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spreading the wages of capital

The Case For Employee Share Ownership:

The Heart Of The Matter Revealed

Webinar

Friday 14 August 2020

spreading the wages of capital

A Word From The Chairman

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Managing Director

Z/Yen Group






Agenda

10:30 – 10:35	Chairman's Introduction
10:35 – 10:55	Keynote address
10:55 – 11:00	Final thoughts
11:00 – 11:15	Questions & Answers

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The Case For Employee Share Ownership:

The Heart Of The Matter Revealed

David Craddock

Founder and Director

David Craddock Consultancy Services

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DAVID CRADDOCK CONSULTANCY SERVICES

Specialist in Employee Share Ownership and Reward Management,
Management Buyouts, Share Valuation
and Investment Education

David Craddock Consultancy Services

The Case for Employee Share Ownership; The Heart of the Matter Revealed

The Underlying Principles: The Core Revelation

From the perspective of the employee mindset

The employees will be more inclined to develop capital value for the company if they have a stake in the capital value that they are creating.

From the perspective of the existing company's shareholders mindset

Employee share ownership is integral to the economics of business growth:

Question: Is it better to own 100% of a company worth £500,000 or to own 75% of a company worth £5,000,000?

How does the company grow from one to the other? Employee Motivation

What does employee share ownership really mean?

David Craddock Consultancy Services

The Heart of the Matter: The Design and Structure of the Employee Share Scheme

- Employee share ownership is truly a multi-disciplinary subject, requiring from the employee share schemes practitioner an awareness of a whole plethora of laws and regulations: Securities laws, Financial Services laws, Tax laws, Employment laws, Trust laws, Data Protection laws, with due application across all countries

- When designing or reviewing an employee share scheme, it is often helpful to the analysis to appreciate that an employee share scheme will, in broad terms, always fall into one of three categories: Share gifting scheme, Share purchase scheme, Share option scheme

- The UK, through the tax-advantaged schemes, previously referred to as tax-approved schemes, and the US , through the tax-qualifying schemes, are the two countries in the world that embrace comprehensive tax reliefs for employee share schemes, either in the form of deferring the tax liabilities, or substituting the income tax regime for a less punitive capital tax regime, or, best of all, providing tax exemption provided certain conditions are met.

- Ironically, the one country where employee share schemes are compulsory, courtesy of the Black Empowerment legislation, South Africa, does not have any tax-relieving legislation.

What does employee share ownership really mean?

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The Heart of the Matter: The Human Resources Dimension

- **The Definition:** Employee share ownership is the establishment of an entitlement for the employees to participation in the benefits that flow from a share interest in the share capital of the company in which they are employed.

- **The Key Question:** The employee communication strategy, coupled with effective human resources management and strong administrative structures, is the lubricant that connects the employee workforce to the employee share scheme. The approach to these elements taps the very heart of the matter, recognising that at root the success of the scheme initiative depends upon the human response from the employees. The key question, therefore, is: how does the human brain think and the human heart beat in response to the employee share ownership initiative?

- **The Research:** The most basic distillation of the research on the reasons why companies introduce employee share schemes is as follows:
  Identification and involvement, Motivation and incentive, Recruitment and retention

- **The Effectiveness:** The research on effectiveness in the UK and the US is extensive, based on a combination of using causation and correlation techniques applied to credible empirical evidence.

What does employee share ownership really mean?

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The Heart of the Matter: The Human Response to the Employee Share Schemes Initiative

All positive employee response is predicated upon the effective communication strategy and the development of an involvement culture.

- **The Identity of Interest:** The identity around the totem of the developing share value, in working with all those who have an interest in the success the company, developing the garden of the company together. Remember Voltaire: "Let us cultivate our garden together", breaking down departmental protectionism.

  Voltaire in Candide:
  "Neither need you tell me" said Candide, that we must take care of our garden".
  "You are in the right", said Pangloss, "for when man was put into the Garden of Eden, it was with an intent to dress it and this proves that man was not born to be idle."

- **The Wages of Capital:** The focus of the incentive of variable return on the basis that the greater the employee work contribution the greater the returns from the labour through extending employee return from just wages/salaries to include dividends and capital gains.

