LONG FINANCE

Why Employee Share Ownership Matters

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EsopCentre

The Z/Yen Group

Why Employee Share Ownership Matters

A Recap Of The Case In 2022

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1. Foreword

Explaining the benefits of employee share ownership these many years has made me realise how easily a big concept can be pigeonholed in a small box. The concept of employee share ownership ought to start from a moral perspective, not least sharing risks and benefits with fellow economic agents. The benefits attach to a number of levels, from the micro to the macro.

At a micro level, employee share ownership seems fair, encourages cohesion, promotes productivity, and provides financial security. At a macro level, employee share ownership encourages longer-term thinking, promotes national productivity, and aids moves to 'sustainability'. At an international level, anyone promoting various forms of 'caring', 'compassionate', or 'stakeholder' capitalism or 'third ways' should take a long, hard look at providing more fervent support for employee share ownership.

Yet, too often the pigeonhole becomes 'tax'. Employee share ownership is a good thing to promote even if you don't believe that tax is a necessary promotional tool. If you do believe that employee share ownership is deserving of tax advantages, then don't lose sight of the wider goals.

That's why I welcome this booklet. It attempts to restate the widest case for employee share ownership regardless of national boundaries. It attempts to re-connect the employee share ownership movement with its deeper benefits, connecting open market economies with environmental, social, and governance standards, in turn linked to long-term sustainability goals.

I hope this booklet promotes discussion that reminds people deep in some thicket of government policies, accounting rules, tax advice, or human relations issues, that their work is part of a big and noble attempt to use that innovative feature of joint-stock companies, the ability to share ownership, for social good.

Malcolm Hurlston

Malcolm Hurlston CBE
Life President, Esop Centre

2. Executive Summary

An Employee Stock Ownership Plan (Esop) is a mechanism to facilitate employee share ownership (ESO) in a company.

Employees are each allocated a quantity of shares which are held for them according to the terms of the Esop. The funds to purchase these shares for the Esop can come from the employees themselves, contributions from the employer, or from external loans.

Esops benefit employees by enhancing their engagement with how their company is run, as well as giving them direct financial reward for their productivity and innovation.

Esops benefit companies through enhanced employee recruitment and retention, and improved economic performance.

From a national policy perspective, Esops can be a powerful instrument for promoting stakeholder capitalism, improving enterprise performance, and delivering societal benefits, such as enhanced environmental, social and governance performance.

Esop schemes align well with the UN's Sustainable Development Goals (SDGs), especially SDG 10 – Reduced Inequalities. Although ESO is not a 'solution', it can help to deliver significant marginal gains across most SDGs (see figure 5), particularly in the development of sustainable, resilient communities.

Four areas of public policy can contribute to support the formation and health of Esops – education, legislation, taxation, and research (particularly around benchmarking and statistics):

- education - in addition to informing employers and employees about the benefits of Esop schemes, policymakers should ensure that participants are aware of the associated risks, particularly if employees will be relying on accumulated Esop shares for their retirement;
- legislation - ensuring that issues. such as listing requirements and voting rights, do not impede the establishment of Esops;
- taxation – this paper emphasises that tax advantages are not fundamental to the establishment of Esops, however, tax benefits can help start-ups and SMEs who are seeking to enhance the recruitment and retention of key staff whilst keeping near-term equity-raising and costs under control. Tax benefits

can help established firms and their employees within a framework of wider community benefit.

- research - benchmarking and statistics are important tools for policy makers seeking to formulate a regulatory and fiscal environment that encourages the formation of Esops. A great deal of existing literature exists examines the human resource effects and economic performance of Esop companies around the world. However, research into the communitarian aspects of Esops as well as their impact on the UN SDGs, is less developed.

ESO contributes to the economy by improving productivity, to social mobility, to levelling up, and to localism, and these issues, rather than simply taxation, should also be front and centre in decision-makers' minds.

3. Preface

This booklet examines the societal case for Employee Share (Stock) Ownership (ESO). It is intended to inform readers about a movement that, whilst several decades old, connects precisely with current societal concerns around environmental, social, and governance (ESG) issues.

As this booklet is intended as an introduction to ESO, it covers a broad range of topics at a high-level. It is intended to recap and summarise why employee share ownership still matters, even more, after decades, and suggest some areas for further research.

Editorial support for this booklet has been provided by the Esop Centre, ProShare, and Equiniti. The principal authors of this booklet, Professor Michael Mainelli and Simon Mills, take responsibility for the contents, yet would like to thank Malcolm Hurlston, Fred Hackworth, and Juliet Wigzell who provided substantial contributions and support.

4. What Is Employee Share Ownership?

Employee share (or stock) ownership programmes (Esops) are formal structures that allow employees to acquire shares (stock) in their company.

Esops can encourage employees to purchase shares in a number of ways;

- **Direct Purchase Plans -** Direct purchase plans are intended to encourage employees to buy shares in their company with their own money. To facilitate this, several countries have established tax-qualified plans that allow employees to buy stock either at a discount or with matching shares from the company. For example, in the USA, employee stock purchase plans enable employees to save money over a specific period of time (typically 6 to 12 months) then use the accumulated funds to buy shares at up to a 15 percent discount (either the price at the time of purchase or the time when they started putting aside the money, whichever is lower). In the UK, share incentive plans allow employees to purchase shares that can be matched directly by the company.
- **Stock Options** - Stock options give employees the option to buy a number of shares at a price fixed, for a defined number of years, into the future. With limited exceptions in various countries, options can be given to any employee under whatever rules the company creates. The aim is that if the share price increases in that time, employees can profit by buying shares below current market rates.
- **Restricted Stock** - Restricted stock, and restricted stock units, give employees the right to acquire or receive shares (by gift or discounted purchase) once certain restrictions have been met. These restrictions may include working a certain number of years or meeting a performance target.
- **Share Gifting Schemes** – These are where the company gives shares to the employees free of charge. These shares normally must be held in a trust structure for a period of time.

