Share Plans Update: April 2013

Contents

Budget 2013 – new developments

The Budget announcements on 20 March 2013 contained some additional modifications to legislation affecting share plans.

Changes to proposals to implement Office of Tax Simplification review

The draft legislation relating to tax-advantaged share schemes published in December 2012 has been modified so that:

- Participants who already have SAYE options will still be able to exercise them on reaching the specified retirement age without retiring. (This will be abolished for SAYE options granted after Royal Assent to the Finance Bill.)
- To widen the range of circumstances when SAYE and CSOP options can be exercised, and SIP shares can be withdrawn tax free, on a takeover offer.
- SIP Partnership Shares may not be subject to forfeiture (even after the ban on other restrictions for plan shares has been removed).
- Companies may, if they wish, limit the value of cash dividends which can be reinvested in a SIP (from 6 April 2013, when the statutory £1,500 pa limit was removed).

'Employee shareholder' status

In addition to the capital gains tax (CGT) exemption already announced, the first £2,000 of share value received by individuals with 'employee shareholder' status will be exempt from income tax and NICs. The new exemptions are expected to apply to shares received from 1 September 2013.

Beneficial loans to employees

From 6 April 2014, the exempt threshold for the cash equivalent of the benefit of employment-related loans is to be increased from £5,000 to £10,000.

Capital gains tax

The rates remain at 18% for basic rate taxpayers and 28% for higher and additional rate taxpayers. The annual exempt amount for 2013-14 is £10,900.

Stamp duty

Stamp duty on the trading of shares in growth markets, such as AIM, will be abolished from April 2014.

Corporation tax

New legislation will make clear that from 20 March 2013:

- Companies cannot deduct IFRS2 accounting expenses for share-based payments, even if the option or award lapses and the employee does not acquire shares. (This should not affect the deduction where awards are cancelled for a cash consideration.)
- In cases where the employee does acquire shares, companies cannot deduct both the accounting expense and the statutory deduction.

Budget and Finance Bill changes by share plan

The Finance Bill makes a considerable number of changes to the legislation for tax-advantaged share plans, mainly based on the recommendations of the review of tax-advantaged share plans, published by the Office of Tax Simplification ('OTS') in March 2012.

Most of these changes will come into effect when the Finance Bill receives Royal Assent, which is likely to be in July 2013. Although the legislation will automatically change the rules of existing approved share plans for certain of the changes, most companies will wish to ensure that their rules are amended so that the new provisions can be clearly identified. Changes will also need to be made to employee booklets and application forms and some updating of administration systems and procedures will be necessary.

HMRC stated in their Employment-Related Shares & Securities Bulletin Number 7, issued on 13 March, that if companies choose to amend their schemes solely to reflect the new legislation those alterations do not require HMRC's approval.

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Share Incentive Plans (SIPs)

Proposed change	Effective date	Action for companies
Electronic communication of scheme information Confirmed that employers can provide scheme information to participants electronically or through a link to a secure website, provided that all participants are notified.	11 December 2012 (announced in HMRC's Employment-Related Shares & Securities Bulletin Number 5).	Many companies have been doing this already. Others will be able to move to paperless communication as soon as it suits them.
Retirement 'good leaver' provisions The 'specified age' is to be removed and companies will be allowed to apply their own definition of 'retirement' (subject to HMRC guidance still to be published).	Date of Royal Assent.	Rules changed automatically, but communication documents relating to 'good leavers' and forfeiture of shares may need amending.
Tax relief on cash takeovers Income tax relief will be available when shares are withdrawn from a SIP on acceptance of a cash takeover offer provided that there was no alternative offer of shares or loan notes.	Date of Royal Assent. Will also affect shares already awarded before then.	No need for changes to Trust Deed & Rules, but communication documents may need amending
Abolition of material interest test The provision which prevents an individual with a material (25%) interest in a close company from participating in its SIP is to be removed.	Applies to shares awarded on or after the date of Royal Assent.	Trust Deed & Rules will be amended automatically.

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Proposed change	Effective date	Action for companies
Use of restricted shares Companies will be able to award shares which are subject to restrictions. Employees must be given details of any restrictions at time of award. The market value of the shares for the purpose of the plan (eg award limits and price paid for Partnership Shares) must ignore the restrictions.	Applies to shares awarded on or after the date of Royal Assent.	Trust Deed and Rules will be amended automatically. However, Partnership/Free Share Agreements and other employee communications will need to be changed if the company wants to impose any restrictions (other than existing forfeiture conditions).
Price paid for Partnership Shares If there is an accumulation period, the price paid by employees can be any of: • the share price at the start of the period • the share price at the acquisition date • the lower of the above two prices (as at present).	Applies to Partnership Share Agreements made on or after the date of Royal Assent.	If a company wants to take advantage of this change, amendments are likely to be needed to the Trust Deed and Rules and employee communications and employees will need to enter into new Partnership Share Agreements.
Limit on reinvestment of dividends The £1,500 limit on the value of dividends which may be reinvested into a SIP to acquire Dividend Shares has been removed.	The limit ceased to apply from 6 April 2013.	Trust Deed and Rules will be amended automatically. However, Partnership/Free Share Agreements and other employee communications may need to be changed.
Restriction on carrying dividends forward The requirement that any dividends held by SIP trustees for 3 years without being reinvested to acquire Dividend Shares must be paid to employees has been removed.	6 April 2013. This also applies to amounts held by the trustees before that date.	Trust Deed and Rules will be amended automatically. However, Partnership/Free Share Agreements and other employee communications may need to be changed.

