

FOCUS ON

Employee share incentives

Employee share incentives give your employees an opportunity to take a stake in your business. In addition to acting as an incentive or reward, they may also help you to recruit and retain valued staff. This should contribute to improving the performance of your business.

There are two types of employee share incentives:

- Share option schemes
- Share award schemes

A share option is the right to buy a certain number of shares in a company at a set price at some point in the future. Employees can generally exercise their options (buy the shares) after a certain period of time (the vesting period).

The employee can exercise their option at the price fixed at the date of grant - regardless of the prevailing market price. They can then decide either to keep the shares or sell them at a profit.

The granting and exercising of options can be made dependent on reaching certain targets, including sales and performance targets.

Share award schemes

Share award schemes involve giving employees actual shares rather than options, either for free or for a lower price than their market value.

Tax issues

An income tax charge will arise when the employee exercises the share option on the difference between the market value of the shares acquired and the price paid for them under the option. National Insurance contributions (NIC) may also be due in certain circumstances.

Similarly, the value of shares given to an employee is treated as employment income - subject to tax and NIC. (The 'undervalue' is treated as employment income where the employee pays a lower price than market value).

“*Under these schemes employees and directors are granted share options which give them rights to acquire shares.*”

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HMRC approved schemes

There are currently four HMRC 'approved' tax-advantaged schemes that provide employees and employers with income tax and NICs advantages. These are:

- Company Share Option Plan (CSOP) – award of options
- Enterprise Management Incentives (EMI) – award of options
- Save As You Earn (SAYE or Sharesave) – award of options
- Share Incentive Plan (SIP) – award of shares

Shares acquired under these schemes are generally free from income tax and NIC with just gains on the ultimate sale of the shares being subject to tax and that at the more favourable rates of capital gains tax (0%, 10%, and 20%). None of these schemes requires prior approval from HMRC before it can be operated. All can be set up and options or shares awarded without needing to seek HMRC approval. Employee shareholder shares

As well as 'employee' and 'worker' and 'self employed', there is an employment status known as the 'employee shareholder' status. 'Employee shareholders' can receive a minimum of £2,000 worth of shares and up to £50,000 worth of shares for taking on this status

The first £100,000 of gains made on shares awarded to employee shareholders are free of capital gains tax on their sale if the shares were worth £50,000 or less on award. This is a lifetime allowance. The first £2,000 of any shares received are free of income tax and NIC.

Choosing your employee incentive scheme

You will need to consider the following questions in deciding which employee incentive scheme will work best for you:

1. Do you want to incentivise your employees by making the award of shares or grant of options dependent on reaching certain milestones – for example, completing a certain number of years of service or on business profitability or sales?
2. Do you want to structure the scheme so that employees only become entitled to shares if you sell the company?
3. Do you want to limit the scheme to certain key employees (for example, those with particular managerial or technical skills)? Or do you want all your employees to be able to participate in the plan?
4. Do you want to tie in key management as part of a business succession plan or in preparation for a sale?
5. Do you want to run a combination of schemes or provide more favourable terms for directors?
6. Does your business meet the qualifying requirements for any or all of the HMRC approved share incentive schemes?

We can guide you through the process of choosing the best employee incentive scheme for you and your business, and then help you to implement and run the scheme going forward - including drafting legal documents, gaining HMRC approval and helping you communicate the new plan to your employees.



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