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HELPING *SHARE* GROWTH



TAX, INCENTIVES AND
EMPLOYEE SHARE PLANS

Best of European policies on employee ownership : the UK

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Who am I ?

- ▶ Tax lawyer of c 30 years experience in employee share ownership
- ▶ Former member of HM Government working party which put together legislation on employee share schemes
- ▶ Author of “Employee Share Schemes” (2-vol looseleaf pub Sweet & Maxwell), the UK textbook on the subject
- ▶ Partner in a leading specialist law firm advising on all aspects of employee share ownership



Background

- ▶ Broadly, the UK has two models of employee ownership of a company:
 - **collective ownership** of shares by a trust for the benefit of employees (past, present and future), the trustee(s) being a subsidiary controlled by the company
 - complex governance structures involving employee representatives as directors of the trustee company;
 - tax advantages if the trust holds a controlling interest in the company;
 - restrictions (to satisfy tax requirements) on commercial freedoms;
 - **individual employee share ownership** i.e. all qualifying employees hold, or have the opportunity to acquire, shares which allows them to benefit from growth in capital value



Collective ownership

- ▶ By far the largest such company is **The John Lewis Partnership**, a large retailer with some 92,000 + employees (which owns 'Waitrose' grocery supermarkets)
- ▶ All other such companies are much smaller in size and numbers of employees (the 2nd and 3rd each have over 10,000, but the 50 largest each has over 300 employees)
- ▶ But, many of those 'top 50' are structured on a 'not for profit' basis
- ▶ Such structures of ownership have been made more attractive by the previous coalition government
 - publishing model documentation (2015)
 - making (minor) changes to company laws (2015)
 - affording generous tax relief on sales of controlling shareholdings to a special type of employees' trust (2015) an "employee ownership trust" or "EOT"

Collective ownership (cont.)



- ▶ The current government has shown less interest in making further changes to enhance this legal/tax regime (which still affords opportunity for tax avoidance, and gives rise to difficulties of share valuation and tax pitfalls).
- ▶ The attraction of converting to such collective employee ownership appears to have been largely driven by the opportunity for private company owners to avoid tax on selling to an employees trust



Individual (direct) employee ownership

- ▶ Many generous tax breaks for allowing both (a) *all* qualifying employees, and (b) selected employees, to acquire shares in their employer company
 - **‘Share Incentive Plans’** (“SIPs”) since 2000 (and much enhanced in 2013/14) allow, within limits, awards of *‘free’* shares to all employees (up to £3,600 pa), and for all employees to purchase *‘partnership’* shares (up to £1,800pa) out of pre-tax earnings, and to do so with an award of free *‘matching’* shares (up to 2 for 1). If held for 5 years, no tax on sale.



Individual (direct) employee ownership

- ‘save-as-you-earn’ (“SAYE”) options : 3- and 5-year share options linked to a savings plan for *all* employees (since 1982) – attractive to larger employers;
- ‘enterprise management incentives’ (“**EMI options**”) tax-favoured share options for *selected* employees of SMEs (since 2000) – and copied by many other countries eg Singapore; Australia;
- tax-favoured ‘company share option plans’ (“*CSOPs*”) for *selected* employees subject to £30,000 limit – since 1984;



Individual (direct) employee ownership

- the UK regime has, since 2003, allowed for the award of shares to employees on the basis that, whilst any existing value acquired is charged to tax as 'earnings', **future growth** in value will, if a tax election is made, be taxed as capital gain (20%);
- this has encouraged the establishment of 'joint share ownership plans ("JSOPs"), and the issue of special 'growth shares' for selected senior employees;
- '*employee shareholder shares*' : (since 2013) selected employees may be invited to accept an issue of new shares in exchange for giving up valuable employment law protections, taxable as 'earnings' if worth over £2,000, but exempt from tax on sale (but now the tax exemption on sale is limited to £100,000 if the shares were issued after March 2016)



Individual (direct) employee ownership

- ▶ Apart from shares acquired by employees under a SIP, on the sale of EMI share option shares or of ‘employee shareholder shares’, there are few tax reliefs or exemptions for employees selling ‘employer company’ shares on leaving
- ▶ there are tax pitfalls if shares are sold back to the company itself – changes are required to the tax rules to assist SMEs and private companies to allow leavers to sell back shares without tax penalties



UK government policy

.....is generally supportive of 'employee share ownership'

Policies have been developed and promoted by one government department but, as the subject is 'rooted' in tax, it is the actions of H.M. Treasury and HMRC (our tax authority) which have made the real changes prompting companies and their owners to consider a transition to a model of either direct or indirect employee ownership (or a combination of both)

such changes are made with caution as there is a long history of companies, large and small, taking full advantage of opportunities for tax avoidance !

The 'devil is in the detail', and as the detail is voluminous, any plans for promoting employee share ownership require much (costly) professional advice.



and the future...?

- ▶ Transfers of controlling interests into collective ownership will increase, but interest amongst larger companies will remain cautious, and that of owners of SMEs will remain largely tax-driven
- ▶ **Share Incentive Plans** (*slide 5*) are becoming more popular amongst smaller employers
- ▶ The idea of 'joint share ownership' is beginning to be understood and may attract political support
 - Employees acquire shares jointly with a trust on terms which provide that, when the shares are sold, the employee receives the growth in value taxed as capital gain



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