

Enterprise Management Incentive Scheme

Are you missing a tax free opportunity?

We all know that retaining quality people is fundamental to growth and business success. Their appetites are more sophisticated and key staff increasingly want an equity share as part of their employment packages; without this commitment they move elsewhere.

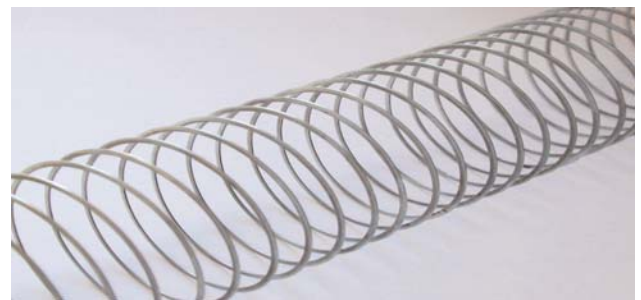
Whilst available research is often anecdotal in this area, it seems that equity participation does assist in retaining people, and certainly does help handcuff key employees.

The difficulty in offering them shares or options to acquire shares, is the tax treatment on both the employer and employee of doing so. Simply giving an individual shares will generate tax charges on that person under the PAYE regime, which may require some shares to be sold to fund that liability - defeating the objective. Alternatively the employer could fund the tax and NIC obligation, but this an expensive proposition.

Many companies are therefore turning to the government sponsored EMI scheme, where tax charges are minimised or extinguished, and the tax breaks available to employees are enhanced.

EMI Scheme Key Features

- Share options may be granted to acquire shares whose initial market value does not exceed £100,000, in a qualifying trading company or group, with gross assets of less than £30m.
- The arrangement offers great flexibility and does not require pre-approval from the Inland Revenue.



- There is no charge to tax on the grant of the option - it will be free of tax and national insurance contributions.
- There is no minimum holding period for the option, and no requirement in relation to the price of the shares themselves under the option arrangement.
- There will be no tax liability on exercise if the option is exercisable within 10 years, and the option exercise price is greater or at least equal to the market value at the date of grant.
- For capital gains tax purposes the date of grant of the option will be the starting point of taper relief for tax purposes. Holding the options for 2 years would therefore bring the individual within the 10% tax rate.
- A company must report the existence of an EMI option with 92 days of grant, and annually thereafter to the Inland Revenue.

See overleaf for two case studies...

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CASE STUDIES

1. Young business

Problem

A client who traded via a limited company and was the sole shareholder needed to retain a key employee, who had developed the business software. The company was in the developmental stage and cash was tight, so there was little flexibility to tie him in with higher remuneration.

Solution

We put in place an EMI arrangement - the employee now has options over 20% of the share capital, and is staying. The second round of financing has been agreed mainly on the back of a stable team.

The employee has no tax to pay and any gains on the sale of the shares held under option will be taxed at 10%.

2. Established business

Problem

A successful established private company had in place phantom share agreements with the Main Board Directors, whereby they received a bonus equal to the amount they would have received in dividends if they had been 5% shareholders. There was also an agreement in place that they would receive the same proportion of any proceeds on the sale of the company.

To give them equity would be expensive as the shares were valuable based on the company's trading results.

Solution

An EMI scheme was used that would push any tax liability out until the options were to be exercised, at the date of a sale, thereby matching any tax due with cash received.

Again any future uplift in the share price will be taxed at only 10% instead of 40%.

CONTACT

If you would like further details on EMI Schemes and how they could work for your business please contact Tax Partner **John Bowes** on the number below, or email him at jbowes@wingrave.co.uk

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