

## EMI state aid approval lapses

**What are the practical implications of the expiry of EU state aid approval for EMI schemes?**

The enterprise management incentive (EMI) regime was introduced by FA 2000 as a way of helping smaller entrepreneurial businesses recruit and retain the best talent. As the tax benefits afforded by EMI are only available to companies with certain qualifying business activities, they involve the provision of state aid. Under EU rules, state aid is unlawful unless it falls within an applicable exemption or if it is seen as compatible with treaty provisions. The current EMI regime was approved by the European Commission in a decision of 9 July 2009 (although it was noted that the UK had put the regime in place many years previously, in breach of EU rules). The approval lapsed on 6 April 2018, and whilst a Commission decision to renew approval has been sought by the UK government, it has not yet been forthcoming.

On 4 April 2018, HMRC issued Employment Related Securities Bulletin No. 27 (April 2018) stating that 'the state aid approval applies to the granting of share options and therefore that share options granted up to and including 6 April 2018 won't be affected by this lapse of the approval'. There is no clarity on the length of time it may take to secure fresh approval, but the UK government is 'working hard to ensure this period is as short as possible'.

**Grant of new EMI options:** In terms of companies wanting to grant EMI options, the best advice is to wait for fresh approval to be secured. The Bulletin warns that 'EMI share options granted in the period from 7 April 2018 until EU state aid approval is received may not be eligible for the tax advantages'. Aid implemented without EU clearance could result in the UK government being required to recover the tax benefits from the option holder.

**If there is a pressing need to grant EMI options ... it would be worth granting on terms which would enable the options to be unilaterally surrendered by the grantor and re-granted when state aid approval is issued**

If there is a pressing need to grant EMI options, perhaps due to the onset of a close period for share dealing purposes or there are other strong commercial drivers, it would be worth granting on terms which would enable the options to be unilaterally surrendered by the grantor and re-granted when state aid approval is issued. The terms of the option would require careful drafting, particularly where they are subject to the achievement of vesting or other performance conditions. Any satisfaction of the conditions or time vesting during the intervening period could be credited under the terms of the replacement option. However, the one-year holding period for the purposes of entrepreneurs' relief would only commence at the time of the replacement option grant, which would need to be notified to HMRC as an EMI option through HMRC's employment related securities service.

A perhaps more challenging issue would be any increase in the market value of the shares during the intervening period. If the full tax advantages are to be secured, the replacement EMI option would need to be granted at the then current market value. Alternatively, the previous exercise price could be maintained, with a commitment by the company to provide a grossed-up bonus to meet the tax liability arising at exercise.

### Exercise of existing EMI options:

Whilst the words of HMRC in the Bulletin that the tax reliefs associated with EMI attach to the 'grant' of the EMI option are to be welcomed, the wording in the approval states clearly that 'the notification covers duration until 6 April 2018, which is the period during which EMI share options can be exercised' (emphasis added). For EMI options exercised in the period prior to the issue of new state aid approval, there remains a residual risk that they may not be tax free. However, it seems unlikely that recovery action would be taken by the Commission, on the basis it is arguable that they have created a legitimate expectation that EMI options granted pursuant to their approval (with a ten-year life span) do not involve state aid. Even if the Commission took action, it is not clear the basis on which recovery could be pursued. It is arguable that the unauthorised tax advantages should apply in respect of the growth in value of the shares from 7 April 2018 onwards and not from the original grant date. Equally, given the wording in the Bulletin which confirms 'HMRC will continue to apply its current guidance and practice, in relation to... options validly granted as EMI share options up to and including 6 April 2018', it is not anticipated they would pursue tax on the exercise of pre-7 April 2018 qualifying EMI options.

Undoubtedly there will be companies in the middle of a sales process, where EMI options will need to be exercised prior to completion. It seems that any tax risk associated by loss of EU approval would be outweighed by the commercial need to get transactions done. However, cautious purchasers may wish to retain a proportion of EMI option proceeds to cover any tax risks, pending further clarity on the position. ■

*Karen Cooper, Cooper Cavendish LLP  
(karen@coopercavendish.com)*