Analysis of the HMRC statistics on employee share schemes 2011

ESOP Centre
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The Employee Share Ownership Centre

Spreading the Wages of Capital

RECORD NUMBERS FOR GOVERNMENT SHARE SCHEMES – BUT CLOUDS GATHER

A record number of companies in the UK operated a government approved share scheme last year, according to the Esop Centre's annual analysis of statistics from HM Revenue & Customs.

However the headline upward movement belies a number of concerning trends.

A record 12,500 companies are operating at least one of the four tax-advantaged government schemes (SAYE Sharesave, Share Incentive Plan, Company Share Option Plan and Enterprise Management Incentive)* but within that some schemes are in decline.

Earlier in the summer Exchequer Secretary David Gauke wrote to the Office of Tax Simplification asking for a fast review. This followed the Centre's call for a common framework to make schemes simpler and more comprehensible. "The statistics show the move could not have been more timely" commented Centre chairman Malcolm Hurlston.

Enterprise Management Incentives

Of the four schemes, only Enterprise Management Incentives (EMI) fared better than the previous year. EMI allows smaller companies to attract key staff using share options with the potential for growth rather than large cash salaries.

According to HMRC 10,610 companies operated an EMI scheme in 2009-10 – an increase of 110 on 2008-09.

However, even EMI had its setbacks. The numbers of companies that issued options under their plans fell from 2,560 in 2008-09 to 2,190. The corresponding number of employees to whom these options were granted also fell from 22,100 to 16,900.

"EMI is inexpensive to the public purse as, on the whole, if a company offering such a plan does well the extra tax revenue generated covers the relief given," said Centre chairman, Malcolm Hurlston.

"The government can do more to promote the scheme with better liaison between the Treasury and Business. It seemingly answers the coalition's prayers as a cheap way to encourage growth in the SME sector."

SAYE Sharesave

Surprisingly, the number of employees to whom options were granted under the all-employee Save As You Earn (SAYE) Sharesave increased by 120,000 people - nearly twenty percent. This is despite 70 fewer companies operating such a plan and the tax-free bonus given through the scheme currently being close to zero.

Centre chairman Malcolm Hurlston explains, "When these options were being offered, share prices would have been depressed. The twenty percent discount available on the option price meant that there were attractive offers there for the taking.

"On top of that, this reflects the trend of increasing personal savings as a reaction to the recession. Sharesave is risk free because if the share price falls employees can opt to have their money back instead of taking up the option at the end of the three- or five-year savings contract."

Company Share Option Plan

Use of the Company Share Option Plan (CSOP) has fallen as it has failed to be promoted and is often unfavourably compared to EMI as an either or choice for directors. However, CSOPs can be offered to part-time and low-paid staff and could be used by many more companies.

At its peak 415,000 employees benefited from a CSOP compared to just 40,000 last year.

"Companies who are asking staff to go part time to balance the books could soften the blow by offering options using a CSOP. That way when the company recovers those members of staff have something to show for their forbearance.

"Although SportsDirect chose a different approach, the £40,000 plus bonus won by its staff shows how option based awards can transform performance and spread capital wealth. Negotiators have missed a trick by not asking for a CSOP."

Share Incentive Plan

Last year 860 companies offered a Share Incentive Plan (SIP) - 30 fewer companies than the previous year.

The small scale of the decrease shows comparative resilience of all-employee plans in the face of the recession.

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"Companies could have cut and run in droves to help balance the books, but the evidence shows they haven't. This gives power to the Centre's case that share schemes add value to the company that can't be measured in numbers alone."

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The Employee Share Ownership Centre is an independent not-for-profit membership organization, established by Malcolm Hurlston in 1988 to inform, lobby and research in the interest of employee share ownership. Its subscription-based membership includes consultants, professional advisers, trustees, banks and companies who have either introduced employee share schemes or intend to do so shortly.

The HMRC statistics on share schemes are available here:
http://www.hmrc.gov.uk/stats/emp_share_schemes/menu.htm

Notes:
Share Incentive Plan ("SIP"): The SIP is an HMRC approved tax-efficient, all-employee plan. There are 4 main elements to the SIP. Companies can choose to use one or more of the following modules: Free Shares; Partnership Shares; Matching Shares; and Dividend Shares.
Under a SIP companies may gift up to £3,000 of shares to each employee (Free Shares) each tax year. Employees can also be given the opportunity to buy shares with up to £1,500 of pre-tax salary in each tax year (Partnership Shares). Where one Partnership Share is purchased companies can award a maximum of two shares for free in return (Matching Shares). Dividends paid on SIP shares can be used to buy up to £1,500 worth of additional shares in each tax year (Dividend Shares). Shares in the SIP must be held in trust.

Save As You Earn ("SAYE")/Sharesave: The SAYE is an HMRC approved plan that allows employees to enter into a savings contract for three or five years. The accumulated savings (plus a tax free bonus at a level set by HMRC) can then be used to fund an exercise of options and purchase of shares. Employees who decide to participate in a company's SAYE plan are granted an option to buy shares at a later date as prescribed by the company. The option vesting period can be 3, 5, or 7 years.
The options can be granted at a discount of up to 20% of the market value of the shares at the date of grant. Participants decide at the outset to contribute up to £250 each month.
Participants who want to exercise their option to buy shares use the accumulated savings plus bonus. All gains realised at this point will be free of Income Tax and NIC liabilities, and subject instead to CGT when shares are sold. For a high proportion of participants the annual CGT allowance is

enough and they pay no tax. Alternatively, the participants can withdraw their savings and bonus and allow the option to lapse (sensible if there is no gain…)

Enterprise Management Incentive ("EMI"): The EMI is a tax favoured plan aimed at younger and smaller companies who want to attract, reward, and retain skilled staff. It allows companies with gross assets of less than £30 million and fewer than 250 full time (or equivalent) employees to grant options over shares up to a value of £120,000 per employee (valued at the date of grant). The EMI does not require formal HMRC approval prior to implementation of the plan.
As long as the exercise price is set at the market value of the shares at the time the option is granted, there will be no Income Tax or NICs charge when the employee exercises the option (provided the exercise takes place within 10 years of the grant). Gains will be subject to CGT after using the employee's annual exemption.

Company Share Option Plan ("CSOP"): The CSOP requires formal HMRC approval prior to implementation. It allows qualifying companies to grant employees, and officers working more than 25 hours a week, options to acquire shares up to a value of £30,000 (calculated at the date of grant). The CSOP is often used by companies which do not qualify for EMI and also by companies which wish to offer participation to part-time and low-wage employees.
The option cannot, under normal circumstances, be exercised before the third anniversary of the date of grant, and any gain on exercise is not subject to Income Tax or NICs. Gains are, instead, subject to CGT after the employee's annual exemption.