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Restricted share schemes

A restricted share scheme grants an employee "restricted" shares in their employer company. The shares are issued with restrictions requiring the shares to be retained on trust for the participant for a fixed period before they can be sold. The employee has beneficial ownership during this period. The fixed retention period is commonly called the 'clog' period.

Structure of a restricted share scheme

The scheme is established by the setting up of a trust or other holding mechanism which holds the shares for the clog period. The restricted shares must be held by a trustee or by a nominee for the participant for the duration of the clog period.

During the clog period, the shares cannot be assigned, charged, pledged as security for a loan or other debt, transferred or otherwise disposed of, other than on death of the participant or certain takeover situations.
The participant must agree in writing to abide by and not to seek to break the clog period.

End of clog period – Sale of shares

Once the clog period has expired the shares can be assigned, charged, pledged as security or disposed of by the participant. CGT may arise on a future exit of the participator from the company, being an assignment, disposal or transfer of the shares. The current rate of CGT is 33%. In calculating the taxable gain, the deemed income taxed on the issue of the shares plus any consideration given is deductible. For instance, in the example to the right, assuming nothing has been paid for the shares, the deductible base cost in the shares would be €20,000. Where the participant holds 5% of more of the ordinary shares in a company, and where other conditions are met, the participant should be able to claim entrepreneur's relief on the sale of the shares. Entrepreneur's relief reduces the rate of CGT to 10% on the first €1m of qualifying lifetime gains.

Tax consequences for employees

PAYE, USC and employee PRSI arise on the award of restricted shares. The tax charge on the grant of shares is reduced by the length of the clog period:

Period of Restriction	Percentage reduction
One year	10%
Two years	20%
Three years	30%
Four years	40%
Five years	50%
More than five years	60%

The tax is withheld by the employer and remitted to Revenue through PAYE.

Example - Cash bonus vs restricted shares

	Market value	PAYE/PRSI
Cash bonus	€50,000	
Employee PAYE/PRSI/USC (assume marginal rate) 52%		€26,000
Employer PRSI @10.75%		€5,375
Total tax cost		**€31,375**
Restricted shares (Five years plus clog):		
Market value shares	€50,000	
Value reduced by clog	(€30,000)	
Taxable value	**€20,000**	
Employee PAYE/PRSI/USC (assume marginal rate) 52%		€10,400
Employer PRSI		nil
Total tax cost		**€10,400**
Tax saving		**€20,975**

"Good leaver/bad leaver" and sale of company

Restricted share schemes can have "good leaver/bad leaver" provisions, for instance which can cater for forfeit on a participant moving employer, etc., during the clog period.

Restricted shares can also cater for events like a market sale or company takeover. In such circumstances, the share restriction can be lifted under drag and tag provisions and the shares sold by the participants. The PAYE is recalculated so that the actual clog period deduction applies.

Company tax relief and reporting requirements

The set up and administration costs of the restricted share scheme should be allowable as a deduction for corporation tax purposes.

Companies awarding restricted shares must include details of the scheme in their annual corporation tax return. Revenue may require a Form RSS1 to be completed by **31 March** of the tax year following the award of restricted share scheme, amendment to a restricted share scheme or the disposal of shares.

Contact

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