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it’s our business

newspad of the Employee Share Ownership Centre

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In this issue

From the life president

Few readers of this column will be unaffected by Fred Hackworth's lead story in this edition of newspad. The government's decision to halve individuals' CGT exemption further to £3k really is a "disaster waiting to happen". The immediate impact will be on employee shareholders but their employers and scheme providers face challenges of equal magnitude.

Fred rightly points out that employee shareholders need to be warned that they face a fine of at least £100 if they miss the deadline filing dates, with possible additional penalties later.

Employers are looking at a world in which taking part in a share scheme, which has mainly and rightly carried some element of risk, is more likely to have negative than positive connotations. Schemes will find their world topsy turvy.

That is why we need a concerted effort, directly with the government and among the employee share ownership community, to make employees fully aware of the unprecedented dangers they face. Act with speed and employees will know who covers their back - and be grateful.

Malcolm Hurlston CBE

Cut in CGT exemption is disaster waiting to happen

from esop expert Fred Hackworth

During the Centre's successful campaign to help dissuade the then Chancellor Sunak from adopting the recommendation of the Office of Tax Simplification to align upwards CGT rates with Income Tax rates, YBS warned that many of its SAYE-Sharesave participants would find it very difficult to fill in - for the first time - HMRC CGT tax liability forms.

The current government's decision to halve again from next April the individual's annual CGT exemption allowance from its current reduced level of 6K to just 3K is a disaster waiting to happen for the share scheme sector.

It is highly probable that many thousands of SAYE participants, and some CSOP participants too, will be caught in this CGT trap when their three-year share schemes mature. The main reason for this is that the share option strike price they were offered when their scheme was launched would have been unusually low because of the Covid pandemic. Thus, it should be comparatively easy for many, though not all of them, to make substantial gains when they cash out next year.

Many of those newly liable to CGT charges will miss the HMRC's filing deadline date and are at risk of being fined at least £100 automatically! The penalty would rise to penal charges after the first few weeks of non-filing. Many SAYE/ Sharesave and CSOP participants will not know where to get the relevant tax advice, even if they can afford it, which some will not. This experience will put off some employee share scheme enthusiasts from participation in future workplace schemes.

This is why the Centre should ask Chancellor Jeremy Hunt for a carve out - from the threatened further cut in the exemption allowance - of the three approved share schemes which are subject to CGT charges - namely SAYE/Sharesave, EMI and the Company Share Option Plan.

How is this CGT tax raid compatible, in the context of employee share schemes, with the government's claimed policy of inclusive capitalism? At the same time share plan administrators need to act in employees' interests.

A separate key issue regarding the second proposed halving of the CGT exemption allowance from next April follows the PM's decision, when Chancellor, to freeze the annual Income Tax personal allowance until 2026. This example of fiscal drag spells trouble for employee shareholders as more and more of them slide into the higher tax band, which starts at 50K a year. It sounds a lot, but not when you consider that train drivers and many junior managers already earn 60K annually. Whereas employee shareholders on basic Income Tax rate currently pay only 10 percent CGT when they exceed their fast diminishing annual exemption allowance, their CGT tax rate doubles to 20 percent once they are subject to higher rate Income Tax.

So not only will many be subject to CGT for the first time next year, when their exemption allowance slips to 3K, but also they will be punished by the imposition of a 20 percent CGT charge once they become higher rate taxpayers, as many inevitably will due to annual pay rises.

Share Plan Mortgage

Amazon has announced that employees can use the capital value of vested Amazon stock as deposit for a house purchase.

This new financial product allows stock to be used for a mortgage deposit by Better.com and is linked to approval of the regular mortgage needed for the balance of the acquisition cost. The product is available both for owner occupied and investment property.

Interestingly, the product does not work like a margin loan. Once the initial capital value for the house purchase is set, there will be no margin calls – even if the Amazon stock price goes down. This allows Amazon employees to use their capital more flexibly, without cash flow risk.

The new product is currently available only in 13 US states, but there are plans to expand that footprint considerably in the near future. Amazon itself does not get involved in the finance. Nonetheless, the company welcomes this flexibility for its employees and is happy to have its name linked to the mortgage product.

