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Non-Discretionary Tax Advantaged Share Schemes: Call for Evidence
HM Treasury
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25th August 2023

Dear Sirs

Non-Discretionary Tax Advantaged Share Schemes: Call for Evidence

ProShare has been campaigning for employee share plan reform for many years now and we welcome the opportunity to respond to this important call for evidence.

ProShare has been the voice of employee share ownership since 1992 when we were established by HM Government, a group of FTSE 100 companies, and the London Stock Exchange to promote wider share ownership. Today, we focus solely on helping to promote employee share ownership in the UK and ProShare is the voice of over 1,750 employee share plan practitioners and professionals, representing 150 advisers, providers and companies, including many of the UK's largest employers.

ProShare is a part of The Chartered Governance Institute UK & Ireland, the professional body for governance, with members in all sectors and a Royal Charter purpose to lead 'effective governance and efficient administration of commerce, industry and public affairs'. With more than 125 years' experience, we work with regulators and policy makers to champion high standards of governance and provide qualifications, training and guidance. The Institute is the professional body that qualifies Chartered Secretaries, which includes company secretaries and governance professionals of all kinds. Our members are, therefore, well placed to understand the importance of stakeholders in organisations and, within companies, of employee share ownership.

ProShare has been publishing an annual report on the state of the Save As You Earn (SAYE) and Share Incentive Plan (SIP) market in the UK for many years now. These are the UK's flagship all-employee share ownership plans and ProShare has been conducting this research, with the invaluable support of our share plan administrator members who provide the data. This data creates an unrivalled window on the Non-Discretionary Tax Advantaged Share Schemes market in the UK.

We noted the comment in the call for evidence (paragraph 1.4) that “Alongside this Call for Evidence, the government has published a final report detailing key findings from the recent evaluation of the SAYE, SIP and the Company Share Option Plan (CSOP). HMRC commissioned London Economics to conduct a quantitative, qualitative, and econometric analysis of CSOP, SAYE and SIP to provide a thorough and independent evaluation of the share schemes. This provides an initial basis from which to explore the effectiveness of SAYE and SIP”. Our members were struck by the differences between this report and our own, in particular the very small sample of share plan participants quoted and we would recommend that HMT consider all data sources when reviewing the responses to the call for evidence.

Additionally, there is some disquiet and confusion with sections of the data, particularly the suggestion that only 150 companies operated SAYE between 2015 and 2019. This seems to refer to new plans only and is at odds with both ProShare’s annual survey and HMRC’s own statistics which show (see table 8) there were 590 live SAYE schemes in 2015/2016.

The UK has a proud and long-standing tradition of fostering Employee Share Ownership (‘ESO’), with tax-advantaged share plans on the statute books since the late 1970s. Over the years, many millions of employees have benefitted from owning shares in the companies for which they work (more than two million employees participated in SAYE and/or SIP in 2022, according to the ‘ProShare SAYE & SIP Report 2022’ (available here), and their employers have benefitted from the correlated productivity boost that these plans in particular bring (see the HMRC & Oxera study on productivity & tax-advantaged share schemes).

Prof Andrew Pendleton and Andrew Robinson wrote an article specifically on SAYE and SIP, using the Workplace Employment Relations Survey. It is notable for finding that higher employee share plan participation rates affect productivity directly and positively, whereas lower participation rates seem to need other forms of engagement to be fully effective.

Finally, with regard to company performance, there is also a meta-analysis of all-employee share schemes around the world - 102 samples representing 56,984 firms - which finds employee share ownership has a positive 4% impact on productivity. Employee ownership is 'statistically significant in relation to firm performance'. Simplifying and improving these key employee share plans will provide a real boost to participation levels, bringing benefits to both employees, in the form of enhanced financial resilience, and employers via the associated productivity uplift.

Save As You Earn (‘SAYE’ or ‘Sharesave’), The Company Share Option Plan (‘CSOP’), the Share Incentive Plan (‘SIP’), and Enterprise Management Incentive plan (‘EMI’) – collectively, the UK’s tax-advantaged plans – all operate in different ways, with varied tax advantages for participating employees and employers, as set out in the relevant legislation. For detailed statistics on how SIP and SAYE are operated in practice, market and industry trends on take-up, and participation rates, please refer to the 'ProShare SAYE & SIP Report 2022' linked to above.