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Proposed change	Effective date	Action for companies
Use of shares transferred from QUESTs The restrictions on the use of shares which have been transferred from (the now defunct) qualifying employee share ownership trusts are being removed.	Applies from date of Royal Assent.	Trust Deed and Rules will be amended automatically.

Savings-Related (SAYE or Sharesave) Share Option Schemes

Proposed change	Effective date	Action for companies
Contributions not from salary SAYE participants can now continue to contribute while on sabbatical leave or on secondment to another job or post in the same organisation.	11 December 2012 (announced in HMRC's Employment-Related Shares & Securities Bulletin Number 5).	Changes to administrative procedures and, possibly, to explanatory documents.
Electronic communication of scheme information Confirmed that employers can provide scheme information to participants electronically or through a link to a secure website, provided that all participants are notified.	11 December 2012 (announced in HMRC's Employment-Related Shares & Securities Bulletin Number 5).	Many companies have been doing this already. Others will be able to move to paperless communication as soon as it suits them.
Abolition of 7-year options 7-year savings arrangements to be removed from SAYE prospectus, which will mean 7-year SAYE options can no longer be offered.	During 2013 (date to be announced).	Rules changed automatically, but communication documents may need amending.

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Proposed change	Effective date	Action for companies
Retirement 'good leaver' provisions Companies will be allowed to apply their own definition of 'retirement' (subject to HMRC guidance still to be published). References to 'specified age' removed. Employees will no longer be able to exercise when they reach the specified age without retiring.	Date of Royal Assent to Finance Bill. Does not apply to SAYE options already granted before then.	Rules changed automatically, but communication documents and administration procedures relating to 'good leavers' may need amending.
Tax relief on business transfer Income tax relief will be available when SAYE options are exercised less than 3 years after the grant date if within 6 months of a TUPE transfer or the employing company leaving the group.	Date of Royal Assent. Application to options granted before then will depend on exact wording of option agreement at time of grant.	Rules changed automatically, but communication documents and administration procedures relating to 'good leavers' may need amending.
Tax relief on cash takeovers Income tax relief will be available when SAYE options are exercised less than 3 years after the grant date if within 6 months of the making of a cash takeover offer provided that there was no opportunity to exchange options for new options over shares in the acquiring company.	Date of Royal Assent or after amendment to plan Rules, if later. Application to options granted before then will depend on exact wording of option agreement at time of grant.	An amendment WILL be required to the plan rules to provide for exercise on the <u>making</u> of a cash offer.
Abolition of material interest test The provision which prevents an individual with a material (25%) into in a close company from participating in its SAYE scheme is to be removed.	Applies to options granted on or after the date of Royal Assent.	Rules will be amended automatically.

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Proposed change	Effective date	Action for companies
Use of restricted shares Companies will be able to grant SAYE options over shares which are subject to restrictions. Employees must be given details of any restrictions at time of grant. The market value of the shares for the purpose of the plan (eg exercise price) must ignore the restrictions.	Applies to options granted on or after the date of Royal Assent.	Rules will be amended automatically. However, option certificates and other employee communications will need to be changed if the company wants to impose any restrictions.

Company Share Option Plans (CSOPs)

Proposed change	Effective date	Action for companies
Electronic communication of scheme information Confirmed that employers can provide scheme information to participants electronically or through a link to a secure website, provided that all participants are notified.	11 December 2012 (announced in HMRC's Employment-Related Shares & Securities Bulletin Number 5).	Many companies have been doing this already. Others will be able to move to paperless communication as soon as it suits them.
Retirement 'good leaver' provisions Companies will be allowed to apply their own definition of 'retirement' (subject to HMRC guidance still to be published). References to 'specified age' removed.	Date of Royal Assent. Does not apply to CSOP options already granted before then.	Rules changed automatically, but communication documents and administration procedures relating to 'good leavers' may need amending.
Tax relief on business transfer Income tax relief will be available when CSOP options are exercised less than 3 years after the grant date if within 6 months of a TUPE transfer or the employing company leaving the group.	Date of Royal Assent. Application to options granted before then will depend on exact wording of option agreement at time of grant.	Rules changed automatically, but communication documents and administration procedures relating to 'good leavers' may need amending.

