

HR Budget Briefing

Client Briefing

Incentives

Today's Budget saw a rebrand of the Company Share Option Plan, alongside updates to the Enterprise Management Incentive regime and a reduction to the Business Asset Disposal Relief lifetime limit. The Government also made a U-turn on its decision to reduce the cash ISA limit.

Rebrand of the Company Share Option Plan: The Government proposes to rebrand the current HMRC-approved Company Share Option Plan ("CSOP"). From April 2027, the CSOP will be known as the Enterprise Management Incentive Scheme 2 ("EMI2"). The rebrand is intended to reflect the role of the CSOP/EMI2 as an "option for growing companies that have moved beyond or are not eligible for" the original Enterprise Management Incentive Scheme ("EMI1").

From April 2027, the maximum value of shares that an individual can hold under CSOP/EMI2 unexercised options (valued at the time of grant) will be increased from £60,000 to £120,000. The increased limit means that, following the rebrand, companies may be able to grant options to employees in certain pay bands wholly within a tax-advantaged employee share plan regime.

The exercise period of CSOP/EMI2 options will also be increased to 15 years from the date of grant (increased from a 10-year exercise period under the current regime). This change will also apply retrospectively, so it will be permitted to extend the exercise period of CSOP options that have already been granted to 15 years.

However, despite the name change from CSOP to EMI2, it appears that the rebranded CSOP/EMI2 regime will not enjoy other flexibilities that are currently available for EMI1 options. In particular, the EMI2 regime will still require the use of market value options which must be held for at least three years before exercise to benefit from tax-advantaged treatment.

Changes to the current Enterprise Management Incentive scheme: The Government also announced changes to the original EMI1 scheme. From April 2027, the exercise period following a disqualifying event will be increased from 90 days to 180 days. The separate notification

requirement for EMI1 option grants will also be removed such that grants will instead be reported to HMRC through the existing EMI1 end-of-year return.

Business Asset Disposal Relief: The Government announced that it will reduce the lifetime limit for capital gains eligible for Business Asset Disposal Relief ("BADR") from £1m to £500,000 from April 2027. Shares acquired under EMI1 schemes currently qualify for BADR provided that certain conditions are met.

ISAs: The Government has decided not to reduce the annual cash ISA limit. The limit remains at £20,000 and will not be reduced to £12,000 as previously announced. The Government will work with industry to explore a new ISA incentive for people investing in a stocks and shares ISA for the first time.

Employment

The Budget reiterated the Government's intention to reform employee non-compete clauses and to launch a consultation regarding the wider use of restrictive practices affecting companies' access to talent.

Non-compete reform and consultation in relation to restrictive practices: The Government confirmed that it will legislate to "make sure that non-compete clauses will no longer be a barrier to hiring" for start-ups and scale-ups and to "ensure that workers in the everyday economy are not prevented from moving jobs". Despite speculation before the Budget that the proposal might be limited to certain sectors, the Government stated that the reforms "will apply across the whole of the economy".

It also confirmed that a consultation will soon be launched to understand the wider use of restrictive practices affecting access to talent. The Government has expressed that it is "keen to work with industry to ensure the action it takes is proportionate, evidence-based, and supports both the dynamism of the UK economy and protection of intellectual property".

The exact structure of any reforms remains uncertain. Importantly, the scope of the consultation appears to cover restrictive practices beyond just non-compete clauses, so employers should be aware that other forms of employee restrictive covenants (such as non-solicitation

and non-dealing clauses) and/or garden leave provisions may be considered.

The Government has confirmed that it will set out more detailed proposals in early 2027.

Paternity pay: From April 2029, there will be a new Parental Allowance for fathers, partners and adopters who do not qualify for Statutory Paternity Pay or Statutory Adoption Pay. This covers people who are self-employed and people who do not meet the current earnings or continuity of employment conditions. That includes those who are recently employed or unemployed, or whose employment has been broken or irregular, provided they have sufficient work and earnings history. Eligible self-employed fathers and partners will receive two weeks' pay at between £27 and the statutory rate (currently £194.32) per week, depending on their National Insurance contributions. Eligible employed or recently unemployed fathers and partners will receive two weeks' pay at the statutory rate or at 90% of average weekly earnings, whichever is lower. Eligible adopters will receive up to 39 weeks' pay on the same basis.

Pensions

The Budget did not make any seismic changes to the world of pensions tax; rather, it proposed a number of small changes, the most significant of which are set out below.

Tax treatment of lump sum death benefits: Currently lump sum death benefits paid on death before age 75 are generally tax free. However, they become taxable if they are not paid out within two years after the scheme knew or could reasonably have been expected to know about the member's death. It is proposed that this will no longer be the case for any payments made on or after 28 October 2026 (even for deaths before that date).

This will be welcome news for schemes, as distributing death benefits can sometimes be a lengthy process and this change will remove concerns about the tax consequences of going over the two-year limit. However, schemes will still need to ensure that they do not unreasonably delay making distributions, as doing so could give rise to potential claims of maladministration.

This announcement will require an immediate change in administration processes.

Consolidation of DC: The Government and Pensions Regulator have been championing the consolidation of small DC schemes for a number of years as larger schemes are perceived to offer better governance and outcomes for members.

The Budget says that legislative changes will be made to facilitate consolidation. This will include expanding the circumstances when a member can keep protected pension ages or lump sum protections when pension rights are transferred. However, no details are given about exactly what changes will be made.

Guided retirement and Retirement Collective Defined Contribution Schemes: The Pension Schemes Act 2026 will require DC schemes to have a default "guided retirement" option which provides members with an income in retirement.

One option which is currently being developed is a proposal for Retirement Collective Defined Contribution (RCDC) Schemes where DC pots will be transferred in on retirement and members will receive an income which can go down as well as up depending on investment performance. The Budget says that where members are transferred into such a scheme and start receiving a benefit, they will be able to convert that pension to a drawdown pension within a set period, if the RCDC scheme chooses to allow that. It also appears that legislation will be amended to allow transfers from drawdown funds to RCDC schemes.

Pension tax allowance: From 2027-28, the state pension will rise above the personal allowance (which is currently £12,570). To address the potential for very small amounts of tax to become due as a result, a new "Pension Tax Allowance" will be introduced from April 2027 for those over state pension age with income (from any source) up to the value of the full state pension (currently £13,036.40).

To avoid a cliff edge where £1 of income over the allowance would make an individual worse off, a taper will apply so that every £3 of income above the state pension will reduce the Pension Tax Allowance by £1. The allowance is worth a maximum of £94 a year and will be maintained up to the end of tax year 2029-2030.

Whilst not of direct relevance to occupational pension schemes, they may face queries from members who are concerned that pension increases may make them worse off if they go over the threshold for the new allowance. Because of the taper, this should not normally be the case.

Terminal illness: It will be possible to pay a serious ill health lump sum where the member is reasonably expected to live for less than a year (which presumably allows for a greater degree of uncertainty than currently). In addition, overseas registered medical practitioners will be able to provide medical evidence.

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