Whilst all these plans have, undoubtedly, helped employees and employers considerably over the years of their operation, some of their design features are very much the product of their respective times. But times change, and so do workforces, workplaces, and the nature of work itself, rendering some of these features irrelevant or even counter-productive. We are increasingly seeing societal change too – changes in worker demographic, in worker attitudes, and in the relationship between employees and employers, for example, the current move from a shareholder to a stakeholder focus in which workers are seen as key stakeholders.
The days of working for one or perhaps two employers for the entire length of one's career are far behind us. The average UK employee's tenure per employer is currently 5 years [according to life insurance firm LV]. In the US, average tenure across the entire workforce is 4.1 years, whereas for those aged 25 to 34, the average is just 2.8 years [source: BBC].

Equivalent UK-only statistics specifically concerning employment tenure are hard to source, however ProShare's research study 'Attitudes to Employee Share Ownership' released in January 2018 found that, far from encouraging retention, the five-year holding period for SIP shares actively discourages eligible employees from participating in the plans. 24% of non-participants surveyed said that they didn't join their employer's SIP because the five-year holding period was too long.

All-employee share plans undoubtedly have some benefit as recruitment and retention tools, but they are viewed today primarily as part of companies' wider benefits packages. In many cases, investment amounts are not sufficiently large for employee share plans to be seen as directly supporting retention – rather their purpose is to align the workforce with shareholder interests, ensuring employees feel they are participating in the company. Consequently, the current leaver rules should be simplified and companies given the flexibility to set their own. Employees are more and more mobile now than they were at the establishment of these share plans. On the basis that share plans are not the retention / recruitment tools they used to be, but that they form a key element of an organisation's employee benefit package, there should not be 'good' and 'bad' leavers, and the plans' benefits should kick in earlier – without a commitment to three or five years.

Tax-advantaged share plans do still work well, but they could work much better; this response sets out some ways in which we, and our members, believe this may be achieved, offering both 'big-picture' proposals and some technical changes to the operation of current plans which will make them more efficient and effective.

Our response to this call for evidence is, therefore, set out in the following sections:

1 Our key policy recommendations for employee share plans

2 Our 'big-picture' proposals for an overhaul of Non-Discretionary Tax Advantaged Share Schemes

3 Our list of minor technical changes to the operation of current plans which we believe will make them more efficient and effective

4 Our detailed responses to the questions in your call for evidence.

ProShare and members of the share plans industry all remain eager to work with policy makers, decision makers, and those with profile and influence in Westminster. We are always keen to help with further assessment, research, evidence-gathering, and analysis of the impact of employee share ownership. In particular, we would be keen to help quantify the economic benefits and cost savings for businesses against any estimated potential cost to the Exchequer linked to the adoption of any of these proposals.

Please do not hesitate to contact us for more details or further discussion.

Yours faithfully,

Murray Tompsett
Head of ProShare

1 ProShare's key policy recommendations for employee share plans

1	Reduce the Share Incentive Plan holding period from 5 years to 2 years (see page 14)
2	Re-classify resignation a 'good' leaver reason for SAYE & SIP (see pages 10 and 15)
3	The establishment of a **Cost-of-Living Share Plan** – a brand new one-year free share offer, modelled on the SIP (see page 7)
4	Introduce an optional 'lookback' feature for SAYE option exercise prices (see page 9)
5	Optional company SAYE contribution on behalf of employees (see page 12)
6	Develop a 'whole-workforce' approach to share plans (see page 6)
7	Review the correction of administrative errors within Non-Discretionary Tax Advantaged Employee Share Plans (see pages 17 and 18)
8	Simplify and make the SIP dividend share tax treatment fair (see page 15)
9	Make SAYE more attractive by allowing companies to increase the option price discount (see page 10)
10	Encourage companies to report on the operation of ESO plans (see page 17)
11	Develop the arrangements for SAYE so that it would attract more favourable accounting treatment under the Accounting for Share-based Payments rules (see pages 11 and 12)
12	Exempt some gains from Non-Discretionary Tax Advantaged Share Schemes from the CGT regime (see page 10)
13	Abolish the 10% of salary limit on employees' SIP contributions (see page 16)
14	Develop a government portal with standard documents for a company to download, and a related app for employee participation, and appointing staff to help companies understand SIP and SAYE (see page 18)
15	Encourage government to develop the institutional support needed to widen rates of employee share ownership (see page 35)

2 ProShare's 'big-picture' proposals for an overhaul of Non-Discretionary Tax Advantaged Share Schemes

Our central premise is that, whilst the composition of UK workforces has changed radically over the past forty years, most of the related employment benefits have not. We believe that the time is right for a comprehensive review of the legislation underpinning employee share schemes. We do not underestimate the potential complexity of such a review, as it will involve amendments to fundamental pieces of legislation such as the Companies Act 2006 (the Act), but the opportunity to make such changes is available to the Government if it truly wishes to embrace modern employee share ownership.

