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Employee Shareholding & Management Package

NEWSLETTER

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BSPCE: an employee share ownership scheme set to become more attractive?

The BSPCE (Bons de Souscription de Parts de Créateurs d'Entreprises) scheme, a key instrument for sharing value within French start-ups, is about to see its value significantly enhanced. On 19 October, the French Minister for Digital Affairs, Jean-Noël Barrot, announced at the 10th anniversary celebrating the existence of La French Tech label that eligible companies would soon be authorised to apply an illiquidity discount to the share subscription price if the warrants are exercised

The details of the reform have yet to be defined by the French tax authorities, who are expected to publish a notice in the Bulletin Officiel des Finances Publiques (BOFIP) in the near future.

Reminder of the scheme

BSPCE warrants are options granted freely to employees and directors of young companies or innovative SMEs, giving them the right under certain conditions, to subscribe to shares in the company at a price (*strike price*) fixed definitively when they are granted.

If the company's value increases during the vesting period of the shares, this scheme offers beneficiaries the prospect of a capital gain when the shares resulting from the exercise of the warrants are resold. This is a powerful tool for companies to attract and retain talent.

However, the conditions for setting the strike price have been the subject of criticism for several months.

For the employees, the drastic fall in the value in many companies over the past 18 months has dashed many hopes of capital gains for many of them, as the strike price set when their warrants were allocated has become higher than the real value of the shares.

For companies facing a real international war for talent, the French scheme is seen as less attractive than some equivalent foreign schemes (United States and United Kingdom), which allow share options to be

issued at more advantageous price conditions for employees.

How is the strike price of BSPCEs set?

In principle, the strike price of BSPCEs must be at least equal to the issue price of the shares set at the time of a fund-raising that took place during the 6 months preceding the issue of the BSPCEs. Failing this, the strike price must reflect the fair value of the shares to which the warrants give the right to subscribe on the date they are granted. Since 2019, this rule has however been relaxed.

The Pacte Act of 2019 first authorised companies to reduce the strike price in the event that the economic value of the shares had dropped since the company's last round of financing.

The French Finance Act of 2020 gave further flexibility to companies, allowing them to apply a discount to the issue price set at the last round of financing in the 6 months prior to the granting of BSPCEs when the value of the shares issued under this scheme was not at least equivalent to that of the shares issued at the time of the round of financing.

Recognition of the illiquidity discount

In addition to these legislative relaxations, some companies, keen to make their BSPCE schemes more attractive to their employees, go further and apply an additional discount to the strike price, justified by the minority and illiquid nature of the shares resulting from the exercise of the warrants. Although the application of an illiquidity discount would respond to a very real economic or financial rationale, in practice the majority of companies granting BSPCEs remain cautious and do not explicitly apply a discount for illiquidity, given the risk of the tax authorities challenging the advantageous tax and social security treatment of BSPCEs.

It is this risk being called into question that should soon disappear, with the Minister for the Digital Economy announcing on 19 October 2023 that the tax authorities would authorise young innovative French companies to apply an illiquidity discount to the strike price of BSPCEs. This would be in addition to discount applied in cases as mentioned previously, where there is a difference in the strike price compared to that of shares issued during a round of financing.

The recognition of this illiquidity discount by the French tax authorities should therefore make this practice more secure and enable eligible companies to offer BSPCEs at a significantly lower price than share price at the time the BSPCEs were issued, all in all, which would represent a higher potential gain for the beneficiaries.

This decision should also enable French start-ups to strengthen their power to attract new talent and thus compete on an equal footing with their British and American rivals.

Lastly, this measure should also be favourable to the tax authorities, since it should result in a greater number of BSPCE plans being exercised by their beneficiaries, higher capital gains being realised and consequently, their taxation.

Although the French tax authorities have yet to give details of this measure in the *Bulletin Officiel des Finances Publiques*, it seems certain that larger discounts will be applied to the strike price of future BSPCE plans, making this particular employee share ownership scheme more attractive.

Grant Thornton Société d'Avocats remains at your disposal to advise you on these issues.

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Value Sharing: a legislation widens the scope of allocation of free shares

Act 2023-1107 of 29 November 2023 transposing the National Interprofessional Agreement (ANI) on the sharing of value within the company, will be effective as **from 1 December 2023**, with the exception of those provisions subject to a specific date of entry into force or requiring the issuance of an implementing decree. The legislation marks another important step forward in the promoting of employee shareholding in France. This is notably achieved through the adoption of concrete measures concerning the free allocation of employees' shares (AGA « Attributions Gratuites d'Actions ») in their company, thereby giving them a direct stake in the company's results and growth.

A loosening of previous overall limits

The overall limits for the allocation of free shares are to set to be loosened considerably.

Companies will now be able to allocate up to 15% (previously 10%) of their share capital in free shares, and this percentage will be increased to 20% for very small and medium businesses (previously 15%).

If the shares are allocated to all employees, the company will be able to allocate up to 40% of the share capital, representing a significant rise compared to the previous limit of 30%.

Revision of individual limits

The revision of individual limits should also be noted. Under the new provisions, only shares held directly by an employee or corporate officer for less than seven years would be included in the calculation of the individual limit of 10% of the company's share capital.

Introduction of the Value Sharing Scheme

One of the new measures is the creation of a value-sharing scheme. This new collective scheme, which is exempt from employer and employee social security contributions but subject to a 20% employer contribution on the date of payment, is intended to increase employee commitment through the payout of a premium after three years.

