



Small Company Employee Share Schemes

Traditionally, employee share schemes have been associated with large quoted companies. However, recent changes in legislation have made such schemes more attractive to smaller businesses. Share schemes allow companies to reward their staff either by giving them free shares in the company or by allowing them to purchase shares at a discount to market value.

Benefits

Research has indicated a clear link between employee share ownership and improved company performance. There are many benefits including:

- Motivated employee effort adds value to the business.
- Where a company is able to offer a share incentive scheme it is likely to become more attractive to potential employees and ease recruitment.
- A common goal of employee share schemes is to promote staff loyalty. This can be achieved by permitting employees to receive their shares or exercise their share options, only after a certain length of time with the company.



Tax Efficient

Employee share schemes that are approved by HM Revenue & Customs (HMRC) have a number of tax advantages for both the employer and the employee.

There are a number of employee share schemes which carry HMRC approval. The two of which are likely to be most attractive to small and medium sized companies are the Share Incentive Plan and the Enterprise Management Incentive Plan.

Share Incentive Plan (SIP)



The Share Incentive Plan was first announced in the 1999 budget. It was originally known as the All Employee Share Plan (AESOP).

The legislation requires the employer to set up a trust to hold the shares awarded under the SIP.

The SIP can be used to award the employee with free shares. There are also tax advantages available if the employee purchases shares in the company. The award of shares can be linked to employee performance.

The employer can award each employee up to £3,000 worth of free shares in any tax year. The employee will not have to pay Income Tax or NICs on the value of the shares received.

There is also the opportunity for the employee to purchase, subject to monthly limits, shares from their gross pay. Provided the conditions

are met no Income Tax or NICs will be paid on the money used to purchase the shares.

Many of the tax advantages available to employees are contingent on the shares remaining within the plan for 5 years.

The company is able to deduct the value of the shares awarded to employees against its taxable profits for Corporation Tax purposes. There is also scope for deducting the costs of setting up the scheme from taxable profits. The employer will not normally be liable for employers' NICs on shares given to or purchased by employees through a SIP.

However, Share Incentive Plans are all employee plans, so they cannot be restricted to particular groups or individuals.

The Enterprise Management Incentives Plan (EMI)

The grant of share options to an employee will allow the employee to purchase a predetermined number of shares at a predetermined price at sometime in the future.

EMIs are tax advantaged share options. They are designed to help small, higher risk companies recruit and retain employees who help them grow and succeed.

Tax advantaged share options with a market value not exceeding £120,000 may be granted to any number of employees of a company.

No charge to Income Tax or National Insurance arises on the grant of a qualifying EMI option.

If an EMI option is exercised within ten years of its grant and the exercise price does not exceed the market value of the shares at the date of grant then no Income Tax or National Insurance will be due.

On a subsequent sale of the shares, the employee will be subject to Capital Gains Tax at the standard rate of 18%. However, due to the application of Entrepreneurs' Relief, where the employee holds more than 5% of the shares in the company, has held them for more than twelve months and works for the company the rate of Capital Gains Tax may be reduced to 10% for the first £1million of gains arising as long as the company is a trading company.

Unlike the SIP, EMI is flexible in the way the grant of options can be restricted to specific employees. The options can be written to include handcuffs, for example stating that the options will lapse if the employee leaves the company within a certain timeframe.

For options to qualify under EMI there are a number of conditions to be met by both employer and employee. These include:

- The shares must be in an independent trading company with gross assets not exceeding £30 million.
- Companies carrying on certain trades will not qualify.
- The total number of EMI options granted can not exceed £3 million.
- Employees must spend at least 25 hours per week working for the company, or if less, then at least 75% of their working time.



Additional Schemes



Tax and legal advice is essential for any company considering an employee share scheme. There are a number of other schemes which although not mentioned in this fact sheet may be better suited to particular individual circumstances

Unapproved schemes can be used to provide greater flexibility, however this is often at the expense of a loss of tax relief.

For further advice and assistance

Monahans can assist you in all areas of employee reward and remuneration.

Please contact Peter Lugg on 01225 472800 or email peterl@monahans.co.uk

or Dominic Bourquin on 01225 472800 or email dominicb2@monahans.co.uk