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Proposed change	Effective date	Action for companies
Tax relief on cash takeovers Income tax relief will be available when CSOP options are exercised less than 3 years after the grant date if within 6 months of the making of a cash takeover offer provided that there was no opportunity to exchange options for new options over shares in the acquiring company.	Date of Royal Assent or after amendment to plan Rules, if later. Application to options granted before then will depend on exact wording of option agreement at time of grant.	An amendment will probably be required to the plan rules to provide for exercise on the making of a cash offer.
Change to material interest test The definition of material interest in a close company changed from a 25% holding to a 30% holding (for consistency with EMI).	Applies to options granted on or after the date of Royal Assent.	Rules will be amended automatically.
Use of restricted shares Companies will be able to grant CSOP options over shares which are subject to restrictions. Employees must be given details of any restrictions at time of grant. The market value of the shares for the purpose of the plan (eg exercise price) must ignore the restrictions.	Applies to options granted on or after the date of Royal Assent. HMRC have confirmed that they now allow CSOP Rules to include a requirement to sign a section 431 election when the shares are acquired.	Rules will be amended automatically. However, option certificates and other employee communications will need to be changed if the company wants to impose any restrictions.

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Enterprise Management Incentives (EMI)

Proposed change	Effective date	Action for companies
Hard copies of documents Confirmation that option agreements do not have to include a hard copy of the Articles of Association or (if relevant) the EMI scheme rules or any shareholders' agreement, provided participants have access to these documents.	11 December 2012 (announced in HMRC's Employment-Related Shares & Securities Bulletin Number 5).	Minor changes may be needed to future option agreements.
Exercise after disqualifying event The period during which an EMI option can be exercised with tax relief after a 'disqualifying event' has occurred is to be increased from 40 to 90 days.	Applies where the disqualifying event occurs on or after the date of Royal Assent.	It may be necessary to amend any EMI plan Rules or option agreements which refer to a 40-day period.
Extension of Entrepreneurs' Relief Entrepreneurs' Relief has been extended to shares acquired through EMI options, even though the individual does not meet the usual 5% shareholding requirement. The one-year holding period applies from the option grant date.	Applies to shares acquired on exercise of an EMI option and disposed of from 6 April 2013. Transitional provisions also apply where the option was exercised during 2012-13 tax year.	None; but employee must claim the Entrepreneurs' Relief from HMRC.

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Approved share plans: self-certification

Following recommendations by the OTS review, the Government is to replace the current HMRC approval requirement for SIP, SAYE and CSOP with a self-certification process, which will apply from April 2014.

The main reason for the delay is that MM&K and other advisers pointed out that there are a large number of 'grey areas' of uncertainty about the requirements for meeting approved status. HMRC have developed their own sets of rules about the qualifying conditions, which are not obvious from the legislation and, even more worryingly, have changed over the years. These include, for example, limitations on exercise of discretion by companies on treatment of 'good leavers' and on whether performance conditions have been met.

HMRC therefore accepted that they will need to provide much clearer guidance in the future and that some parts of the current legislation will need to be simplified. A further announcement is expected this summer.

Office of Tax Simplification: Unapproved Schemes Review

Following several months of research and consultation with companies and their advisers, the OTS published its recommendations on unapproved share schemes on 16 January 2013. These included some potentially useful improvements to tax legislation which impacts on these schemes, which it describes as "a tangle of complexity, creating costs and traps for companies and their advisers, uncertainty for employees, and ongoing burdens for HMRC".

At the time of the Budget, the Government announced that it would be consulting on the recommendations before deciding how to proceed. A consultation paper is expected in May 2013.

A. The 'marketable' security

Employees are currently liable to pay income tax when they are awarded shares free (or pay less than market value, eg on exercise of an option), even if there is no market for the shares and so they cannot be sold to raise the funds to pay the tax charge.

Under the first OTS proposal, an employee who received shares (or other employment-related securities) which were not 'marketable' – capable of being sold for cash – would not be subject to income tax until the shares became capable of being sold, unless the employee specifically elected to be taxed at acquisition (eg so that any future increase in value would be subject to CGT instead of income tax).

B. International assignees

The current UK tax treatment of international assignees is extremely complicated and confusing, with the position differing between different types of share award, particularly for awards granted before an employee became resident in the UK.

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A more consistent approach is recommended, which would aligning the liabilities of assignees with the general earnings tax treatment. This would also be consistent with the approach recommended by the OECD. The OTS recommend that a corporation tax deduction should be allowed when income tax becomes payable but the employee is seconded from an overseas company.