There are two other stock-linked staff reward frameworks, Phantom Stock and Stock Appreciation rights:

- **Phantom Stock** - Phantom stock is a contractual agreement between the employer and employees to bestow a cash payment at a designated time or in association with a designated event in the future, tied to the market value of an equivalent number of shares of the corporation’s stock.
- **Stock Appreciation Rights** - Stock appreciation rights (SARs) and phantom stock are very similar plans. SARs provide the employee with a cash payment

based on the increase in the value of a stated number of shares over a specific period of time.

However, the argument could be made that Phantom Stock and Stock Appreciation Rights are not Esop schemes but other forms of performance-linked bonus schemes. Furthermore, if they are tied to board room remuneration, they could provide perverse incentives (such as encouraging unprofitable mergers and acquisitions which drive up stock prices only temporarily) that run counter to the spirit of Esops.

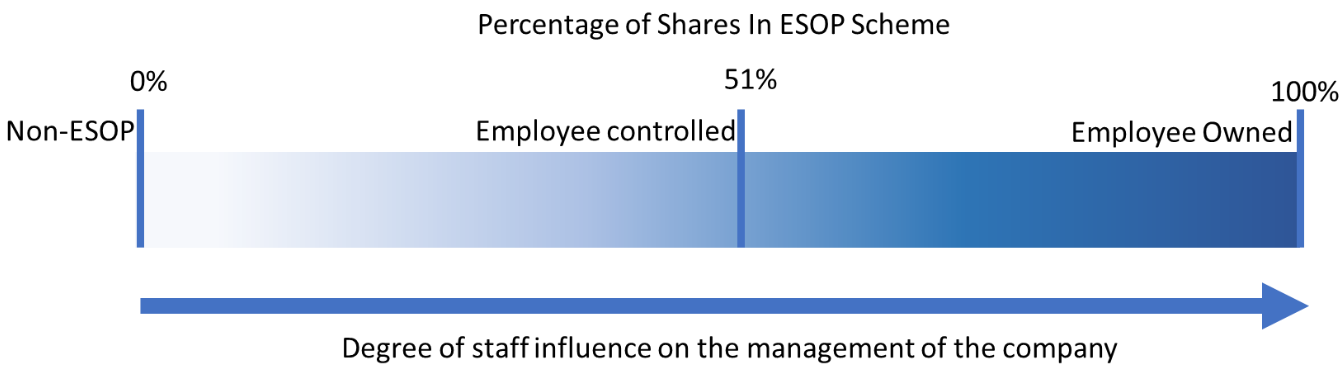
Equally stock options can be seen to be somewhat against the spirit of Esops. While it is true that less buoyant markets and new requirements to 'expense' options have lessened their attractiveness, it is arguable that options should never be used for management remuneration. Options increase in value as volatility increases, thus rewarding managers who create volatility in their company's shares. Empirical studies show that shareholders value companies with lower volatility, so options perversely give managers incentives to decrease shareholder value. Thus options, *ab initio*, divide the interests of managers and shareholders. Genuine equity in 'restricted' stock and longer-term incentives based on competitive benchmarks are theoretically preferable. Nevertheless, so long as options are an option, particularly where they help reduce tax, quick-fixers will opt for these non-optimal methods.

5. What Are Employee-Owned Companies?

Employee ownership is a business where all employees have a 'significant and meaningful' stake (see figure 1). A company with an employee share ownership scheme on does is not necessarily employee-owned – much depends on capital structure, control mechanisms, listing rules, or share options and other 'triggers'. Where shares are held by employees, their ownership can either be direct or indirect:

- **Direct employee ownership** means that employees hold shares which give them the same rights as other shareholders in directing how the company is managed. These rights include:
  - Attending general meetings or appointing proxies to exercise any relevant rights to attend, speak, and vote at a meeting of the company;
  - Voting on company affairs – and where employees own more than 50 percent of a company's shares they may pass ordinary resolutions;
  - Inspection of directors' service contracts.
- **Indirect employee ownership means that a company is owned** (in full or in part) by a trust on behalf of its employees. The trust represents the interests of employees in directing how the company is managed.

Figure 1: Esop Schemes And Staff Influence On Management



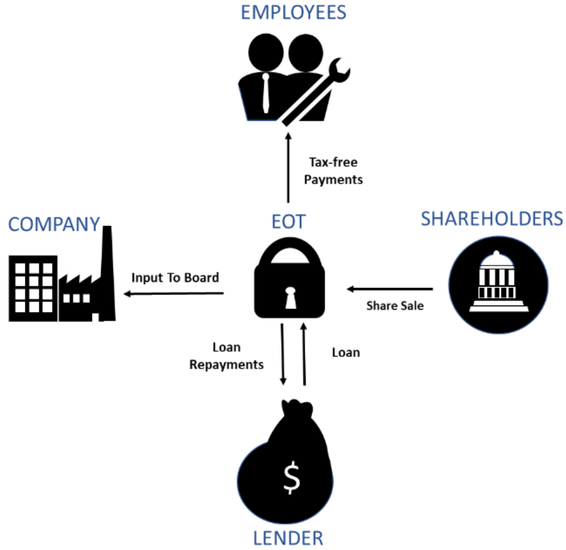
In both models, the interests of employees may be guarded through representation, such as an employees' council or other consultation group, and a constitution defining the company's values and its relationship with employees may be drawn up. This may result in the appointment of employee-directors to the board of the company, with the same responsibilities as other directors.

6. Why Would A Company Choose Employee Share Ownership?

There is no limit on the size of firms choosing to implement Esop schemes, although, small and medium-sized firms are particularly well represented. There are two primary reasons for an organisation to choose to implement Esop schemes:

- **Enhancing employee recruitment and retention** - This tends to be a motivational factor for larger organisations, but it can also be a critical way for start-ups to attract and retain key staff when cash flow is tight. In a competitive business landscape, employees are key competitive differentiators and retaining talent has become a matter of paramount importance. Because they have high employment standards, invest in, and engage staff, Esop businesses are better at recruiting and retaining talented, committed staff[1].
- **Succession planning and ownership transition** - For smaller, privately owned businesses, when an entrepreneur is seeking to retire, they may wish to reward the employees who have contributed to the success of their venture. Rather than winding a business up, or selling a business to a competitor, they may choose to sell the business to their staff. Various mechanisms exist to facilitate this, one of the most common is the establishment of an Employee Ownership Trust (see figure 2).

