).
- Second Amount - £420,000 salary for the period November 2013 to November 2018 (60 months), which the Panel consider you might have received from a hypothetical alternative business.

First Amount - £480,000 Salary Compensation Amount

The £480,000 amount should be apportioned between the period in which you were an employee of the business (November 2006 to April 2007), and the period after the termination of that employment (May 2007 to November 2018) as follows:

Earnings - section 62 of the ITEPA

The award in our example has been calculated for the period of 144 months from November 2006 to November 2018. In this period, you were an employee for 6 months from November 2006 to April 2007.

So, the amount relating to the period in which you were an employee is:

$$£480,000 \times 6 \text{ months} / 144 \text{ months} = £20,000$$

This amount will be taxed as earnings from the employment. It will also be subject to Class 1 National Insurance contributions.

Termination payment - section 401 of the ITEPA

The award in our example has been calculated for the period of 144 months from November 2006 to November 2018. Your employment was terminated in April 2007, you were not an employee of the damaged business for the 138 months from May 2007 to November 2018.

So, the amount relating to the period after the termination of the employment is:

$$£480,000 \times 138 \text{ months} / 144 \text{ months} = £460,000$$

The amount that exceeds £30,000 (£460,000 less £30,000 is £430,000) will be taxed as a termination payment. It will not be subject to National Insurance contributions.

Second Amount - £420,000 Salary Compensation Amount

The £420,000 element is not taxable as Employment Income, because it does not relate to an actual employment or office held by you. Instead, this amount will be taxed as Miscellaneous Income.

For the avoidance of doubt, to the extent that income received under this heading is not otherwise charged to Income Tax, it will be taxed as Miscellaneous Income.

2. Type of award: Compensation for the loss of, or reduction in, pension benefits or the value of a pension pot, if you were employed in a damaged business (or hypothetical business) or prevented from being employed in another business as a result of the fraud.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

However it is likely that paragraph 11 of ESC D33 applies. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

3. Type of award: Compensation for the loss of, or reduction in, dividends and/or other distributions, if a shareholder of a company (or hypothetical company) with a direct or indirect interest in a damaged business (or hypothetical business).

HMRC's view: This type of award will be 'revenue' in nature and taxed as Miscellaneous Income.

4. Type of award: Compensation for bank fees, default interest and charges, and interest charges on alternative borrowings.

HMRC's view: This type of award will be 'revenue' in nature. If you claimed these as a taxable deduction when working out the taxable profits of the business, or you claimed tax relief for the costs, then these compensation payments will be taxed as Miscellaneous Income.

Otherwise, amounts you receive under this heading will not be taxed.

5. Type of award: Compensation for the loss of, or reduction in, interest, if a provider of debt to an entity (or hypothetical entity), with a direct or indirect interest in a damaged business (or hypothetical business).

HMRC's view: This type of award will be 'revenue' in nature and will be taxed as Miscellaneous Income.

6. Type of award: Compensation for the loss of, or reduction in, share of profits, if the direct owner or co-owner of a damaged business (or hypothetical business).

HMRC's view: This type of award will be 'revenue' in nature and will be taxed as Miscellaneous Income.

7. Type of award: Compensation for the loss of, or reduction in, the value of shares, if a shareholder of a company (or hypothetical company) with a direct or indirect interest in a damaged business (or hypothetical business).

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

You have suffered a loss in connection with an underlying chargeable asset: the shares. As explained in paragraph 9 of ESC D33 this amount is taxed to Capital Gains Tax as it is derived from the shares. A proportion of the allowable costs of the shares may be deducted in calculating the gain chargeable to Capital Gains Tax as it will be a disposal or part-disposal of those shares. For more information about part-disposals please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg12730p>.

Even if you receive the compensation for shares that you no longer hold, paragraph 9 of ESC D33 will apply. When you stopped owning the shares, it's likely that you already used any allowable costs of the shares in the Capital Gains calculation, even if no tax was due because any gain was below that year's annual exempt amount. This means it's unlikely that you will be able to deduct any allowable costs and your compensation is likely to produce a gain.

If you receive compensation (under this type of award), in relation to a hypothetical company or business, paragraph 11 of ESC D33 applies. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

8. Type of award: Compensation for the loss of, or reduction in, the value of debt, if a provider of debt to an entity (or hypothetical entity) with a direct or indirect interest in a damaged business (or hypothetical business).

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

As explained in paragraph 9 of ESC D33 the sum received is derived from the debt and the tax treatment will depend on whether that debt was a chargeable asset for Capital Gains Tax purposes.

