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Share schemes including share option schemes

Granting employees' rights over shares in their employer company can often be a very tax efficient way of remunerating employees.

Key share schemes

Key share schemes include:

- Restricted share schemes;
- Unapproved share option schemes;
- Save As You Earn (SAYE) schemes; and
- Approved Profit Sharing Schemes (APSSs).

Restricted shares

Restricted share schemes (clog schemes) provide a tax efficient means of rewarding employees by granting shares which must be held for a certain number of years prior to disposal ("the clog").

The grant of the shares is subject to income tax at the marginal rate, PRSI and USC. However, the restriction or clog on the disposal reduces the amount chargeable to income tax by a certain percentage depending on the length of the clog period. The amount not charged to income tax can be reduced by between 10% and 60% depending on how long the employee must wait before selling the shares.

This reduced amount will also be added the base cost for the shares on their subsequent disposal for capital gains tax purposes.

It should be noted that no employers' PRSI is chargeable if restricted shares are granted to an employee.

Unapproved share option schemes

Unapproved share option schemes allow the holder of the option to buy shares in the future at a pre-determined price even if the shares are worth more at the time. Options are often used to retain and motivate selected key staff in a company.

Income tax on the exercise of the option is charged on the difference between the price paid (option price) and the market value at the date of exercise of the share option. This tax is known as Relevant Tax on Share Options (RTSO) and is payable to Revenue by the employee, along with Universal Social Charge (USC) and employee PRSI, within 30 days of exercise.

If the option can be exercised more than seven years from the date of grant and is granted at less than market value, Revenue may tax the employee on the grant of the option at the marginal rate.

Capital Gains Tax (CGT) is payable on disposal of the shares acquired on exercise and is charged based on the difference between the proceeds of disposal and the combined amount of the purchase price paid, the amount chargeable to income tax and the cost, if any, of the option itself. It is sometimes possible to combine a share option scheme and a "clog" scheme to reduce the income tax arising on exercise even more. No employer PRSI applies to share option gains.

Save As You Earn (SAYE) schemes

Such schemes, where approved by Revenue, allow employees to save part of their after-tax salary over a three-year period. At the end of the three-year period, the employee can use those savings to purchase shares in their employer company at a discount**. Membership of this scheme must be made available to all employees.** The minimum savings amount is €12 per month and the maximum is €500 per month. This makes it a suitable method for rewarding employees of all levels.

The shares can be purchased at a discount of 25% of their market value at the beginning of the three-year savings period. **No charge to income tax arises on the purchase at this discounted price**. There is no obligation to acquire shares and the savings can be withdrawn at the end of the 3-year period without giving rise to an additional tax liability for the saver.

Generally speaking, no employer PRSI arises on benefits under this scheme.

Revenue Approved Profit Sharing Schemes (APSS)

Under an APSS no income tax is chargeable on employees in respect of shares received up to an annual limit of €12,700 in a tax year, and there is also favourable income tax treatment on any growth in the value of the shares. Such schemes allow employees and directors to convert a profit sharing bonus or portion of salary into shares in their employer company.

No income tax is payable on the amount of salary forgone. Salary forgone is not chargeable to USC or PRSI at the time that it is foregone. Instead, USC and PRSI are charged on the initial market value of the shares that are appropriated in lieu of salary forgone. However, where employers chose to do so, they may deduct and pay USC and PRSI when salary is forgone.

The shares must be left in a special trust for two years, but the employee can only dispose of the shares on an income tax-free basis after 3 years. There is no additional liability to USC or PRSI on a disposal of the shares.

Where however the employee sells the shares within three years, income tax is charged at 100% of the value of the shares at the date of sale and there is a charge to USC and PRSI. This holding period may not apply where shares are transferred from an Employee Share Ownership Trust (ESOT) to an APSS subject to certain conditions.

The disposal of shares will also be subject to capital gains tax, if they are disposed of at a gain.

APPS schemes are open to every full-time director or employee and every part-time employee, as long as they are chargeable to tax under Schedule E and who satisfy the qualifying period (not more than three years).

However, shares may not be awarded to any individual holding a material interest (more than 15% of the ordinary shares) in the company where it is a close company. The cost of providing shares in an APSS and the costs of running the scheme are tax deductible for the company subject to certain conditions. Generally speaking, no employer PRSI arises on benefits under this scheme.

Conclusion

The above is a very brief overview of some of the key features of share and share option schemes. To realise their full benefits, proper planning and detailed advice should be sought.

For further information contact:

Name: Marie Bradley, Bradley Tax Consulting
Address: 14 Upper Leeson Street, Dublin 4
Tel: +353 1 400 4123
E-mail: marie.bradley@bradleytaxconsulting.ie