28. United Kingdom

This country profile is based on the country chapter of the PEPPER IV Report (co-authors Natalia Spitsa, Andrew Pendleton and Fred Hackworth). The co-authors of the 2014, 2018 and 2020 updates were Jens Lowitzsch and Graeme Nuttall, that of 2023 Graeme Nuttall.

Profit-sharing plans first appeared in the UK in the 19th century. Employee share ownership (ESO) plans became better known from the 1950s. These plans, however, remained small in number until, starting in 1978, tax incentives for ESO plans were introduced. By 2020/2021 16,330 companies maintained HM Revenue & Customs tax advantaged ESO plans.[362] Following the abolition, from 2000, of a tax advantaged cash profit-sharing plan (the Profit-Related Pay Scheme), the only tax advantaged plans were share-based until the introduction of an income tax exemption for certain qualifying bonuses paid by companies controlled by employee-ownership trusts (EOTs) in 2014. The EOT has had a significant positive impact in growing the UK employee ownership sector with the number of EOTs exceeding 700 by the end of 2021.[363] There continues to be Government support available for new and existing public service mutuals, which numbered around 115 in 2018.[364] The Department for Digital, Culture,

[362] All figures in this Section are for United Kingdom tax years (6 April to 5 April) and are either up to or for the tax year 2020/2021 unless otherwise stated. They are from Employee Share Schemes Statistics to 2020/2021, HM Revenue & Customs, June 2022.

[363] https://www.rm2.co.uk/resources/blog/2021-was-another-bumper-year-for-employee-ownership-trusts/, accessed Sept. 2023.

[364] https://www.gov.uk/government/collections/public-service-mutuals#research-and-evidence, Sept.2023.

Media and Sport's Mutuals Support Programme 2 (MSP2) supported 44 projects between March 2018 and January 2020. An evaluation of MSP2 found "increased employee engagement and cultural change" in organisations. [365]

Four tax-advantaged ESO plans operated in 2020/2021. The majority of companies (98%) operated only one type of plan. The breakdown is as follows: There are two "all-employee" ESO plans, that is, Share Incentive Plans (SIPs) operated by 820 companies and Savings-Related Share Option Schemes (SRSOs) (also known as Sharesave or SAYE Schemes) operated by 480 companies. SIPs were introduced in 2000 and the number of companies operating a SIP peaked at 940 in 2006/2007 declining to average just over 800 in recent years. A steady decline in the number of SRSOs can be seen over the period 2000/2001 to 2013/2014 from 1,110 to 440 increasing to somewhat to average around 480 over recent years. There are two "discretionary" or "selective" ESO plans: Company Share Option Plans (CSOPs) operated by 1,170 companies and Enterprise Management Incentives (EMI) share option arrangements operated by 14,310 companies. A substantial decline in the number of CSOPs can be seen from 4,270, in 2000/2001, to 1,050 in 2013/2014, since when the number has been between 1,140 and 1,200. The EMI arrangement was introduced in 2000/2001 with the number of EMI arrangements exceeding the total number of other tax advantaged plans by 2004/2005. The number of EMI arrangements has increased in almost every tax year since its introduction, averaging around 1,100 additional EMI arrangements in each recent year. EMI arrangements account for the 88% overall increase since 2009/2010 in the number of tax advantaged plans.[366]

In March 2022, there were 195 employee-owned companies, including worker co-operatives, operating in Scotland.[367] 146 of these were Scottish headquartered with 5,350 employees and a combined turnover of GBP 691 million a number that had risen to around 165 in Press reports in March 2023. The number of Welsh employee-owned companies has started to grow significantly too. In June 2022 there were 38 such companies in Wales, with eight created in the previous six months.[368] The total was 63, including worker co-operatives, by May 2023.[369] The significant growth in the number of employee-owned companies in Scotland and Wales, and elsewhere in the UK, is attributed to the success of the EOT.