By way of example, our suggestions that we believe would be beneficial to the development of a more modern employee share ownership landscape in the UK are:

- Facilitating a 'whole-workforce' approach
- Introducing a Cost-of-Living Share Plan
- Reduce the Share Incentive Plan holding period from 5 years to 2 years. Reducing the SIP holding period enjoys near unanimous support across our membership and has been a longstanding ask of the industry. We provide more detailed information about this in the next section.

- **Facilitating a 'whole-workforce' approach**

Entitlement to an array of workplace benefits depends largely on one's employment status. Are you an employee? A worker? Are you on a fixed-term contract? Do you work in the 'gig' economy? Are you on a zero-hours contract? Are you self-employed? This maze of different statuses affects what companies are permitted to offer to each subset within their workforce.

The inconsistencies and complexities that bedevil these varied statuses have already been covered at length in The Taylor Review, so we will not reiterate them here. In addition, the recent IR35 legislation was intended to tackle deliberately inappropriate treatment on the border between employees and contractors, and reduce tax 'leakage'.

The central point is that a significant proportion of the UK workforce is in informal contracts, working on zero-hours or in the 'gig economy', or employed through third parties; many of these individuals are paid on a weekly basis. Some companies would like the flexibility to treat these workers as part of their workforce and include them within share plans.

What we seek to focus on here is the inability of companies to offer share schemes to certain growing sections of their workforce, because individuals in these subsets do not fit neatly into the definition of 'employee' as set out in the relevant share schemes legislation. Many of the large employers that ProShare is proud to call members would like to have the choice of whether to offer share plans more broadly within their workforce as they recognise the motivational and productivity boosting effects these plans bring. But the law, as it currently stands, prevents them from doing so.

To turn this aspiration into legal reality would require analysis and re-working of the employee share schemes exemptions from shareholder pre-emption rights within the Act, followed by analysis of the changes required within the relevant schedules of the Income Tax (Earnings and Pensions) Act 2003. We strongly believe that the financial, productivity and wellbeing benefits of offering share plans more broadly within companies' workforces would be considerable, for the employer, for the workforce and for the UK economy as a whole.

- **Cost-of-Living Share Plan**

A new Employee Share Plan (a so-called Cost-of-Living Share Plan or Exceptional Bonus Share Award) should be created, designed specifically for employees on lower incomes.

Given the cost-of-living crisis and the potential for a free share offer to provide financial relief to employees, we would encourage the Government to establish a short-term scheme, ideally with a 12-month minimum holding period required to receive full tax relief (currently this period for a SIP is 5 years). The format of the plan would be similar to the Free Share element of the SIP, with important differences to allow companies to target lower paid employees, particularly relevant at a time when the UK is experiencing a sharp increase in the cost-of-living.

Just under 50% of companies with SIPs already offer free shares to employees. But under current rules, Free shares must be awarded to all employees on similar terms: employees must either all receive the same number of shares, or the allocation can be by reference to objective criteria such as remuneration, e.g. if a percentage of earnings is awarded as a value of shares, that percentage must apply to all participants. None of the factors can be applied in a way which produces a "nil award" (no shares) for any qualifying employee.

We envisage the Cost-of-Living scheme would only be available to those workers whose earnings are below a pre-agreed income threshold. Higher earning workers would not be eligible to participate. Under a SIP, up to £3,600 of Free shares can be issued per employee per annum. We propose keeping this total annual Free share threshold (on average, in those companies where Free share offers are made, they are much lower than this). Alternatively, there could be a separate annual Free share threshold for this new category of Free shares. This would help reduce complexity with no requirement to calculate overall thresholds across two types of awards. Scope should be included for the administration of the 'new' category of free shares to be dealt with separately to the current SIP, e.g. having a separate plan just for the new category of Free shares. Having two categories of Free shares with different tax-free periods within one plan would be administratively complex.

