

SHARE SCHEMES

General

There are a number of share option and share purchase schemes, which receive favourable tax treatment. They represent a means of rewarding and incentivising employees on a tax efficient basis. A share option is an offer to an employee of a right to purchase shares at a future date at an agreed term for fixed amount.

If share options are "unapproved" an income tax charge can arise on the difference between the market value at the date of exercise of the option and the cost i.e. the option price. It is deemed a benefit in kind. This tax applies at the date of exercise of the option. If the shares can be readily convertible into cash then National Insurance Contributions, may also be payable. When shares acquired under an unapproved option are disposed of, a further Capital Gains Tax charge may arise. The employment income taxable at the time of exercise is deducted.

Where the option is granted under an approved share option scheme no tax arises at the date of granting of the option or the exercise. Capital Gains Tax only applies at the time of actual disposal of the shares. The cost of the option and the cost of the shares are deducted. Non UK residents do not pay Capital Gains Tax. UK residents pay Capital Gains Tax of 18%.

There are four types of schemes which receive favourable treatment. Each must comply with certain conditions and be approved by HM Revenue and Customs

- SAYE Schemes
- Company share option plans
- Enterprise management initiative schemes
- Share and incentive plans

Where shares are gifted to an employee or purchased at a discount price, the difference is subject to income tax and potentially National Insurance contribution.

SAYE

A Save as You Earn (SAYE) allows employees to pay a maximum of £250 per month into a SAYE scheme for a period of 3, 5 or 7 years (depending on the scheme design). At the end of the scheme period, the money can be used to exercise the share options. No income tax arises on the grant of the option or on the exercise of the option i.e. the purchase of shares. CGT treatment only applies.

In order to qualify for approval by HMRC, a SAYE scheme all employees must be able to participate in the scheme on similar terms. The price is usually met by employees out of SAYE accumulated savings. The price at which the shares are offered must not be less than 80% of the market value of the shares, when the option was granted. Any employees earning more than 25% of the company are ineligible. The costs of setting up the scheme are allowable.

Company Share Option Plan

Under this type of scheme, the company has greater discretion in allocating options. The aggregate value of the options is potentially greater than under SAYE.

Eligible employees must be either full time directors or full time or part time employees. Directors with a material interest of more than 25% are ineligible. The option must be exercised between years 3 and 10. The price must not be materially less than their value at the time of the grant. There is a £30,000 limit on the value of the shares which a participant may hold or on exercise at a time.

The costs of setting up the scheme are allowable as a tax deduction to the employer. Participation in the scheme need not be extended to all employees nor be on equal terms.

Enterprise and Management Scheme

The Enterprise and Management Scheme allows options to be granted to select employees in smaller companies. The rules are more generous than for share option plans. Options up to £100,000 can be granted to selected employees. Under this scheme, no Income Tax or National Insurance contributions are charged on the grant or exercise of the option provided the price was at least market value at that time.

If an exercise price was granted at a discount, the charges are based on the difference between the market value at the date of the grant and exercise, if any. There are no limits to the number of employees who may benefit although the total value of options may not exceed £3,000,000. An employee must work for the company at least 25 hours per week or at least 75% of his working time. If working less he must not have a material interest in the company i.e. more than 30%.

The company must be undertaking a qualifying trading company. Trades such as development are excluded. The Company's gross assets must not exceed £30,000,000. An employee may not be granted options over shares worth more than £100,000 at the time of the grant. Options taken under a company's share option plan must also be taken into account.

Options must be exercised within 10 years of the grant and may be granted at a discount or a premium.

Share Incentive Plans

Share Incentive plans allow employers to give shares to their employees, to purchase shares without an income tax charge. The sale of shares would be subject to CGT.

There are a number of different mechanisms for a Share Incentive plan. An employer may give up to £3,000 in shares per year. The amount received will usually depend on financial performance. The employer may be allowed to buy shares on a 1 to 2 basis i.e. two free shares for every one they buy. The cost is deducted from pre-tax salary to a maximum of 10%. The employer may choose to issue further free shares on a 2 to 1 basis.

The plan must be available to all employees of a company or group employees. The employee must have no material interest in the company. There must be no arrangements for loans to employees. The plan shares must be held for at least 5 years.

Provided the shares are held for 5 years, there is no income tax or National Insurance liability. If shares have been held for between 3 and 5 years, income tax is charged on the lower of the initial value or the value of the date of withdrawal. CGT is charged in the normal way.

This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.