Government publishes its response to ‘employee owner’ share scheme

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Government publishes its response to ‘employee owner’ share scheme

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In December 2012, the Department for Business, Innovation and Skills published its response to a consultation on how to implement the new ‘employee owner’ scheme, whereby employees will forfeit major employment rights in exchange for taking a stake in their business.. This is an unusually fast response from the Government who only announced the scheme at the conservative party conference in October 2012.

To recap, the scheme will apply to employers who give employees shares worth between £2,000 and £50,000. These shares will be sold back to the employer for a reasonable price and will be exempt from Capital Gains Tax (CGT) at the point of sale. However, in return the employee must give up key employment rights including unfair dismissal, redundancy and the right to request flexible working.

The consultation received widespread criticism from a variety of organisations of which only three out of 184 said they would take up the new status. Irrespective of this feedback, the Government is progressing ahead with an implementation date of April 2013.

The Government’s response modifies its original proposals. These include:

- renaming ‘employee owner’ contracts to ‘employee shareholder’ contracts;
- removing the upper threshold of £50,000 which would allow companies to offer more shares under the scheme, although the exemption from CGT would remain capped at £50,000;
- clarifying that shares should be fully paid up and issued free to the employee shareholder;
- creating a power for the secretary of state to increase the minimum share value of £2,000;
- allowing shares to be issued by non-UK registered companies;
- allowing shares to be issued by both the employer and its parent company; and
- changing the notice period for early return from

additional paternity leave from six weeks to 16 weeks to ensure it is consistent with the rules regarding maternity/adoption leave.

One of the biggest obstacles to employers taking up this opportunity would be that granting shares to staff triggers an immediate income tax and National Insurance charge. Very few employees would sign up to such an arrangement if they had to pay the tax themselves so in order to get any take up, an employer would have to bear the tax itself, so even if only £2,000 of shares were to be granted, assuming the employee is a 40% taxpayer, another £1,200 of tax would need to be paid. If the employer paid this, this would itself be a taxable benefit triggering a further charge to tax of £480 so the total cost to the employer, with employer's NICs would be over £4,000 – around about the median award for unfair dismissal. When you combine that upfront cost to the employer with the uncertainties that the shares may have been overvalued and so the whole thing may not work, the complexities and legal cost of set up of the new regime and the fact that most employees leave their employers without thinking of claiming unfair dismissal, you can see why this is looking like it will only be of interest to a niche of employers, such as technology start ups.

The Government is reviewing whether to reduce the income tax and National Insurance contribution liabilities that arise when shares are issued to employee shareholders; and whether to issue further guidance regarding share valuation and forfeiture. The answers to those questions will determine whether the scheme is viable. Watch this space.

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