Even if the debt has been repaid, the treatment set out in paragraph 9 of ESC D33 will apply.

There's more guidance about ESC D33 at the end of this paper.

Your award may be exempt from tax, under section 251 of the TCGA92, if the original debt would have been exempt from tax under this section.

Section 251 of the TCGA92 states that most debts are exempt from Capital Gains Tax except in the case of a debt on security. If a debt is capable of being held as an investment, and sold at a profit, it is likely to be a debt on a security. Debts on securities are, however, a complex area. For more information please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg53400p>.

9. Type of award: Loss of, or reduction in, the value of a business, if the direct owner or co-owner of a damaged business (or hypothetical business).

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

You will need to consider ESC D33 and determine whether paragraph 9 of ESC D33 or paragraph 11 of ESC D33 applies.

If your award is derived from the loss of, or damage to, an underlying chargeable asset, the treatment in paragraph 9 of ESC D33 applies. A proportion of the allowable costs of the underlying chargeable asset may be deducted in calculating the gain chargeable to Capital Gains Tax as the sum received is treated as a disposal or part-disposal of the underlying chargeable asset. For more information about part-disposals please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg12730p>.

If you've received compensation and there is no underlying chargeable asset, paragraph 11 of ESC D33 applies. This may apply if you receive compensation (under this type of award) in respect of a hypothetical company or business or, where there were no chargeable assets held by the business. If paragraph 11 of ESC D33 does apply this may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

10. Type of award: Compensation for costs incurred (not giving rise to a corresponding asset), including professional fees, that would have been avoided if the fraud had not occurred.

HMRC's view: If you claimed these costs as a tax deduction, when working out the taxable profits of your business, your award will be subject to Income Tax, as it's Miscellaneous Income.

If you did not claim these costs as a tax deduction when working out the taxable profits of your business, this part of your award is a 'capital' sum. Accordingly, it

will not be chargeable to Income Tax. However, you may be liable to pay Capital Gains Tax on any gains made.

To work out the correct tax treatment, you'll need to identify exactly what costs your award relates to. If your award relates to different types of costs that you've incurred, section 52(4) of the TCGA92 requires that compensation for those costs be apportioned for tax purposes, on a just and reasonable basis. For more information please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg14771>.

HMRC would expect any apportionments you carry out for tax purposes to be consistent with any workings the Foscett Panel have done to determine the amount of your award.

If the costs that you have incurred are an allowable cost under section 38 of the TCGA92, you will be allowed to deduct these costs when calculating your gain.

If the Foscett Panel has awarded you compensation in respect of an underlying asset that is chargeable to Capital Gains Tax as well as an award for the costs associated with seeking that compensation, then the treatment described in paragraph 9 of ESC D33 will apply. You should include both sums in your calculation of the charge to Capital Gains Tax in respect of that asset as described in paragraph 9 of ESC D33. The following example shows when this may apply.

Example 2

You incurred £10,000 professional fees to try and receive compensation for the loss in value of shares that you still hold. You originally purchased the shares for £150,000.

You are subsequently awarded £50,000 compensation by the Foscett Panel because of the loss in value of the shares and this is treated in the way described in paragraph 9 of ESC D33. The agreed value of the shares when the compensation is received is £125,000. You are also awarded £10,000 compensation by the Foscett Panel to cover the cost of the professional fees.

The computation is as follows:

<i>Compensation for loss in value of shares</i>	<i>£50,000</i>
<i>Plus, compensation for associated professional fees</i>	<i>£10,000</i>
<i>Equals, total compensation</i>	<i>£60,000</i>
<i>Less, cost of professional fees*</i>	<i>(£10,000)</i>
<i>Less, part-disposal cost of shares: £150,000 x [£50,000 / (£50,000 + £125,000)]**</i>	<i>(£42,857)</i>

<i>Equals, total gain</i>	<i>£7,143</i>
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** We consider that the professional fees are an allowable cost under section 38 of the TCGA92 and can be deducted in full from the compensation that you have received.*

For more information about section 38 of the TCGA92 please see

<https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg15150p>.

*** The allowable cost should be apportioned by reference to:*

A = the compensation received for the loss in value of the shares, and

B = the value of the shares when the compensation is received

The calculation of the allowable cost is: cost of shares x A / (A+B).

For more information about part-disposals please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg12730p>.