  Brian Clough, the famous football manager, once said:
  "Look after the ball and the ball will look after you."
  In all regards, look after your employee share ownership programme and, yes, your employee share ownership programme will look after you!

What does employee share ownership really mean?

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The Heart of the Matter: The Human Response to Employee Share Schemes Initiative (Continued)

The Human Potential Dynamic

- The release of the entrepreneurial spirit within companies, encouraging each individual employee to think like an entrepreneur within his or her employment, contributing their ideas and creativity to the business in a thoroughly accountable way, resolving the potential conflict between creativity and accountability.

- The realization of the human potential of the employees through an appeal to natural human instinct in an environment that encourages co-creation with other employees at all levels of the business. Remember the thesis projected by Aristotle of enlightened self-interest compared with the sacrificial model projected by Plato: Aristotle wins every time because of the appeal to natural human instinct! Enlightened self-interest is the fuel that drives the car.

- The regulation of the business through progressive employee empowerment policies to facilitate self-regulating behaviour in the interest of company order and organisation and indeed productivity and performance, policies that breathe life and vitality into the business.

  Edmund Burke:

  "Manners are more important than laws as it is upon manners that laws depend."

What does employee share ownership really mean?

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The Origins of Employee Share Ownership in the UK: The Quiet Revolution

The Commonwealth Protectorate

Shared ownership has interested writers and thinkers since ancient times. However, the writings of Peter Cornelius Plokhoy date back to the days of the Commonwealth Protectorate under Oliver Cromwell in England. It was Plokhoy who established one of the first co-operative commonwealths in 1659 and it is said that Plokhoy's writings inspired the establishment of the Scott Bader Commonwealth in 1951.

The Quiet Revolution

The interest in employee share ownership in the UK prior to 1978, although spasmodic and when present typically of a temporary nature, was always honourable and of good intent, relying upon a combination of entrepreneurial benevolence, Christian ethics and practical industrial relations. The initiatives in employee share ownership were spirited and focused, fuelled by the momentum of the industrial revolution. However, success was limited, so much so that the development of the subject against the historical backcloth of revolution in Europe and the fall of monarchical dynasties was coined "The Quiet Revolution".

What does employee share ownership really mean?

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The Origins of Employee Share Ownership in the UK: The Quiet Revolution (Continued)

The South Metropolitan Gas Company in 1889

- Almost certainly the first UK initiative with a recognisable all-employee share scheme structure was established by the **South Metropolitan Gas Company in 1889**. It recorded the scheme in its minutes under the name "Co-Partnership".

- Under the arrangement, part of the employee's bonus was invested in the shares of the company. Some ten years later, in 1898/1899, the company introduced elected employee directors from those employees who had completed at least ten years service and had at least £180 invested in the company's shares.

- The scheme developed with certain guarantees on retention under which the shares were not sold without permission. At the same time the employees were encouraged to buy more shares from their own resources. On leaving the company, or on death, the shares were bought back by the company from the employees.

What does employee share ownership really mean?

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International Congress of Profit Sharing in Paris in 1889

In Europe the year 1889 was also significant for the platform that was given to the subject at the **International Congress of Profit Sharing in Paris**. The conclusions of the meeting were summarised as follows:

"The idea is very simple. The principle is that all workers shall become partners in the business in which they work: such partnership will confer the right to share in prosperity or profit, to share in the ownership of capital on a pre-determined basis fixed well in advance, and to come into knowledge and consultation about the operations of the business, as a statement of principle."

- From this early stage, therefore, employee share ownership was set within the context of **industrial partnership** and **employee education**.

- Perhaps the most interesting structural principle to emerge from the meeting was the operation alongside each other of **profit sharing** and **employee share ownership**. It was in the tax-approved all-employee profit-**sharing employee share scheme**, introduced in the UK by the Labour Government in 1978 under the influence of the "Lib-Lab Pact", that the unity of these two policies was subsequently legislated to such practical effect, winning positive response from UK companies.

The UK Cross-Party Political Appeal

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The Modern UK Experience

The consensus across all the political parties in the UK is illustrated through the following successive legislative actions:-

- The introduction by the Labour Party in 1978 of the profit-sharing employee share scheme as the first tax-approved employee share scheme in the UK, as a requirement made by the Liberal Party under “The Lib-Lab Pact”.