Figure 2: Simplified Model Of An Employee Ownership Trust



[1] **Saylor T. (2017)** *Esops Help Some CPA Firms With Retention, Succession,* Journal Of Accountancy https://tinyurl.com/pkv6e54t

7. Why Would Staff Choose Employee Share Ownership?

There are significant advantages to staff from employee share schemes. Of course, there are potential financial incentives, as Esops can offer an additional form of remuneration, often tax-effective. This can be enhanced still further if companies choose to give employees discounted or free shares or to match shares bought with additional shares. The schemes can encourage a savings culture allowing employees to better provide for their families futures or their retirement (although this is tied to the success of the business).

One advantage, that research indicates is even more attractive than the financial incentive, is that by acquiring shares in their company, employees effectively become co-owners of their company. This means that employees are more effectively engaged with the company's decision-making, either by taking part in the annual general meetings or through other channels, such as the presence of an employee representative on the board.

As a result pay[2], training[3], health and safety[4], and working conditions are significantly better in Esop firms, and when employees are more engaged, performance and job satisfaction increases and absenteeism is reduced.

Start-up companies typically have very limited funds and cannot offer their employees the same job security as established firms, as a result they often find it challenging to attract and retain talented employees. In several countries, such as the US and UK, Employee Share Ownership is a commonly used tool to aid in the attraction and retention of employees and studies have shown that this has met with some success.

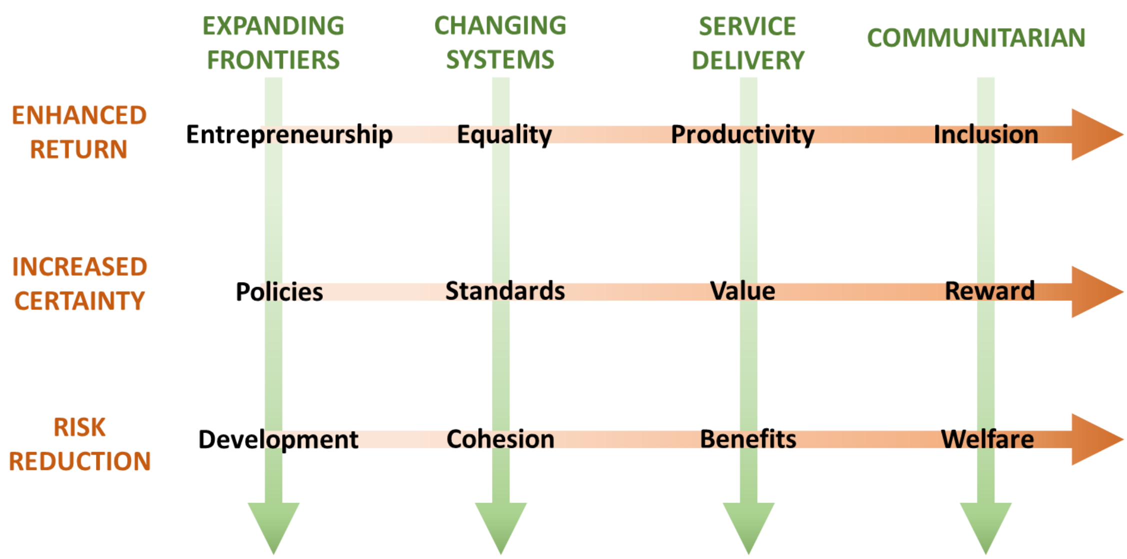
Employee ownership means that staff have a direct say in the future of their company. This mean that they can influence investment and procurement decisions (for example by encouraging procurement from local suppliers), and as they are likely to understand the issues affecting the local community, they can ensure that their company is a 'good neighbour'.

[2] **Bernstein J. (2016)** *Employee Ownership, Esops, Wealth, And Wages*, ESCA https://tinyurl.com/arja5hpk
[3] **Pendleton A & Robinson A (2011**) Employee Share Ownership And Human Capital Development: Complementarity In Theory And Practice https://journals.sagepub.com/doi/abs/10.1177/0143831x10387650
[4] **Rutgers School Of Management & Labor Relations (2020)** *Employee-owned firms In the covid-19 pandemic: How Majority-Owned Esop & Other Companies Have Responded to the Covid-19 Health and Economic Crises,* The Employee Ownership Foundation https://tinyurl.com/8vjmwt4u

8. How Does Employee Share Ownership Benefit Society?

The societal benefits of Esop schemes are summarised in figure 3. This diagram draws on a classification technique from "Evidence of Worth"[5] developed by Z/Yen Group for assessing organisational impact. Evidence of Worth assesses the delivery of benefits through four types of desired outcome – Expanding Frontiers, Changing Systems, Service Delivery, Communitarian – contrasted with three types of risk/reward information – Enhanced Return, Increased Certainty, Risk Reduction.

Figure 3: Esop - Schemes Evidence Of Worth



Expanding Frontiers

Studies have shown that Esops generally outperform non-employee-owned businesses where employees do not have a significant stake in ownership or the right to participate in decision-making[6]. In part this could be a reflection of the fact that inclusive and open organisations tend to out-out perform closed and authoritarian ones. Equally, open and inclusive organisation are more likely to adopt Esop schemes. A side effect of Esops is that the likelihood of takeovers is reduced when Esops are announced[7], almost certainly as a result of enhanced

[5] **Harris I, Mainelli M & O'Callaghan M (2002)** *Evidence Of Worth In Not-For-Profit Sector Organisations* Journal of Strategic Change, Volume 11, Number 8, John Wiley & Sons, pages 399-410 https://tinyurl.com/hny97est

[6] **Lampel J, Bhalla A & Jha P (2010)** *Model Growth: Do employee-owned businesses deliver sustainable performance?* https://tinyurl.com/4a773ykh

[7] **Beatty A. (1995)** *The cash flow and informational effects of employee stock ownership plans Journal of Financial Economics*, vol. 38, issue 2, 211-240 https://tinyurl.com/58ujmbxy

scrutiny by employees concerned about job security and investment issues[8], as well as perhaps concerns by acquirers about employee opposition.