You must pay Capital Gains Tax on the total gain amount if this is above the annual exempt amount (AEA). The AEA is set at £12,300 for individuals for 2022/23 and you pay tax on the total gains you receive in the year (less losses) that exceed this amount.

If the Foskett Panel has awarded you compensation which does not relate to an underlying asset which is chargeable to Capital Gains Tax as well as an award for the costs associated with seeking that compensation, this will fall under paragraph 11 of ESC D33. You should include both sums in your calculation of the gain that falls under paragraph 11 of ESC D33. The following example shows when this may apply.

Example 3

You incurred £10,000 professional fees to try and get compensation for additional taxation that you suffered as a result of the fraud.

You are subsequently awarded £50,000 compensation by the Foskett Panel because of the additional taxation that you suffered and this falls under paragraph 11 of ESC D33. You are also awarded £10,000 compensation by the Foskett Panel to cover the cost of the professional fees.

The computation is as follows:

<i>Compensation for additional taxation</i>	<i>£50,000</i>
<i>Plus, compensation for associated professional fees</i>	<i><u>£10,000</u></i>
<i>Equals, total compensation</i>	<i><u>£60,000</u></i>
<i>Less, cost of professional fees*</i>	<i>(£10,000)</i>
<i>Equals, total gain</i>	<i>£50,000</i>

** We consider that the professional fees are an allowable cost under section 38 of the TCGA92 and so can be deducted from the compensation that you have received.*

For more information about section 38 of the TCGA92 please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg15150p>.

The total gain will fall under paragraph 11 of ESC D33. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

If the Foskett Panel has awarded you compensation in relation to additional borrowing costs you suffered as a result of the fraud as well as associated costs incurred with restoring your credit record, then compensation you receive because of the additional borrowing costs and also any associated costs will fall under paragraph 11 of ESC D33. You should include both sums in your calculation of the gain that falls under paragraph 11 of ESC D33. The following example shows when this may apply.

Example 4

As a result of the fraud, you incurred additional borrowing costs due to a poor credit rating. You incurred £10,000 fees to restore your credit record.

You are subsequently awarded £50,000 compensation by the Foskett Panel because of the additional borrowing costs. You are also awarded £10,000 compensation by the Foskett Panel to cover the cost of the fees.

The computation is as follows:

<i>Compensation for borrowing costs</i>	<i>£50,000</i>
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<i>Plus, compensation for associated costs</i>	<u><i>£10,000</i></u>
<i>Equals, total compensation</i>	<u><i>£60,000</i></u>
<i>Equals, total gain</i>	<i>£60,000</i>

** We consider that the fees incurred (£10,000) are not an allowable cost under section 38 of the TCGA92 and so cannot be deducted from the compensation that you have received.*

The total gain will fall under paragraph 11 of ESC D33. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

11. Type of award: Compensation for the loss of certain other types of income (not dealt with under other types of award) that would have been received if the fraud had not occurred e.g. lost maintenance and child support payments.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

However it is likely that paragraph 11 of ESC D33 applies. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

12. Type of award: Compensation for assets lost or sold at undervalue, resulting in lost net benefits (net of the benefits obtained from the proceeds, if any) and/or lost value.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

In some cases, the asset for which you have received compensation may be exempted from Capital Gains Tax, so you'll first need to consider if your award is exempted from Capital Gains Tax under either:

- the chattels exemption, at section 262 of the TCGA92; or
- the wasting assets exemption, at section 45 of the TCGA92.

The word 'chattel' is a legal term meaning an item of tangible, movable property - something you can both touch and move. Your personal possessions will normally be chattels.

If your award is less than £6,000 and relates to a chattel, there will be no charge to Capital Gains Tax. If your award is more than £6,000 and relates to a chattel, the charge to Capital Gains Tax may be restricted.

A chattel which is a wasting asset will be exempt from Capital Gains Tax. An asset is 'wasting' if it is expected to last 50 years or fewer from the time you acquired it. Most chattels will be wasting assets. Exceptions would include jewellery and antique furniture.

For more guidance about these exemptions please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg76550subc> and <https://www.gov.uk/government/publications/chattels-and-capital-gains-tax-hs293-self-assessment-helpsheet>.

If neither of these exemptions apply to your award, you'll need to consider if there's a chargeable asset underlying your award.

As explained in paragraph 9 of ESC D33, if you can identify an underlying chargeable asset from which your award is derived, this amount is taxed to Capital Gains Tax.