- The initiatives by the Conservative Governments under Margaret Thatcher through the introduction of the 1980 savings-related share option scheme and the 1984 executive share option scheme.

- The New Labour initiatives through Finance Act 2000 to introduce Enterprise Management Incentives and the Share Incentive Plan.

- The Conservative/Liberal Democrat Coalition to encourage “The Enterprise Reliefs” with further reliefs for Enterprise Management Incentives, the Enterprise Investment Scheme and Entrepreneurs Relief with a Special Entrepreneurs Relief introduced for Enterprise Management Incentives.

The UK Cross-Party Political Appeal

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The Coalition Government: The Golden Era

- During the years of the Coalition Government from 2010 to 2015, employee share ownership in the UK experienced "a golden era": at first in the attention given to the subject by government ministers and then through the introduction of detailed legislation to give expression to that interest. From within that government, the Prime Minister, the Chancellor of the Exchequer and the Secretary of State for Business, Innovation and Skills were united in wanting to encourage 'the enterprise reliefs' of Enterprise Management Incentives, the Enterprise Investment Scheme and Entrepreneurs Relief.

- In terms of new bespoke tax-advantaged scheme arrangements, the Conservative Chancellor introduced and championed in 2013 "the shares for rights" scheme while the Liberal Democrats pioneered the introduction in 2014 of the "employee-ownership trust" as the key response to the recommendations of The Nuttall Review of Employee Ownership that had been commissioned by the British Government and was published in 2012.

- Additionally, the employment-related securities legislation has continued to evolve through a combination of statutory changes and developing best practice, building on the foundations laid down through Finance Act 2003.

The UK Cross-Party Political Appeal

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The Coalition Government: The Golden Era (Continued)

- On top of all that, the tax simplification initiatives of the Coalition Government introduced some well-received changes to the tax-advantaged schemes (previously known as the tax-approved schemes), thereby enhancing still further the attractiveness of these schemes.

- Throughout the period from 2010, the employee share trust has continued to be a supporting mechanism for employee share scheme initiatives. The challenge to the use of trusts for employee share ownership came through the introduction of the concept of "disguised remuneration" and the consultations that government invited on this matter. Thankfully consistent lobbying through determined action from the practitioners secured for the employee share trust a significant array of exemptions in Finance Act 2011 for the use of employee benefit trusts for employee share scheme purposes.

- Other legislative initiatives of significance include the revamp of the treatment of "internationally mobile employees" through Finance Act 2014 and changes through Finance Act 2016 to the rules relating to "transactions in securities".

The UK Cross-Party Political Appeal

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The UK Experience: The Political Objectives

The objectives that have been embraced by all mainstream UK political parties since 1978 are as follows:-

For the Conservative Party under Margaret Thatcher and John Major

- To recognise identity of interest for all persons involved in the business with an interest in the company's success (the share as "the totem" for unity).
- To assist in improving industrial relations through consensus corporate attitudes.
- To promote self-sufficiency and self-reliance for individual employee share owners.

For the Labour Party under Tony Blair and Gordon Brown

- To encourage higher levels of productivity and profitability.
- To assist the policy of "Enterprise with Fairness".
- To facilitate redistribution through wealth creation.

For the Coalition under David Cameron, George Osborne and Vincent Cable

- To encourage enterprise.
- To help starter businesses.
- To minimise the bureaucracy attached to share schemes.

The Appeal Across Political Persuasions

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Why Worldwide Political Consensus?

- In seeking to understand the political consensus, whether in the UK or worldwide, the analysis becomes complex for the reason that the subject represents a different emphasis to different political persuasions as follows:-

- For the conservative political persuasion, it represents proprietorial rights.
- For the capitalist political persuasion, it represents the benefits of ownership.
- For the liberal political persuasion, it represents individualism and freedom.
- For the socialist political persuasion, it represents redistribution of wealth.
- For the consensus political persuasion, it represents a practical basis for unity.
- For the economic political persuasion, it represents a basis for economic delivery.