A look at the social security and tax arrangements for AGAs

Since 1 January 2018, free shares which are awarded have benefited from a special regime. The gains made on them of less than or equal to €300,000 are taxable on the progressive income tax scale with a 50% tax allowance applied.

Any gains over the €300,000 threshold are treated as a salary and subject to social security contributions on earned income at a rate of 9.2%. Capital gains on the sale of such shares are subject to a 30% flat tax rate.

From a social perspective, the gains achieved from free share allocations are exempt from social security contributions but are still subject to CSG and CRDS contributions when the shares are sold.

Point of Attention: Modifications in free share allocation schemes

Allocations of free shares (AGAs) benefit from favourable tax and social security treatment, provided that they are granted in accordance with the criteria set out in the French Commercial Code. Changes to such AGA schemes are legally possible but must comply with certain conditions. For example, they must be approved by an Extraordinary General Meeting and be in the interests of the company.

However, it should be noted that any significant amendments made could result in the original scheme being considered as a wholly new and created scheme. This in itself could mean the scheme is no longer deemed as qualifying for favourable tax and social security treatment.

In such a case, a new vesting period could well be established, adversely affecting the preferential treatment associated with the original scheme set up.

Companies should therefore take great care when drawing up free share schemes, by making provision for the possibility of amendments, equally ensuring that these amendments do not substantially alter the original purpose and benefits of the scheme.

This implies a careful analysis of the performance criteria and the conditions attached to the vesting and holding periods.

A promising future for employee shareholding

The year 2023 marks a significant turning point for employee shareholding in France. The easing of the limits on the allocation of free shares, together with favourable tax and social security regimes, opens up new opportunities for companies and their employees.

This initiative is reflected in a number of large-scale initiatives by leading companies. For example, in September 2023, Renault launched a new employee shareholding operation aimed at increasing the employees' share of its total capital to 10% by 2030.

This move by the French group, involving 98,000 of its employees in 29 different countries, illustrates the growing commitment of major companies to including their employees in the very heart of the shareholding process.

Similarly, the Tech giant Sopra Steria, has had overwhelming success with its "We Share 2023" employee share ownership scheme, involving extensive employee participation both internationally and nationally, reflecting a growing trend towards employee shareholding in the technology sector.

These examples, as well as the global trend of companies putting free share schemes into place, demonstrate the growing importance attached to involving employees in the results and governance at a corporate level.

They are clear steps towards a more inclusive economy, where employees play an active role in the strategic direction of their company.

Grant Thornton Société d'Avocats remains at your disposal to advise you on these issues.

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Management packages: companies increasingly exposed to the risk of these being reclassified as salaries

The reclassification of gains made from management package as salaries presents a risk both for the beneficiaries in the event of tax reassessment, and for companies when social security contributions are charged to them. The French Court of Cassation's decision on 28 September in regard to share warrants (BSAs « bons de souscriptions d'actions ») increases the risk and impact of such reclassifications.

Since a ruling in 2019 (no. 17-24.470) the French Court of Cassation had considered that share subscription warrants (BSAs) were subject to social security contributions "from the moment they are offered and available to employees in return for or in conjunction with work and acquired by employees **on preferential terms**".

The trigger point for social security contributions to be paid was the "effective availability of the benefit". In other words, the moment when the share warrants become vested and could be exercised and transferred. Not only was this the point at which the contributions were due, it was also the point at which **the statute of limitations would start to run**.

Moreover, such warrants subject to social security contributions, had to be evaluated on the basis of the value of the warrants at that specific date in time.

In its decision of 28 September 2023 (no. 21-20.685), the Court of Cassation issued a number of reminders and clarifications before reversing its position.

- Reminder and clarifications

The qualification of preferential nature follows a global evaluation. The absence of a granted discount at the time of shares being issued is merely an indicator of a preferential nature. The mere absence of a financial

advantage in itself does not call into question the existence of preferential conditions.

The **correlation between an employment relationship and share warrants** acquired on preferential terms could be retained even when individuals were no longer working for the company at the point in time when share warrants were exercised.

- Reversal of position

The trigger point for the payment of social security contributions is now considered to be **the effective date of actual transfer or exercising** of the share warrant and no longer the date of "effective availability of the benefit".

The first impact for companies is the **deferral of the starting point for the statute of limitations** to the actual time of transfer or exercise (as opposed to the effective availability).

The ruling also increases the burden of social risk, since the benefit of a share warrant is no longer valued at the point in time when the beneficiary had the possibility of exercising it, but at that point in time when it is actually exercised or transferred.

As such, the value of a share warrant could potentially have increased considerably at the actual date of transfer or exercise.

Companies that thought they no longer bore the risk of tax or social reclassification may find themselves once more at risk as a result of the deferred starting point of the trigger event. This risk is potentially much greater than initially estimated.

To date, there is still no satisfactory legislative solution in place to secure the interests of the investing employee/executive, and it is therefore all the more essential that companies assess any potential risk related to the reclassification of their management packages as salaries.

For the time being, most developments are focusing on company value-sharing through the existing legal provisions. These measures and schemes provide security for both the company and the employee: stock options, free shares, the employee share ownership scheme of BSPCEs, and not forgetting the much-awaited law on the sharing of company value.

When the objectives and conditions so permit, it would be worth looking into possible options for implementing more secure benefit and employee share ownership arrangements.

Grant Thornton Société d'Avocats remains at your disposal to advise you on these issues.

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Our Employee Shareholding & Management package brochure



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