Introduction

Many employers give directors and employees the opportunity to acquire shares in their companies on advantageous terms. Their aim is to provide a performance incentive and often a form of 'golden handcuff'.

Share schemes offer employees a chance to benefit from the future growth of the company and encourage them to identify with it. Often the benefits are lost if the employee leaves. Employees are therefore more likely to be loyal to the company. Share schemes may offer the employee shares or options to acquire shares.

Share schemes that are approved by HM Revenue and Customs (HMRC) offer tax and national insurance contributions (NICs) advantages not available to unapproved schemes. However, approved schemes must meet various conditions and compliance obligations, which can be quite onerous.

Despite the advantages of giving employees an interest in the company, employers should consider all the issues carefully before introducing a share scheme.

- Employers should remember that the value of shares can be affected by many issues apart from the efforts of the employees. For example, share values can rise and fall with economic and trading conditions generally. Where the shares are listed on a stock exchange, market fluctuations can have a major impact. As a result, some employees could become disenchanted with the arrangements.
- From the employer's point of view, 'golden handcuff' arrangements, which tie an employee to a company, can prove expensive if the employer wishes to end a contract prematurely.
- The shares must be easily disposable. This should be no problem for listed companies, but could present difficulties for private companies.
- It is important to consider carefully how the arrangements will be taxed. Capital gains tax (CGT) is charged at a lower rate than income tax. This gives approved schemes, in which the growth in value of shares is taxed as a capital gain, an advantage over unapproved arrangements, which generally give rise to a charge to income tax.
- Some approved schemes are costly for the employer to administer. This makes them less suitable for smaller companies. However, the rules for EMI share options are designed to minimise administration costs and the scheme is targeted at the smaller company.

This section outlines the various schemes available and their advantages and disadvantages. It can only be a guide, and professional advice must always be sought in individual cases. In this section, the word 'employee' always includes director unless otherwise stated.

Acquisition of shares

Broadly, employees can acquire shares in the following ways:

- By being issued with the shares for no consideration.
- By buying the shares either at full market value or at an undervalue.
- By being granted an option to buy shares at some future time, either at full market value or at an undervalue.

Approved schemes

The shares can be acquired through one of several share schemes approved by HMRC. These schemes generally ensure that if the conditions are met, no liability to income tax arises. This

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means that there is no tax to pay until (and if) the shares are sold for a profit and that the employee's liability is to CGT. In addition, under an approved scheme, there is generally no liability to NICs provided that the conditions are met. CGT has the following advantages:

- CGT is levied at 18%, compared to basic rate income tax of 20% and higher rate income tax of 40%.
- Shares acquired under employee schemes may qualify for entrepreneurs' relief, which in effect reduces the CGT rate to 10%. However, there are several conditions, the most problematic one being that the employee must own at least 5% of the ordinary shares and voting rights in the company for at least one year before the disposal.
- The first £10,100 of capital gains in 2009/10 is exempt from tax. This amount charged to income tax would produce a liability of up to £4,040 in respect of a higher-rate taxpayer. However, the tax advantages come at a price, as approved schemes impose several stringent conditions.

Unapproved schemes

Where the employee's acquisition of shares is not under an approved scheme, tax charges can arise in the following circumstances.

- Where an employee acquires shares at less than their market value, there is an immediate income tax charge on the difference between the price paid for the shares and their market value.
  - Where the shares are readily convertible assets, ie they can be sold on a stock exchange or there are arrangements in place that allow the employee to sell the shares for cash, NICs are payable on the same amount.
  - Where the shares are readily convertible assets, the tax and NICs are collected through the PAYE system. In other cases, the employee will normally be responsible for paying the tax under self-assessment.
  - Attempts to make private company shares disposable, in order to increase the attraction of a share scheme, could make them readily convertible assets.
- Income tax and employer's NICs are charged if the shares are acquired at their market value but payment for them is deferred. In effect, the deferred payment is treated as if it were a loan to the employee under the same benefit in kind rules as an actual loan. This charge is not imposed on employees who earn at a rate of less than £8,500 a year and are not directors.
- If shares are acquired by the exercise of an option, the employee is liable to income tax when the option is exercised. The charge is on the difference between the market value of the shares when the option is exercised and the price paid for the shares, less any amount paid for the option.
- NICs are charged on the exercise of a share option where the shares are readily convertible assets.
  - The charge is on the same amount as that on which income tax is charged.
  - It is possible for the company and employee to agree that the employee will meet some or all of the employer's NIC liability. The agreement must be made when the option is granted. Where this occurs, the amount on which the employee is liable to income tax in respect of the share option gain is reduced by the NICs passed on.

