SLAUGHTER AND MAY

Incentives Bulletin

April 2020

Welcome to the April edition of our Incentives Bulletin, updating you on the latest developments in remuneration and share schemes. Much of the recent focus in recent weeks has been on the impact of the **COVID-19** pandemic on employees and their incentive arrangements, and you will have seen our separate briefings on this topic. In this Bulletin, we look at some of the other issues which you should be aware of: the proposals announced in the **UK 2020 Budget** relating to employee incentives, the UK Government's proposed **consultation on the enterprise management incentive (EMI) scheme**, the reduction of **HMRC's official rate of interest on employment-related loans** and the UK Parliament's consultation on the draft legislation implementing recommendations from the **"loan charge" review**. We end with a timeline of **key dates** in employee incentives coming up in the near future.

UK 2020 Budget

Summary and key practice point:

The headline message from the Budget is that entrepreneurs' relief is to be retained, despite recent speculation that it would be abolished in its entirety.

The principal change is the reduction in the maximum lifetime amount of gains that an employee can make when disposing of shares, on which entrepreneurs' relief can be claimed. Entrepreneurs' relief reduces the effective rate of capital gains tax an individual pays on a sale of shares to 10%. The 2020 Budget reduces the amount of gains that can be subject to this favourable regime from £10 million to £1 million. Two classes of employee are going to be most affected by these changes:

- Individuals who hold a material stake (at least 5%) in their employing company; and
- Holders of tax-advantaged Enterprise Management Incentive (EMI) options. EMI

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option holders can benefit from entrepreneurs' relief (regardless of the size of their shareholding), provided that the period between the grant of the option and the sale of the underlying shares is at least two years. It is noted that the UK Government estimates the change to the lifetime limit will have an impact on around only 120 individuals holding EMI options or shares acquired under EMI options.

This change will affect disposals made on or after 11 March 2020, although, where contracts for the disposal of shares have been exchanged before 11 March 2020 but completion has not yet occurred (and for certain exchanges of shares made before 11 March 2020), special rules apply.

Review of Enterprise Management Incentive (EMI) scheme

Summary and key practice point:
The Chancellor announced that the UK Government will undertake a review of the EMI regime. The EMI regime governs a tax advantaged share option scheme focussed on smaller, high-growth companies, and is an effective way for qualifying companies to incentivise their employees by way of tax efficient equity-based awards. The purpose of the review is to ensure that the scheme provides adequate support for high-growth companies to recruit and retain the best talent in order to scale up effectively, and examine whether more companies should be able to access the scheme.

As the EMI regime constitutes "state aid" for EU competition law purposes, the direction that the review takes will depend on the upcoming negotiations with the European Union, but on the basis that HMRC recently confirmed that EMI's state aid approved status will apply until at least the end of the transition period (i.e. 31 December 2020), EMI continues to be available for qualifying companies.

Annual CGT allowance

The standard annual exemption from capital gains tax has been increased to £12,300 for the 2020/21 tax year.

COVID-19: Incentives issues

The COVID-19 pandemic continues to cause economic uncertainty and have a profound impact on global financial markets. You will have seen our separate briefing on Employment and Incentives Issues of 19 March 2020 which outlines some of the common issues with which companies are continuing to grapple.

IR35 reforms postponed until April 2021

The UK Government has announced that changes to the IR35 off-payroll working rules in the private sector have been delayed by 12 months in response to the business uncertainty surrounding COVID-19. The legislation is now expected to take effect on 6 April 2021, rather than 6 April 2020.

Official rate of interest on employment-related loans

The UK Budget provides a fall in the official rate of interest on employment-related loans from 2.5% to 2.25% with effect from 6 April 2020.

Under Part 3C of Chapter 7 of the Income Tax (Earnings and Pensions) Act 2003, tax is generally chargeable on an employment-related loan to the extent it is interest-free or carries a rate of interest rate lower than the official rate. The cash equivalent of the benefit of the loan – being the difference between the amount of interest that would have been payable at the official rate and the amount of interest (if any) actually paid – is typically treated as earnings from the employment, and is subject to tax at the individual's marginal income tax rate as well as class 1A (employer only) National Insurance contributions.

Disguised remuneration: Loan charge Parliamentary debate

On 19 March 2020, MPs debated the UK Government's response to the independent review of the disguised remuneration loan charge. The "disguised remuneration" rules were introduced in 2011 as part of HMRC's strategy to counter the use of employee benefit trust arrangements to avoid or defer tax liabilities on amounts HMRC considered to be employment income.

MPs involved in the session were critical of both the independent review, led by Sir Amyas Morse, and the Government response, including the Government's rejection of some of the recommendations in the report and the prospect of HMRC pursuing retrospective action. The debate closed with the House resolving that the loan charge is an "unjust and retrospective tax", noting that the law on the loan charge was not settled until 2017 and calling on HMRC to cease action in relation to loans made before 2017.

Horizon scanning

What key dates and developments in employee incentives should be on your radar?

6 July 2020	HMRC deadline for filing annual share schemes returns for 2019-2020
31 December 2020	Transitional arrangements under the UK-EU withdrawal agreement expected to end unless extended
6 April 2021	Off-payroll working rules (IR35) come into force for the private sector

We are also expecting interesting case law developments in the following key areas in the coming weeks (although the release of the relevant judgments is likely to be impacted by COVID-19):

- Employment-related securities options: *HMRC v Vermilion Holdings Limited* (The Upper Tribunal to determine HMRC's appeal against the First-tier Tribunal decision that share options granted by a company to a director were not employment-related securities; they were not issued by reason of his employment).

- IFRS 2: *HMRC v NCL Investments Ltd* (The Court of Appeal to determine whether account debits mandated by IFRS 2 in relation to the grant of employee share options were deductible in the employing company's corporation tax computation). The case relates to the law as it was before amendments made by Finance Act 2013 came into force.

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Dated April 2020

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