UHY Hacker Young
Chartered Accountants

A guide to long-term incentive plans

April 2023

Helping you prosper

Contents

Introduction

What's the purpose of this report?

Over recent years, we have seen an increasing number of SMEs looking to retain key staff, attract new employees and increase the level of engagement across their workforce through the use of long-term incentive plans. It isn't just us though, in a recent HMRC report, they found for the tax year ending 2021, there were a total of 16,330 companies operating one of HMRC's tax-advantaged share schemes – an increase of 6% for the prior year and 88% since 2010.

However, there isn't a one-size-fits-all employee share scheme as each business will have different objectives and characteristics. HMRC has four tax-advantaged schemes which are the Enterprise Management Incentives (EMI) scheme, Company Share Option Plans (CSOP), Save As You Earn (SAYE) & Share Incentive Plans (SIP), but there are also Phantom Shares and Growth Shares to consider. In our experience, the most popular scheme tends to be the EMI scheme, so this guide provides more information on that scheme than the others.

At UHY, we have tax specialists that are able to advise on and implement these long-term incentive plans. This guide intends to give you a general overview so we would always encourage a call with one of our experts so they can discuss which options would be suitable for you, based on your unique requirements and circumstances.

If you would prefer to watch an overview video on Long Term Incentive Plans, you can find one here.

Should you have any questions with long-term incentive plans and wish to discuss how they could work for your business, please do not hesitate to contact Alison Price on a.price@uhy-uk.com or James Price on j.price@uhy-uk.com (or 01462 687 333 for both).

EMI Share Options

EMI share option schemes are designed both to recruit and retain employees and to motivate them to achieve a successful exit.

One of the most popular LTIPs in recent years is the Enterprise Management Incentive (EMI) scheme.

This section outlines the key parts of an EMI scheme and explains some of the tax benefits. We have also included a fictional case study in the next section to illustrate how a plan might play out.

An Overview:

EMI share option schemes are designed both to recruit and retain employees and to motivate them to achieve a successful exit. The scheme allows the company to grant tax-effective incentives to employees known as Enterprise Management Incentive (EMI) options.

Is there eligibility criteria for the EMI scheme?

To qualify for the scheme, your company must be trading, independent and have:

- Fewer than 250 full-time employees.
- Gross assets of £30m or less.

There are also excluded activities such as banking, farming and property development. There are also criteria for employees that would be eligible such as their tax residence and the amount of working time that is committed to the company.

If your company doesn't qualify, a CSOP could be a good alternative.

What is a Share Option?

An option is the right to acquire shares in a company at a future date for a specified price.

An employee does not have to pay anything when an option is granted. However, they do not actually become a shareholder until they exercise the option and pay the Exercise Price. Once they have exercised the option, they will become a shareholder and be entitled to all the rights of a shareholder, such as the right to vote at shareholder meetings and to receive dividends on shares. In some cases, it may be desirable for the options to be held over a different share class to those already in issue.

Employees will not normally be able to exercise their option until an exit occurs (see below) and/or they have reached a milestone in respect of, for example, length of service or attainment of stipulated performance criteria.

What Happens When a Share Option is Granted?

Employees will be sent two copies of an Option Agreement. The Option Agreement will set out the principal terms of the option.

Those agreements are signed and witnessed with copies retained by both the employee and the company. The grant of options must be notified to HMRC within 92 days of the agreements being signed. However, from April 2024, this deadline will be extended from 92 days to the 6th July following the end of the tax year.

It is advisable, prior to the Exercise Price being specified in the Option Agreement, for HMRC to be approached with a view to obtaining their agreement to a proposed market value for the shares to be put under option. This provides a degree of certainty over the tax position on an eventual exercise and sale.

Once HMRC are notified of the grant of EMI options by a company, it creates an expectation that an annual return will be completed and submitted in respect of each tax year by 6 July following the end of the relevant tax year. That annual return will report any lapsed options (see below) and any options that have been exercised by employees.