Given that companies already have the choice to issue free shares to all employees, it is envisaged that this change would not have a net cost to the Treasury. Rather, firms are likely instead to choose to use this more flexible scheme to focus support on employees on lower incomes, rather than increasing the overall value of the Free share issue. This reflects investors' current expectations of companies renumeration practices, namely, to focus on lower paid employees over salary increases to higher paid executives.

3 ProShare's list of minor technical changes to the operation of current plans which we believe will make them more efficient and effective

There are a number of relatively minor technical changes which the Government could choose to implement. For clarity and ease of review, we will review each tax-advantaged plan in turn, putting forward proposals to mitigate or resolve known issues with their operation, and citing the relevant supporting evidence.

Save As You Earn (SAYE)

- Introduce a 'lookback' feature for SAYE share option exercise prices.
- Re-classify resignation as a 'good' leaver reason.
- Exempt some gains from Non-Discretionary Tax Advantaged Share Schemes from the CGT regime.
- Develop the arrangements for SAYE so that it would attract more favourable accounting treatment under the Accounting for Share-based Payments rules.
- Optional company SAYE contribution on behalf of employees

SAYE is essentially a savings scheme, facilitated through company payroll, with an option to use those savings to buy shares at a discounted option price. The fact that savings are made by direct post-tax deductions from employees' pay via payroll makes saving more achievable. A recent piece of research by YBS Share Plans, the University of Durham and the University of Leeds, Financial behaviour and decision making, found that, amongst employees they surveyed, 28% had no other means of saving and 40% said that, without their employer's SAYE scheme, they would otherwise spend the money as opposed to saving it.

Based on monthly payroll deductions, SAYE makes it easy for employees to save, improving their financial and mental wellbeing and in turn correlating strongly with improved focus and productivity at work. Employee share ownership is achieved if the participant saves for their agreed 3 or 5-year term and then opts to use those savings to buy shares at the option price. Participants who choose to exercise their option have no further income tax or NICs to pay on the exercise, but may have a CGT liability on any gain. ProShare's latest SAYE & SIP Report found that 51% of SAYE participants chose to keep their SAYE shares at maturity, though they had the opportunity to sell them.

SAYE has stood the test of time and continues to benefit 1.3 million UK employees [source: ProShare SAYE & SIP Report]. Whilst the recent re-introduction of SAYE Bonus Rates has been well received, it should be noted that during periods of declining share prices, employees become less engaged, and when participants opt to leave the SAYE, the accounting treatment is harsh

Be that as it may, SAYE remains a brilliantly easy way for employees to save (many of whom wouldn't save at all otherwise). It is also a very 'safe' plan from a risk-profile viewpoint. Savings are held by a licensed savings carrier, accessible to participants at any time, and covered by the Financial Services Compensation Scheme (FSCS). Capital is only at risk from the point that the participant decides to use their savings to buy the shares under option (and even then, this is cushioned by the option price discount of up to 20% which around 80% of companies utilise). Both of these factors are incredibly important in the current and foreseeable environment. However our members have asked that any participant's money saved in SAYE savings accounts be protected under FSCS, in addition to any other monies protected by FSCS and held in the same institution. Where an individual already has £85,000 protected with that institution, SAYE FSCS protection would be over and above this amount.

So – how to make SAYE work more efficiently regardless of prevailing market conditions? Our members have put forward a number of suggestions, bullet-pointed at the start of this section. We'll take of these in turn, starting with the introduction of an optional 'lookback' feature for SAYE share option exercise prices.

- **Introduce a 'lookback' feature for SAYE share option exercise prices**

Currently, if a company's share price has not performed well, and the option price, which is set at the start of a 3 or 5 year saving term, is higher than the market price at the end of that term (the maturity date), the only rational course of action for participants is to accept the repayment of their savings and allow the option to lapse six months from the maturity date. Giving companies the choice to have a 'lookback' feature would involve the option price being reset to the market price at the maturity date, if the option price as calculated at the grant date was 'underwater' (i.e. higher than the current share price), with the relevant option price discount being applied to calculate the new, reset, option price. The number of shares under option (and granted) would remain fixed and would not be recalculated due to an option price reset. Any savings not used to buy the fixed number of shares would be repaid, meaning a larger 'residue' cash repayment would be made at maturity.

