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EMPLOYEE OWNERSHIP LAWYERS

EMI Share Options

An Enterprise Management Incentive (EMI) option provides statutory tax relief for employees on their financial gains and is particularly suited to smaller companies.

Under Enterprise Management Incentive (EMI) options, a company's UK employees can acquire shares by first being granted options to acquire them. Statutory tax relief means that they do not pay income tax or National Insurance (NI) on their gains. It is more flexible than the CSOP, has higher financial limits and potentially a better tax treatment. However, EMI options are only for smaller companies and certain trades are excluded.

How does it work?

Employees whom you have selected will be offered an EMI **option** to buy shares in your company at a certain point in the future. If those employees decide to buy those shares ("*exercise the option*") the price that they pay for those shares will usually be their value *at the time when the option was granted.*
The hope would be that by the time the option was exercised the value of the shares would have risen, so the employee will be paying what has by then become a discounted price.

There is no obligation on an employee to exercise an option, so if share value doesn't rise the employee would be unlikely to exercise.

EMI benefits from an extremely advantageous tax treatment on any growth in share value between the dates of grant and exercise.

How might an EMI plan benefit your company?

You can provide your key employees with a financial reward, the value of which is directly determined by the success of your business and which may be taxed at a significantly lower rate than a cash bonus.

You can encourage commitment from your key people by stating that they may only exercise their option if they stay with the company.

How does the tax work on EMI options?

As long as the option exercise price is not less than the market value of the shares at the time of option grant:

- *There is no income tax or NI on any financial benefit received by the employee.*
- *When shares acquired through exercise of EMI options are eventually sold, capital gains tax (CGT) will be due on option gains (the amount by which the sale price exceeds the exercise price). CGT is normally payable at 18% or 28% in respect of capital gains generally, but on the sale of shares obtained under EMI options can be 10% provided that the shares are sold a year or more after the grant of the option, and the holder has been a director or employee for a year or more prior to the sale.*

Your company will often be able to claim a deduction against corporation tax for the full amount of an employee's option gains.

What happens if a participant leaves?

If you want to use your EMI plan to encourage participants to stay with the company, you could:

- *stipulate that unexercised options will lapse if an employee leaves; or*
- *allow them to exercise if they were leaving only for "good reasons"; or*
- *allow options to be exercised in stages, after certain time periods had elapsed.*

Employees whose options lapse will never enjoy any benefit from holding their option.

What happens if an employee exercises the option?

Once an option has been exercised, the holder becomes a shareholder, and the rights attaching to the shares are governed by the articles. These may include leaver provisions in respect of shares.

Does your company qualify?

- EMI is only for companies with *gross assets* of no more than £30m
- 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 have a *permanent establishment in the UK*
- Companies with 250 or more employees are *excluded*
- 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.

In this table we attach our own ratings for EMI options for tax efficiency, ease of setting up and overall incentive and reward value:

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EMI share options
How it works

An option – the right to buy shares in the future at a fixed price.

TAX EFFICIENCY (INDIVIDUAL)	TAX EFFICIENCY (COMPANY)	EASE OF SETTING UP	OVERALL INCENTIVE AND REWARD VALUE
★★★★★	★★★★☆	★★★★☆	★★★★★
No income tax (IT) or National Insurance (NICs) unless disqualified. CGT on sale of shares, potentially at 10 % .	Corporation tax (CT) deduction on option gains. No NICs.	No pre-clearance necessary, although option grants must be notified to HMRC.	Very simple to explain, no risk, very tax efficient. Limited to £250,000 of shares per person.

Other issues

Limited to smaller companies (assets <£30m and <250 employees) carrying out “qualifying activities”.

If you would like to explore how an employee share scheme might be introduced in your company, please contact us for an initial discussion.

We are happy to meet at our offices without charge or commitment and will be very pleased to hear from you.

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