Share incentive plans

Share Incentive Plans (SIPs) are tax-advantaged share plans which allow flexible awards on an all-employee basis.

What is a SIP?

A SIP is a tax advantaged plan that allows employees to acquire shares in one or more of the following ways:

— By purchasing shares from pre-tax salary;

— As an award from the employer (either to match shares purchased by the employee, as a stand-alone award, or both); and

— By reinvesting dividends paid on employees' shares within the SIP.

Share are held on behalf of participants by a special employee share ownership trust for as long as they remain within the SIP.

How do SIPs work?

Employers can choose to offer one or more of the following components.

Partnership shares

Employees can purchase shares each year worth **up to £1,800** or, if lower, 10% of their pre-tax salary. The employer can set a lower maximum limit if it wishes.

Monthly salary deductions can be used to buy shares immediately, or built up over a period of up to 12 months before being used to buy shares.

Where deductions are accumulated, the employer determines whether employees buy shares at their market value at the start of the period, the end of the period, or at the lower of those two prices.

Alternatively, shares may be purchased on an occasional 'lump sum' basis (e.g., when annual bonuses are paid).

Employees can stop and restart salary deductions, and withdraw their partnership shares and any accumulated cash from the SIP, at any time.

The employer can cap the number of shares available to satisfy partnership share purchases.

Matching shares

The employer can choose to match partnership shares purchased by employees in a ratio of up to 2:1 (i.e. to award additional shares worth up to **£3,600 each year**).

It is possible for the employer to impose a cap, such that only partnership share purchases up to a certain value are matched.

Employees must be required to hold matching shares within the SIP for between three and five years.

Free shares

Each SIP participant can receive a stand-alone award of free shares worth **up to £3,600 each year**.

Subject to certain conditions, these awards can vary between individual employees based on their length of service, remuneration and/or hours worked.

Free share awards can also vary between participants depending on individual, business unit, or corporate performance against objective measures. The level of performance based free share awards must be determined using one of two permitted methods.

Employees must be required to hold free shares within the SIP for between three and five years.

Dividend shares

Participants can be allowed, or required, to reinvest some or all of any dividends received on shares held in a SIP into additional shares in the company. There is **no limit** on reinvestment into dividend shares.

Employees must be required to hold dividend shares within the SIP for three years.

What is the tax treatment?

SIPs offer income tax, social security (NIC) and Capital Gains Tax (CGT) advantages if certain conditions are met**.**

Acquisition of the shares

Employees won't pay income tax or employee's NIC when they acquire shares through a SIP. There will be no employer's NIC or Apprenticeship Levy charges for the employer to pay either.

The employer should be able to claim a corporation tax deduction in respect of the employees' salary used to purchase partnership shares, together with any additional costs of providing those shares.

When free or matching shares are acquired by employees, the employer can usually claim a corporation tax deduction equal to the market value of the shares when they were originally acquired by the plan trustee.

Deductions should also be available for the costs of establishing and running a SIP.

Withdrawal of shares from the SIP

Income tax and NIC charges can arise if partnership, matching or free shares are withdrawn from a SIP within five years of when they were acquired. These are summarised below:

Date of award		Third anniversary		Fifth anniversary
Partnership Free Matching	Income tax and NIC on market value at withdrawal except in certain good leaver or change of control circumstances	Free Matching	Income tax and NIC on lower of — Initial market value — Market value at withdrawal	Income tax and NIC free
		Partnership	Income tax and NIC on lower of — Salary used to buy shares — Market value at withdrawal	

If dividend shares are withdrawn from a SIP within three years, the cash dividend used by buy those shares will be subject to income tax.

Participants must remove their shares from a SIP on ceasing employment. But an early withdrawal of SIP shares can still qualify for relief in certain change of control or 'good leaver' situations.

Sale of the shares

Any growth in value of shares held within a SIP will be free of CGT. This means that no CGT should be payable if shares are retained in a SIP until they are sold.

If shares are withdrawn from a SIP prior to their disposal (e.g. when a SIP participant ceases to be in relevant employment), CGT may be payable when the shares are sold.

CGT is currently charged at standard rates of 10% and 20%, which apply depending on individual circumstances.

The CGT annual allowance (or other CGT reliefs) might reduce or eliminate any CGT charges.

Shares that employees get under a SIP can also potentially be transferred CGT free to a tax advantaged Individual Savings Account within 90 days of being withdrawn from a SIP. This could allow any subsequent growth in value to be free of CGT.

How can SIPs be used?

SIPs are 'all employee' arrangements. This means that all eligible employees must be invited to participate.

As the employer can offer one or more components of a SIP, and change the type of share awards offered from year to year, SIPs are very flexible. For example:

— Annual performance bonuses can be delivered in whole or in part by an award of free shares;

— Partnership shares can be offered alongside salary sacrifice or other optional remuneration arrangements to let employees 'flex' how they receive their total reward; and

— Employees can effectively buy shares at a discount by acquiring partnership shares with a matching share element (where a group operates a US tax advantaged employee stock purchase plan, this approach could provide broadly similar tax advantaged benefits to UK group employees).

The annual SIP limits are generous. As total benefits of up to **£9,000** in the form of partnership, matching and free shares can be provided to each employee each year, the associated NIC savings and cash flow advantage for the employer can help manage the overall cost of total employee reward.

SIPs can also operate alongside other tax advantaged share plans.

What kind of shares can be used in a SIP?

In summary, shares used in a SIP can carry any rights and restrictions, but must be:

— Fully paid-up, non-redeemable ordinary shares; and

— Listed on a recognised stock exchange **or** issued by a company that is under the control of a listed company **or** issued by a company that is not under the control of another company.

If partnership or dividend shares are subject to compulsory transfer provisions (e.g., on cessation of employment), employees must receive the price paid for those shares or, if lower, their market value, on disposal.

Additionally, if the company has more than one share class, the SIP shares must be either 'employee-control' or 'open market' shares.

Broadly, 'employee-control' shares are a class of shares that gives employees control of the company. Shares will be 'open market' shares if the majority of shares of that class are not held by employees.

These additional conditions can potentially make it challenging for companies with more than one class of shares to implement a SIP.

Which employees are eligible?

All UK resident employees of nominated group companies must be eligible to participate in a SIP.

However, subject to certain conditions, the company is able to set a minimum service period of up to 18 months.

Find out more about how a SIP can deliver for your business

Contact us to talk through how SIPs can increase workforce engagement and help you grow your business.

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