EMPLOYEE SHARE OWNERS: A GIFT THAT COULD KEEP GIVING?

The UK Government appears to be firmly committed to its idea of employee share owners – employees who give up their employment rights in exchange for tax free shares. Is this, as some have suggested, a half-baked plan that is doomed to fail or should companies and employees grab the Chancellor's gift horse (just don't look too closely at the teeth)?

Share Giveaway

The proposals on employee share ownership have been branded as ill thought out and unfair on employees. But are they really that bad? The key proposal is to allow companies to give shares worth between £2,000 and £50,000 to employees in exchange for them giving up certain employment rights. Disposal of the shares acquired under the scheme will be free from capital gains tax. Sounds quite good when you put it that way.

The proposals were heavily criticised when they were announced last October and the Government has admitted that very few responses to its consultation welcomed the proposals. Despite this, it remains committed to the scheme and we now have draft legislation covering some of the tax aspects of it.

Think Before You Speak?

There is a real sense of "making it up as we go along" with the proposals. For example, the Government has said employees cannot pay anything for the shares but they must still be issued fully paid, making it unclear how the company law requirements are supposed to be satisfied. We now have the draft capital gains tax rules but the income tax treatment is still to be resolved.

The shares awarded to the employee must have a minimum value at the date of issue of £2,000 and a maximum value of £50,000 (more shares can be given but these will not be tax free on sale). Some will see this as a generous bonus by the employer. How valuable are the employment rights anyway to the majority of employees? But if an employee is given shares income tax and (often) national insurance contributions will be charged on the value of those shares. So the employee is effectively paying to give up their employment rights and receive the shares. Suddenly the bonus does not feel quite so generous anymore.

The Government has said it is looking at ways of reducing the up-front tax impact for employees. One suggestion is to treat the first £2,000 worth of shares as tax free. That may be OK if you only get the minimum value of shares but it is not much use if you get £5,000 or even £50,000 worth. At least the Government recognises that it needs to sort out this issue.

Don't Give Up Hope

George Osborne said he wanted to create a nation of employee share owners with his proposals; it is hard to see the current proposals achieving this. However, in the right circumstances an employee could benefit considerably. After all, they are being given free shares and tax free proceeds when the shares are sold.

Management teams on private equity transactions may be one beneficiary of the proposals. Sweet equity awards could be made to fall within the scheme with a minimal impact on traditional private equity structures. The individuals involved are, by nature, entrepreneurs who are prepared to accept some risk. Throw in tax free proceeds and there may be a use for the scheme after all.

The merit of the proposals can only really be fully assessed once the Government confirms the proposed income tax treatment. Further details are expected soon. In the meantime it may be a little premature to write off George Osborne's proposals completely. Watch this space.

If you would like to discuss to discuss the employee shareholder proposals in more detail, please do not hesitate to contact Peter Morley or Lawrence Green.

Peter Morley
T+44 113 284 7022
E peter.morley@squiresanders.com

Lawrence Green
T +44 121 222 3394
E lawrence.green@squiresanders.com