According to the 3rd and 4th European Company Survey (ECS), a survey of more than 27,000 human resource executives across Europe conducted in five-year intervals, in 2019 35.3% (2013, 26.5%; 2009 8.3%) of companies with more than 10 employees in the United Kingdom offer their employees profit-sharing and in 2013 8.3% (2009, 6.2%) some form of share-ownership schemes (the question regarding share-ownership schemes was not included in the 2019 ECS). The 6th European Working Conditions Survey (EWCS), a regular household survey which covered 35,765 random-

[365] Evaluation of the MSP2, NatCen Social Research, September 2020, accessed Sept. 2023.

[366] Since tax advantaged plans involve events which are not all reported to HM Revenue and Customs, it is impossible to determine the exact number of employees participating in plans at a given moment. The official statistics do not distinguish between plans in listed companies and private companies. Many companies combine one or more tax advantaged plans with non-tax advantaged plans (no statistics are available).

[367] Scottish Employee-Owned Business Census 2022, Co-operative Development Scotland, 31 March 2022.

[368] https://www.gov.wales/employee-ownership-day-economy-minister-sets-out-plans-double-number-employee-owned-businesses, accessed Sept. 2023.

[369] Video call between Cwmpas and Graeme Nuttall on 24 May 2023.

ly selected individuals in the EU 28, shows that in 2015 19.1% (2010, 12.8%) of British employees were taking part in profit-sharing while 8.7% (2010 5.2%) of them were participating in share-ownership schemes.

a) General Attitude

Successive United Kingdom Governments have committed themselves to supporting employee financial participation (EFP) plans and promoting widespread individual share ownership for reasons both ideological and pragmatic. These include making enterprise more democratic, developing financial markets and fostering social welfare. Various non-governmental organisations in the United Kingdom promote ESO in all its forms, including ProShare, which promotes ESO, and the Employee Ownership Association which promotes the employee ownership of companies. Employers' organizations generally support EFP plans. Trade unions over the years have taken a dim view of EFP on the grounds that it would undermine the traditional collective bargaining process. This was their reason for strong past opposition to Profit-Related Pay Schemes. In 2013 the Trades Union Congress (TUC) published its principles of acceptable employee ownership.[370]

Reforms 2011-13 – From 2011 to 2013 the Office of Tax Simplification reviewed the complexities of ESO plans, both tax advantaged and non-tax advantaged. This enabled the Government to undertake a significant package of reform to the tax rules for ESO plans. These reforms simplified the tax rules and made it easier for private companies to introduce tax advantaged ESO plans. In 2012 the Government commissioned the Nuttall Review of Employee Ownership. This provided a comprehensive appraisal of the situation of employee ownership in the country and proposed a wide range of initiatives to promote the employee ownership business model in the British economy (Nuttall 2012). The Nuttall Review defined "employee ownership" as "a significant and meaningful stake in a business for all its employees" and explained that "What is 'meaningful' goes beyond financial participation. The employees' stake must underpin organisational structures that ensure employee engagement". This report resulted in a number of significant Government initiatives and legal reforms[371]. Amongst other initiatives, in October 2012 the Government adopted an Action Plan on Employee Ownership and included in the Budget 2013 a financial provision from 2014-15 to further incentivise growth of the employee ownership sector. In terms of legislative reforms, in 2013 the British Government reformed the Companies Act 2006 in favour of ESO plans and in 2014 introduced tax exemptions for "indirect" ownership of shares on behalf of employees, through EOTs. This was a significant change in emphasis from only supporting the ownership of shares directly by employees and means there are now tax advantaged arrangements for all the main forms of employee ownership. The Government's view (in October 2018) was that following its support for the Nuttall Review recommendations on awareness-raising and simplifying relevant regulations it is now for the private sector to grow employee ownership. The United Kingdom had an additional tax advantaged arrangement for certain shares issued from 2013 to 2016 to those with "Employee Shareholder" status. In exchange for giving up various employment law rights an individual was awarded at least GBP 2,000 of shares in their em-

370 https://www.webarchive.org.uk/wayback/archive/20171001181011/http://touchstoneblog.org.uk/2013/07/trade-unions-and-employee-ownership-a-good-mix-lost-in-the-myths/.

