**Reward & Retirement Provision Assignment 3 Notes**

**(Part 3 – Flexible Benefits and Salary Sacrifice)**

**(Chapter 1 Company Share Plans - Chapter 2 Flexible Benefits)**

*Recommended Time: 3 hours*

1. **Explain why a company may wish to provide a share plan for its employees.**

**5 marks**

Part 3 Chapter 1.1

Answer should cover:

* + - Motivational tool for improving employees’ commitment and alignment to the company
    - Alternative to cash profit sharing
    - Individuals who have a stake in the company they work for are, it is hoped, going to have a greater interest in its financial performance and a better understanding of the need for profit
    - Company Share Option Plans and Enterprise Management Incentives can be used as a form of long-term bonus incentive for senior employees and executives
    - Companies going public for the first time may seek to allay the fears of its employees by awarding free shares or by giving them an opportunity to buy shares on favourable terms at the time of flotation
    - Can be used by start-up businesses to attract talented employees as alternative to salary and bonuses

1. **Outline the eligibility, savings and duration restrictions that apply to approved save as you earn share option plans.**

**20 marks**

Part 3 Chapter 1.2

Answer should cover:

Eligibility

* + - Intended for all or most employees
    - Can include employees of subsidiary companies
    - Company can set qualifying period of employment – not exceeding five years

Savings restrictions

* + - Fixed monthly amount (in multiples of £1) between £5 and £500
    - Company may set a lower maximum limit
    - For a period of three or five years
    - Earn interest through terminal bonus at a rate which is fixed by HMRC

Duration restrictions

* + - Option to buy shares after three or five years
    - Company may restrict choice

1. **A new employee is looking at joining your company’s Share Incentive Plan (SIP) and has asked for information on the shares that can be purchased through the SIP. Prepare an email to the employee confirming the different ways shares are purchased, any restrictions that apply on the values purchased, and the tax implications.**

**20 marks**

Part 2 Chapter 1.4

Answer should cover:

*Types of shares:*

• Free shares:

* + - * + £3,600 limit in any tax year
        + The company can set a qualifying period of employment, but this may not exceed 18 months

• Partnership shares:

o Limit of lower of £1,800 or 10% of income for the tax year

• Matching shares:

* + - * + Employers can give up to two free matching shares for each partnership share the employee buys
        + The company can set a qualifying period of employment, but this may not exceed 18 months

* + - * Dividend shares

*Tax:*

* + - * Tax free provided that they are held for five years in the SIP trust. Reduced tax is payable if they are withdrawn between three and five years from the award date
      * For dividend shares, no tax if held in SIP trust for at least 3 years
      * Special provisions apply for retirees and other circumstances such as death and redundancy.

1. **As your company’s Benefit Consultant, you have been asked to prepare a report for presentation to the Board regarding the introduction of an unapproved share plan. Your report should include:**

* + **The reasons why a company may operate an unapproved share plan**
  + **Who they are designed for**
  + **The characteristics of the types of unapproved plans**
  + **Typical conditions to be met before employees are entitled to shares** • **The taxation position when employees become entitled to shares.**

**30 marks**

Part 3 Chapter 1.5

Answer should cover:

* + Reasons for operating such a plan for executives/ senior employees, including restrictions of unapproved arrangements –The tax-free limit under the all employee approved plans is too small to be of value for executive plans and these plans do not allow for any discretion or performance related payment. For a number of years, CGT rates were aligned with Income Tax rates – in this situation the advantages of approved share plans over unapproved plans were greatly diminished, particularly for executives with other sources of capital gains (and therefore no tax-free annual allowance left). Even the approved share option plan (CSOP) has a limit of £30,000 that in today’s world is inadequate, so some sort of unapproved top up is essential. Increasingly, the share option mechanism has been seen as unattractive to companies, who have switched over the years away from share options toward “restricted share” plans.
  + Characteristics of an unapproved option plan - can be identical to a CSOP except for there being no ceiling on award sizes (other than any required by shareholders). Consequently, these plans allow for complete discretion on participation, the type of share under option and the size of individual awards. Indeed, many companies operating share option plans have dispensed completely with the CSOP and operate an unapproved plan only for simplicity
  + Characteristics of a restricted share plan - Instead of the employee receiving a benefit equal to the growth in the share price since the award date, holders of restricted shares are entitled to the entire value of the share without any requirement to make a payment on “exercise”. This obviously means that a restricted share awards is more valuable than an equivalent option award – by a factor of around 3:1 – so is normally accompanied by proportionately smaller awards, thus conserving shares for the future. Restricted share plans are also attractive to employees when share prices fall. Under an option plan, this wipes out any potential benefit from the plan, while under a restricted share plan the benefit remains, though reduced in value.
  + Performance targets option - typically incorporate some sort of company financial performance target that has to be met over the three years before the employee can get any shares – this is generally on a sliding scale between zero delivery and full delivery. For this reason, restricted share plans are often referred to as performance share plans
  + Taxation of any gains - because these plans are unapproved, the gains made by employees are taxed as income on the date that the employee becomes entitled to the shares. In the case of an option, the tax is on the gain in share price since award, while in the case of a restricted share the tax is based on the entire value of the shares. National Insurance contributions are also levied on both employee and employer. Any subsequent share sale may trigger a further Capital Gains Tax charge on gains since the date of entitlement to the shares.

1. **Outline the advantages and disadvantages of a flexible benefits plan.**

**10 marks**

Part 3 Chapter 2.2 and 2.3

Answer should cover:

*Advantages:*

* + Providing choice to meet individual needs of employees
  + Aid recruitment and retention
  + Ability to introduce new benefits at relatively low cost
  + Sharing costs with employees
  + Harmonising benefits if various benefits are provided to different sections of employees through mergers and acquisitions
  + Support culture change by moving from employer control to employee choice

*Disadvantages:*

* + Complexity and costs to set up
  + Administration
  + Inappropriate choices made by employees
  + Communication burden
  + Risk of higher insurance premiums as a result of member choices
  + Potential lack of buying power of smaller companies

1. **Outline what a Lifetime Individual Saving Account is and how it works.**

**5 marks**

Part 3 Chapter 2.6

Answer should cover:

* + - Introduced in April 2017
    - Designed to help young people simultaneously save for a first home and for their retirement
    - Age limitations
    - Contribution limitations
    - 25% Government bonus
    - Tax privileges
    - Access to funds

1. **Outline the key stages of a communication strategy for rolling out new flexible benefits.**

**10 marks**

Part 3 Chapter 2.7

Answer should cover:

* + - Communication should take place at every stage of the lifecycle of a flex project
    - Communication strategy for flexible benefits should address four key stages:

Stage 1 - Initial Research Stage 2 - Pre-Launch

Stage 3 - The Launch Stage 4 – Review