C. ‘Safe harbour’ employee shareholding vehicle

There are numerous tax traps involved when companies use employee benefit trusts (EBTs) to hold their shares for the purpose of share plans – including inheritance tax, CGT for the trustees, charges for loans by close companies to their participators and stamp duty. These were made considerably worse by the introduction of the ‘disguised remuneration’ legislation in 2011, which imposed early income tax charges when shares (or other assets) were ‘earmarked’ for employees, unless the arrangements fitted into one of a series of complex exemptions.

The OTS recommends the introduction of an employee shareholding vehicle, possibly a statutory ‘safe harbour’ EBT, which, if certain conditions were met, would provide automatic exemption from these various charges. Interestingly, one of these conditions is that the vehicle must be resident in the UK, which has raised the alarm in the many trust companies in the Channel Islands which currently act as EBT trustees.

D. Form 42

This annual return to HMRC for unapproved share plans is complex to complete and it is unclear to what extent the information provided is actually used by HMRC. The OTS thinks there is a strong argument for curtailing the amount of information collected on the form. It recommends online filing in the short term and integration into real time information (RTI) over a longer horizon.

E. PAYE simplification

Where share plans are concerned, the deadline for companies to account for PAYE, which is the 14^{th} day of the tax month following the one in which an income tax liability arises, can be difficult or impossible to comply with. There are now potentially large penalties for late payments. The OTS recommended an extension of the deadline for PAYE arising from employment-related securities to 60 days after the end of the tax month.

Another onerous deadline is that employees must make good the PAYE liability arising from share plans within 90 days; otherwise they are subject to a further income tax charge, under section 222 of ITEPA 2003. This charge is not reversed even when the employee does eventually pay the tax. The OTS recommends the removal of this charge if the tax is in fact made good. Alternatively, the deadline should be extended until 6 July following the end of the relevant tax year.

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Share valuation

Valuation of shares acquired by employees can cause uncertainty and potential penalties for private companies, and also for listed companies which operate joint share ownership plans (JSOPs) and similar arrangements.

The OTS made a number of recommendations, including:

- Increased availability of pre-transaction valuations for unapproved share plans.
- Better provision of information about valuation methodologies.
- Automatic acceptance of the closing price for companies whose shares are traded on markets which are not recognised stock exchanges, such as AIM.
- Discontinuing the quarter up valuation for listed companies, using the closing price instead.

New shareholder employment status

After an initial rejection by the House of Lords, the Growth and Infrastructure Bill has now been passed. This includes the creation of a new employment status of 'employee shareholder' from September 2013. Individuals with this status will lose certain of their employment rights, such as unfair dismissal, flexible working, training and redundancy pay.

To give an incentive for employees to agree this new status, employers will be required to give them shares worth at least £2,000. As mentioned above, the first £2,000 worth of such shares will be exempt from income tax and NICs. As a further incentive, capital gains on shares which were worth up to £50,000 at the time of their original receipt will be exempt from CGT.

There has so far been very little enthusiasm for this new employment status. It is only likely to be attractive to individuals if there is potential for substantial increases in the share price. We anticipate that it is most likely to be adopted in private-equity and similarly financed businesses.

What HMRC's share plan statistics show

When the previous Government launched the SIP in 2000, it stated that it wanted "to encourage more companies, particularly smaller and unquoted ones, to offer all-employee share plans". HMRC's statistics show that it has failed to meet this goal.

The number of companies with live SAYE schemes has fallen from a peak of 1,400 down to 680 in 2010-11. While about 1,600 Profit Sharing Schemes had been approved by 2000-01, the SIPs which replaced them totalled 880 live plans in 2010-11 (and shares were only appropriated in 520 of these). You can see more details at:

http://www.mm-k.com/content/documents/employee-share-plans/Number%20of%20share%20plans.pdf

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The present Government has launched a stream of initiatives to increase employee ownership and the OTS believes that, if accepted, its own recommendations will go a long way to opening up employee ownership to many more companies and employees. However, we believe that the current 'approved' share plans will need to be made substantially more flexible if the Government's goal is to be achieved over the next 10 years.

6th July deadline for share plan annual returns

There is a legal requirement to submit to HMRC an annual return in respect of each HMRC tax-advantaged share plan operated by the company (or its group), as well as a separate form in respect of certain other transactions involving employment-related securities. The deadline for filing each return for the tax year 2012-13 is 6 July 2013.

The annual return forms are listed below:
Form 40 - EMI share options
Form 34 - SAYE share options
Form 35 - CSOP share options
Form 39 - SIP share awards
Form 42 - share, option and other awards of securities not falling within the above.

Form 42 is particularly complex and some parts cannot be completed without a good understanding of the underlying legislation. **Please contact MM&K for advice on completing any of these forms.**

HMRC is currently revising all these forms and plans to introduce online filing for them from the 2014-15 tax year.

This Share Plans Update is intended to give readers an overview of recent share plan developments. Companies should take appropriate professional advice on their particular circumstances before taking action on any of these issues.

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