The type of exit most often seen is a share sale. This is where a new owner takes over the company by buying a controlling interest in its shares. If this happens, employees may be allowed to exercise their options.

How Do Exit Events Work?

The type of exit most often seen is a Share Sale, where a new owner takes over the company by buying a controlling stake in its shares and employees may be allowed to exercise their options. The Board of Directors of the company would be responsible for making sure employees get sufficient notice and sufficient time to exercise their options ahead of a sale completion.

The new owner is likely to want to acquire the shares from the employees, and if that's the case, the Option Agreement should compel employees to sell even if they don't want to (a 'drag along' clause). However, the new owner (if it's another company) may also offer employees the opportunity to exchange their existing option for a new option over its shares.

The other types of exit that might be considered are an asset sale whether the company sells all of its trade and assets to another party, leaving a shell company with, perhaps, a large sum of cash; and a listing where the company's shares are placed on a stock market. This guide only covers a share sale style of exit.

Where there is a time-based exercise event written into the Option Agreement, let's say five years on from the date of the Option Agreement, the mechanics work the same way as for an exit.

How Options Are Exercised?

Employees must complete and sign an exercise notice (in a set format which the company should supply) and return it to the company, stating how many shares they wish to acquire. Often the company will only allow the employees to submit one exercise notice so the number of shares on the notice will generally be whatever the full entitlement of the employee is.

The employee's entitlement may be calculated with reference to specified performance criteria. There are no rules as to how to apply such criteria but you would need them to be attainable and transparent for them to properly motivate staff.

The employee must also pay the Exercise Price. This is the price for each share as set out in the Option Agreement, multiplied by the number of shares they wish to acquire.

Where there is an exit and a third party is going to immediately buy the shares from the employees, payment is normally made by way of a deduction from their eventual sale proceeds, and the solicitor acting for the selling shareholders will usually facilitate that.

If any Income Tax or National Insurance Contributions (NICs) are due in relation to the exercise (see tax considerations below), where there is an exit the company may require a deduction to be made from the employee's sale proceeds. Alternatively, the employee may have responsibility for settling the tax themselves.

The company may require employees to sign additional documents, such as tax elections, a shareholders' agreement, or any documents that may form part of the exit process.

What Happens if an Employee Leaves?

If an employee either gives or receives notice of termination of employment, their right to exercise their option should be suspended. If their employment is terminated at the end of their notice period, or if they cease to be an employee in any other circumstances, their option will lapse. However, this position may be overridden when an employee is held to have been unfairly dismissed.

If an employee leaves after they have become a shareholder it is likely that the company will wish for the employee to sell their shares either to other existing shareholders or to the company itself. The company can make this so by including automatic transfer provisions in the company's articles or in a Shareholders' Agreement – 'good' and 'bad' leaver situations can also be contemplated.

How do Options Lapse?

There are various circumstances that can give rise to an employee's option lapsing. These include:

- an attempt to transfer, assign, or create a charge or mortgage over the option;
- the passing of the tenth anniversary of the grant date (this as per the legislation on EMI schemes);
- the death of the employee, albeit there is some relaxation in the legislation for the employee's personal representatives to exercise an option on the employee's behalf, assuming the agreement allows it;
- if the employee leaves the company as explained above; or
- if the employee becomes bankrupt or makes a voluntary arrangement with creditors.

What are Disqualifying Events?

If a Disqualifying Event happens, this may have an adverse effect on the tax treatment of EMI options.

There are several kinds of Disqualifying Event, most of which relate to the company (e.g. a loss of independence, or a change of activity), and are therefore outside of the employee's control. For this reason, the Option Agreement may allow for an exercise of the option upon a disqualifying event occurring.

Disqualifying Events also include ceasing to be an employee of the company or a failure to attain the working time commitment required by the legislation.

