

Share Plan Facts

Why have a Share Plan?

Improve your profits? Your employees now own something – shares – whose value rises or falls according to how well your business is doing. They may also generate an income – dividends – depending on performance.

Get the best people? Share plans can attract new employees and – by providing a deferred reward – encourage them to stay

Provide an income tax free benefit? In the UK, share plan benefits can often be income tax and National Insurance (NI) free, as the Government wants to encourage companies to run share plans. And any benefit to employees is treated as a business expense

Do Share Plans work?

- In 2001, Harvard Business School found a productivity improvement of up to 17% in UK listed companies with employee share plans

- A 1992 investment of £100 in UK companies with an employee share plan would by June 2003 have grown to £349, compared with £161 if invested in the FTSE AllShare Index (source: *Equity Incentives*)
- When Rover Group set up its share plan, absenteeism fell from 22% to 2%

What would be best for my company?

There are four different plans with **tax incentives in the UK**, described below.

If none of these suit your company there are many other choices – generally known as **unapproved plans** – but employees are likely to pay income tax and NI on any benefit.

Share plans with tax incentives

Selective plans – you can choose who participates:

Company Share Option Plan (CSOP). An employee is given an option to buy shares at today's price, after 3 to 10 years. If they do exercise, they don't pay income tax or NI on their gains

Enterprise Management Incentives (EMI) Similar to a CSOP, but with no minimum 3 year period, and superior tax breaks. EMI is only for smaller companies in certain trades

The technical bit - shares must pass these tests:

- Be in a company not controlled by another unless (for CSOP, SAYE and SIP) listed
- Ordinary shares, fully paid, not redeemable

And, apart from EMI:

- Not subject to any restriction unless (for CSOP and SAYE) it applies to all shares of the same class or (for SIP) it applies to all ordinary shares -although SIP shares can have certain limited rights e.g. non-voting
- If the company has more than one class of share, then (for CSOP and SAYE) *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 of the company

All employee plans – everyone may to join:

SAYE options. Employees are given an option to buy shares at today's price (or less 20%) in 3, 5 or 7 years time, and must save each month to build up the money to exercise the option (but they can keep it at the end if they don't exercise). If they do exercise, they don't pay income tax or NI on their gains

Share Incentive Plan (SIP). Employees can:

- Be given shares tax free (*Free Shares*); and/or
- Buy shares out of their pre-tax pay (*Partnership Shares*; and
- If they buy Partnership Shares, be given matching free shares (*Matching Shares*)

Are there limits on the tax incentives?

SAYE An employee may not save more than £250 a month, or less than £5

SIP An employee may not:

- Be given Free Shares worth more than £3,000 a year
- Spend more than £1,500 a year on Partnership Shares, (or 10% of annual pay if less)
- Be given more than two Matching Shares for each Partnership Share they buy

CSOP An employee may be granted options over shares with a maximum £30,000 value

EMI An employee may be granted options over shares with a maximum £100,000 value, £3 million for the whole company

Unapproved share plans

Income tax (and NI where shares can be traded) is normally payable on financial benefits under an unapproved plan:

Options	Free shares
Restricted shares	Shares held in a trust for an employee

Under unapproved plans involving shares in which there is a market (e.g listed on London Stock Exchange), both employer and employee pay National Insurance

2003-04 NI rates

- *Employee (primary)* – 11% on any earnings between £91 and £610 a week, plus 1% on anything above that
- *Employer – (secondary)* 12.8%

Capital Gains Tax (CGT)

When an employee sells their shares, they may have to pay CGT on the shares' growth in value:

- **For SAYE, CSOP and EMI options**, on the difference between exercise and sale price
- But for **SIP shares**, there is no CGT
- **For unapproved options and unapproved free shares**, on the difference between market value when the shares are acquired and their sale

Reducing CGT

- £8,200 annual exemption
- Taper relief reduces the rate of CGT depending how long the shares have been held*:

Period	Higher rate taxpayer	Lower rate taxpayer
Less than 1 year	40%	20%
1 to 2 years	20%	10%
2 years or more	10%	5%

* assumes shares are business assets

Will the cost of any benefit be an expense in our accounts?

- *Share purchase*. No, unless you allow a discount
- *Free shares*. Yes
- *Options*. Not presently, but this is likely to change under new accounting rules. A value will have to be placed on the option when it's granted, which will be spread as a company expense over the option's expected life.

Listed companies – making sure your investors are happy with your share plans

As a listed company you'll need to think about

- Guidelines from ABI and NAPF
- Regulations on director pay requiring information in annual reports and annual shareholder vote – the *Directors Remuneration Report Regulations 2002*
- UK Listing Authority Rules

ABI Guidelines on share plans – some key parts

- Shareholder approval for any new plan
- Max of 5% new issue shares for executive plans
- Max of 10% of new issue shares for share plans overall
- Stretching performance targets for selective (executive) plans

Share plan statistics

It's estimated that about 3.5 million UK employees participate in an approved share plan. And the Inland Revenue also has these numbers:

2001-2002	Number of employees	Average value of options
CSOP	270,000	£7,000
SAYE	1,300,000	£2,100
EMI	20,000	£15,200
2002-2003	Number of employees	Average value of shares
SIP	1,500,000	Partnership £100 Free £430 Matching £90

To find out more, please contact Robert Postlethwaite:

robert.postlethwaite@consortes.com

+44 20 7470 8805

www.consortes.com

This is a general guide only and should not be treated as advice. Professional advice should always be taken.

© Consortes. All rights reserved. July 2004