The Comparison between the USA and Europe

- Within the USA, the subject gathered momentum from 1956 onwards when Louis Kelso's work with Peninsula Newspapers in Palo Alto, California, came to the attention of Senator Russell Long whose pioneering work led to the institution of fiscal encouragement for the introduction of ESOPS in companies.
- The acceleration in the development of employee share ownership, particularly in the UK and the increasing interest throughout the rest of the world, has, though, coincided with the discrediting of communism and the pre-eminence of the market approach to economics heralded in by the fall of the Berlin Wall in 1989 and the formal enactment for the dissolution of the Soviet Union in 1991.

The US Perspective: Key History

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The Forerunner in the Subject: Why?

- The development in the US was unhindered by the class divisions in Europe, which the inhabitants of the North American continent had left behind with the enlightened migrant's resolve to succeed in the New World of the Americas.
- In the USA, the development of employee share ownership benefited from the demographic advantage of the practical way in which the North America continent became populated. As the immigrants arrived on the east coast they moved west, claiming the land as they travelled. However, even after all the land had been claimed more immigrants continued to arrive so rather than engage in conflict over land ownership and occupation, the supply of which was now exhausted, the frontier-men established agreements on sharing and farming the land.

The Early US Statutory Initiatives

- ***The Revenue Act 1950*** established the statutory basis for the principle that capital gains should be taxed under the capital gains tax regime rather than the more punitive income tax regime which imposed higher rates of tax with no exceptions for share option gains.
- ***The Employee Retirement Income Security Act 1974 ("ERISA")***, inspired by the work of Louis Kelso, recognised ESOPS as a special form of defined contribution pension plan that as well as receiving contributions had the power to borrow money to fund the purchase of shares.

The US Perspective: Case Studies

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An Electronics Company based in Northern California

The company is quoted on NASDAQ with over 35,000 employees worldwide. With a history of employee share ownership since its foundation in the early 1980s, in spite of the NASDAQ listing, more than 65% of its shares are owned by employees. The directors resolved to extend their employee share plans into their European operations in France, Sweden and Finland for senior executives. The main motivation behind this initiative was to encourage full fertilisation of ideas between executives across the countries and to create a “corporate glue” across the senior management team. The challenge in implementation was the volatility of the share price, arising from the uneven supply of shares when groups of employees are able to sell.

A Circuit Boards Manufacturer based in Silicon Valley

This private company has operations in the US and the UK with around 100 employees in each jurisdiction. The directors resolved to introduce a share scheme in the US based on 70% of the remuneration paid in shares and with the free trading of shares between employees. The challenges in implementation were significant in the context of the freedom in which the scheme was to operate and can be summarised as, firstly, to establish scheme arrangements that allocated shares on the basis of performance and merit and, secondly, to establish responsible regulation in the share trading.

The European Perspective: Context

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The Role for Employee Share Schemes

- If properly recognised, employee share ownership has a role to play in Europe as a contribution to reducing unemployment levels, to reinforcing sustainable industries, to encouraging private companies and to acting as a variable in macro-economics.
- However, each individual country across this diverse continent must embrace the subject, rather than be reliant a directive from the European Union, as currently there is no substantive equivalent to the substantial infrastructure of the US tax-qualifying schemes or the UK tax-advantaged schemes.

The Axis of Power between France and Germany

- At the heart of the European Union is the axis of power that exists, although sometimes awkwardly, in the relationship between France and Germany.
- Substantive government initiatives on employee share scheme by the two lead nations of France and Germany could, in the context of a European Union that regards unhindered migration of employees as one of its fundamental tenets, result in the wider development of the subject across the European Union states in order for those states to remain competitive as employers for individuals from all states.
- Given the disparity in macro-economic profile that each of the European Union states has, it is important that each state determines the structure of employee share scheme that best suits its economic requirements and, at the same time, is consistent with the culture of the predominant ethnic peoples in each state.

The European Perspective: Social Market

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The French Experience

- It is true that the French Commercial Code has long facilitated a tax-qualifying employee share plan. Additionally, there is a history within France of a statutory company savings scheme for which each employee makes an individual decision as to whether or not they will participate in the scheme.