Up until now, apart from a margin loan, employees would have had to sell their Amazon shares to raise their house deposit cash. That has tax consequences when it involves withdrawing stock from long-term tax protected status. It also locks them out of future capital growth. What's the chance that 30 years from now (2053), the Amazon share price will be down on today?

Why does it matter? - Equity compensation is an increasingly important part of total earnings for many employees. This is strongly true in some sectors like high-tech, but the multi-year capital value of employer equity can be very significant in many other cases too.

This offering by Better.com removes the margin loan risk from the Amazon employees. It is likely that the lender has entered into an equity hedge arrangement to facilitate the overall risk-return profile of the mortgage product. That hedge cost will be baked into other aspects of the overall product offering no doubt; there is no free lunch.

As equity compensation unfolds in future years, we can expect other providers and companies to offer similar arrangements. Connecting employee equity plans with life important capital value decisions, such as your house purchase demonstrates the ability of share plans to deliver long-term capital results if correctly managed.

Damian Carnell of Centre member **CORPGRO** commented: "The launch of one employee equity linked mortgage product for only one company in a few US states might not feel particularly significant. However, viewed as a pathfinder product, we can expect rapid expansion between companies and geographies, and a ripple effect within the mortgage lender industry.

"This kind of linkage between regular financial products and the specialist world of employee share ownership could be significant. But not all products will be good value for money. Employers must take care in linking the company brand to these arrangements, so that non-subsidised equity mortgage offerings are not too steeply priced.

"The use of financial engineering behind the scenes to allow risk abatement for employee share ownership is welcome, but rare."

In *Newspoint,* Corpgro recently reported on the Cap Gemini Esop arrangements, which similarly have a risk transfer mechanic invisible to employees. Cap Gemini employees now own about eight percent of the total capital in issue, worth several billion Euros, in all about equal to the biggest institutional shareholder.

"While employee share ownership is now widespread, the link to long-term capital value needs to be better explained by employers and better understood by employees."

HMRC launches new SAYE bonus rate mechanism

Following its announcement in June 2022, HMRC has updated the mechanism for calculating the bonus rate applicable to savings arrangements for UK tax advantaged SAYE/Sharesave plans.

Participants in a UK SAYE plan must enter into a linked savings arrangement with an authorised savings carrier to save a specified amount per month over a three or five-year period. Under the savings arrangement, the participant will potentially become entitled to a tax-free bonus - essentially this is interest which accrues on their savings, and is paid at the end of the savings period. The bonus is calculated based on a rate which is fixed at the start of the savings contract.

The “early leaver rate” is a different (lower) bonus rate which applies where a participant leaves within the three or five-year savings period (but after making 12 monthly contributions).

The bonus rate is currently nil and has been set at this level since 2014. The bonus rate is set in accordance with an automatic mechanism which, until June 2022, was linked to market swap rates.

With effect from August 18 2023, bonus rates will now be calculated with reference to the Bank of England base rate (the ‘Bank Rate’), which HMRC states will give greater certainty and transparency for users. However, the new mechanism will only apply to new invitations made to the SAYE after this date and not to existing savings contracts.

Provided the Bank Rate remains at 3.25 percent or above, it is likely that bonuses will become payable. Given that the Bank Rate is currently 4.5 percent (and currently showing no signs of going down in the immediate future), bonuses are likely to apply to savings contracts entered into from August 18 this year for the first time in almost a decade.

If bonuses do become payable, what will this mean for UK SAYE? - The obvious implication is that participants will normally become entitled to receive interest on their savings, in the form of a tax-free bonus whenever the Bank Rate is at or above 3.25 percent. Note the interest is paid by the savings carrier as a term of the savings contract – it is not an additional payment by the employer group.

However, there is another potential benefit too. Where a bonus is payable, it can also be included in the amount of the savings the participant will make over the life of the savings arrangement. This amount is called the ‘expected repayment’ and is a feature of the SAYE regime itself, so applied equally under the previous bonus mechanism.

