

# An Upheaval for Share Schemes but Significant Tax Reliefs Remain

## *Employer withholding (PAYE) for Share Awards*

With effect from 1 January 2011, employer payroll withholding (PAYE) is required for share awards to employees and directors (excluding share options). As such, company shares are treated the same as other non-cash benefits and companies need to make the necessary arrangements to ensure payrolls correctly capture this new item. Prior to 2011, PAYE withholding did not apply and employees were obliged to account for the liabilities arising through self-assessment.

## *Self-assessment remains for income tax on Share Options*

The pre 2011 system of self-assessment on share options continues. This requires that option holders remit the income tax due within 30 days of exercise along with the Form RTSO1.

## *Universal Social Charge (USC)*

All share awards, including shares delivered through Revenue approved schemes, have been brought within



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In the past six months, there have been many legislative changes and related announcements in Ireland which impact on the tax and social security (PRSI) treatment of share awards. Given the upheaval, it is timely to reflect on what the changes mean for companies and participants. This article also looks at the attractive tax efficiencies that remain available through properly structured share incentive arrangements.

the charge to the USC with effect from 1 January 2011.

- In the context of share options, the USC must be remitted within 30 days of exercise by the option-holder.
- USC liabilities on share awards (i.e. other than share options)

must also be collected through the PAYE system.

There are two key points regarding the USC which make it somewhat more problematic than the income levy it replaces, as follows:

- the USC applies to all Revenue approved share plans (see below) which brings with it an additional PAYE complexity in terms of how to collect USC on shares that are otherwise free of taxes; and
- the USC rate of 7% applies to practically all gains (whereas the maximum 6% income levy only applied to income in excess of €174,980).

## *PRSI*

In March, the Minister for Finance confirmed the charge to PRSI (both employer and employee) will not apply where share based remuneration “... was the subject of a written agreement, entered into between the employer and the employee before 1 January 2011”. On 10 May 2011, this was refined further by the Minister for Finance when, as part of the Jobs Initiative,

he announced that no employer PRSI charge would be applied. The legislative changes required to underpin this clarification have yet to be published, however, it is expected that employee PRSI only will be collected on share based remuneration. Furthermore, it is expected that this employee PRSI liability will not apply to:

- options granted in 2010 or earlier but vesting/exercised in 2011 or later;
- restricted stock units (“RSUs”) awarded in 2010 or earlier which vest in 2011 or later; and
- shares held in any Revenue approved employee share ownership trust prior to 1 January 2011.

**Period of Grace**

In recognition of the difficulties employers face in gathering data and implementing payroll changes, a “period of grace” has been announced. Companies have until the 30 June 2011 to regularise any outstanding PAYE liabilities on share awards delivered in the first half of 2011. This means that any outstanding 2011 liabilities may be settled by the P30 (payroll tax) filing date of 14 July 2011 (23 July for those filing electronically through the online ROS facility).

**2. WHY MIGHT A COMPANY CONSIDER INCREASING SHARE PLAN PARTICIPATION?**

Despite the changes introduced in recent months, share based reward remains one of the more tax

efficient mechanisms by which employers can reward their staff. This is notwithstanding the additional USC and employee PRSI charges than have been imposed. Three popular plans are summarised below. They can often be introduced alongside incentive arrangements linked to financial or other targets over a period of time whilst simultaneously offering tax reliefs that would not otherwise be available.

**(i) Restricted Shares**

Restricted share plans are usually structured to deliver shares to senior staff. There are certain broad principles that must be integrated into any plan so as to ensure tax reliefs are available and it is critical that all these elements are reflected in the scheme documentation.

The tax relief is available at the point beneficial ownership of the shares transfers to the employee and the relief largely hinges on whether the company makes the award subject to an absolute clog or restriction on disposal. Each year of restriction can deliver a 10% abatement on the taxable amount as follows:

Restricted Period	Reduction in taxable value
1 year	10%
2 years	20%
3 years	30%
4 years	40%
5 years	50%
> 5 years	60%

**Potential Advantages**

- No employer PRSI exposure which is more attractive for companies when compared to most other benefits.
- Scope to reduce up-front tax charge.
- Company could make awards through these plans conditional on achieving specific corporate goals/objectives, thereby motivating employees to act in accordance with agreed business plans.
- Assuming rising share prices, employees can also benefit from the longer term capital appreciation.
- Any uplift in the share price (net of abatement) between the acquisition and sale would be liable to capital gains tax, currently at a rate of 25%.

**Potential Disadvantages**

- If the share price falls, employees could potentially have paid tax on a higher market value.
- The restriction on disposal of shares must be absolute (death being one of the few exceptions!).
- Employees must fund their liabilities (collected through PAYE system) on the acquisition of the restricted shares without recourse to the underlying asset.

**(ii) Revenue Approved Profit Sharing Schemes (APSS)**

An APSS is a tax efficient means of distributing shares to employees. A typical structure used by many companies is to offer employees a choice of receiving shares as an

alternative to cash bonuses. The main benefit is that income tax does not apply on APSS shares. The key features of an APSS include the following:

- subject to limits including an annual employee cap of €12,700, employees can acquire the shares free of income tax;
- the company will generally get a tax deduction for the costs incurred;
- shares must be held in a trust for three years;
- employer PRSI savings should be available;
- there must be an employer contribution, but this can be funded from various sources, including increased profits, cost reductions, gainsharing or certain discretionary bonus payments;
- it is possible to use bonus plans which deliver rewards by reference to corporate or individual performance, and such mechanisms are becoming increasingly popular as organisations seek to align corporate performance strategies with reward frameworks;
- APSS's must be available to all employees on similar terms; and

- an APSS can include a 'salary foregoing' feature which offers a means for APSS participants to significantly augment their tax relief.

### *(iii) Savings-Related Share Option Schemes (SAYE)*

An SAYE is a Revenue approved arrangement under which a company grants share options to all employees. Separately, the SAYE scheme is linked to a formal savings contract between employee participants and a third party financial institution. At the end of the savings period, typically three or five years, employees have sufficient capital to fund the exercise of the options and thus acquire the underlying shares. The key features of these plans include:

- options granted through an approved SAYE scheme will not be liable to income tax on grant or exercise;
- the USC and employee PRSI will only apply at exercise;
- the costs of establishing an approved SAYE scheme are deductible for corporation tax purposes;
- an SAYE scheme must be open to all employees on similar terms;

- the option price may be discounted by up to 25% of the market value on grant; and
- similar legislation is available in the UK such that UK parent companies often find it attractive to extend a UK scheme to Irish group companies.

### CONCLUSION

Share plans in many organisations have come through a turbulent time over the past three years. Furthermore, there may be a perception that the recent tax and PRSI changes have eroded the attractiveness of share plan structures in Ireland. However, in the current competitive environment I believe employers are likely to look to share plans as a means of incentivising and retaining employees, particularly where they are used in conjunction with a properly structured reward package and are optimised to deliver the tax efficiencies which are available. This is particularly the case now that the Irish Government has decided to continue the long standing employer PRSI exemption on share based remuneration.

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