Even if you receive the compensation for an underlying chargeable asset that you no longer hold, paragraph 9 of ESC D33 will apply. When you stopped owning the asset, it's likely that you already used any allowable costs of the asset in the Capital Gains calculation, even if no tax was due because any gain was below that year's annual exempt amount. This means it's unlikely that you will be able to deduct any allowable costs and your compensation is likely to produce a gain.

If your award cannot be linked to a chargeable asset, paragraph 11 of ESC D33 applies. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

13. Type of award: Compensation for assets sold at their market price that, with the benefit of hindsight, would have increased in value if they had continued to have been held, resulting in lost net benefits (net of the benefits obtained from the proceeds) and/or lost value.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made.

In some cases, the asset for which you have received compensation may be exempted from Capital Gains Tax, so you'll first need to consider if your award is exempted from Capital Gains Tax under either:

- the chattels exemption, at section 262 of the TCGA92; or
- the wasting assets exemption, at section 45 of the TCGA92.

The word ‘chattel’ is a legal term meaning an item of tangible, movable property - something you can both touch and move. Your personal possessions will normally be chattels.

If your award is less than £6,000 and relates to a chattel, there will be no charge to Capital Gains Tax. If your award is more than £6,000 and relates to a chattel, the charge to Capital Gains Tax may be restricted.

A chattel which is a wasting asset will be exempt from Capital Gains Tax. An asset is ‘wasting’ if it is expected to last 50 years or fewer from the time you acquired it. Most chattels will be wasting assets. Exceptions would include jewellery and antique furniture.

For more guidance about these exemptions please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg76550subc> and <https://www.gov.uk/government/publications/chattels-and-capital-gains-tax-hs293-self-assessment-helpsheet>.

If neither of these exemptions apply to your award, you’ll need to consider if there’s a chargeable asset underlying your award.

As explained in paragraph 9 of ESC D33, if you can identify an underlying chargeable asset from which your award is derived, this amount is taxed to Capital Gains Tax.

Even if you receive the compensation for an underlying chargeable asset that you no longer hold, paragraph 9 of ESC D33 will apply. When you stopped owning the asset, it’s likely that you already used any allowable costs of the asset in the Capital Gains calculation, even if no tax was due because any gain was below that year’s annual exempt amount. This means it’s unlikely that you will be able to deduct any allowable costs and your compensation is likely to produce a gain.

If your award cannot be linked to a chargeable asset, paragraph 11 of ESC D33 applies. This may mean that no Capital Gains Tax is payable.

There’s more guidance about ESC D33 at the end of this paper.

14. Type of award: Compensation for hypothetical assets that would have been purchased and, with the benefit of hindsight, would have increased in value if they had been acquired and held, resulting in lost net benefits (net of the benefits obtained from retaining the proceeds) and/or lost value.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made. So far as Capital Gains Tax is concerned, it will fall under paragraph 11 of ESC D33. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

15. Type of award: Compensation paid directly to a Trustee in Bankruptcy, corresponding to amounts owed to creditors.

HMRC's view: This type of award will be a 'capital' sum, so it will not chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made. So far as Capital Gains Tax is concerned, it will fall under paragraph 11 of ESC D33. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

16. Type of award: Compensation paid directly to a Trustee in Bankruptcy, corresponding to amounts owed to the Trustee in Bankruptcy, or that will become due to the Trustee in Bankruptcy, for the provision of his or her services.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax on any gains made. So far as Capital Gains Tax is concerned, it will fall under paragraph 11 of ESC D33. This may mean that no Capital Gains Tax is payable.

There's more guidance about ESC D33 at the end of this paper.

17. Type of award: Compensation for distress, inconvenience, hardship, pressure, and impact on personal life, where it gave rise to an event of economic loss.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax. So far as Capital Gains Tax is concerned, it will be exempt from Capital Gains Tax by section 51(2) of the TCGA92. For more information please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg13030>.

18. Type of award: Compensation for damage to reputation, where it gave rise to an event of economic loss.

HMRC's view: This type of award will be a 'capital' sum, so will not be chargeable to Income Tax but you may be liable to pay Capital Gains Tax. So far as Capital Gains Tax is concerned, it will fall under either:

- section 51(2) of the TCGA92 and if so it is exempt from tax; or
- paragraph 11 of ESC D33, which may mean that no tax is payable.

There's more guidance about section 51(2) of the TCGA92 and ESC D33 at the end of this paper.

19. Type of award: Compensatory interest.

HMRC's view: If your award includes any amount of interest, the interest element is subject to Income Tax. As it is 'yearly interest' in respect of compensation the Bank will be obliged to deduct Income Tax from the payment at the basic rate. The Bank will inform you of the amount of the interest element and of the tax deducted.

