

Enterprise Management Incentive ("EMI") Factsheet

Attract, retain and reward your key employees with an EMI plan

- ▶ An EMI plan is a tax advantaged share plan set out in legislation that can be implemented by qualifying companies.
- ▶ EMI plans are designed specifically for smaller, entrepreneurial businesses in the UK looking to grow their operation and EMI helps them to attract, retain and incentivise the talent required for that growth, by allowing them to share in the company value that they help create.
- ▶ An EMI plan provides employees the opportunity (the option) to purchase shares (known as the exercise date) in their employing company or its parent company, at some point in the future, for an agreed fixed price (exercise price), which is set at the time the share options are agreed (known as the grant date).

How an EMI plan works

- ▶ The employer determines the circumstances when an option can be exercised by an employee as part of the EMI design stage. It is a discretionary plan, so can be offered to selected employees.
- ▶ Most commonly, an option will be 'exit only', meaning that it can only be exercised when the company is sold, or there is some other type of exit event, such as a listing. It is also possible to provide other exercise triggers such as pre-determined timeframes or more specific conditions being met.
- ▶ Typically, if an employee leaves, their option can no longer be exercised and the option will lapse.
- ▶ An employer can also decide if an option will be subject to performance, or other vesting conditions.
- ▶ The market value of the shares under option can be agreed with HMRC at the date of grant and this is then used to determine the exercise price to be paid to acquire the shares. The exercise price can be set at, above or below the market value agreed. If the exercise price is set below the market value, there are tax consequences to consider.
- ▶ Each employee can hold an EMI option over shares (which must be fully paid up, non-redeemable ordinary shares), worth up to £250,000 at the time of grant, which is subject to company-wide cap of £3m for all EMI option holders.

Tax treatment of EMI options

Granting an EMI option

- ▶ There is no income tax, NIC or Apprenticeship Levy ("AL") to pay on the grant of an EMI option.

Exercising an EMI option

- ▶ If the exercise price is set at or above the market value as at the grant date, an employee should not have to pay any income tax or employee's NIC. Additionally, there should be no employer's NIC or AL for the employer to pay.
- ▶ If the exercise price of an option is less than the market value of the shares as at the grant date, or if one or more certain qualifying conditions cease to be met prior to the exercise of an option, there may be some income tax and potentially NIC and AL liabilities that could arise.
- ▶ When an option is exercised, an employer can claim a corporation tax deduction equal to the difference between the market value of the shares at exercise and the exercise price paid.

Sale of the shares

- ▶ Generally, on a disposal of shares, there may be a Capital Gains Tax ("CGT") liability. The current rates are 10% and 20% and the relevant rate will depend on an individual's circumstances.
- ▶ Shares acquired via an EMI plan can potentially qualify for Business Asset Disposal Relief ("BADR"), formerly Entrepreneurs' Relief. This can reduce the CGT rate to 10%, subject to an individual's lifetime limit, which is currently set at £1m.

- Capital gains realised on the disposal of shares acquired via an EMI plan should benefit from BADR if the shares are sold at least two years after the grant date and during that time, the company was a trading company (or the parent company of a trading group) and the EMI plan participant was an officeholder or an employee.
- An employee may also benefit from other CGT reliefs, such as the CGT annual exemption, which may reduce or eliminate any CGT liability.

Company requirements

- In order to qualify, a company must meet the following conditions when an option is granted:
 - o The company must be UK resident or have a UK branch;
 - o The company must not be a subsidiary of another company, or be under the control of another company;
 - o The company's gross assets must not exceed £30m;
 - o The company must have fewer than 250 full time equivalent employees; and
 - o The company must carry on a qualifying trade.
- There are additional points to consider where the company has subsidiary entities.

Qualifying trade

- A company will be qualifying unless a substantial part of its trade is made up of excluded activities.
- Excluded activities include:
 - o dealing in land or financial instruments;
 - o dealing in goods otherwise than in the course of an ordinary trade of wholesale or retail distribution;
 - o banking, insurance, money-lending, debt-factoring, hire-purchase financing or other financial activities;
 - o leasing;
 - o receiving royalties or licence fees for certain intellectual property;
 - o providing legal or accountancy services;
 - o property development;
 - o farming or market gardening;
 - o holding, managing or occupying woodlands, any other forestry activities or timber production;
 - o shipbuilding, coal and steel production;

- o operating or managing hotels or comparable establishments; and
- o operating or managing nursing homes or residential care homes.
- These conditions also apply to groups of companies.

Eligible employees

- An EMI option can only be granted to employees who work for the company for at least 25 hours per week.
- Employees who work less than 25 hours per week can still be granted an EMI option if at least 75% of their working time is spent on working for the company or group.
- It should also be noted that employees with a material interest in the company, taken to be 30% or more of a company's ordinary share capital, cannot be granted an EMI option.

This Fact Sheet has been carefully prepared, but has been written in general terms and should be seen as broad guidance only. The factsheet cannot be relied upon to cover specific situations and you should not act upon the information contained therein without obtaining professional advice.

Your Key Claritas Contacts

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