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- If the shares are sold for more than their market value at the acquisition date, the profit is liable to CGT. The profit is essentially the sale price less the sum of:
  - ➢ The amount paid for the shares,
  - ➢ The amount paid for the option, and
  - ➢ Any amount taxed as income because the shares were bought for less than their market value.
- There can be an income tax charge at other times:
  - ➢ Under some arrangements, such as the removal or variation of a restriction or the creation or variation of a right, designed to artificially boost the value of the shares held by employees, or
  - ➢ Where there is any artificial manipulation of the value of shares, or
  - ➢ Where the shareholder receives a special benefit.
- Where shares are subject to forfeiture (for example, if performance targets are not achieved) or may be converted to another class (with a resultant increase in market value), income tax may be charged at the time when the risk of forfeiture is lifted or the shares are converted. The charge is on the amount (if any) by which the open market value of the original interest immediately after the event in question exceeds the sum of the amount paid for the shares and any amounts on which income tax was charged previously in respect of the shares.
- Similar income tax charges apply to gains on a variety of other financial products used to remunerate employees.
- There have been many attempts to use arrangements involving shares to circumvent tax on employment income. Since 2005, promoters of tax avoidance arrangements involving employment income have had to disclose them in advance to HMRC. Legislation to block such schemes can therefore be announced quickly and can have retrospective effect.

Despite the tax charges, some companies have successfully operated unapproved employee share schemes for many years. Their main advantage is their flexibility, because they do not have to conform to the statutory conditions imposed upon approved schemes. This allows the company freedom to tailor the scheme to the needs of the company and to reward only those employees it wishes to reward.

Research institution spinout companies

Universities and other research institutions that own intellectual property (IP) sometimes develop that IP further through companies created in association with the researchers from the institution who worked on the project. These companies are commonly referred to as spinout or spin-off companies.

Often the research institution will transfer the IP to the spinout company for little or no monetary consideration. The researchers may be given the opportunity to acquire shares in the company at a very low value in recognition of their research contribution.

This transfer of potentially valuable IP to the spinout company could trigger liability to income tax and, in some cases, NICs on the researchers who acquire shares. The charge would be based on the increase in value of the shares resulting from the transfer of IP.

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No income tax and NICs arise in these circumstances, provided four conditions are met:

- There is an agreement to transfer IP from a research institution to a spinout company.
- A researcher acquires shares in the spinout company either before the IP transfer agreement is made or within 183 days thereafter.
- The opportunity to acquire shares was available by reason of the researcher's employment with the spinout company or research institution.
- The researcher is involved in research related to the IP transferred.

The researcher is liable to CGT in the usual way on any eventual disposal of the shares.

Corporation tax

In order to encourage employee share acquisition under HMRC approved or unapproved arrangements, companies can claim a corporation tax deduction for the market value of the shares when the employee acquires them, less any amount the employee pays for the shares. In the case of unapproved schemes, the deduction is normally the amount on which the employee is taxed.

- The shares must be fully paid-up non-redeemable ordinary shares. They must be either listed on a recognised stock exchange or be in a subsidiary of a listed company or a company not controlled by any other company.
- The shares must be in the employing company or a parent of that company in a 51% group. There is an extension for consortium companies.
- The corporation tax relief is given in the accounting period in which the employee acquires the shares and, in the case of an unapproved scheme, is liable to income tax on the acquisition.

HMRC approved schemes

- The tax pitfalls associated with unapproved schemes can be avoided to some extent under four types of HMRC approved share schemes. They are:
    - ➢ The share incentive plan.
    - ➢ Enterprise management incentive share options.
    - ➢ The savings-related share option scheme.
    - ➢ The approved company share option plan.
- These schemes can include employees of companies controlled by the company that established the scheme, as well as the company's own employees.
- An employee may not participate in a savings-related share option scheme, SIP or CSOP if they, together with any associates, can directly or indirectly control 25% of the ordinary share capital of the company. The limit is 30% for EMI share options.
- Approved schemes other than EMIs must have formal HMRC approval before the tax advantages are given. A notification process applies to EMI schemes instead. HMRC will only grant approval if the schemes strictly adhere to conditions laid down by statute. The conditions are designed to prevent abuse of the tax advantages. They include rules about

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who may participate, the shares that can form part of the scheme and the price to be paid for the shares.

