

INFORMATION SHEET

ENTERPRISE MANAGEMENT INCENTIVE SCHEME [EMI]

(Updated January 2014)

The Enterprise Management Incentive Scheme [EMI] was introduced by the Inland Revenue in 2000 to help smaller companies to attract and retain key employees, by way of tax-efficient share options.

General Requirements

Share options will only qualify for the favourable EMI tax treatment if the options are granted for commercial reasons in order to recruit or retain employees. They must not be issued as part of a scheme or arrangement the main purpose of which is to avoid tax.

The Issuing Company

The company must be an independent trading company with gross assets of no more than £30,000,000 and no more than 250 full time equivalent employees. It must operate on a commercial basis and carry on a qualifying trade. Generally the trade must bear an element of commercial risk and not be highly asset dependent; businesses such as dealing in land and securities, banking, leasing, legal and accountancy services, farming, operating hotels or care homes are excluded activities.

For groups of companies, the issuing company must be the holding company, and its subsidiaries must be at least 75% owned by the holding company. The group must not consist mainly of excluded activities; furthermore at least one company must meet the activities test on a stand alone basis.

There should be no more than £3,000,000 in qualifying options in existence.

The Employee

The employee must work for at least 25 hours per week for the issuing company or group, or have at least 75% of his/her working time committed to the issuing company or group.

The employee must not own more than 30% of the ordinary issued share capital of the issuing company, nor rights to more than 30% of the assets of the company on a winding up.

The limit for options is £250,000 per employee, calculated on the market value of the options at the time they are granted.

The employee will only be eligible under the EMI scheme as long as the conditions above are satisfied. Once the conditions have been breached the options must be exercised within 40 days of the date of the breach for the tax benefits to be retained.

The Options

The share options must be for ordinary, paid up, non-redeemable share capital, and must be required to be exercised within 10 years of the grant. The options must not be assignable.

The terms of the option must be in writing and set out the exact terms and conditions of the option.

The issuing company needs to notify the Inland Revenue of the existence of the option, in a prescribed manner, within 92 days of the grant, and report annually on the options in existence. Note new rules for registration and filing become effective from April 2014 and April 2015 effectively, see later.

The Inland Revenue will give advance clearance of the eligibility of an EMI scheme and will also consider valuations of the market price of options being granted.

Taxation

There is no income tax charge on the receipt of an EMI option.

Where the option is granted at the market value at the date of the grant, there is no income tax payable on the exercise of the option. Where the grant is at less than market value, income tax will be charged on the difference between the market value of the shares at the date of the grant and the grant price.

Capital gains tax is payable on the eventual gain made on the sale of the exercised options. The price paid on the exercise of the option is the base cost for capital gains tax purposes (there is also a credit for any income tax paid). Capital gains tax will be calculated on the difference between the exercise price (plus any tax credit) and the price at which the shares are sold, less taper relief (abolished from April 2008) and annual exemptions.

Legislation

The detailed legislation covering EMI schemes is contained in Schedule 5 of the Income Tax (Earnings and Pensions) Act 2003.

This Information sheet is based on tax legislation and guidance in January 2014. It is intended to give a broad outline of the EMI scheme, the requirements for both employers and employees, and the tax treatment of share options issued under the EMI scheme. Please contact us for a more detailed discussion of the operation of the scheme and how it will apply to you.

EMI Scheme - changes to the law effective from April 2014.

The changes affect the way that HM Revenue & Customs (HMRC) administers EMI options.

From April 2014, an employer must register online any:

- already granted, but currently unexercised, EMI options
- any EMI options granted from that date

New registration requirements are also being introduced in relation to any unapproved arrangements currently recorded on Form 42;

From April 2015, further changes are being introduced, including:

- the requirement to file all information returns online
- the application of automatic penalties for late filing
- notices to file and reminders will no longer be issued

If any EMI options are not registered by 6 July 2015, the employer will not be able to file online returns in relation to those options, and late filing penalties will apply.

Furthermore, unregistered EMI options will lose their tax-advantaged status. Which means they will be treated in the same way as unapproved options. So whilst it is the employer that has to comply with these new requirements, any individual holding EMI options should make enquiries now to ensure their employer is aware of the changes and will take appropriate action.

The above is a guide only. Specific advice must always be taken. Cube Partners Limited can not accept any liability for any action or lack of action in respect of this information sheet.