Good or bad leaver provisions can be contemplated to outline what happens with the shares for any staff leavers.

Tax Considerations for EMI Schemes

Upon the grant of the option: No tax or NIC is payable when options are granted to the employees. The employees do not have to report the grant of the option to HMRC themselves, but it will be reported to HMRC by the company.

Upon the exercise of the EMI option: Where an Exercise Price for the shares is at least as much as the market value at the time of the option being granted, the employees do not have to pay any tax or NIC when they exercise their options. If the Exercise Price for the shares is below that market value then tax and (where shares are treated as being readily convertible to cash – i.e.. just before a sale of the whole company) NIC will be payable.

If any Income Tax arises employees exercise their options, how tax is assessed and collected depends on whether the shares are deemed readily convertible assets (RCAs) at the time of exercise.

This will be the case if a sale of the company to a third party is imminent.

If the shares are RCAs, any Income Tax will be collected through the PAYE system and employees' National Insurance will be payable. If the shares are not RCAs, the Income Tax is paid by way of a Self-Assessment tax return, and no National Insurance is payable. Employees may require some guidance from the company in these areas.

If the shares are RCAs when the options are exercised, the company will be required to pay Employer's NICs (the 2023/24 rate being 13.8%). Some option agreements require the employees to compensate the company for employer's NICs in relation to the employee's particular option exercise.

When an employee sells the shares acquired through an EMI option, they may be liable to Capital Gains Tax (CGT).

The amount charged to CGT is calculated as follows:

- take the sale proceeds and deduct any costs of sale, such as transaction costs;
- deduct the exercise price paid; plus any amount of which the employee was liable to income tax on exercise of the option; then
- deduct whatever amount of the CGT annual exemption is available (the annual exemption is £6,000 for the 2023/24 tax year, which is set to reduce to £3,000 for the 2024/25 tax year).

If there are at least 24 months between the date of the option being granted and the share sale, it's possible that the employee will be entitled to claim 'Business Asset Disposal Relief' (BADR). BADR provides that up to £1 million of an individual's lifetime gains will be taxed at 10%.

BADR will not normally apply if an EMI option is exercised following a Disqualifying Event and BADR can be lost or restricted if shares are subsequently transferred by the employee.

Any gain that is not covered by BADR will be taxed at the normal CGT rate, which currently is either 10% or 20% depending on the amount of other income of the employee for the tax year.

If CGT is payable on the sale of shares, the employee will need to pay this via the self-assessment system. Again, employees may require guidance from the company in this area.

No tax or NIC is payable when options are granted to the employees. The employees do not have to report the grant of the option to HMRC themselves, but it will be reported to HMRC by the company.

The EMI Scheme – A Case Study

In this fictional case study, we illustrate how an EMI scheme may play out…

Bootroom Boys Ltd is a long-established sportswear business. It is wholly owned by William Shankly, who has led the business to great success but feels it is now time to hand over the baton as the company looks to reach the next level over the next five years or so. There is a strong management team behind Shankly, notably Mr. Robert Paisley who is the de-facto Managing Director, and Ms. Roni Moran who is the Finance Director. Shankly feels that it is essential for both Paisley and Moran to be retained in the business in order for the five-year plan to be delivered and for Bootroom to be an attractive and saleable asset at the end. Shankly has consulted with his (superb) accountants who have recommended implementing an EMI Scheme.

