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Transactions and Share Schemes - Step Plan

by **Gillian Dully**

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27th September 2024 | by Gillian Dully

If you are considering the sale of your business and have an employee share scheme or incentive arrangement in place, there are several issues to consider in advance.

Corporate transactions, to include, corporate mergers and acquisitions, share sales, asset transfers and re-organisations will impact on any share schemes or incentive arrangement operated by the business.

Type of Deal

The type of deal involved will determine how the share scheme or incentive arrangements ought to be treated in the context of the overall transaction.

First Steps

Firstly, a seller ought to clearly identify the nature of the transaction being contemplated (e.g. is it a share sale, an asset transfer, a merger, a re-organisation etc…).

In a share sale, the employer entity does not change so the share scheme may be capable of continuing in its current form or the relevant transaction may trigger a realisation event for the participants. However, if shares or options have been granted over shares in another target group entity, then depending on what entities are being acquired, the scheme may not be capable of continuing in its present form.

Next Steps

Once the deal type has been established then various factors require careful advance consideration to include the following: -

- What type of scheme does the business operate? For example, is the scheme a Revenue approved arrangement (e.g. Save as you Earn Scheme, an Approved Profit-Sharing Scheme, a Restricted Share Scheme or an Employee Share Ownership Trust) or is it an unapproved share option scheme, growth share scheme or some other type of employee incentive scheme?
- What type of business is involved? For example, is it a regulated or listed entity?
- Does the business operate in multiple jurisdictions and where are the participating employees working?
- Are any participants a director or consultant rather than an employee?
- Have any pre-transaction re-organisations occurred in the target business or are they contemplated?

It is important that the documentation governing the share scheme or arrangements is carefully reviewed well in advance of the proposed transaction to assist in identifying any potential issues, preparing a step plan for any remedial steps required or other actions to be taken prior to completion of the transaction.

The constitution of the target entity and any relevant shareholders' agreements should also be reviewed to identify how scheme shares are to be treated, whether such shares can be sold as part of the sale process and what consents, if any ought to be obtained.

A buyer (or other contracting party) will likely be very focused on any share scheme or similar incentive arrangements operated by the target business.

If a share sale or asset sale is involved, a buyer will carry out a legal and tax due diligence review of any share schemes/employee benefits in place for employees of the target and will want to know in advance how the arrangements are affected by the transaction and how the seller proposes to deal with the schemes in the context of the overall transaction.

A seller should obtain legal and tax advice at the outset to clearly identify all relevant issues so that a tailored step plan can be formulated to deal with the scheme or arrangements.

Key questions to be considered by a seller at an early stage include the following: -

- Will the transaction affect the scheme or arrangement?
- Will the scheme be capable of continuing in its current form?
- Will options or shares vest?
- Will automatic acceleration of vesting apply?
- Will scheme participants be affected by the transaction?
- Will scheme participants be able to participate in the transaction (e.g. by selling their shares or receiving a payment)?
- what obligations/restrictions will be imposed on the target business:
- what powers or discretion can the target business exercise, if any?
- what notifications/filings need to be made?; and
- any relevant time frames for actions to be taken.

Depending on the nature of the corporate transaction, the existing scheme documentation may contain provisions dealing with the corporate event, but it is not uncommon for scheme documentation to be amended in advance of the transaction (subject to the scheme's amendment power and any relevant regulatory/legislative provisions).

Typically, the rules of a share scheme provide for the treatment of the shares or options in the event of a transaction and the board of directors of the target company, (**the "Board"**) may have discretion in terms of the treatment of the shares or options.

Assuming the Board has discretion under the scheme documentation, it will need to determine the treatment of any outstanding options and/or scheme shares in advance of a sale, obtain advice on the tax and legal implications of such proposed treatment, agree the proposals with the buyer and draft appropriate documentation and communications to employees to give effect to such proposal.

A buyer may not want the scheme to continue post-acquisition and may insist on a specific approach being adopted, for example, that unexercised options be exercised, scheme shares be sold, or scheme rights be cashed out as part of the sale process and the scheme terminated with effect from completion. A buyer is also likely to want to put in place their own form of incentive arrangements for key employees' post-acquisition.

Employee Communications

An important part of the transaction process will involve managing employee communications and a buyer is likely to want to have oversight of such communications.

Conclusion

It is important that a seller seeks professional legal and taxation advice at the earliest opportunity to ensure they are in complete control of share scheme matters in advance of any corporate transaction and to seek to avoid any complications or delays during the transaction process.

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