Evidence on Esop company performance is patchy and sometimes old, a sign that Esop research could perhaps use some revitalisation. Nevertheless, the employee ownership index compiled by Field Fisher Waterhouse LLP (2012)[9] showed that listed companies that are at least 10 percent employee owned outperformed the FTSE All Share Index by an average of 10 percent from 1992. There is evidence that firms with Esop schemes have enhanced long term and strategic thinking, with a measured reduction of nearly a quarter in failure rates for Esop firms compared with non-Esop companies over a 12 year period in the US[10]. This echoes recent studies which show that Esop companies showed more resilience than their non-Esop peers during the covid-19 pandemic[11].

Changing Systems

Esops can be attractive propositions for senior managers as they provide a means to enhance employee participation whilst at the same time maintaining 'conventional' management hierarchies and patterns of control. For unions the collective nature of share-holding in Esops allows employees greater influence in management decision making.

Research indicates that pay[12], health and safety[13], and working conditions are significantly better in Esop firms. There is also some evidence of improved inclusion and equality measures, such as representation of ethnic & religious minorities, women in senior management positions, and equal work for equal pay. However there is limited research to support a conclusion that firms with high inclusion and equality measures with Esop schemes perform better in financial or survival terms than non-Esop firms with high inclusion and diversity measures.

[8] **Freeman S. (2007)** *Effects of Esop Adoption and Employee Ownership: Thirty years of Research and Experience*, University of Pennsylvania Working Paper https://tinyurl.com/sm9r2z78

[9] **Fieldfisher LLP (2012**) *Employee Ownership Index* https://tinyurl.com/94vd3vra

[10] **Park, R., Kruse, D. and Sesil, J. (2004)** *Does Employee Ownership Enhance Firm Survival?* Advances in the Economic Analysis of Participatory & Labor-Managed Firms, Vol. 8 https://tinyurl.com/3r3ff9au

[11] **Rutgers School Of Management & Labor relations (2021)** *Employee-Owned Firms In The Covid-19 Pandemic* *https://tinyurl.com/8vjmwt4u*

[12] **Bernstein J. (2016)** *Employee Ownership, Esops, Wealth, And Wages*, ESCA https://tinyurl.com/arja5hpk

[13] **Rutgers School Of Management & Labor Relations (2020)** *Employee-owned firms In the covid-19 pandemic: How Majority-Owned Esop & Other Companies Have Responded to the Covid-19 Health and Economic Crises,* The Employee Ownership Foundation https://tinyurl.com/8vjmwt4u

Inclusion and equality may increase in importance as larger corporates seek to manage reputational risks through their supply change. In turn, inclusion and equality measures appear to be increasing in importance to investors.

From a political perspective, certain policy makers see Esops as a useful mechanism to generate employee commitment to 'enterprise culture' and the market economy which weakens employee attachment to traditional trade unionism. Other policy makers see Esops as an opportunity for workers to benefit from the fruits of their labour[14] and have a greater say in the terms of their employment.

Whichever perspective is taken, industrial disputes are rarer in firms with Esop schemes. Furthermore, empirical evidence suggests that Esops have a direct impact on earnings of management, i.e. equality. Esops motivate employees to monitor management remuneration more closely, thus reducing managerial opportunism, and Esops help managers take the long-term view of the firm, lessening the motivation for short-term earnings distortion[15].

Service Delivery

Managers in companies with Esop schemes share more information about the company and consult with staff more frequently than non Esop companies. Information sharing leads to enhanced productivity.[16] Staff have a stake in a firm's success and they have more incentive to manage their, and their peers', time effectively.

Companies with employee ownership schemes are more innovative – with information flowing more smoothly from the shop floor to the board room. As a result, staff in employee-owned businesses tend to be more entrepreneurial and effective at value creation[17].

[14] **Murphy M (2005)** *The Esop At Thirty: A Democratic Perspective* 41 Willamette L. Rev. 655 https://tinyurl.com/dpyhw74
[15] **Jiraporn P (2007)** *Esops and earnings management: an empirical note* https://tinyurl.com/2r2sm8zv
[16] **Javed T. (2018)** *Impact Of Employee Ownership On An Organizational Productivity: A Mediating Role Of Psychological Ownership* Academy of Accounting and Financial Studies Journal 22(2):1-12 https://tinyurl.com/2prt5zaz
[17] **Garfatta R. & Zorgati I. (2021)** *Employee Stock Ownership And Value Creation: Evidence From System GMM Estimates*, Managerial Finance https://tinyurl.com/y59hnaxc

Communitarian

This last factor is the hardest to quantify and is sparsely researched, however, it is potentially the most powerful incentive for policymakers to facilitate the creation of Esop programmes.

Market economies have been engines of human development and prosperity. Financial exclusion, financial crises, poverty, inequality, and the rising tide of environmental problems challenge societal confidence in the ability of market economies to deliver a better tomorrow.[18] The World Economic Forum addresses this tide of disillusion with the concept of 'Globalization 4.0'.[19] Globalization refers to the breaking down of trade barriers driven by technology and the movement of ideas, people, and goods. The concept of Globalization 4.0 refers to the linking of waves of globalisation to three phases of industrial revolution – steam, oil, electronics - and finally the fourth, data. Globalization aims to look beyond stockholder capitalism to stakeholder capitalism and places inclusion at its heart.

Stakeholder capitalism is the concept that corporations should be oriented to serve the interests of all stakeholders, not just shareholders but customers, suppliers, employees, and local communities. Under this philosophy, a company's purpose is to create long-term value and not to maximize profits and enhance shareholder value at the cost of other stakeholder groups.

This esoteric concept, once the purview of Marxist economists, has found fertile ground as issues that were once considered secondary for CEOs and boards have become important determinants of firms' capacity to create and sustain economic value. Climate change, water management, child labour, ethical treatment of suppliers and other 'soft' issues are increasingly recognized as bottom-line issues in a world of widespread speedy communication where a public image can change quickly.