This would mean that companies avoid the situation where SAYE is simply a savings scheme, which has a de-motivating effect on participating employees and is burdensome to the P&L in terms of the associated accounting treatment.

It would ensure that employees were able to exercise their options and acquire shares, regardless of the company's share price performance, thereby enabling the scheme to deliver on its overriding objective of employee share ownership. It would also ensure that companies could avoid the P&L impact of the arbitrary and punitive nature of IFRS2 share-based payments accounting treatment of lapsed options in this circumstance.

- **Make SAYE more attractive by allowing companies to increase the option price discount**

As illustrated in the annual ProShare SAYE and SIP Survey Report, around 80% of companies offer the maximum 20% discount to the option price for SAYE participants. Many of our members feel that by increasing the maximum discount permitted, employees would find the offer of an SAYE more attractive and would be more likely to participate as they are more likely to realise a gain on their savings.

We hear again and again from our members that their share plan participants are amongst the most engaged, productive, high performing, financially resilient, and content employees. So whilst all-employee share plans might not be the recruitment and retention tools they once were, a more engaged and content workforce, and one with fewer financial worries, helps reduce employment 'churn', thus aiding retention.

One other example quoted to us where more flexibility would be helpful is to allow SAYE share plan contributions from employees' pre-tax salaries to make plans more attractive – although this would have implications for National Insurance contributions.

- **Re-classify resignation as a 'good' leaver reason.**

Re-classifying resignation as a 'good' leaver reason would help employers who take the more progressive and pragmatic view that employees usually have more than one reason for moving on to a different employer. In the experience of employer members, it is rare that a pending SAYE maturity will override all other reasons driving an employee to resign. Employees' reasons for resigning are many and varied – a new role with a new employer may present the opportunity of a pay-rise, new challenges, career progression, relocation, and other more appealing or relevant workplace benefits such as flexible working patterns. Currently, at least as far as their SAYE plans are concerned, an employee who resigns from their employer is treated in the same way as one who is dismissed for gross misconduct – this is unfair and does not promote an agile national workforce.

- **Introduce an employee share plan threshold, exempting some gains from Non-Discretionary Tax Advantaged Share Schemes from the CGT regime**

If there is a Capital Gains Tax (CGT) charge on the sale of shares received through an SAYE plan, the gain is based on the acquisition cost of the shares, i.e., the Option Price (applicable if there is no Income Tax charge on the exercise of a SAYE option).

The CGT tax-free annual allowance is reducing to £3,000 from 6 April 2024, meaning that many more employees will need to understand and comply with the CGT consequences of exercising and then selling their SAYE shares. Many, if not most, participants will not have had to report a capital gain via self-assessment, nor indeed via the 'real time reporting' method, and this reduction in the annual allowance creates a significant non-compliance risk for SAYE participants through lack of understanding (regardless of all efforts from employers). It also serves to put employees off participating in future, and may well have an impact on HMRC resources following up on minor underpayments of CGT.

Our members believe that, in order to maximise take-up of SAYE plans, an annual exemption from the CGT regime for gains of up to £10,000 from Non-Discretionary Tax Advantaged Share Schemes should be introduced. After all, SAYE is a **tax-advantaged** share plan but much of the advantage is lost with recent and incoming CGT changes.

If this is not acceptable to HMT, then an alternative might be to amend the CGT treatment for shares received through an SAYE plan so that the acquisition cost of the shares is based on the higher of the market value of the shares on the date of exercise or the Option Price. Employees transferring their SAYE shares to an Individual Savings Account (ISA) within 90 days of exercise do not have to pay CGT when they sell those shares. This proposal would mean that employees wishing to sell shares immediately would receive similar tax benefits without the need to open an ISA. The transfer of SAYE shares to an ISA would continue to have value where employees wish to keep their shares with future gains sheltered from CGT. However, this would not be available to employees acquiring shares in a private company.

- **Develop the arrangements for SAYE so that it would attract more favourable accounting treatment under the Accounting for Share-based Payments rules**

A key issue that is regularly raised across our membership is the way SAYE is treated for accounting purposes. Since 2009, amendments to accounting standards, under International Financial Reporting Standards 2 (IFRS 2), have seen harsh accounting treatment of SAYE option plans.