The ‘expected repayment’ is used to calculate the number of shares subject to the SAYE option. A bigger expected repayment therefore ultimately increases the number of shares subject to an SAYE option. This means participants can buy more shares and maximise the value they are receiving from the SAYE plan.

Suzannah Crookes of Centre member **Tapestry Compliance** commented: “Existing plan participants should note that the change will only apply to savings contracts entered into on or after August 18 2023. Any change in the mechanism for calculating the bonus rates will not, of itself, impact existing contracts in any case as the rate has already been specified at nil.

“A simplification of the bonus rate calculation mechanism is likely to be seen as good news, especially after a number of months of waiting to see what the new mechanism would be. The increased transparency over rates is to be welcomed – the previous mechanism linked to market swap rates was very difficult for most participants (and others) to understand. Now, the rate is clearly linked directly to the Bank Rate and HMRC has published the applicable bonus rates, so there is no need to run complex calculations.”

HMRC launches new SAYE bonus rate mechanism *more*

Lynette Jacobs of Centre member **Pinsent Masons** commented that companies who operate an SAYE scheme need to understand the implications for them and their employees of the increase in bonus rates from August 2023, and whether they would increase the number of shares that can be acquired under their SAYE scheme to reflect the tax-free bonus available.

"The impact of the application of a bonus rate should be discussed with finance and company secretarial colleagues. While the bonus rate will be funded by the savings carrier, the impact of offering a bonus on the accounting cost of the SAYE scheme and the increase in potential dilution – since more shares will need to be issued in connection with the SAYE – will need to be modelled and understood.

"Where UK employers have overseas participants in an international version of the SAYE scheme, they will also need to consider the potential differences between UK and overseas participants, to the extent interest is not already received on savings made by overseas participants in the SAYE or the implications of the company funding a bonus for those overseas participants to align them with their UK counterparts" she said.

CBI to lay off workers in attempt to cut wage bill by a third

The *Guardian* reported that the UK's most prominent business lobby group, the Confederation of British Industry, is to lay off a swathe of its workers as it fights for survival amid a crisis prompted by multiple sexual misconduct allegations.

The CBI needs to cut its wage bill by a third within months, staff were told at an all-hands meeting on June 1, according to sources with knowledge of the discussion, with management aiming to initially use voluntary redundancies to trim costs.

A spokesperson for the lobby group, which employs 300 people, confirmed it had to make "difficult decisions" including cutting its salary base by a third, along with other "cost-saving measures". "It will be a smaller and refocused organisation in the future," they said.