Research has found that firms with Esop schemes significantly outperformed[20] non-Esop companies not just in terms of environmental impacts, but across a range of social indicators. This is likely to be because they are more deeply invested in their staff, and thus have a deeper involvement in and concern for

[18] https://news.gallup.com/poll/240725/democrats-positive-socialism-capitalism.aspx
[19] WEF 2018 ***Globalization 4 – What Does It Mean?*** https://www.weforum.org/agenda/2018/11/globalization-4-what-does-it-mean-how-it-will-benefit-everyone/
[20] **Stranahan S. & Kelly M. (2020)** *Ownership design for a sustainable economy,* Fifty By Fifty https://tinyurl.com/y9jt6ysm

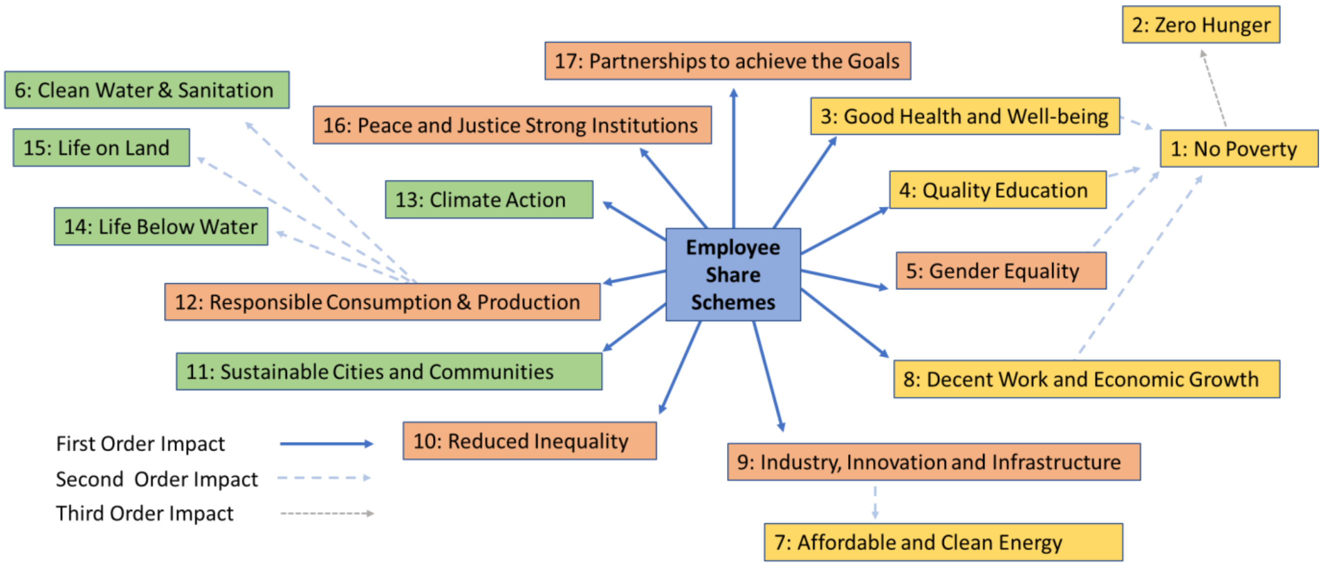
the communities they operate in, making them less vulnerable to reputational risk.

Concern for environmental performance is reflected in more innovative approaches to tackling issues such as air pollution, water quality, waste management, traffic congestion, biodiversity, and climate change, as well as education, and other social concerns across the Environmental Social and Governance (ESG) spectrum (see figure 4).

Figure 4: Environmental Social & Governance Issues

From a strategic perspective, Esop schemes align well with the SDGs, with direct impact links to the majority of them (see figure 5), and perhaps quite direct to SDG 10 – Reduced Inequality. Although Esops do not 'solve' or 'attain' any SDG, they can help to deliver marginal steps towards achieving SDGs, particularly in the development of sustainable, resilient communities.

Figure 5: Esops & Delivery Of The SDGs



9. What Are The Disadvantages of Employee Share Ownership?

For Employees

For employees, the most significant risk is share price volatility (when an employee needs money, share values may not be at an optimum level) and liquidity (employees of private companies may not be able to sell the shares easily). Employees should consider the length of the qualifying period (the length of service required for employees to qualify for shares), and the tax implications (leaving before the period specified in the share plan could mean employees may have to repay tax relief). Waiting for the right value to sell shares may tie reluctant employees to a job they would otherwise leave, potentially affecting both their own and their colleague's morale and productivity.

For Businesses

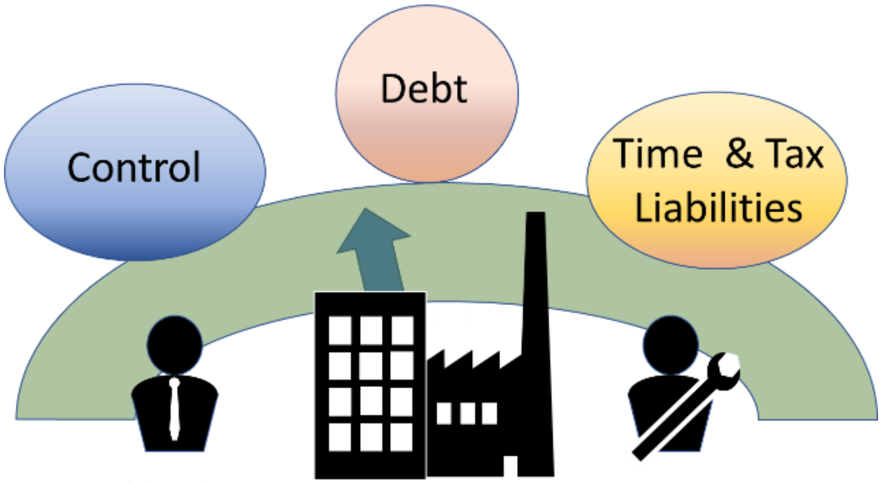
For all companies setting up an Esop there are short-term costs drawing it up and getting it approved, plus the long-term costs of managing the scheme and record-keeping over time. Cash flow management can also become more complex if there is a need to buy back the stock of departing employees[21].