In 2021, ProShare commissioned a major report from the Social Market Foundation (SMF) looking at ways to improve and widen the use of employee share schemes. "*A stake in success: Re-imagining employee share plans for the 2020s*[1]", from which the next two paragraphs are taken.

"Under IFRS 2, companies have to estimate the value of SAYE options on grant and spread the cost over the period until they vest. However, employee participants may stop making their monthly contributions for a variety of reasons, resulting in the SAYE options lapsing.

"Although logic might suggest that, if an employee stops saving under an SAYE savings contract, say two years into a five year option, with the result that the connected share option lapses, the company should be able to write back two-fifths of the estimated costs that it has taken against profits. However, under IFRS2, the company

[1] https://www.smf.co.uk/wp-content/uploads/2021/05/A-stake-in-success-May-21.pdf

cannot reclaim the two-fifths and has to expense the other three-fifths of the costs immediately, even though no shares will ever be issued [and no benefit has been received by the employee]. The UK Accounting Standards Board declared that this accounting treatment was **"harsh, if not penal"** in relation to savings related share option plans, although these objections were not reflected in the final position of the International Accounting Standards Board."

There are circumstances in which a share-based payment can be granted as a replacement for another share-based payment that is cancelled, and principles of modification accounting are applied. Our members believe that the SAYE rules should be amended as necessary so that SAYE is exempt from this IFRS2 requirement.

Whilst we accept that this may be outside the scope of this Call for Evidence and, indeed, beyond the gift of HM Treasury, our members believe that the Government should set up a review to investigate the impact of IFRS 2 on SAYE with guidance issued on how to manage accounting for cancelled SAYE contracts, considering how the principles of modification accounting can be practically applied. This could be taken in conjunction with our proposal above for the introduction of a 'lookback' feature for SAYE share option exercise prices.

Feedback that we have received is that the accounting treatment of SAYE is a major disincentive to companies considering offering these plans.

- **Optional company SAYE contributions on behalf of employees**

Currently, eligible employees are invited to join the company SAYE - typically on an annual basis - and can decide whether or not to join, and the amount that they wish to save each month.

As an optional feature companies could help employees with their SAYE savings by making a 'Company Contribution' towards employees' overall monthly savings. For example, using an amount of £10 per month, the company would pay each employee a gross amount that, after tax and NIC deductions, would mean they would receive a net amount of £10 per month. £10 would then be deducted from employees each month to be used as SAYE contributions. Employees would still be able to contribute a maximum of £500 per month across all SAYE plans, but anything over the £10 per month would be deducted from salary as per the current process.

This initiative gives all employees the opportunity to participate in SAYE and to benefit from any rise in the share price during the savings term, regardless of their level of salary.
More employees would be encouraged to save, and overall SAYE take-up would increase, encouraging employees to save and improve their financial security and resilience. This would be particularly helpful for lower income

workers who currently find they do not have enough money left over each month to participate in their company's employee share plans.

There would be no requirement for companies to make a Company Contribution; it would be the company's choice. There is also some support for companies to run this as an auto-enrolment process. Pension auto-enrolment has been successful. Combining a Company Contribution with auto enrolment would maximise participation, but employees would be able to opt out should they not wish to participate on religious or other grounds.

Share Incentive Plan (SIP)

- **Reduce the 5 year holding period to 2 years**
- **Simplify and make the SIP dividend share tax treatment fair**
- **Re-classify resignation as a 'good' leaver reason**
- **Abolish the 10% salary limit on employees' SIP contributions**

SIP encourages employee share ownership from the outset of an employee joining the plan, through four different share elements which companies may choose to offer:

1. Free Shares
2. Partnership Shares
3. Matching Shares
4. Dividend Shares.

These shares, once awarded (Free, Matching) or purchased (Partnership, Dividend), are required to be held in a SIP Trust on behalf of participating employees, for at least three years (Dividend) or five years (Free, Partnership, Matching) before they may be sold without attracting an income tax charge or NICs for the employee (and usually the employer too, in the form of ERs NICs).

ProShare's research study '*Attitudes To Employee Share Ownership*[2]' released in 2018 found that, far from encouraging retention, the five-year holding period for SIP shares actively discourages eligible employees from participating in the plans. 24% of non-participants surveyed said that they didn't join their employer's SIP because the five-year holding period was too long.