- In his mind's eye, Shankly feels that the business will be worth circa £10m if they hit the growth and profitability outlined in the five-year plan (he recently had an unsolicited offer for the business of £3m which was rejected out of hand) but he's conscious that this may only be the case if Paisley and Moran will remain part of the business post-sale, he is therefore aware of the balance to be struck between offering the two of them enough of a potential stake to be exciting, but not so exciting that it is enough money for them to walk away from the business themselves, something around the 5% each mark is what he has in mind.
- Shankly knows the individuals well, and knows that they can be trusted to deliver results so doesn't see a need to apply any performance criteria to the scheme.
- If it transpires that the business isn't sold to an external party after the five-year plan period, Shankly has indicated that he would hang on to the business for an indefinite period, and would prefer not to have a shareholder relationship with Paisley and Moran. The ability to exercise options will therefore be limited to an exit event.
- Shankly feels that it's reasonable for there to be a price to be paid for the shares upon exercise and that a neat solution would be to equate the price to be paid with whatever the market value per share is when agreed with HMRC. This will mean there's no Income Tax or National Insurance to be paid when the options are eventually exercised. This market value will incorporate a substantial minority discount when agreed with HMRC, though the plan is that such a discount will be of no relevance on an exit.

Fast forward five years, and sure enough, a US company, Carpetbaggers Inc, have made a £10m offer to buy Bootroom's entire share capital which, despite having some misgivings about the buyer, Shankly has decided to accept. So, what happens now?

What does it mean for the option holders, Paisley and Moran? The numbers are explained on the next page…

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BOOTROOM BOYS LIMITED

Valuation for the purposes of granting EMI options			
Earnings based approach - Beginning			
Year ended		Revenue	EBITDA
31/12/2022	Forecast	£8,500,000	£900,000
31/12/2021	Actual	£7,200,000	£720,000
31/12/2020	Actual	£6,500,000	£600,000
Earnings multiple range		Low	4
		High	5
Enterprise value range		Low	£2,960,000
		High	£3,700,000
Equity value range		Low	£3,630,000
(see Note 2)		High	£4,370,000
Average of equity value range			£4,000,000
Value split			
W Shankly	1000	89.93%	£3,597,112
R Paisley	56	5.04%	£201,439
R Moran	56	5.04%	£201,439
	1112	100.00%	£4,000,000
Minority discount	(see Note 3)		0.7
Market value of all shares under option			£120,863
Market value per share			£1,079

Valuation for the purposes of granting EMI options			
Earnings based approach - End			
Year ended		Revenue	EBITDA
31/12/2027	Forecast	£15,400,000	£1,800,000
31/12/2026	Actual	£14,200,000	£1,650,000
31/12/2025	Actual	£12,300,000	£1,450,000
Earnings multiple range		Low	5
		High	6
Enterprise value range		Low	£8,166,667
		High	£9,800,000
Equity value range		Low	£9,183,334
(see Note 2)		High	£10,816,667
Average of equity value range			£10,000,000
Value split			
W Shankly	1000	89.93%	£8,992,806
R Paisley	56	5.04%	£503,597
R Moran	56	5.04%	£503,597
	1112	100.00%	£10,000,000
Minority discount	(see Note 3)		n/a
Market value of all shares under option			£1,007,194
Market value per share			£8,993

Potential outcome for single employees from the scheme		
Capital Gains Tax (CGT) payable		
Sale proceeds		£503,597
Less: Base cost	(see Note 4)	-£60,432
		£443,165
Less: Annual exemption		-£6,000
		£437,165
*Tax payable		£43,717
Income Tax payable		
Market value at date of grant		£60,432
Less: Exercise price	(see Note 4)	-£60,432
Amount subject to Income Tax		£ -
Tax payable		£ -
Overall picture		
Sale proceeds		£503,597
Price paid for shares		-£60,432
Income Tax payable		£ -
CGT payable		-£43,717
Net proceeds		£399,449

*With Business Asset Disposal Relief

Note 1 – Earnings Multiple Range

As a company establishes a record of consistent growth and profitability, it becomes more valuable. This is reflected in an increase in the multiple applied (in this case) to a three-year average of EBITDA. This is for illustrative purposes only.

Note 2 – Enterprise v Equity Value

Most profitable companies will have cash (or let's say an amount of net current assets) on their balance sheet that is surplus to their short-term working capital requirements. Any purchaser would be required to pay for such excess, and in this case, we have assumed the amounts to be £670,000 in the beginning, and £1,016,667 at the end so that we end up with nice round numbers!