Some Esops borrow to finance the scheme (a leveraged Esop). Leveraged Esops add debt to the company's balance sheet and may have an impact on how others view the creditworthiness of the business[22]. Because company shares are purchased with borrowed funds in a leveraged Esop, a company may find it difficult to service the additional debt if business declines.

For small firms, an issue for consideration is the dilution of share ownership - as more shares are issued each share becomes a smaller percentage of the company – for family-owned firms, this could mean losing control of the business. For very small companies, cost-benefit analysis is recommended to determine whether an Esop scheme is worth pursuing, however for larger companies the case for adopting some form of Esop is more clear cut.

[21] **Buxton D & Gilbert R (2005)** *Esop: A Four-Letter Word? Liquidity and Perpetuation: Pros and Cons* World Business Academy Viewpoint Issue 19 Volume 3 https://tinyurl.com/4tkf8v92
[22] **Tararsi R (2012)** Esops Butcher Joseph Hayes Merchant Bankers https://tinyurl.com/2fmk9r7v

Figure 6: Achieving The Right Balance



10. Public Policy Frameworks For Encouraging Esops

From a public policy perspective, employee ownership can increase participation in the market economy, encourage capital formation, improve labour-management relations, increase productivity, and even generate more profitable firms. A further long-term policy benefit is that, as employees build up their wealth, state payments for welfare, unemployment benefit, and pensions may be reduced[23]. Policy makers have four levers to encourage Esops – education, taxation, legislation, and research (particularly around benchmarking and statistics).

Education

In addition to informing employers and employees about the benefits of Esop schemes, policymakers should ensure that participants are aware of the associated risks, particularly if employees will be relying on accumulated Esop shares for their retirement.

Taxation

Whilst not a precondition for the formation of Esops, there are some key building blocks in developing tax policy that can encourage and support their formation. Most pertinent are:

- **Capital Gains Tax (CGT)** - CGT is charged on gains that accrue when chargeable assets are disposed of by an individual. A sale or a gift of shares is normally treated as a disposal and a taxable gain or loss will accrue accordingly, so a shareholder who sells shares – for instance to an EBT – may be liable to CGT on his or her gains. CGT relief will provide an incentive for the creation of Esops.
- **Income Tax** – Providing a partial exemption from income tax (and related employment taxes) on a certain amount of a bonus or equivalent payment made by an entity within an indirectly employee-owned structure to employees of a company within that structure enables Esop companies to deliver a higher post-tax income to their employees at no extra cost to the company.

[23] **Blasi J. & Kruse D.(1991)** *The New Owners: The Mass Emergence of Employee Ownership in Public Companies and What It Means to American Business* Harper Business ISBN-10 : 0887305091 https://tinyurl.com/2y4y7k9v

Legislation

Legislative support for Esop schemes varies greatly from country to country however, common features include strictures on qualifying periods for participation, structures to hold shares on behalf of employees and listing rules. Table 1 is meant to provide a flavour of the legislative regimes of selected countries while not purporting to be up-to-date.

Table 1: International Legislative Frameworks

Country	Legislation	Year
Australia	There is no single piece of legislation regulating the establishment or administration of Esops in Australia. Companies proposing to offer securities to employees must ensure they comply with the Corporations Act 2001. Changes to the tax treatment of Esops took effect on 1 July 2015. https://www.ato.gov.au/general/employee-share-schemes/ess-basics/	2015
Austria	The Worker Participation Foundation Act 2017 developed Employee Participation Foundations to hold and purchase shares, exercise shareholder's rights and transfer returns to the employees. https://home.kpmg/xx/en/home/insights/2017/07/flash-alert-2017-16.html	2017
Belgium	Stock options were first specifically provided for in Belgian income tax legislation in 1984 (qualifying stock options), amended in 1999. This income tax law stipulated that the benefit of stock options was, under certain conditions, free of income tax. https://tinyurl.com/3mmh8raw	1984
China	The China Securities Regulatory Commission (CSRC) issued the Circular on the Interim Administrative Measures for Employee Stock Ownership Plans of Listed Companies on August 4, 2012, in order to regulate and guide the listed companies in implementing the Employee Stock Ownership Plans (Esop) and other related activities. https://tinyurl.com/496bxb9x	2012

Croatia	The Croatian Law on the Transformation of Enterprises Under Social Ownership 1991 (Transformation Law) gave employees, including managers and former employees, the right to buy shares at a discount proportional to their years of employment, starting at 20 percent and adding one percent for every working year up to a maximum of 60 percent. https://tinyurl.com/yj2fw9ay	1991
Denmark	Provision is made for the issuance of shares to employees under The Tax Assessment Act (Consolidated Act No. 1017 of 28 October 2011). Share options are granted on either a discretionary or all-employee basis. https://tinyurl.com/3mpctz7r	2011
France	"*FCPE de reprise*" (employee buy-out mutual funds) were introduced into the French system of employee financial participation (EFP)in 2006 to allow employees to take over their employer company under preferential conditions. https://tinyurl.com/auvmyecb Another Esop scheme aimed at start-ups is the BSPCE (*Bon de Souscription de Parts de Créateur d'Entreprise*), in effect an Esop stock option. https://tinyurl.com/ee7h3jxv	2006
Hungary	Hungarian Esop are US patterned, based on the Law on Esops of 1992 (Act XLIV of 1992), amended in 1995. https://tinyurl.com/ezbj87a4	1995
Ireland	KEEP (Key Employee Engagement Programme) is a tax-advantageous share option scheme introduced specifically for certain qualifying SME companies for their employees or directors in the 2017 Finance Act. https://tinyurl.com/9crh8b9c	2017
Kenya	The Kenyan legislation governing Esops includes: The Companies Act 2015 section 446 (b)(c), the Income Tax Act, The Finance Act, the Trustees Act, Capital Markets Authority Collective Investment Schemes Regulations 2001 with United Kingdom's statutory schemes regulations provide necessary guidance as to the structure of the main schemes used today. https://tinyurl.com/2a443je3	2015