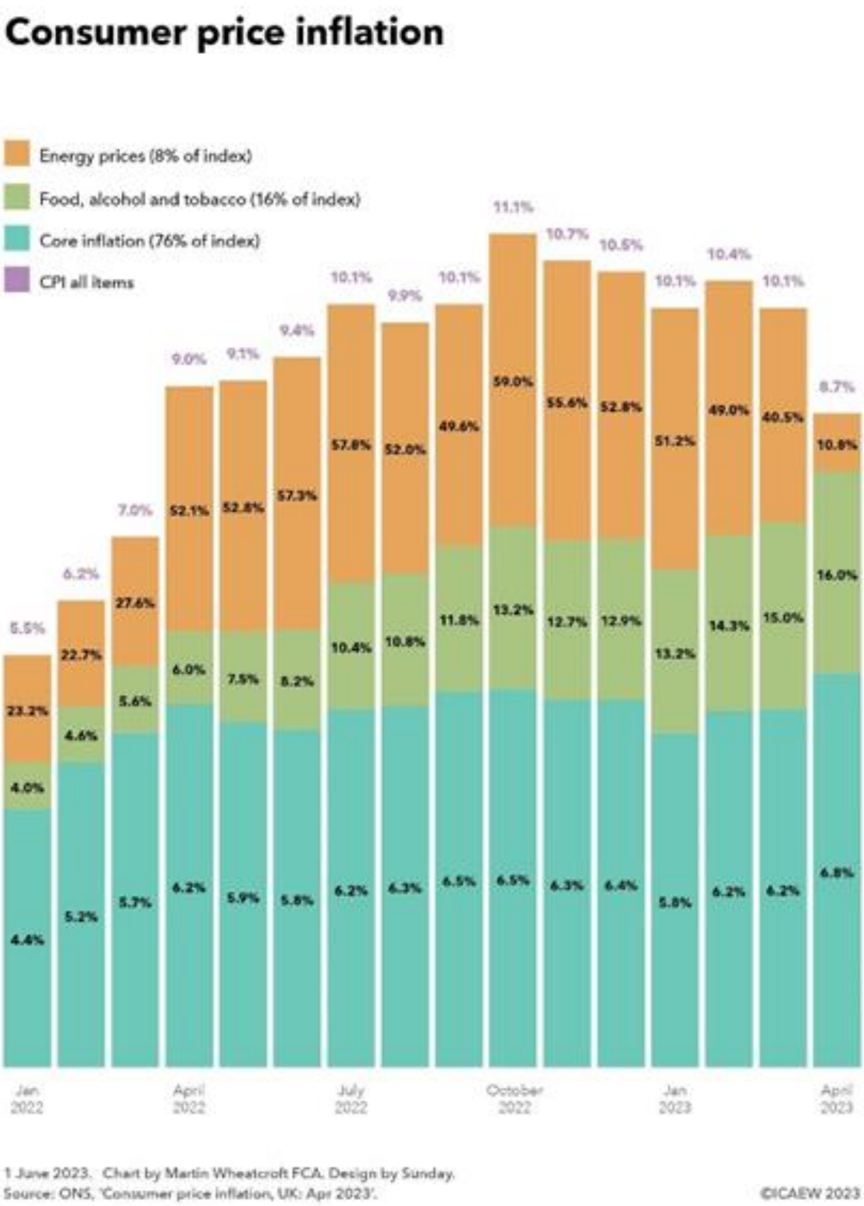
On May 31 the CBI opened a confidence vote on its future and laid out a prospectus detailing plans for a reformed culture and governance. The result of the vote is expected to be released shortly after a June 6 extraordinary general meeting with members. Meanwhile the chambers of commerce have announced plans for a lookalike body.

Consumer price inflation

On June 1, the Institute of Chartered Accountants in England and Wales published a chart that illustrates how 'core inflation', energy price rises, and food, alcohol and tobacco price inflation contributed to a lower than expected fall in the overall rate of inflation in April 2023.

The good news is that planned cuts to domestic energy prices in July, together with other price rises last summer falling out of the year-on-year comparison, should feed through to a much lower headline rate of inflation over the next few months, reducing the pressure on wage settlements and other input costs that are currently driving up prices across the whole economy.

Despite that, the markets believe that further interest rate rises may still be necessary on top of the actions already taken by the Bank of England, potentially risking overtightening that could worsen the cost-of-living crisis and the squeeze on businesses.



The cost of greening business

There are no hard and fast rules to making a business more sustainable, but a tailored and holistic approach to sustainability that meets a company's strategy and aims may pay in more ways than one.

Depending on the size, sector and nature of a business, making a company sustainable can range from fairly straightforward to hugely complex. What is clear, however, is that there is a cost attached.

Luma Saqqaf, ceo of Ajyal Sustainability Consulting, said: "There is no doubt moving towards sustainability comes at a cost for businesses. That cost depends on what you want to do, what shifts you want to make and over what period of time."

It can be a question of sourcing products from local suppliers, which in turn will lower transport costs, boost local jobs and local businesses, to as complex as overhauling products and raw materials. However, Birgit Breitschuh, a partner at consultants Oliver Wight EAME, warned that there may be unintended consequences.

"Certainly, sourcing more locally will reduce the carbon impact through lower transportation costs. However, there are often hidden money and energy costs from bulk buying, such as the cost of the warehouse space and heating consumed while it is all stored for long periods, or even obsolescence. Sometimes, when companies look into it, they find it was not only poor for sustainability, but also not such a wise financial decision in the first place," she said.