The Advocacy of The Social Market in Germany

- The social market that was embraced by West Germany would appear to be a natural fit for employee share ownership with its capacity to combine wealth creation with welfare reform, i.e. redistribution through performance and effort.
- The social market economy as a concept represented initially a reaction against monopoly power in the days of the post-WW2 reconstruction. As a precaution against a future dictatorship in either the business sense or the political sense the recognition of the social market as an organising principle in economic and social life was embraced by the Christian Democrats in 1949 for the subsequent endorsement by the Social Democrats in 1959.
- The objective of this post-WW2 initiative was described by Jeremy Leaman in “The Political Economy of West Germany 1945 to 1985” as “the deproletarianisation and decentralisation of the German economy” where by “deproletarianisation” is meant “inclusiveness” and by “decentralisation” is meant “individual empowerment”, again testimony to the natural fit for share schemes within the social market model.

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Employee Share Schemes

All Best Wishes for Your Business Initiative
from David Craddock
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The Esop Centre’s *newspad*, edited by Fred Hackworth, is a monthly publication providing in-depth coverage of the main international news in the employee share ownership field.

NB Reminder: The email address of Fred Hackworth, editor of *newspad*, has now changed to: fred_hackworth@zyen.com (please note the under-score). Please send all press releases, company bulletins and news items for *newspad* to the above address. Thank you.

August 2020

In this month’s edition:

- CGT probe fears over share scheme tax rates
- Roadchef trustee pledge – we’ll fight to the end
- *Shares for Salary* scheme at the Daily Mail group
- Gift staff 15 percent of the equity, investor urges Countrywide
- Taps turned on for ousted water ceo
- Book now for Jersey share schemes for trustees seminar September 25

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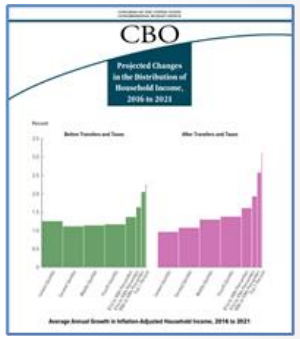

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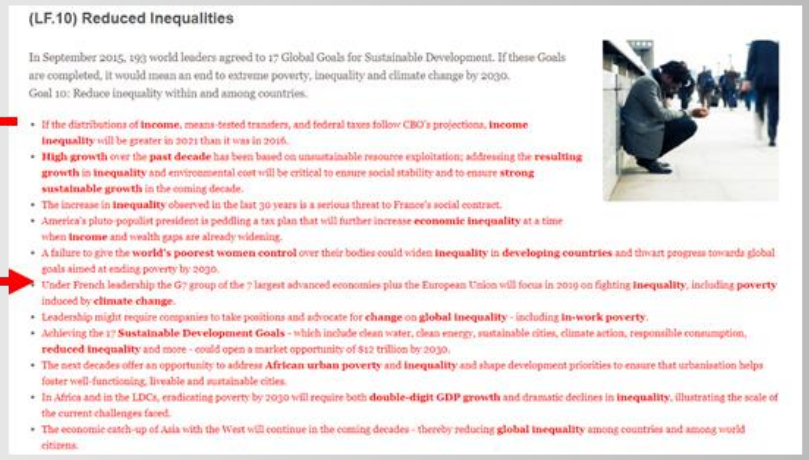
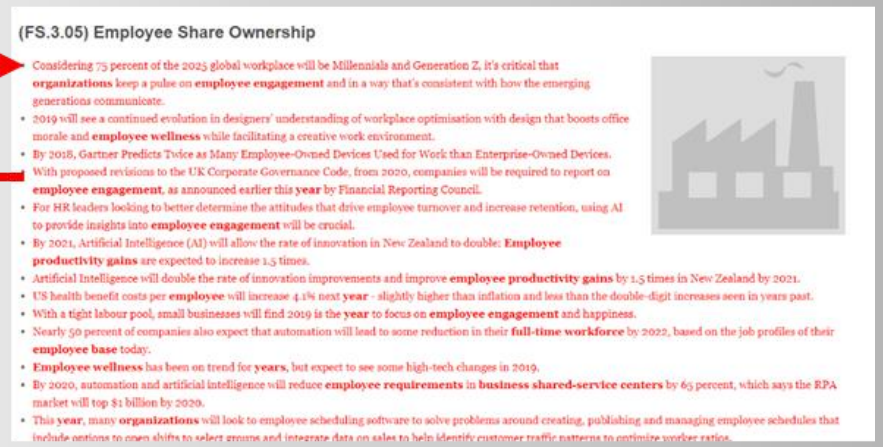


(LF.10) Reduced Inequalities

In September 2015, 193 world leaders agreed to 17 Global Goals for Sustainable Development. If these Goals are completed, it would mean an end to extreme poverty, inequality and climate change by 2030.
Goal 10: Reduce inequality within and among countries.