- The HMRC address for share schemes is:

  Employee Shares and Securities Unit Room G52 100 Parliament Street London SW1A 2BQ Telephone: 020 7147 2843/2853 Fax: 020 7147 2747 Email: shareschemes@hmrc.gsi.gov.uk

Share incentive plans

SIPs are a tax-advantaged all-employee share scheme introduced in 2000. The SIP replaced the approved profit sharing scheme and has in common with it the requirement that shares are held in a trust for an initial period. Shares can be allocated to employees without payment or purchased by employees out of pre-tax salary. Employers are able to match shares purchased by employees. Dividends from plan shares can be reinvested to acquire further shares.

Who may participate?

All UK full- and part-time employees must be allowed to participate in the scheme on the same terms, although benefits can, to a certain extent, be linked to salary, length of service or hours worked.

- The company may impose a qualifying period of employment of up to 18 months. This period cannot vary for different groups of employees. Employment with associated companies can be aggregated.
- Employees are only allowed to participate in one SIP at a time, but may join in successive SIPs established by connected companies in the same tax year, for example, if they transfer employment within a group.

Qualifying conditions

- Employees can acquire shares in four different ways:
  - ➢ The company can give employees ‘free shares’ with a market value of up to £3,000 each year. Some or all of these can be awarded to employees for reaching objective performance targets provided certain conditions of the scheme are satisfied.
  - ➢ Employees can buy ‘partnership shares’ out of gross salary, before tax and NICs. The amount of partnership share money deducted from salary must not be more than 10% of the salary, with a maximum of £1,500 a year.
  - ➢ The company can give up to two ‘matching shares’ to the employee for each partnership share purchased. They are given free of cost and must be provided to all participants on exactly the same basis.
  - ➢ Employees are allowed to reinvest up to £1,500 of dividends paid on shares within the scheme a year into further shares. Reinvestment must take place within 30 days of the trustees receiving the dividend. The employee does not have to pay higher rate income tax on dividends that are reinvested.
- Shares must be held within a trust established for the purpose. Partnership shares can be withdrawn at any time. Free and matching shares must be held within the trust during a minimum holding period set by the company, which must be between three and five years. Dividend shares must be held until five years after the award of shares on which the reinvested dividend was paid.

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- Shares must come out of the trust when an employee leaves. The company can require forfeiture of free and matching shares if an employee leaves the company before the end of a specified period, which may not be more than three years from the date the shares are appropriated. Shares cannot be forfeited where the employment ends because of injury or disability, redundancy, retirement, death or certain changes in control of the company.

- A plan cannot be established by a company whose business consists substantially of providing services to an associated company or to persons who control the company. This excludes, for example, service companies formed by accountants' and solicitors' partnerships.

- There can be no loans to employees associated with the plan.

- The shares must meet a number of conditions:

    - They must be fully paid and irredeemable.

    - They must be listed shares, or unlisted shares in a company not controlled by any other company, unless that other company is a listed non-close company. A close company is basically one controlled by five or fewer people.

    - They must not be subject to restrictions other than restrictions affecting all the shares in the company, or certain restrictions permitted under the scheme rules. For example, the shares can have no voting rights or limited voting rights, and there can be provision for forfeiture if the employee leaves the company.

Tax considerations

- There is no income tax or NIC liability when shares up to the specified value are appropriated to an employee.

- If shares are withdrawn during the first three years after appropriation, income tax is charged on the market value of the shares at the time of withdrawal.

- If free or matching shares are withdrawn between three and five years from appropriation, income tax is payable on the lower of the market value at appropriation and the market value at withdrawal.

- If partnership shares are withdrawn between three and five years from acquisition, income tax is payable on the lower of the amount paid for the shares and the market value at withdrawal.

- The withdrawal of dividend shares within three years will result in an income tax charge on the original dividend for the tax year in which the shares are withdrawn.

- All classes of shares can be withdrawn free of income tax and NICs after five years.

- CGT is charged only on any increase in value of the shares after they come out of the plan. The growth in value while the shares are in the plan is free of tax. Employees who leave their shares in the plan until they want to sell them will have no CGT to pay.

- Shares can be transferred directly into a stocks and shares individual savings account (ISA) within 90 days of coming out of the plan, subject to the normal ISA subscription limits. They can be similarly transferred into any registered pension arrangement.

    - Transfer of the shares to an ISA is free of CGT, but transfer into a registered pension scheme is not.