There is no single rule for implementing a sustainability programme. It can be as complex or as simple as a company wants it to be. The starting point for business leaders is to identify which environmental, social and governance issues are critical to their company because of the impact, risk or opportunity.

The US government and European Union have just announced billion-dollar investments in sustainability programmes to achieve their net-zero goals and attract inward investment. Although the UK government has been criticised for being slow to back sustainability programmes, some grant funding is available.

Photo by Towfiqu barbhuiya on Unsplash

EVENTS

Webinar

Esop Sofa – newspad review webinar re-scheduled to Aug 1

Thank you to everyone who took part in April's discussion on possible responses to the government's call for ideas on SIP and SAYE. The Centre's next *Esop Sofa-newspad Review* will be at 11:00am on Tuesday August 1 (re-scheduled from June 21). Join our panel of share schemes experts for in depth discussion of their pick of articles featured in recent editions of "*It's Our Business*", newspad of the Esop Centre. Registration is open.

Thank you to our previous hosts of the Esop Centre British Isles Employee Share Plan Symposium

Baker McKenzie.
MACFARLANES
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EMPLOYEE OWNERSHIP

New EOTs:

- PR and communications agency Skout
- Veterinary Clinic Cornerstone
- One of the first American software companies to adopt a novel ownership structure is an open source software company, CodeWeavers.
- Cleaning and maintenance company Principle Cleaning Services
- Logistics giant Cardinal Global Logistics
- Training provider HIT Training
- Built environment publisher Place North West
- Heritage and high-end, bespoke homes developers Carreg Construction
- Catering and refrigeration firm KF Bartlett
- Multi-disciplinary property surveying company Dot Surveying

Exec reward

Calls for US-style executive pay in the UK are misguided

Julia Hoggett, ceo of the London Stock Exchange, made headlines recently with her view that UK-based executives should be paid more to tackle the increasing sense that 'London is being left behind'.

Couched in the broader debate about UK corporate competitiveness, her views have found sympathetic ears among some (but by no means all) asset managers, prompting suggestions of an 'emerging divide' within the City over executive pay.

However, executive pay is not the main criterion creating a lack of competitiveness in the London market. Regulation, taxation and buyouts by private equity firms all play a part, as does the reality that after Brexit there has been some transference of capital to the continent.

Contrary to recent headlines, UK executive pay is competitive. Indeed, UK executive pay is high in comparison to European peers and is certainly much more competitive than pay rates in Asia. A key reason executive pay in the UK is below US peers is because pay in the US is seldom opposed and has run rampant.

At the upper end of the spectrum in the UK, a FTSE 30 ceo is likely to be on a package that can deliver £5-10m per year. This is an ample reward structure that needs no further enhancement; we continue to see pay packages ratcheted upwards – with bonus and LTIP maxima drifting higher.

The US is and has always been an outlier where ceos can typically earn $15-20m with fewer performance obligations and hurdles. A race to the top is placing increasing emphasis on greed rather than the pride and privilege of heading up a major FTSE100 business.

"While pay is an important issue in the UK market we don't believe it is the most important issue driving companies away," Kimon Demetriades, stewardship analyst at Allianz Global Investors, which oversees €506bn of assets, told *Financial News*.

Netflix shareholders withhold support for executive pay package

On June 1, *Reuters* reported that Netflix Inc shareholders withheld their support for the company's executive pay package, in a non-binding vote that followed a call by striking Hollywood writers to reject the proposed 2023 compensation.

The Writers Guild of America West had urged investors to vote against the compensation offered to Netflix's top executives, arguing such a vote would be "inappropriate" during the strike, which has entered its fifth week.

Exec reward *more*

Hollywood writers say the bosses make too much.

Many of the concerns motivating the current Writers Guild of America's strike — from streaming residuals to the looming threat of AI displacement — are distinctly 2023 problems.

But, speaking from a picket line outside Fox Studios in Century City, Mike Royce framed the WGA's campaign in terms of a more timeless struggle: Workers make too little, and bosses too much.

