

Enterprise Management Incentives (EMI)

What is EMI?

EMI is a share option plan targeted at smaller companies. It is the most tax efficient share plan available in the UK, probably in Europe. Make EMI one of the first you consider if you think your company might qualify.

How does it work?

EMI is a share option plan. This means that employees chosen to participate are granted an option to buy shares in your company, paying a fixed price if they do decide to buy the shares (*exercise the option*.) Often the price will be the value of the shares when the option is granted. There is no obligation to exercise the option, so if the share price doesn't rise employees would be unlikely to exercise.

EMI benefits from an extremely advantageous tax treatment on any difference between market value on the dates of grant and exercise – see **Tax treatment**.

Does your company qualify?

- EMI is for smaller companies only – with *gross assets* of no more than £30 million
- Companies running certain businesses *are excluded*
- Your company must be *independent* - it must not be a subsidiary of or controlled by another company
- Your company must operate *wholly or mainly in the UK*
- Shares used must be *ordinary shares* – but they need not have all the rights of ordinary shares; so, for example, they may have no voting rights attached

Do your employees qualify?

- Any employee who is to participate must work for the company for *at least 25 hours a week*, or if less, for at least 75% of their working time
- Anyone holding *30% or more* of your company's ordinary shares won't be eligible

Are there any limits?

- Options may not be granted over shares with a market value in total (measured at the time each option is granted) of *more than £3 million*
- For each employee, there is a limit of *£100,000*

Tax treatment

Assuming the option exercise price doesn't exceed the market value of the shares at the time of option grant:

- There is no income tax or National Insurance to pay when the option is granted.
- There is no income tax or National Insurance on the difference between the value of the shares upon grant and upon exercise – so if the exercise price is set at market value on the date of grant, there won't be any income tax or National Insurance when the employee exercises the option.
- If the option exercise price is less than market value on the date of grant, income tax (and possibly National Insurance) will be payable on exercise, on the difference between the exercise price and market value on date of grant.
- When shares acquired through exercise of EMI options are eventually sold, capital gains tax (CGT) will be due on option gains (the difference between exercise price and sale price). CGT is normally payable at a rate of 40% but taper relief will often result in a significantly reduced rate of CGT.

Taper relief is usually available when shares are owned outright (under most share option schemes, this is the date when options are exercised). However, under EMI, taper relief becomes available from the date when the options are **granted**, so the largest reduction of CGT will happen much sooner for an EMI optionholder than any other optionholder.

For example, where taper relief is available at the *business assets rate* (which is often likely to be the case), the following rates will apply:

Time between option grant and exercise	Rate of CGT for higher rate taxpayer
Over two years	10%
Between one and two years	20%
Less than one year	40%

Could anything affect the tax treatment?

If certain things happen between option grant and exercise so that the options cease to qualify under EMI, income tax can become payable on gains up to the date of exercise.

The main *disqualifying events* are:

- the company becoming controlled by another company
- the company's trade ceasing to qualify
- the optionholder ceasing to work for the company or sufficient hours a week
- an individual being granted EMI options over shares with a value of more than £100,000.

How many companies have EMI plans?

According to the Inland Revenue, by 2004 approximately 4,900 UK companies had granted options under EMI, of which we estimate that 300 are AIM listed and 100 are smaller listed, the remaining 4,500 being private.

Is there any accounting impact?

The Accounting Standards Board is to require a company providing share-based benefits for its

employees to show that as a cost in its accounts. However, this will not apply to smaller companies whose accounts are prepared under FRSSSE.

Many companies paying UK corporation tax may now claim as a deduction against corporation tax the value of any benefit provided through options

How do we find out more?

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