371 Nuttall Review of Employee Ownership – a guide to source materials http://tinyurl.com/FieldfisherEO19.

ployer or parent company. There is a capital gains tax exemption when these Employee Shareholder shares are sold. This "shares for rights" scheme was widely criticised. The tax advantages were abolished for new Employee Shareholder shares arrangements from December 2016.

Devolved legislatures support – There is strong support for EFP and employee ownership in Scotland and Wales. Backed by the Scottish Government, an industry leadership group launched in August 2018 and called "Scotland for EO" aims to increase this number to 500 by 2030. This initiative adds to the work of Co-operative Development Scotland, an arm of the Scottish Government, working in partnership with Highlands and Islands Enterprise that supports company growth through collaborative and employee ownership business models.[372] There is also support for employee ownership from the Welsh Government[373], supported by Cwmpas (formerly the Wales Co-Operative Centre).[374]

b) Legal and Fiscal Framework

All EFP plans fall into one of two categories: tax advantaged and other, non-tax advantaged, plans. At one time all tax advantaged plans had to be approved by HM Revenue & Customs. In 2014 this approval process was replaced by self-certification. Some non-tax advantaged plans may still be referred to as "Unapproved Plans". Tax advantaged share and share option plans enjoy substantial tax and national insurance contributions (NICs) exemptions, as set out primarily in the Income Tax (Earnings and Pensions) Act 2003, especially for employees. Non-tax advantaged plans may be introduced at the employer's discretion but receive no special tax incentives. Tax advantaged plans must conform to tax law requirements; non-tax advantaged plans are more flexible. Non-tax advantaged plans may be used for granting shares, options or cash equivalents without conforming to the requirements imposed on tax advantaged plans and may be operated alongside tax advantaged plans. Following the phasing out, from 2000, of a Profit-Related Pay Scheme, all tax advantaged EFP plans had been ESO plans. This changed in 2014, because of the findings of the Nuttall Review, with the introduction of an income tax exemption for certain qualifying cash bonuses paid by companies controlled by EOTs. UK Governments have promoted the concept of what is called a public service mutual. This is an organisation that delivers public services (such as community health care) but has "spun-out" of the public (state) sector and has employee control embedded within its organisation. This can be employee control through ESO. For a period, the Mutuals Information Service managed by the Cabinet Office's mutuals team, encouraged and supported the establishment of public service mutuals.

aa) Share Ownership

Share plans may be tax advantaged or non-tax advantaged. Under current legislation there are four main tax advantaged plans, one share plan with several variations (SIP) and three share option plans (SRSO, CSOP and EMI). As already noted, SIP and SRSO are broad-based "all-employee" plans, while CSOP and EMI may be restricted to se-

[372] https://www.scottish-enterprise.com/support-for-businesses/business-development-and-advice/employee-ownership, accessed Sept. 2023.

[373] https://businesswales.gov.wales/socialbusinesswales/employee-ownership, accessed Sept. 2023.

[374] https://employeeownershipwales.co.uk/, accessed Sept. 2023.

lected employees. Some forms of non-tax advantaged plans are quite widespread: Growth Share Plans, Long-Term Incentive Plans (LTIPs), Restricted Shares Plans and Unapproved (i.e., non-tax advantaged) Option Plans. Growth Share Plans, LTIPs and Restricted Shares Plans are predominantly confined to executives. Unapproved Option Plans may be used to "top-up" awards under a tax advantaged plan. The following section will cover only rules concerning tax advantaged plans.

The two years of 2012 and 2013 saw some crucial legislative reform in the field of ESO in the United Kingdom. A consultation on improving the operation of internal share markets was launched in 2012 following the publication of the Nuttall Review. This consultation resulted in "The Companies Act 2006 (Amendment of Part 18) Regulations 2013" that came into force on 30 April 2013. This legislation allows for shareholder approval of off-market share buy-backs by a simple majority, and where the share buy backs are connected to an employees' share scheme (a term defined in the United Kingdom Companies Act) allows for this approval to be granted in advance. Further, it gives private limited companies greater freedom to finance the share buy backs by allowing for such companies to pay for shares they buy back (in connection with an employees' share scheme) in instalments (if the seller agrees) and by introducing a simplified regime for buying back shares out of capital (in connection with an employees' share scheme) and involving small amounts of cash. In addition, the legislation allows all companies to hold shares bought back in treasury. The legislation retains the need for shareholder approval where necessary to protect the interests of shareholders and creditors. These provisions are deregulatory and voluntary and largely limited to buy backs linked to employees' share schemes (Nuttall 2013).