Note 3 – Minority Discount

It is accepted that small stakes in private limited companies do not, in isolation, carry full pro-rated value due to the lack of ability to control the company's affairs and the general lack of marketability. Holdings of 5% should justify a discount, from the pro-rated value, of at least 70%. This discount would not be of relevance on an Exit as Shankly, Paisley and Moran will be selling to Carpetbaggers Inc on exactly the same terms.

Note 4 – Exercise Price

Most times it is decided to set the exercise price (i.e. what employees need to pay for the shares) at the market value agreed with HMRC. This would mean that they would not need to pay any income tax or NIC when they came to exercise the options. This figure then becomes the employee's base cost for the purposes of CGT.

As a company establishes a record of consistent growth and profitability, it becomes more valuable.

Company Share Option Plans (CSOP)

CSOPs are a popular alternative for companies that aren't eligible for the EMI scheme.

The most popular share incentive scheme tends to be the EMI scheme. However, many companies won't be eligible to implement EMI schemes, potentially due to their size (i.e. over 250 employees or gross assets of more than £30m) or their trade not qualifying.

For these companies, their next port of call is often another one of HMRC's approved share option schemes: Company Share Option Plans…

The Similarities to the EMI Scheme:

CSOPs are very similar to EMI schemes, as shown by the below key points for CSOPs:

- CSOPs allow companies to grant options to employees to acquire shares in a company at a future date.
- Companies can apply different vesting conditions for the granted options.
- Normally, no income tax or NIC is payable until the options are exercised.
- Once the sales are sold or transferred on exercise, the gains will be subject to the favourable capital gains tax regime.
- It is a discretionary scheme so select directors and employees can be chosen for the scheme.

The Differences to the EMI Scheme:

However, there are some key differences which we'll outline below:

- Firstly, whilst the EMI scheme's share options cannot exceed £250,000, CSOPs have a lower limit of £60,000 for any one person (this increased from £30,000 from April 2023).
- The price payable for the shares on the exercise of a CSOP option cannot be less than their market value on the grant date. This is possible to do for EMI schemes, but additional Income Tax & NIC's may be due when this is the case.
- Unlike the EMI scheme which has a £3m limit for the total shares that can be granted, no such overall company limit applies for CSOPs. Whilst, both schemes are discretionary schemes, the absence of a limit means they can be set up as an all-employee plan if desired.
- Employees don't need to meet any hours worked per week criteria to take part in CSOPs.
- One of the main benefits of EMI schemes for employees is that there's the prospect of the capital gains qualifying for Business Asset Disposal Relief (BADR), meaning the gain is taxed at 10%. However, unlike the EMI scheme, the usual requirement of owning at least 5% of the shares in the company to qualify for BADR relief applies. Therefore, either 10% or 20% CGT will be payable depending on the amount of other income the employee earns within the tax year.

Save As You Earn (SAYE)

Save As You Earn (SAYE), sometimes referred to as a Saving Related Share Option Scheme, is another tax-advantaged share option plan.

One of the key differences between SAYE schemes and the EMI & CSOP schemes that we've already covered is that it's an all-employee plan. Therefore, it should be open to all employees and cannot have individual performance targets built-in.

However, if this key difference isn't crucial to your objectives from a share scheme, please read on…

An Overview:

The SAYE scheme allows all employees to save up to £500 per month with a savings contract of either three or five years. This amount should be fixed by each employee at an amount between £5 to £500 (although, companies can set a minimum of £10 rather than £5 if they wish) and is then equally deducted from their salary throughout the period.

When the share options are granted, a fixed price is determined for which the shares can be acquired for. This fixed price can include a maximum discount of 20% of the market value.