- A company is entitled to a corporation tax deduction when it pays into a SIP trust subject to certain conditions, the main ones being:

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- The trustees acquire at least 10% of the total ordinary share capital of the company within one year of the initial purchase of shares made with the payment. Shares already awarded to employees will count towards this 10% if they are still held within the trust.

- At least 30% of the shares acquired with the payment are transferred to employees within five years and all the shares are transferred within ten years.

- The company can deduct the market value of free and matching shares in calculating its taxable profits in the period in which the shares are appropriated, provided that corporation tax relief has not previously been given for the company's payment to the trust for the purchase of those shares.

- The company's costs of operating the plan are tax deductible.

The administration of such schemes can be complex and burdensome. The employees are entitled to have and exercise all the rights of the shares allocated to them. Trustees are therefore obliged to ensure that the participants are informed of rights and scrip issues, takeovers, etc.

Acquisition of shares by the trustees

Two special reliefs are available where shares are transferred to a trust set up under a SIP. They enable the trustees to acquire shares without the company having to continually issue new shares to support the plan.

- Individuals can claim a form of CGT rollover relief on a transfer of shares to a trust set up under a SIP, subject to meeting a number of conditions.

- Shares held by a qualifying employee share ownership trust (QUEST) on 26 November 2002 can be transferred to a trust under a SIP without any income tax liability or loss of corporation tax relief for the company, on leaving the QUEST. There is no longer any corporation tax relief for company payments to QUESTs.

Enterprise management incentives

EMIs allow a company that meets certain qualifying conditions to grant qualifying options to any number of employees. Qualifying options enjoy a number of tax advantages as compared to unapproved options. Unlike the other tax-advantaged share schemes, it does not require advance HMRC approval. Instead, a simple notification process applies. EMIs are a great deal more flexible than approved CSOPs.

Employees are granted options to acquire shares with no restriction on the exercise price. The options must be capable of being exercised within ten years of their grant.

Who may participate?

- Any number of employees may hold qualifying options at any one time. Options do not have to be made available to all employees and the terms can be individually tailored.

- The employee must work for the company for at least 25 hours a week or, if less, at least 75% of the employee's working time must be spent on the business of the company.

Qualifying conditions

- Options must be granted for commercial reasons in order to recruit or retain an employee and not for the purpose of tax avoidance.

- The company must satisfy several conditions:

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- It must not be a 51% subsidiary of another company or otherwise under the control of another company.
- It may have 51% subsidiaries. However, if the business of the subsidiary consists wholly or mainly of holding or managing land and buildings, it must be a 90% subsidiary.
- Its gross assets must not have a balance sheet value of more than £30 million.
- It must have fewer than 250 employees (full-time equivalent).
- It must exist wholly to carry on one or more qualifying trades and must either be carrying on such a trade or be preparing to do so.

- A trade qualifies if it:
  - Is carried on wholly or mainly in the UK,
  - Is conducted on a commercial basis, and
  - Does not consist of excluded activities.
- The main excluded activities are:
  - Dealing in land or shares.
  - Banking, insurance or other financial activities.
  - Most leasing.
  - Providing legal or accountancy services.
  - Property development.
  - Farming, market gardening or forestry.
  - Operating or managing hotels, nursing homes or residential care homes.
  - Shipbuilding, coal and steel production (for options granted on or after 21 July 2008).
- The shares must be ordinary shares that are fully paid up and not redeemable. They can be subject to restrictions and to risk of forfeiture if, for example, performance conditions are not met.
- An employee may hold unexercised qualifying options up to a value of £120,000, calculated by reference to the market value of the shares at the time the option is granted. An employee who has reached this limit may exercise some and then be granted further options, but these further options will not qualify if they are granted within three years of the previous grant of qualifying options. Unexercised options under a CSOP must be counted in determining whether this limit has been exceeded.
- The total value of shares in the company in respect of which unexercised EMI options exist must not be more than £3 million.
- The company and employee must give notice to HMRC within 92 days of the grant of any option on form EMI1. This is available on the HMRC website (www.hmrc.gov.uk/shareschemes/emi/emi1.rtf). The notice must contain a declaration that the requirements of the EMI scheme are met.
- Where the company or the individual breaks the conditions of the scheme – for example, the employee leaves – the option is disqualified unless it is exercised within 40 days of the

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disqualifying event. An option will also be disqualified if the employee is granted options under a CSOP such that the total options held then exceed £120,000.

- There are provisions for replacement options to be issued following a takeover, but only if the acquiring company can satisfy certain conditions of the scheme.