Further, the Government introduced a capital gains tax exemption and income tax exemption to promote employee ownership in the UK. Both these exemptions help simplify indirect employee ownership and, in particular, the capital gains tax exemption encourages its use as a solution to the growing challenge of finding a business succession in SMEs. The capital gains tax exemption is granted when a controlling interest in a company is transferred to an EOT. The capital gains tax exemption applies from 6 April 2014 (Finance Act 14 Sch 37 Pt 1) and is unlimited in amount. Instead of a trade sale or other forms of exit, owners may now opt for an EOT buy-out as their succession solution. There is also from 1 October 2014 (Finance Act 2014 Sch 37 Pt 2), an exemption from income tax (but not NICs) of GBP 3,600 per employee per tax year for certain bonus payments made to all employees of a company where an EOT has a controlling interest. This provides a cash alternative to operating a SIP. The EOT is a more restrictive form of the employee trust previously more commonly used in the United Kingdom (the so called "section 86 trust" because it meets the requirements in section 86 Inheritance Tax Act 1984). The differences between an EOT and a section 86 trust are acceptable in the context of a trust that is designed to acquire, and hold shares indefinitely on behalf of the employees. One additional restriction is that the EOT must not include a power for the trustee to make loans to beneficiaries. A key difference relates to who must benefit from any distribution from the EOT. A section 86 trust usually defines its beneficiaries by reference to employment with a particular body but can limit the class of beneficiaries to 'all or most' of the persons employed by the body concerned and only selected employees may, in fact, benefit. In contrast, in an EOT, essentially, every employee of the relevant company or group must be an eligible employee, except for certain excluded participators. A same terms requirement permits differing amounts to be paid to eligible employees, but every such employee must receive something if there is a distribution. The Government considered a change in English trust law to allow employee trusts to last forever instead of limiting their life to 125 years but deferred action on this idea.[375] Apart from this legislation several tax advantaged ESO plans operate in the United Kingdom to promote direct employee ownership:

Tax advantaged Share Plans – *Share Incentive Plan (SIP)* The SIP was introduced in the Finance Act 2000 to replace the 1978 Approved Profit Sharing Scheme on which it is partially modelled. Several possible modifications made it more flexible. The employer company sets up a trust to serve as an intermediary in allocating shares to employees. The shares may be allocated without cost ("free shares"), at a discount, or at full price ("partnership shares"); also, the employer may match the employee's partnership shares ("matching shares"). Dividends paid on all shares may be reinvested in additional shares ("dividend shares"). Each plan is subject to specific requirements which, if met, confer substantial tax advantages on both employees and the employer company. These generally take the form of exemption from both personal income tax and NICs. The plan must include all employees, with the possible exclusion of those employed less than 18 months, and the same general provisions must apply to all participants. Tax exemptions are valid for all versions of the plan after the shares have been held for five years, or earlier if the employee terminates his employment on account of injury, disability, redundancy, retirement or death; also, if transferred under the Transfer of Undertakings (Protection of Employment) Regulations, or on the employer company ceasing to be an associated company. Shares sold immediately after withdrawal are exempt from capital gains tax. Regulations specific to each type of award are as follows:

Free shares cannot be withdrawn from the trust during a holding period of three to five years. However, if the employee withdraws the shares or his or her employment ceases between the third and fifth year for reasons other than above, personal income tax and NICs are payable on the lesser of market value on the award date and the market value on the withdrawal/cessation date. If the employment ceases for other than the stated reasons before the end of the three- year holding period, full personal income tax and NICs are imposed. An employee's award of free shares in the plan is limited to GBP 3,600 per tax year (from the 2014/15 tax year).