At the end of the three or five-year period, employees then have the flexibility to either buy the shares or take the cash. This effectively makes it risk-free from the employee's perspective, as they can purchase the shares if the market value has increased from the original exercise price, or take the cash if otherwise.

What are the Tax Implications for Employees?

No tax is payable on the grant of the SAYE options and no income tax or NIC's are paid on the exercise of the option. When the shares are disposed of, capital gains tax would be payable on any gains made. Given the lower cap (certainly in relation to the EMI & CSOP plans), it's very common that no CGT is payable due to the annual allowance (£6,000 as of the 2023/24 tax year, set to reduce to £3,000 for the 2024/25 tax year).

Employees also wouldn't pay CGT if the shares are transferred to either an Individual Savings Account (ISA) or to a pension (but conditions, such as when the shares are transferred, apply).

At the end of the scheme, the interest and any bonuses accrued on the savings would be tax-free too.

When are the Options Exercised?

Usually, the SAYE options aren't exercised until after the three or five-year savings contract. However, events such as a company sale can trigger an early exercise event. Like with the other schemes, 'good leaver' conditions can also be established so options are exercised early. Employees are also able to stop saving at any point (where the contributions will be repaid) or they can defer payments if needed.

The SAYE scheme offers a tax-advantageous way to offer share options to all employees.

Share Incentive Plan (SIP)

Similar to the SAYE scheme, the SIP is another tax-advantaged all-employee plan. This allows employees to be awarded shares that are then held in a trust, usually for five years so the full tax benefits are received.

What types of companies operate SIPs?

The employing company must normally be listed on a recognised stock exchange. If it's not directly listed, then it must either be a subsidiary of a listed company or otherwise not under the control of any company. In combination, the cost of setting up and running the scheme and the 'all-employee' requirement, means SIPs are usually more suited to large companies.

How do they work?

Under a SIP, employees can be offered a combination of the below:

Free Shares – employees can be offered up to £3,600 of free shares per year. These would have holding periods between three to five years before they can be withdrawn in normal circumstances.

Partnership Shares – in addition to the free shares, employees can purchase 'partnership shares' of up to £1,800 a year (or 10% of their salary if this is less). These are purchased out of pre-tax salary.

Matching Shares – employers are also able to offer two free matching shares for each partnership share. This effectively creates a discount on the shares for the employee.

Dividend Shares – companies offering SIPs to their employees can require (or allow) any dividends that are paid on the above shares to purchase 'dividend shares'.

In total, with the free, partnership and matching shares, this can allow up to £9,000 shares for an employee per year.

What are the tax implications for Employees?

In general, the advantage of SIPs for employees is that no income tax or NIC's will be due if the shares remain in the plan for at least five years. However, there are tax implications if not, as we outline below:

When shares are acquired - no income tax or NIC's is paid on the value of any of the shares (including on dividends to purchase dividend shares)

When shares are withdrawn after 5 years – no income tax or NIC to pay.

When shares are withdrawn from the plan within 3 to 5 years - For free, matching and partnership shares, income tax is payable on the lower of the market value when the shares were acquired (or the salary used to acquire them, in the case of partnership shares) or the market value when they were withdrawn from the plan. No income tax or NIC is due on the dividend shares.

When shares are withdrawn from the plan within the first 3 years – income tax is payable on the market value of the free, matching and partnership shares. Any dividends that were used to buy shares are taxed as dividends.

From a Capital Gains Tax (CGT) perspective, no CGT is payable when the shares are withdrawn, even if they are then sold immediately. However, if they are disposed of at a later date and a gain has been made since the withdrawal, then CGT would be due (providing the gain isn't covered by the individual's CGT allowance).

SIPs, through a combination of shares, allow employees an entitlement of up to £9,000 shares per year

Growth Shares

As the name suggests, growth shares allow employees to be rewarded by the *growth* of the company's market value.

If you wish to reward employees immediately through equity, then growth shares may be your preferred solution. Here employees are awarded actual shares as opposed to options over shares.

