Briefing Note: Employee Ownership

Introduction

Companies considering including employees in their ownership structure have a number of options available to them. They are well-advised to invest some time in reviewing the available structures, the various advantages and disadvantages and their own priorities, in the light of their current and future business needs and circumstances. This note briefly sets out some of the structures available.

This guide should not be relied upon as legal advice and you should contact us for advice on your specific circumstances.

Briefing Note
Reviewed June 2020

For detailed advice on all Corporate Law matters please contact:

Mark Williams
Corporate Partner

mark.williams@gabyhardwicke.co.uk

Or

Gemma Ritchie
Associate Solicitor

gemma.ritchie@gabyhardwicke.co.uk

01323 435955

01323 435900

Why might a company consider including employees in its ownership structure?

Various factors could be of relevance, including:

- Strategic reasons, such as succession planning. For example, a family company might wish to remain independent but, if there are no family members who are willing to be involved in the business in the future, a transfer of some or all of the ownership to employees might be a solution.
- A company may wish to reward employees in a way which differs from standard salary and bonus, which might include a share in any growth in the company's value, annual profits or both.
- Tax efficiency could be a material factor, as the company might be able to use one or more of the tax-advantaged arrangements for employees.
- There may be employee relations reasons such as fostering the loyalty of employees.

What models are available?

Broadly speaking, there are two models for employee ownership:

1. Employees can acquire shares personally, which they might then be able to sell at a later date. Such shares may have voting and/or dividend rights attached to them.
2. Shares can be held on behalf of employees on a long-term basis in an employment benefit trust or employee ownership trusts.

Where it is important that employees should be able to participate in growth in their company's value, personal share ownership should be the aim. We won't focus on employee ownership trusts or employment benefit trusts in this note but please contact us for further advice and guidance if this is of interest.

Please also see these articles:-

Employee Ownership Trusts and Enterprise Management Incentive Schemes

Individual employee ownership

There any many types of individual employee ownership schemes. Some of the main schemes include:

© Gaby Hardwicke June 2020

Enterprise Management Incentive Schemes (EMIS)

EMIS options are tax-favoured options aimed at smaller companies wanting to incentivise and retain key employees. Such companies can grant employees options to acquire shares, with no income tax or national insurance contributions on any increase in the value of the shares, if the options are granted at market value. Any gain realised will be subject to capital gains tax.

EMIS options can be granted over the shares of any company, provided the following requirements are met:

- The gross assets of the company must not exceed £30 million at the time of grant.
- The company must be independent of other companies.
- The company must have only qualifying subsidiaries.
- The company must be a trading company, or the parent company of a trading group, with a qualifying trade.
- The company (or a subsidiary with a qualifying trade) must have a UK permanent establishment.
- The company must have fewer than 250 full-time employees.
- The employee to whom the option is granted satisfies certain requirements as to their working time and does not hold a material interest (usually in excess of 30% of the shares) in the company.

EMIS options must:

- Take the form of a written option agreement between the grantor and the employee.
- Be capable of being exercised within 10 years after the date of grant.
- Prohibit the transfer of any of the employee's rights under them.
- If capable of exercise after the employee's death, not be capable of exercise more than one year after death.
- Set out:
    - details of any restrictions applying to the shares under option that could make them restricted securities;
    - any conditions affecting the terms or extent of the employee's entitlement under the option, such as performance conditions;
    - the date of grant;
    - the number or maximum number of shares under the option;
    - the exercise price or the method for determining it; and
    - when and how the option may be exercised.

- Be notified to HMRC's Small Company Enterprise Centre on or before the day falling 92 days after grant.

Share Incentive Plans (SIPS)

SIPS are all-employee share plans that provide employees with the opportunity to acquire shares (as opposed to share options). If statutory conditions are met, a SIP can be approved by HMRC and favourable tax treatment can result.

Companies can choose to offer free shares and/or partnership shares. In respect of awards of partnership shares, the company can also decide whether to offer matching shares. Any dividends payable on the shares in the SIP can be reinvested in further shares, known as dividend shares. The shares are acquired upfront (this is different from all other approved share plans, as the participant is a shareholder from the outset), and are held on the participant's behalf in a trust.

Awards are free of income tax and national insurance contributions if they are held in the SIP for 3 to 5 years (depending on the type of shares) or if they are withdrawn from the plan early because the employee ceases employment for a "good leaver" reason.

Conclusion

Employee share ownership is a key tool in engendering loyalty and retaining key members of staff. There are various ways of achieving this, however it may be that ownership is not desired by company or the employee. Other means of achieving loyalty and retention may be available (e.g. bonuses) and you should contact us to discuss these options further. Whatever arrangement is put in place will require careful legal drafting and implementation.

If you would like to know more about this topic or our legal services, please contact Mark Williams on 01323 435955 or mark.williams@gabyhardwicke.co.uk

Gaby Hardwicke Solicitors
33 The Avenue
Eastbourne
East Sussex
BN21 3YD

Tel: 01323 435900
Fax: 01323 435901
www.gabyhardwicke.co.uk

© Gaby Hardwicke June 2020