"If they don't have any money to give us raises, then how did they — the executives in the C-suite — amass such record salaries?" asked Royce, co-creator of TNT's "Men of a Certain Age" and the co-showrunner behind Netflix's "One Day at a Time" reboot. "The difference between ceo pay and worker pay has never been greater in most industries, but in this industry it's even worse," found *Los Angeles Times* analysis.

One in three Amazon shareholders unhappy with executive pay practices

On the May 24, Amazon held its annual general meeting, where a record number of proposals – 33 – came up for vote. This meeting was important to those tracking sustainability and governance themes both at US companies, and worldwide.

Among the management proposals, executive compensation was a key area of dissent for Amazon shareholders – as it often is at many companies.

Almost 32 percent of the company's shareholders voted not to approve the company's executive compensation in the "Say on Pay" proposal this year. That equates to over 38 percent opposition from independent shareholders, if we adjust the calculation to exclude the 12.3 percent shareholding of executive chair Jeff Bezos and other Amazon board members.

Vistry shareholders revolt on executive pay

More than 47 percent of Vistry Group shareholders voted against the company's remuneration report at its annual meeting on May 18.

The housebuilder, known as Bovis Homes prior to its acquisition of Galliford Try's housebuilding businesses in 2019, saw just 52.9 percent of its shareholders vote in favour of the pay-package motion.

The vote was on executive pay in 2022, a period that saw chief executive Greg Fitzgerald who was on a base salary of £726,000, awarded a total package of £3.4m including bonuses and incentive payments.

Exec reward *more*

Proxy adviser company PIRC was among those that recommended voting against the report. In advice reported by *Construction News* it highlighted issues including the excessive variability of the chief executive's pay and the 28:1 ratio of his compensation compared with the average Vistry employee.

At its last agm, only 2.3 percent of shareholders voted against the executive pay package. Such votes are advisory rather than binding.

Pearson suffers shareholder revolt over executive pay

Former *FT* owner Pearson has suffered a shareholder revolt over executive pay as investors in the London-listed education group expressed their unhappiness over the prospect of larger payouts in the future.

According to the *Financial Times*, more than 46 percent of votes cast in a binding vote at the company's annual general meeting at the end of April were against a new remuneration policy, the latest in a string of protests after chief executive Andy Bird took home $8.5mn last year.

Aligning incentives matters: ESG in executive compensation

With proxy season upon us, "Say on Pay" may no longer be tied to financial metrics, such as return on invested capital and earnings per share growth. Companies are now increasing the resources spent on measuring, disclosing, and setting targets around ESG initiatives that have operational implications.

According to a recent IBM study that surveyed 2,500 executives in 22 industries and 34 countries, 76 percent believe ESG is central to business strategy.

While ESG information is proliferating across many industries, online investing community *Seeking Alpha* asks whether ceos and other key decision-makers have any "skin in the game" to help make their ESG ambitions a reality.

Target setting is futile if you do not incentivise the achievement of those targets. While operational performance can be clearly evaluated, quantifying success in terms of ESG factors remains subjective and nebulous.

Exec reward *more*

Executive pay linked to climate risk sends misleading progress message

Meanwhile, *IPE Magazine* reported that the significant increase in the integration of climate metrics into executive compensation schemes suggests a fundamental disconnect between performance and pay outcomes, according to recent research conducted by Pensions & Investment Research Consultants (PIRC).

Of the largest global listed companies employing climate metrics, there was an average vesting level – the proportion of a bonus paid out – of 80 percent, highlighting the gap between corporate payout culture and the reality of the impacts of climate change on the environment and society.

In its research PIRC uses Glencore as a case study to note this disparity. At its 2022 annual general meeting, Glencore's climate transition plan was opposed by nearly a quarter of the total shareholder base – the largest single vote against any climate plan put to UK shareholders in 2022.

Despite concerns raised by shareholders, the element of the variable incentive scheme that captures performance on climate-related metrics vested in full.

PIRC's analysis found a significant number of companies employing climate metrics in their pay schemes, especially in Europe. But often these are bundled in as part of broader ESG targets making them of questionable value even if they were more challenging than is the case currently.