Tax considerations

- No income tax or NICs are charged on the grant of a qualifying option.
- On exercise of a qualifying option within ten years of its grant, income tax is charged only on any amount by which the exercise price is less than the market value of the shares at the date the option was granted. NICs are charged on the same amount if the shares are readily convertible assets. HMRC has a procedure for agreeing market value at the time the option is granted.
- Any gain on the eventual disposal of the shares is subject to CGT, benefiting from the 18% tax rate and the annual exemption. This is reduced to an effective rate of 10% if entrepreneurs' relief is available). The base cost of the shares is the amount paid for them under the option plus any amount on which income tax was charged when the option was exercised.
- If an option is disqualified, any increase in market value of the shares between the dates of grant and disqualification of the option remains exempt from income tax.
- The costs of setting up and running a scheme are tax deductible.
- Companies are entitled to a corporation tax deduction for the market value of the shares when the employee acquires the shares under the option, less any amount the employee pays for the shares.

Approved savings-related share option schemes

The approved savings-related share option scheme allows employees to be granted a number of options to acquire shares linked to a SAYE contract. They can exercise the options under certain conditions when they have saved enough funds. The employee is not obliged to take up the options and can simply withdraw the proceeds of the savings contract tax-free.

Who may participate?

All full- and part-time employees must be allowed to participate in the scheme on similar terms, except that part-time directors may be excluded. The company is allowed to impose a qualifying period of employment of up to five years.

Qualifying conditions

- Employees must save between £5 and £250 a month under an approved SAYE contract with a bank, building society or other authorised financial institution.
- The price at which shares may be acquired must be stated when the option is granted. It must not be less than 80% of the market value of the shares at the time of the grant.
- Options cannot normally be exercised before the bonus date under the SAYE scheme. Schemes are for three or five years, with the choice in respect of the five-year contracts to extend to seven years (in which case the option date will be the second bonus date).
- Options may be exercised early where the employee dies or where employment ends because of injury, disability, redundancy or retirement. The option must be exercised within six months or, in the case of death, within twelve months.

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- Options must normally lapse where the employee leaves the employment within three years, except in the circumstances described in the preceding bullet point. Schemes can allow employees to exercise options within six months, if the part of the business where the employee works leaves the group or company operating the scheme.
- If the employment ends after three years, the scheme may allow the employee six months in which to exercise the options. Schemes may also allow employees to exercise options within six months after the bonus date if the employee remains employed by a company associated with the one that set up the scheme.
- Schemes can provide for options to be exchanged where the granting company is taken over.
- The shares must be fully paid, irredeemable and not subject to any restrictions. They must be quoted shares, or unquoted shares in a company not controlled by any other company, unless that other company is a quoted non-close company. A close company is basically one controlled by five or fewer people.

Tax considerations

- No income tax or NIC liability arises on the grant of the option or when the option is exercised, provided it is not exercised within three years of the option being granted. No income tax or NICs are charged on any increase in the value of the shares between the date the option was granted and the date it was exercised.
- Once the shares are acquired, their base cost when calculating CGT on any future disposal is the amount paid for the shares under the option plus any amount paid for the option. Market value is not substituted.
- Interest and bonuses earned under the SAYE contract are tax-free.
- Companies are entitled to a corporation tax deduction for the market value of the shares when the employee acquires the shares under the option, less the amount the employee pays for the shares.

Approved company share option plans

The approved CSOP is a flexible tax-advantaged share option scheme as, unlike SIPs, there is no all-employee condition, which means it can be used to reward select individuals. However, there is a limit of £30,000 on options granted to any one individual under the scheme, meaning that EMI share options are a more attractive prospect in those companies that qualify for the EMI scheme.

Under the CSOP, employees are granted options to acquire shares at their market value at the date the option is granted. The options may be exercised, and shares acquired, between three and ten years after their grant.

Who may participate?

This scheme does not have to be open to all employees. In general, companies have used this scheme to reward directors and senior employees.

- The scheme cannot include part-time directors. A part-time director is one who works less than 25 hours a week for the company, excluding meal breaks.
- Part-time employees are excluded from schemes approved before 1 May 1995, unless the scheme’s rules have been amended since then to include them.

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Qualifying conditions

- Options may not be exercised tax-free within three years of their grant, except where the employee leaves because of injury, disability, redundancy or retirement, or on the employee's death.
- Unexercised options lapse after ten years.
- However, if, exceptionally, options are exercised within three years (other than in the permitted circumstances) or more than ten years after their grant, income tax and NICs will be payable under PAYE.
- The value of shares over which options may be held cannot exceed £30,000.
- The price at which shares can be acquired must be fixed at the time the option is granted and must not be less than the market value of shares of the same class at that time.
- The rules governing the type of share that can be acquired are broadly similar to those under savings-related schemes.

