

BULLETIN 5 — July 2008

Employee Share Schemes

Employee share schemes are a powerful and tax-efficient tool in attracting and retaining key employees, but have recent changes to the capital gains tax (CGT) regime made them less attractive? And what is the effect on the different types?

Enterprise Management Incentive (EMI) Scheme

This scheme is aimed at smaller organisations, requiring relatively little effort to set-up and administer.

The main features are:

- unlisted company operating a scheme must satisfy eligibility criteria
- grant of an option is tax-free, up to ten years in advance
- provided the option has been granted at open-market value, as agreed in advance with HMRC, no tax liability arises when the option is exercised
- the company can benefit from a corporation tax saving based on the open-market value of the option at the time it is exercised
- maximum of £120k in options per employee
- discretionary scheme, so options can be granted on a selective basis

Once exercised, the employee may wish to sell their shareholding, which can present difficulties for an unquoted company. To allow for this, the employer will need to either arrange a trade sale at some point in the future, or arrange to have an employee share ownership trust set-up.

Finally, the question of the capital gain the employee will make on selling his or her shares. Under the old CGT rules, business asset taper relief could be applied to almost all exercised options as it would begin at the time the option was granted, meaning a CGT charge of 10% when the exercised options were sold by the employee. Now that all taper reliefs have been abolished, CGT is payable at a flat-rate of 18% regardless, which is certainly simpler but not really good news.

The new Entrepreneurs Relief is available but there are quite restrictive qualifying criteria to satisfy, including a minimum holding requirement of 5% (including voting rights).

Approved Company Share Option Plan (ACSOP)

ACSOP's are generally taken-up by larger organisations (now, any with more than 250 employees), and smaller companies that fail the qualifying company criteria for the EMI scheme.

They do not compare well overall with the EMI scheme, and place additional restrictions in some areas. The maximum allowed under option per employee is also a lot less, at £30k. Entrepreneurs Relief is not available at all, and so all capital gains are charged at 18%.

Please contact us if you'd like to discuss this or any other operational issues relating to charitable or not-for-profit organisations.

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