The differing tax treatments for Free, Partnership and Matching shares up to 3 years, and between 3 and 5 years (as set out below), are confusing and hard for most eligible employees to understand. This makes the plan challenging for employers to communicate effectively to their workforces, and in turn lessens take-up rates and undermines the plan's primary intention to create and foster broad-based employee share ownership.

[2] https://www.proshare.org/assets/files/research/proshare-attitudes-to-employee-share-ownership.pdf

ProShare strongly recommends the removal of the 5-year holding period, and proposes the introduction of a 2 year holding period for all SIP shares. This single holding period is more attractive to potential participants, and, crucially, is simpler to understand, communicate and administer. This is an extension of a consistent and long-term request from industry, supported by the CBI, share plan issuers, and the SMF who all favour a reduction to the holding period.

Firms operating SIPs are agreed that reducing the holding period would increase employee participation without impacting on productivity. A ProShare survey found that 93% of companies offering a SIP believe the 5-year period is too long, and 35% of companies that don't currently offer a SIP, but do offer another form of employee share plan, would offer a SIP if the holding period was reduced.

SIP shares income tax & NIC treatment

	Years 0–3	**Years 3–5**	**Years 5+**
	Full tax	*'Lower of' tax*	*No tax*
Free shares	Value at date shares withdrawn from SIP	Lower of value at award and at date shares withdrawn	No tax
Partnership shares	Value at date shares withdrawn from SIP	Lower of deductions used to purchase and value when shares withdrawn	No tax
Matching shares	Value at date shares withdrawn from SIP	Lower of value at award and at date shares withdrawn	No tax
Dividend shares	Tax on dividend received	No tax	No tax

- **Simplify and make the SIP dividend share tax treatment fair**

The tax treatment for dividend shares exiting the SIP is anomalous and unfair, especially in its interaction with the recent reduction of the annual dividend tax allowance from £5,000 to £2,000, which decreased to £1,000 from 6 April 2023 and is due to decrease further to £500 from 6 April 2024. It penalises individuals who have, in good faith, saved and invested through their employer's SIP, many of whom would not normally ever have to complete a self-assessment tax return. SIP participants who withdraw their shares from their plan (as anything other than a 'good' leaver) currently suffer tax on up to three years' worth of their dividend shares, the cumulative value of which may only be set against that single tax year's dividend tax allowance and must be reported via self-assessment tax return.

A fairer way of taxing dividend shares when they are withdrawn from the SIP in taxable circumstances i.e. where a participant leaves their employer as a 'bad' leaver, would be to allow their cumulative value to be set against the value of the taxpayer's dividend tax allowance for the three preceding tax years. These are shares which have been acquired solely as a result of the employee's participation in their employer's tax-advantaged SIP, after all, and will have been awarded in proportion to their other SIP shares (be they Free, Partnership or Matching shares, and pre-existing Dividend shares).

- **Re-classify resignation as a 'good' leaver reason**

Re-classifying resignation as a 'good' leaver reason would help employers who take the more progressive and pragmatic view that employees usually have more than one reason for moving on to a different employer. In the experience of employer members, it is rare that a pending SIP share 'maturity' date will override all other reasons driving an employee to resign. Employees' reasons for resigning are many and varied – a new role with a new employer may present the opportunity of a pay-rise, new challenges, career progression, relocation, and other more appealing or relevant workplace benefits such as flexible working patterns. Currently, at least as far as their SIP shares are concerned, an employee who resigns from their employer is treated in the same way as one who is dismissed for gross misconduct – as with SAYE leaver treatment, this cannot be considered fair or just. It may also be better to do away with pejorative wording altogether - *good / bad* to become *standard / non-standard*.

- **Abolish the 10% salary limit on employees' SIP contributions**

The amount of Partnership Share money deducted from an employee's salary must not exceed £1,800 in any tax year or 10% of the employee's salary for the tax year. Where an employee leaves the company, and his or her deductions are more than 10% of salary from the start of the tax year to the date of leaving, the excess deduction (over and above the 10% salary limit) must be returned to the employee through the payroll (and must therefore be subjected to PAYE and NICs).

Our members believe that the removal of the 10% cap would simplify the plan, allow lower paid employees to decide for themselves how much they could afford, and create more flexibility around using lump sum Partnership contributions. The number of individuals affected by this each year is small, but each one is significantly time-consuming. With the advent of the National Minimum Wage legislation, this restriction became obsolete and should be removed.