Korea	Shortly after the Korean War, in 1958 the Yuhan Corporation established South Korea's first employee stock ownership plan (Esop) to resolve labour disputes. The Capital Market Act of 1968 established employee ownership requirements and created the legislative environment surrounding Esops. Esops were originally intended for public companies and required 10 percent of newly issued shares to be allocated to employees. https://tinyurl.com/4u5p24yh	1968
New Zealand	The Securities Act 1978 made it difficult for employers to offer share or option schemes to all but the most senior executives without a prospectus and investment statement, with severe penalties for non-compliance. These complexities were largely swept away by the Financial Markets Conduct Act 2013 (the FMCA). https://tinyurl.com/2s2z83z8	2013
South Africa	As part of its strategy to enhance the economic stake of its citizens the South African Government enacted the Broad-Based Black Economic Empowerment Act. A key plank in this strategy was the encouragement of Esops. To encourage Esops, the government passed the Revenue Laws Amendment Act in 2004. The Act changed the State's taxation of amounts derived from broad-based Esops in favour of employees and employers. Previously, tax treatment did not encourage the transfer of free or discounted shares within the confines of broad-based plans. https://tinyurl.com/zzvrvxhw	2004
United Kingdom	In 1978 the UK introduced the tax-approved Profit Sharing Employee Share Scheme. Now there are four direct Tax-Advantaged Share Schemes (TASS), the Company Share Option Plan (CSOP), the Save-As-You-Earn (SAYE) or Sharesave Plan, the Share Incentive Plan (SIP), and the Enterprise Management Incentive Plan (EMI Plan). https://tinyurl.com/yjn3efh8	1978
United States	The United States is credited with being the originator of the modern Esop movement with legislation that encouraged the creation of Esop schemes under ERISA. Employee Retirement Income Security Act of 1974	1974

A key aspect of the development of a legislative framework that supports the development of Esops is not the creation of new legislation, but ensuring that existing financial legislation does not impede their creation. Quite often listing rules and or restrictions on voting rights for employees or their representatives unnecessarily constrain Esop development. With respect to voting rights, information needs to flow in both directions, and employees who own company stock should have good access to information on the state of the company, either through employee representatives or trustee meetings on the board or by regular newsletters.

Research

While there is a reservoir of international research examining the economic and financial cases for Esop schemes, international comparison and benchmarking is not easy, and longitudinal research is patchy. A number of national centres have been established which seek to encourage the establishment of Esops within their jurisdictions, including:

- Australia https://employeeownership.com.au/
- Canada https://www.esopcanada.ca/
- Europe http://www.efesonline.org/
- France https://www.fondact.org/
- Germany https://agpev.de/
- India https://www.esopdirect.com/
- Japan http://jeoa.org/
- Korea www.esop.or.kr
- South Africa http://www.saeoa.org/
- UK https://esopcentre.com/
- UK https://proshare.org/
- US https://esopassociation.org/

These organisations, alongside the large body of published research, enable policy makers to explore the performance of policy and legislative approaches to Esop schemes. Benchmarking and statistics also provide a common good for Esop companies and the support industry of scheme providers.

For Esops, tax is frequently an important consideration, but hopefully this paper pulls ESO a bit out of the 'tax mire' as the principal point of discussion about Esops, and helps readers see ESO's broader benefits.

Although the case for Esops is strong, further research could assist policy makers in better designing interventions that strengthen their impact. Significant research gaps exist, particularly on the communitarian impacts of Esop schemes and their impacts on the delivery of the SDGs. There are significant policy discussions underway that could provide valuable opportunities for research, such as:

- Employee ownership trusts – how might these be best structured and what have results been so far?
- Pay cuts & employee equity – how might proposals for employees to opt for equity in adverse circumstances be fairly designed?
- Employee voice – is there a case for identifying the employee vote as a separate category of voting result compared with institutional investor votes?
- Employee shareholder share voting – how to provide voting, particularly in listed companies, when employee shares are being managed by an intermediary?
- Employee shareholder stock lending – how do employee shareholders get value when stock is lent?
- Gig workers - how might gig workers best participate in shared ownership?

Appendix A – Esop Timeline

Esop TIMELINE		
Employee Share Ownership	Year	**The Esop Centre**
First Esop launched in US by Louis Kelso.	1956	
Introduction of the tax-approved Profit Sharing Employee Share Scheme by UK government.	1978	
UK government Introduces of the tax-approved Savings-Related Share Option Scheme.	1980	
Government introduces the Share Option Scheme (tax-approved).	1984	
	1986	Employee Share Ownership Centre created.
Margaret Thatcher introduced the Quest or qualifying esop to meet the Centre's request. In practice it built on Lib-Lab pact legislation created in the last year of the Callaghan government	1989	Sister organisation, **European Centre for Employee Ownership** formed for events in Davos and Cannes.
Gordon Brown launched Employee Management Incentives (EMI) : "the most innovative and popular share options based incentive plan ever invented in the western world“. UK government Introduces of the tax-approved Share Incentive Plan through the Finance Act 2000	2000	Senior Centre members played a major role in the conception and development of EMI.
	2008	Pathfinder event in Dubai establishes the **World Centre for Employee Ownership.**
The Con-Lib Coalition comissioned the Nuttall Review of Employee Ownership which culminated in the	2012	**Malcolm Hurlston** receives the Rémy Schlumberger award from

creation of the Employee Ownership Trust (EOT). Sir Norman Lamb was minister of state. Its merits lie most in business continuity and localisation of employment.		International Association for Financial Participation in Paris.
Finance Act of 2014 introduces the EOT	2014	
	2015	The Centre joins the OECD's Business Advisory Group.
	2016	Centre launched the first of its British Isles Share Schemes Symposium, with the aim of encouraging reform of broad-based UK ESO schemes.
	2002-2018	Centre was the lead UK collaborator with the EU in driving at least half a dozen multi-national projects to improve employee take-up of financial participation schemes within EU member states.
	2020	Centre management passes to **Z/Yen** Group Limited.