Your final tax position will depend on your individual circumstances but in general, the position will be as follows.

If you're liable to higher or additional tax on the interest element of your award, you must declare the interest to HMRC or include it in your Self Assessment tax return, if you complete one. You can access guidance on how to do this here: www.gov.uk/tell-hmrc-change-of-details/income-changes

Please note: The size of the interest payment may mean that you become a higher or additional rate taxpayer in the year of receipt.

If you are a non-taxpayer and have had tax deducted from the interest, you can make a claim to have the tax repaid to you by HMRC. For details on how to do this, go to the GOV.UK website here: www.gov.uk/government/publications/income-tax-claim-for-repayment-of-tax-deducted-from-savings-and-investments-r40

Some of the interest element of your award may be covered by your Personal Allowance, your Personal Savings Allowance or the starting rate for savings. You can find guidance on this here: www.gov.uk/apply-tax-free-interest-on-savings

Under the Personal Savings Allowance (PSA), basic rate taxpayers can receive up to £1,000 of savings income, and higher rate taxpayers can receive up to £500 of savings income, without any tax being due. Savings income includes all interest, including interest paid as part of a compensation award.

Therefore, even if you are a basic or higher rate taxpayer you may still be able to claim a tax refund if all or part of the interest element of your award is covered by your tax allowances.

Interim Payments

It is possible that the bank may make an interim payment to you after a Minded to Decision is made but before a Final Decision is made.

If this happens then the bank should specify which part of the award the interim payment relates to, then the tax treatment of the interim payment will follow the tax treatment which would apply to the final award.

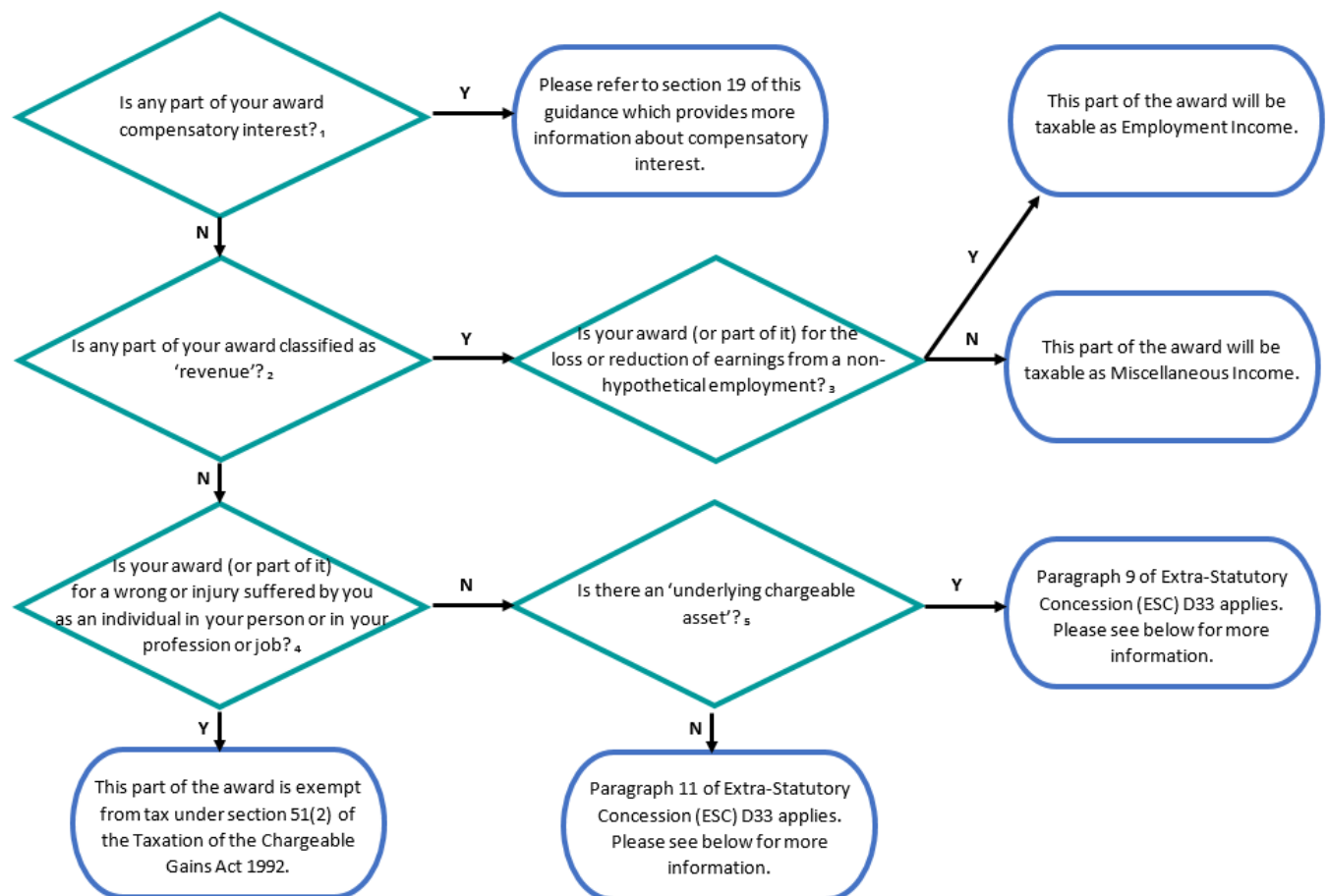
Any taxable income which arises from an interim payment should be returned in the self-assessment return for the year of receipt.