- If the distributions of **income**, means-tested transfers, and federal taxes follow CBO's projections, **income inequality** will be greater in 2021 than it was in 2016.
- **High growth** over the **past decade** has been based on unsustainable resource exploitation; addressing the **resulting growth** in **inequality** and environmental cost will be critical to ensure social stability and to ensure **strong sustainable growth** in the coming decade.
- The increase in **inequality** observed in the last 30 years is a serious threat to France's social contract.
- America's pluto-populist president is peddling a tax plan that will further increase **economic inequality** at a time when **income** and wealth gaps are already widening.
- A failure to give the **world's poorest women control** over their bodies could widen **inequality** in **developing countries** and thwart progress towards global goals aimed at ending poverty by 2030.
- Under French leadership the G7 group of the 7 largest advanced economies plus the European Union will focus in 2019 on fighting **inequality**, including **poverty** induced by **climate change**.
- Leadership might require companies to take positions and advocate for **change** on **global inequality** - including **in-work poverty**.
- Achieving the 17 **Sustainable Development Goals** - which include clean water, clean energy, sustainable cities, climate action, responsible consumption, **reduced inequality** and more - could open a market opportunity of $12 trillion by 2030.
- The next decades offer an opportunity to address **African urban poverty** and **inequality** and shape development priorities to ensure that urbanisation helps foster well-functioning, liveable and sustainable cities.
- In Africa and in the LDCs, eradicating poverty by 2030 will require both **double-digit GDP growth** and dramatic declines in **inequality**, illustrating the scale of the current challenges faced.
- The economic catch-up of Asia with the West will continue in the coming decades - thereby reducing **global inequality** among countries and among world citizens.



(FS.3.05) Employee Share Ownership

- Considering 75 percent of the 2025 global workplace will be Millennials and Generation Z, it's critical that **organizations** keep a pulse on **employee engagement** and in a way that's consistent with how the emerging generations communicate.
- 2019 will see a continued evolution in designers' understanding of workplace optimisation with design that boosts office morale and **employee wellness** while facilitating a creative work environment.
- By 2018, Gartner Predicts Twice as Many Employee-Owned Devices Used for Work than Enterprise-Owned Devices.
- With proposed revisions to the UK Corporate Governance Code, from 2020, companies will be required to report on **employee engagement**, as announced earlier this **year** by Financial Reporting Council.
- For HR leaders looking to better determine the attitudes that drive employee turnover and increase retention, using AI to provide insights into **employee engagement** will be crucial.
- By 2021, Artificial Intelligence (AI) will allow the rate of innovation in New Zealand to double: **Employee productivity gains** are expected to increase 1.5 times.
- Artificial Intelligence will double the rate of innovation improvements and improve **employee productivity gains** by 1.5 times in New Zealand by 2021.
- US health benefit costs per **employee** will increase 4.1% next **year** - slightly higher than inflation and less than the double-digit increases seen in years past.
- With a tight labour pool, small businesses will find 2019 is the **year** to focus on **employee engagement** and happiness.
- Nearly 50 percent of companies also expect that automation will lead to some reduction in their **full-time workforce** by 2022, based on the job profiles of their **employee base** today.
- **Employee wellness** has been on trend for **years**, but expect to see some high-tech changes in 2019.
- By 2020, automation and artificial intelligence will reduce **employee requirements** in **business shared-service centers** by 65 percent, which says the RPA market will top $1 billion by 2020.
- This **year**, many **organizations** will look to employee scheduling software to solve problems around creating, publishing and managing employee schedules that include options to open shifts to select groups and integrate data on sales to help identify customer traffic patterns to optimize worker ratios.

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