Partnership shares are purchased by the trust from a part of the employee's pre-tax remuneration according to the employee's agreement with the employer company. The shares are purchased either within 30 days of pay deduction or at the end of a specified accumulation period of up to 12 months. An employee is limited to GBP 1,800 per tax year (or 10% of an employee's annual gross salary) (from the 2014/15 tax year). After the five-year holding period or termination of employment for the given reasons, the employee is exempted from personal income tax and NICs, and the employer exempt from NICs. If the employee withdraws the shares or his employment ends for a reason other than those stated between the third and fifth year, personal income tax and NICs are paid on the lesser of the amount of the employee contributions for purchase and the market value of shares on the date of withdrawal/cessation.

Matching shares can be offered by the employer company up to two matching shares for each partnership share. These are allocated to the employee on the same day as

[375] http://www.fieldfisher.com/publications/2014/06/the-employee-ownership-business-model.

partnership shares are acquired. The holding period is the same for matching shares as for free shares. Dividends per annum may be used to purchase *dividend shares*. The general holding period for dividend shares is three years. If these shares are withdrawn or employment ends for other than stated reasons within five years of their acquisition, the employee is liable for personal income tax on the dividends used to purchase the shares. However, there is no liability for NICs.

Tax advantaged Share Option Plans – *Savings-Related Share Option Scheme (SRSO) or Sharesave or SAYE Scheme*, was introduced by the Finance Act 1980. It must apply to all employees, except possibly those with relatively short service. The basic structure of the plan is as follows: the employee enters into a Save-as-you-earn (SAYE) contract with a designated bank or building society, agreeing to save a specified monthly amount (GBP 5 to GBP 500) by deduction from after-tax remuneration for three or five years (a seven-year contract was withdrawn in 2013) and the employer company grants him share options for the maximum number of shares he will be able to purchase at the exercise price with his SAYE savings. The SAYE contract could include a tax-free bonus added to savings on completion, the amount depending on the term of the contract and the rates are set by HM Treasury. However, the rates have been set at 0% since December 2014, an approach confirmed in June 2022.[376] The share exercise price can be up to 20% under the market value of the underlying shares at the time of the grant. At maturity of the SAYE contract, the employee is entitled to choose whether to exercise the option and retain or sell the shares or take the savings and any bonus in cash. These requirements fulfilled, the employee is not liable for personal income tax or NICs at grant or exercise. However, they must pay capital gains tax on the sale of shares.

Company Share Ownership Plan (CSOP) was introduced in 1984 as a Discretionary Share Option Plan and re-launched in 1996 under the current name with amended requirements. It is a discretionary plan which is often limited to executives but can also be broad-based. It is often connected to performance results, i.e., a certain goal must be reached before the option can be exercised. The following requirements also apply: the value[377] of outstanding options per employee must not exceed GBP 30,000 at grant; the exercise price may not be less than market value at grant; the exercise period may not be shorter than three nor longer than 10 years after grant.[378] These requirements fulfilled, the employee is not liable for personal income tax or NICs at grant or exercise. Proposed changes to CSOP rules will, in particular, increase the individual CSOP limit to GBP 60,000.[379]

Enterprise Management Incentives (EMI) was introduced by the Finance Act 2000 in order to help small, higher risk companies to recruit and retain highly qualified employees. It applies to companies with gross assets of less than GBP 30 million[380] and (from 21 July 2008) fewer than the equivalent of 250 full-time employees. The plan can be selective. Approval of HM Revenue & Customs is not required, but it must be

376 https://www.gov.uk/guidance/employment-related-securities-bulletin-43-june-2022.

377 The value is equal to the number of shares multiplied by the exercise price.

378 Before 2003, an additional requirement had to be fulfilled: the exercise period had to be not less than three years after any previous tax-free exercise. This requirement was abolished.

379 Finance (No. 2) Bill, 21 March 2023; Spring Budget 2023, HM Treasury, March 2023.

380 Originally, the volume of assets was GBP 15 million (until 2003), but it was considered necessary to increase it substantially.