Tax considerations

- No income tax or NICs are charged on the grant of the option.
- No income tax or NICs are charged on the exercise of the option or on any increase in the value of the shares between the date the option was granted and the date it was exercised, provided the exercise date is more than three years after the grant.
- Income tax is payable on a gain from a share option exercised within three years of grant except where the early exercise is due to injury, disability, redundancy, retirement or death. This tax is collected through PAYE and NICs are also payable.
- Any gain on the eventual disposal of the shares is subject to CGT, benefiting from the 18% tax rate and the annual exemption. The base cost of the shares is the amount paid for them under the option plus the amount paid for the option.
- The costs of setting up a scheme are tax deductible.
- Companies are entitled to a corporation tax deduction for the market value of the shares when the employee acquires the shares under the option, less the amount the employee pays for the shares.

Alternatives to share schemes

As an alternative to providing shares, a scheme could be structured to give employees a cash payment geared to any increase in value of the company shares. Such schemes, known as 'phantom' share schemes, enable employees to participate without actually owning shares. Income tax and NICs are charged when the employee receives the cash.

Such arrangements free the employer from much of the administrative burden imposed by the approved share schemes. However, employees forgo the advantages of CGT rather than income tax, and the wholly tax-free uplift in the value of shares held in the SIP. The employer also has to pay NICs at 12.8%. The employee has to pay NICs at 11% on a cash payment, insofar as it falls below the upper earnings threshold for the appropriate pay period, and at 1% on the excess.

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Ancillary matters

Tax returns and further information

All events that give rise to income tax liability must be shown on the share schemes pages of the self-assessment personal tax return. There are comprehensive notes to aid completion.

Detailed guidance on share schemes can be found on the share schemes pages of the HMRC website (www.hmrc.gov.uk/shareschemes/). Guidance on share schemes can also be found in HMRC's Share Schemes Manual (www.hmrc.gov.uk/manuals/ssmmanual/HTMl/ssm01/01_0002_SSM1.1.htm).

Information on all the share schemes is also available by post from:

Employee Shares and Securities Unit Room G52 100 Parliament Street London SW1A 2BQ

Company returns

The approved schemes each have their own requirements for making returns to HMRC.

Where a company grants share options or issues shares to employees outside an approved scheme, it must complete form 42 and submit it to HMRC by 6 July following the end of the tax year. Companies incorporated during the tax year can complete a simplified version of form 42 provided the shares issued to employees and directors have no restrictions.

Multiple acquisitions under share schemes

Employees who acquire shares on the same day at different prices under different share schemes are able to elect that the shares with the lowest gain are deemed to be disposed of first. Without this election, all shares acquired on the same day, together with any other shares of the same class that the employee holds in the company, are normally treated as a single pool with a single overall acquisition value.

The Companies Acts

The company must ensure that the proposed scheme is within the provisions of its memorandum and articles of association. Loans can be made to employees, but not to directors, so that they can participate in employee share schemes, subject to the conditions laid down by the Companies Act.

Financial Services and Markets Act 2000

The scope of the Financial Services and Markets Act 2000 is wide. A company that is not authorised under the Act could breach the Act's provisions by recommending the acquisition of its shares as an investment. Expert advice should be sought with regard to the literature to be distributed to employees.

Stock Exchange rules and investment committee guidelines

If the company or its holding company is listed on the London Stock Exchange, the Financial Services Authority's (FSA's) Purple Book (formerly the Stock Exchange Yellow Book) will lay down rules that schemes must comply with. It will also generally require approval of the scheme in a general meeting.

The investment committees, which consist of some major institutional investors, also set several constraints on employee share schemes, aimed partly at preventing their investments from being diluted by employee shareholdings. Companies need only comply with the guidelines where they have significant investors that are members of the various investment committees, who might otherwise refuse to approve the scheme.

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Conclusion

With the variety of schemes available, it is important to seek professional advice when setting up a scheme to ensure that the scheme chosen represents the ‘best fit’ for the company’s needs. In this way, the envisaged aims can be met, and both the employer and employees can benefit. Further information can be obtained from the HMRC website at www.hmrc.gov.uk.

This guide is for general information only and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking action on the basis of the contents of this publication. The guide represents our understanding of the law and HM Revenue & Customs practice as at September 2009, which are subject to change.

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