DON'T LET THE HEAD-HUNTERS POACH YOUR KEY STAFF

Growth Shares

There have been some head-turning trends in the number of companies seeking to incentivise employees and attract the best talent using government-backed equity planning opportunities.

Although the EMI scheme discussed in our July newsletter has become the obvious scheme of choice for many due to the generosity of its tax relief, the development of bespoke share schemes is also gaining momentum.

Many varied and flexible share plans are increasingly being used by companies to enthuse and empower key workers. Such plans also help recruit employees, boost team morale, grow the business, and reduce staff turnover. There is a great deal of flexibility and variation in the design and implementation of equity incentive arrangements. Equity can be structured to give employees rights which 'flower' over time as specific performance criteria are met or give employees 'growth' value over and above a base line hurdle value.

What are growth shares?

Growth shares are a special class of share, which offer a flexible mechanism for allowing employees to share in the future success and growth in value of their employing company. For many reasons, existing shareholders may wish to lock away historical value, and this can be achieved by offering employees a special class of share, often known as a flowering or growth share. This arrangement allows for the existing value of the company to be frozen for the benefit of the existing shareholders only.Going forward, the scheme participants who own the new growth shares or flowering shares, only benefit from the increase in value of the company, depending on the performance of certain targets or hurdles.

Giving team members a 'slice of the pie' is a powerful incentive for them to remain focused on the growth of the business and gives employees a greater depth of responsibility to drive the business forward to increased profitability and success.

What is the beneficial tax treatment of growth shares?

Growth share tax planning can offer attractive tax benefits to the employee, as no income tax or employee's NIC is payable when the growth shares are acquired provided full market value is paid. Also, growth shares generally have a very low initial value as all historical company value remains with the existing shareholders and so any small upfront 'hope value' should be manageable cost for the employee.

Future growth in value of growth shares may trigger capital gains tax liabilities on an employee when the growth shares are eventually sold. Capital gains tax is currently 10% and 20% for the disposal of shares and tax advice should be sought at the time of disposal to determine which rate applies. Employees may also benefit from the annual capital gains tax allowance on a sale of growth shares.

In comparison to income tax rates and NIC charges on salaries and bonuses, capital gains tax rates on a future disposal of growth shares are very favourable.

What is the benefit of growth share schemes planning for the employer?

If trend patterns continue, we are likely to see more job roles advertised with share opportunities, and a jump in the number of companies seeking to incentivise and handcuff their key management teams to the business, using employee share schemes.Equity growth share planning is also a useful tool for start-up businesses that may want to conserve cash, business owners looking towards retirement or exit, and companies looking to recruit and retain the best talent. In times of economic downturn employee share scheme planning can also be used as an alternative to costly and tax inefficient employee bonuses or pay rises. Share schemes are flexible, tax efficient tools that can fuel growth and, if desired, also offer business owners an opportunity to consider their succession planning strategy.

The government is continuing its efforts to raise awareness of the tax benefits of these schemes, and statistics suggest that UK employees received tax savings in excess of £110m in 2019-20, and £760m in 2020-21 using an approved equity incentive scheme. Share schemes are no longer the preserve of the large multinational corporates. HMRC statistics indicate that almost 16,000 companies registered for one of the government incentives schemes in 2020 and their use by small family companies and start-ups has been on the rise, particularly over the last 10 years. They are now widely regarded as a valuable tool for companies wanting a flexible way for employees to share in future success.

If you would like to talk through how growth shares or equity planning schemes can help your business please contact us:

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