Deductions from awards

It is possible that the Foskett Panel may make a deduction from your award for amounts you have already received as compensation from the bank. If this happens you should treat the deduction as being made against one of the capital elements of your award.

General Considerations

The flowchart below, summarises how to work out the tax treatment for the award you've received.



¹ It is likely the Foskett Panel will separately identify the amount of any compensatory interest in its award.

² Generally, part of an award will be classified as 'revenue' if the nature of the payment that it replaces would have been classified as 'revenue'. Any part of an award that is not compensatory interest and that is not classified as 'revenue' is classified as 'capital'. Payments of the nature of income are classified as 'revenue'.

³ Section 1 of this paper explains what type of amounts are considered as Employment Income and Miscellaneous Income.

⁴ For more information about section 51(2) of the TCGA92 please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg13030>.

⁵ Any 'capital' amounts of compensation you've received, are derived from the legal claims you have made - called a right of action. This means that for all 'capital' awards, where section 51(2) of the TCGA92 doesn't apply you'll need to

calculate the charge to Capital Gains Tax and you'll then need to consider ESC D33. You'll need to determine whether paragraph 9 of ESC D33 or paragraph 11 of ESC D33 applies.

Paragraph 9 of ESC D33

Paragraph 9 of ESC D33 applies when you have a chargeable asset underlying your award. It explains that your award is taxed on the basis that the amount is derived from the underlying chargeable asset. For more information about chargeable assets please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg11700p>.

You'll need to apply the part-disposal rules because a proportion of the allowable costs of the underlying chargeable asset can be allowed as a deduction when working out the gain. For more information about part-disposals please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg12730p>.

This approach applies even if you're no longer the owner of the underlying chargeable asset at the time you receive the capital award (for example, you've sold it). In that situation it is likely that you would have already included all of the allowable costs when working out the earlier disposal of that asset, so the receipt of the capital award will result in a gain.

Any relief or exemption that was or would have been available on the disposal of the underlying asset (whether it's still held or not), will apply to a capital award that's from that underlying asset.

Paragraph 11 of ESC D33

Paragraph 11 of ESC D33 applies if your award did not derive from an underlying chargeable asset but from the legal claims that you have made – called a right of action. Paragraph 11 of ESC D33 treats as exempt from Capital Gains Tax the first £500,000 of a capital sum that derives from a right of action.

If you receive an award which falls under paragraph 11 of ESC D33 in excess of £500,000, HMRC may extend the exemption to the full amount of the capital sum received, if you make a claim to HMRC and that claim is accepted. You need to meet four conditions for HMRC to accept your claim.

The first condition is that the right of action was acquired in connection with goods or services that the Bank provided as part of their trade, profession or vocation. HMRC's view is that you have met the first condition.

As the first condition has been met, the second condition will not need to be considered here.

The third condition will be met if you did not acquire the right of action by means of a spouse's or civil partner's transfer. You will need to consider whether you have met this condition.

The fourth condition will be met if you did not acquire the right of action from another person for money or money's worth. You will need to consider whether you have met this condition.

If your claim to extend the exemption is refused, or is not made, you'll need to work out the charge to Capital Gains Tax on the amount of the award that's above £500,000.

For more information about ESC D33 and how to make a claim, please see <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg13020> and <https://www.gov.uk/hmrc-internal-manuals/capital-gains-manual/cg13021>.