Two individuals, one American and one British, working together, have had an enormous impact on the development of ESO thinking globally.

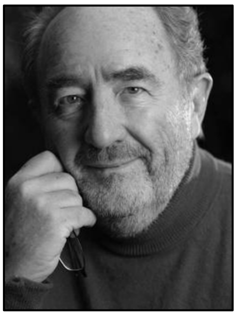
Louis Orth Kelso (1913 –1991) was a political economist, corporate and financial lawyer, author, lecturer and merchant banker who is chiefly remembered today as the inventor and pioneer of the employee stock ownership plan (Esop), invented to enable working people without savings to buy stock in their employer company and pay for it out of its future dividend yield.

Kelso created the Esop in 1956 to enable the employees of a closely held newspaper chain to buy out its retiring owners. Two years later Kelso and his co-author, the philosopher Mortimer J. Adler, explained the macro-economic theory on which the Esop is based in The Capitalist Manifesto (Random House, 1958). In The New Capitalists (Random House, 1961), the two authors present Kelso's financial tools for democratising capital ownership in a private property, market economy. These ideas were further elaborated and refined in Two-Factor Theory: The Economics of Reality (Random House, 1967) and Democracy and Economic Power: Extending the Esop Revolution Through Binary Economics (1986, Ballinger Publishing Company, Cambridge, Massachusetts; reprinted 1991, University Press of America, Lanham, Maryland), both co-authored by Patricia Hetter Kelso, his collaborator from 1963.

Kelso regarded the Esop and Consumer Stock Ownership Plan (1958) as pragmatic proof that his revolutionary revision of classical economic theory, and the financial techniques he derived from this new perspective, were sound and workable in the economic and business world.

In 1971, Louis Kelso founded Kelso Bangert & Company as a merchant bank that would be both an adviser and investor in mergers and acquisitions involving employee stock ownership plans. The firm, which would later come to be known as Kelso & Company, would transition towards private equity investments in the late 1970s and would raise its first private equity fund in 1980. Today Kelso & Company is a $10 billion private equity firm and was among the 50 largest private equity firms globally.

In a biographical summary written for the National Center for Employee Ownership in 1988, Kelso described "the area in which first I alone, and then, beginning about 25 years ago, Patricia and I, have made our contribution to the world of economics and corporate (and other) finance. The Kelso contribution lies partly in the area of macro-economic discovery, and partly in practical ways to implement and make good use of those discoveries in human affairs."



Malcolm Hurlston CBE is the Life President of the Employee Share Ownership (Esop) Centre, which he founded in 1988, and chaired till 2022. He is a serial social entrepreneur who brought credit counselling and employee share ownership plans to Britain.

Malcolm started his career in journalism after national service in which he became a Russian interpreter and interrogator and was commissioned, and three years at Magdalene Cambridge as an open major scholar. He moved into public affairs after two years, mainly to safeguard the insurance industry but also to promote Taittinger champagne. He conceived the Birmingham-based trades union bank Unity in 1980 and at the same time started his own consultancy firm Hurlstons. In addition to insurance and drink, he was active in the co-operative sector, big pharma, oil and gas, retailing and television.

The time of all staffers at Hurlstons was spent in part on public interest activity, which included starting the Foundation for Credit Counselling now known as StepChange, Registry Trust which is responsible for the Registry of County Court Judgments, the Proof of Age Standards Scheme, Orbis and the Standing Committee on Reciprocity among many others, including the Centre.

He sits on the boards of Registry Trust and the UK Shareholders Association and chairs the Financial Inclusion Centre. He recently set up and chairs the charitable CIC, Action for Financial Inclusion, and in April 2021 joined the Pensions minister's MidLife MOT Board. His work in financial services was recognised in the Queen's New Year Honours List 2013 when he was awarded a CBE.

Appendix B – Significant Studies On The Case For Employee Share Ownership

Year	The Case For Employee Share Ownership Studies
1986 + 1987	"How well is employee ownership working" studies by Michael Quarry and Corey Rosen support productivity benefits from ESO.
1988	US general accounting office study draws the link between ESO and productivity.
1991	Peel and Wilson Study found that 'Shared Capitalism' aided reduction of absenteeism.
1998	Hewitt Associates study shows enhanced performance and productivity of Esop companies.
2001	"Shared Modes of Compensation and Firm Performance in the UK" study by prof. Richard Freeman (Harvard & LSE) and Martin Conyon (University of Pennsylvania) found increased added value following introduction of SIP free shares arrangements.
2010	The Matrix Evidence showed ESO companies are associated with higher productivity levels.
	Lampel Report (Cass Business School) concluded that ESO companies have greater capacity to create jobs, and maintain consistency of performance.
2011	Davies Study (Napier University Business School) found that employee job satisfaction was higher in ESO companies.
2012	Cass Business School Report (produced in conjunction with BIS) finding that employee-owned businesses performed better during periods of economic recession than non-employee-owned counterparts.
	Lampel Report identified causation between longer term focus of ESO companies and employee creativity/innovation.

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esopcentre.com
The Employee Share Ownership (Esop) Centre is a non-profit subscription-based organisation which draws from over 30 years of experience to inform, lobby and research in the interest of developing all forms of broad-based employee share ownership plans in the UK and Europe. The Centre works with governments, the European Commission, businesses, and employee organisations to build widespread support for employee share ownership and spread the wages of capital.

Members include listed and private companies operating, developing, or interested in establishing employee share plans, as well as professional experts providing share plan services covering accountancy, law, administration, design, and trusteeship. The Centre's regular conferences, seminars, and lobbying activities provide the ideal space for industry leaders wanting to communicate their needs to government and network with their peers.

www.zyen.com
Z/Yen is the City of London's leading think-tank. Z/Yen helps organisations make better choices – our clients consider us a commercial think-tank that spots, solves, and acts. Our name combines Zen and Yen – "a philosophical desire to succeed" – in a ratio, recognising that all decisions are trade-off. Z/Yen particularly promote societal advance through better decisions about technology and finance. Z/Yen manages the Esop Centre.

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