The report also raises concerns that, now boards appear to have adopted climate metrics that pay out too easily, investors may become distracted by engaging over pay rather than focusing on transition plans and emissions reductions.

The structural problems evident in current attempts to link pay and climate change highlighted in the research are emblematic of the fundamentally flawed attempt to tie a diverse and often conflicting set of business priorities to rewards.

PIRC has long been of the view that these priorities should be considered as directors' duties – required to promote the success of the company, not optional extras to be rewarded if achieved.

Conor Constable, stewardship manager at PIRC, said: "We question the view that a performance metric representing a fraction of the total opportunity available to executives is a credible tool to drive more desirable climate outputs."

He added: "These metrics are neither easily measurable nor sensitive to the decision making of executives. If stakeholders are serious about holding decision makers accountable on issues such as climate change, it is necessary to pivot away from highly complex and opaque compensation structures to a renewed focus on the duties of directors and their legal obligation to be responsible for the impact of a company's operations on the community and the environment."

France

Société Générale confirms the launch of a global Eso programme

French-based multinational financial services company Société Générale confirmed the launch of a new global employee share ownership programme allowing eligible current employees and retired former employees of the Group to subscribe for a capital increase reserved for them on preferential terms. The subscription period for the share offer runs from June 1 to 15 (inclusive).

The settlement-delivery of the shares should take place on July 24 2023.

This transaction implements the 21st resolution of the general meeting held on May 17 2022. The principle of this operation, approved by the board of directors on February 7 2023, was made public in page 14 of the report published on April 17 2023 on the resolutions submitted to the general meeting of May 23 2023 and, before that, in the table of financial authorisations provided in section 3.1.7 of the Universal Registration Document dated March 13 2023 which has been updated, on page 33 of its first amendment dated May 12 2023.

India

Esop payouts, plummet among start-ups amid funding winter

As the so-called start-up funding winter lingers on, employee stock ownership plan payouts among fledgling companies have hit the skids. Employee earnings from Esops have come down from the highs of almost $400 million in 2021 to less than $100 million this year, according to equity management platform Qapita.

While the funding slowdown has had no significant impact on the issuance of Esops, a liquidity crunch has caused the once-overflowing well of Esop buyback programmes to run dry.

Start-up funding in India hit new heights in 2021 when investments reached a total of $44.5 billion. Since then, capital has become much harder to come by. Total funding fell to almost half in 2022 at $26.6 billion, while start-ups raised just $2.8 billion in the first quarter of this calendar year, according to data from Tracxn, a market intelligence platform.

Homefirst allots 65,000 equity shares as Esop

On May 27, Home First Finance Company India Ltd announced, through a regulatory filing, the allotment of 65,000 stock options under the Homefirst Esop Scheme 2021.

Each stock option entitles the holder to apply for one equity share of the company at a face value of Rs.2/- each.

USA

Esop owns lion's share of leading manufacturer

The share register of Mayville Engineering Company Inc discloses that The employee share scheme owns the lion's share in the company with 42 percent ownership.

Institutions have 39 percent. Institutions will often hold stock in bigger companies, and it would be expected that insiders would own a noticeable percentage of the smaller ones. Institutional investors commonly compare their own returns to the returns of a commonly followed index. So they generally consider buying larger companies that are included in the relevant benchmark index.

The fact that institutions own a respectable stake in Mayville Engineering implies the analysts have looked at the stock and like what they see.

Esops are growing in popularity as a great way to exit

According to data from the US Small Business Administration, more than half of small-business owners are over the age of 50 and, as these business owners age, many are starting to think about succession planning.

One growing option is to sell the business to its employees, often gradually through an Employee Stock Ownership Plan. According to data compiled by the National Center for Employee Ownership there are nearly 7,000 Esops in the US which employ more than 13.5 million people and own more than $1.1 trillion in assets.

But as popular as they are, creating an Esop takes planning and a certain type of culture.

An Esop can take various forms, but generally setting one up involves creating a separate entity that's owned by a company's employees, with the ownership determined based on a variety of factors from compensation to tenure to job position.

"You can exit your business over years and still retain control," said Susan Hoesly a principal at Verit Advisors.