These are likely to be ordinary shares in the capital of a company, but they could be ordinary shares with different characteristics to what we might call 'full' shares – specifically they may only enjoy rights to capital where the company is sold above a certain threshold, or they may not have voting rights. Having multiple types of ordinary shares also means that the directors can declare dividends at different levels for the full shareholders and the growth shareholders.

How Do They Work?

Take a company which is worth £5m. A new type of growth share might be issued to employees which gives the employees 5% of the overall shares in issue. However, it could be made so that they only have a right to participate in equity value above £5m. The initial value of the growth shares will therefore be very low on award because at the time of issue the equity value all belongs to the 'full' shares. Consequently, the employees do not need to pay very much for the shares and even if they paid below whatever market value was determined at the time of issue, there won't be much Income Tax to pay.

As far as selling this plan to the employees is concerned, they need to think about what happens if the company were to be subsequently sold for £10m, the growth shares would have a right to 5% of the value in excess of £5m – i.e. £250,000. This gain would be subject to the more favourable capital gains tax rules including Business Asset Disposal Relief at 10%.

There may be a need to consider how shares are dealt with if and when an employee leaves ('good' and 'bad' leaver provisions), and perhaps drag and tag clauses on an exit.

All of this can be dealt with in the Articles of Association so no need for a Shareholders Agreement, there is no real interaction with HMRC during this process. Unlike with a share option plan there are no accounting entries to be considered beyond the original issue of the shares.

Phantom Shares

If you do not want to part with equity in your business then there are other options available, one of which is phantom shares. Unfortunately, there are no tax advantages here whatsoever - we are effectively talking about a deferred bonus arrangement.

Unlike normal annual bonuses, the idea is that the employee has to stick around for a set period or until, perhaps, an exit event in order to get their hands on the bonus.

The quid pro quo of no tax advantages is complete flexibility in the way the scheme is designed, and the absence of any sort of reporting requirements to HMRC.

A phantom plan would typically contain the following features:

- payment to an employee is contingent on them remaining in employment and attaining specified individual and/or company performance targets.
- a lump sum cash payment at the end is determined by a notional share price growth from the date of award to the date of exercise.
- a clear and consistent approach to valuing the company so that notional share price growth can be tracked.
- provisions for early payment in the event of a sale or flotation.
- frequent communication with plan participants so that they are aware of the value being created.

The employees will see Income Tax (probably at the higher rates) and national insurance deducted when the pay-out occurs. The employer will also pay National Insurance, the 2023/24 rate is 13.8%.

Corporation Tax relief will not be available until the pay-out occurs – for arrangements that constitute cash-settled share-based payments, this is going to correspond with the accounting entries with a lump sum expense booked at the pay-out date.

One extra point to consider is that a potential purchaser is going to have to consider the impact of the bonus pay-out on the company’s cash position. Too big an amount could be seen as being a poison pill and turn out to be a deal-breaker. It is probably sensible therefore for the company to think about a cap on the overall amount to be paid out from the scheme.

In essence, a phantom share scheme is a deferred cash bonus arrangement and no actual shares are involved so the existing shareholders equity positions will not be diluted.

The Next Step

If you have any questions about long-term incentive plans or would like to know how they could work for your business, please contact our long-term incentive plan experts:

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As tax partner, Alison's main role is providing tax advisory and compliance services to corporate clients. Alison is both a fellow member (FCA) of ICAEW and a Chartered Tax Advisor (CTA). Alison works with owner-managed businesses focussing on all business tax issues, including share option schemes.

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James Price is a partner at UHY who heads up corporate finance, both in respect of delivering transactions, advisory and valuation services to clients and in raising the firm's profile amongst the wider business community. James is an expert in employee ownership, both through shares and share option schemes and the utilisation of Employee Ownership Trusts.

James is passionate about enabling business owners to achieve their long-term objectives and is seen as a valued partner in the business journey.