

SAYE options (Sharesave)

What are SAYE options?

They allow UK employees to participate in share options without having to pay income tax or National Insurance (NI) on their option gains.

How do they work?

Imagine that:

- *In 2005 your company wishes to offer each of its employees a share option. This allows them, after a fixed period of time has passed, to buy a fixed number of shares at today's share price (£1.25 per share) or at a discount of up to 20% on that price (£1 per share). The company decides to grant the option with a £1 exercise price;*
- *Each employee will only be granted the option if they agree to save a fixed amount per month for a minimum of three years, so that the total of their savings and interest will provide enough money for them to exercise their option;*
- *One employee, Justin, decides to save £100 per month for three years. After three years, this will give him £3,600 plus a tax free interest bonus of £190 (rate from 1 September 2004), total £3,790. He is granted an option to buy 3,790 shares.*
- *three years later (2004) the share price has increased to £2.50. Justin uses his savings to exercise his option in full, paying £3,790 for shares which are now worth £9,475, so making a gain of £5,685.*

Normally Justin would have to pay income tax and possibly NI on this £5,685 benefit (even though it may only be a paper gain if he hasn't yet sold the shares). However, because the option is an Inland Revenue-approved SAYE option, he doesn't have to do so.

So is it completely tax free?

No, if Justin sells the shares – which he might do either immediately or after some time – he will

then have to pay capital gains tax (CGT) on any gain he has made up to the point of sale. But it will often be much better to pay CGT than income tax or NI:

- *there is an additional tax free slice - £8,500 for 2005-2006*
- *taper relief can significantly reduce the rate of CGT*
- *unlike income tax or NI, CGT is due only when he sells the shares, and so when he has some cash to pay his tax bill.*

What happens if an employee doesn't wish to exercise their option?

There is no obligation to exercise and if the option isn't exercised, the employee may simply keep the savings and bonus.

Can we choose which of our employees are granted SAYE options?

No, SAYE is an all-employee plan, so you must invite all employees to participate, or all employees who have worked for the Company for a specified minimum period (which can be set at up to five years).

Is SAYE the only way to have options free of income tax and NI?

No, there are two other option plans providing similar benefits for UK employees, CSOP and EMI. Neither of these are all-employee plans, so you can choose who participates.

Are there any limits?

The maximum monthly savings allowed per employee is £250. The *savings period* can be

either three or five years.

The *option period* can be the same as the *savings period*, or under a five year savings period the *option period* can be extended to seven years. In all cases, the option can be exercised within six months of the end of the option period.

What happens to leavers?

Any employee who leaves due to redundancy, injury, disability or retirement must be allowed to exercise a proportion of their options linked to the amount saved so far and any accrued interest. Any option gains are not subject to income tax or National Insurance.

What happens if our company is taken over?

You should plan ahead for this. Your SAYE plan could stipulate that a proportion of options, linked to the amount saved and accrued interest, becomes exercisable even though the option period is not yet complete

But if any are exercised within the option period, income tax and possibly NI will be due on option gains.

Can my company have SAYE?

Most independent companies will be able to meet the requirements of the SAYE legislation, but you will need to look at them carefully – preferably with professional help. Granting SAYE options over shares in a company which is controlled by another is an immediate problem, unless either of the companies is listed.

Shares must be:

- *in a company not controlled by another (unless listed)*
- *ordinary shares, fully paid, not redeemable*
- *not subject to any restriction unless it applies to all shares of the same class*

And (if the company has more than one class of share) *either* a majority of the class of shares used must not be held by directors or employees

or (very unusually) that class of shares must give employees control.

How many companies have a SAYE plan?

According to the Inland Revenue about 700 companies had an SAYE plan, involving over two million employees, at April 2003. 44 were in AIM listed companies and 216 in smaller, fully listed companies.

What is the 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. For listed companies, this will apply in respect of financial years beginning on 1 January 2005 onwards. For unlisted (including AIM) companies, the starting date is 1 January 2006.

However, this will accounting treatment will not apply to smaller companies whose accounts are prepared under FRSSE.

Are there any benefits for the company?

Apart from the potential commercial benefits of a carefully designed SAYE plan (employee motivation, creating a sense of ownership and fostering commitment), any gains enjoyed by employees may be treated as an expense of the employer company for corporation tax purposes.

Is there anything else I need to know?

Yes, there is more information you'll need to understand before deciding whether an SAYE plan may be the right solution.

How do we find out more?

Please contact Robert Postlethwaite rmp@postlethwaiteco.com or Sarah Anderson sa@postlethwaiteco.com

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