Cross-plan proposals

- Encourage companies to report on the operation of ESO plans.
- Review the Correction of Administrative Errors within Non-Discretionary Tax Advantaged Employee Share Plans.

- **Encouraging companies to report on the operation of ESO plans**

The Financial Reporting Council should encourage firms to include information in annual reports, or alternatively, on company websites, covering what type of employee share plans are operated, the extent to which each plan is taken up by eligible UK-based workers, and the average value of an employee's plan-based shareholding. This information should be reported regularly and in standardised form, for the use of investors pursuing an ESG agenda. In this ESG context, reporting authorities should regard companies' adoption and uptake of ESO as a key measure of engagement with their workforce. A good parallel here is gender pay gap reporting requirements which have prompted firms to take steps to reduce gender pay disparities.

- **Review the Correction of Administrative Errors within Non-Discretionary Tax Advantaged Employee Share Plans**

Many of our members at both plan issuing companies and plan administrators have raised concerns about the disparity of treatment between plan participants and customers of every other financial services product. It is felt that the approval rules need to include guidance or a framework so that administrative errors, which are not the fault of the underlying participant, can be corrected in a way where the individual is restored to the position they would have been in had the error not been made.

Currently, these types of error are not always being corrected due to fear that by doing so, the approved status of the entire scheme could be withdrawn. Where plan issuers are seeking external legal advice, this stance is being reinforced as the HMRC shows no forbearance within approval rules for the correction of errors.

This would seem to make the share plans environment an outlier when compared to all other financial services products, and recent Consumer Duty regulation shines a light on this. If we compare the treatment of administration errors with pension, savings plan, or unitized long term savings products (where fair treatment of the customer would be to restore the individual to their entitled position), treatment of administration errors within tax-advantaged employee share plans appears to be in conflict with TCF principles and Consumer Duty regulations.

This point can be illustrated using frequent examples of error.

Example 1: A good leaver is mistakenly processed as a bad leaver and their share options lapse as a result. The recourse open to the participant is a lengthy complaints process, and possibly a FOS referral, as opposed to a reconstitution of records to correct the error. The error could have been created in payroll, in data transfer, or by the plan administrator.

Example 2: A participant contribution, or multiple contributions, missed due to payroll error, or incorrect information being held, results in a delayed maturity date for the participant. This could lead to an inability to enrol in a subsequent plan, and possibly even to the lapse of the participant's share options. Where this is not the fault of the individual, instead of reconstituting records from retrospectively applied funds, the participant is forced into a complaints process or into accepting a loss. This is clearly a poor outcome for participants and will impact low earners especially as they may have planned and budgeted their finances around their employee share plan.

SAYE – if in the time passed since the error is identified the exercise period has started (or even finished), there is no way to extend the exercise period to correct the issue, thus leavers are disadvantaged.
SIP – where a good leaver is processed as a bad leaver, shares may have been sold to cover tax, and subsequently reported. Unravelling this type of transaction is incredibly complex and time consuming and ultimately a disincentive for companies to operate these share plans. If the leaver rules resulted in the same outcome for all leavers other than cases of dismissal, corrections would not be necessary and participants and leavers would not be disadvantaged.

- **Increase government support to include developing a government portal with revised standard downloadable company documents, and an app for employee participation, and appoint staff to advise companies on the availability of SAYE and SIP, and the opportunities they bring**.

One significant area of cost reported to us, particularly by private companies, is that of plan set up. In the same way that there is a 'model' set of Articles of Association provided by the government, a government portal with standard documents for a company to download – similar to the Etassum39000 and Etassum28000 manuals – and a related app through which straightforward plans can be managed and participants can interact, would be highly beneficial. It is felt that this may encourage companies to offer share plans, especially smaller private companies, whilst also enabling employees to participate and interact with the plan.

We would also like to see the appointment of people to work for the Department for Business and Trade (DBT), educating and promoting the opportunities of employee share ownership locally, including engaging with local professional firms. The Welsh Government has done this to promote Employee Ownership Trusts and employee share plans with success.

4 ProShare's detailed responses to the questions in your call for evidence.

Please note that Qs 1, 2, 3, 4, 5 and 7 of the consultation are answered online.

Respondent's profile:

6. If you are responding on behalf of a representative body or think tank, please briefly describe the body, its objectives, and its members.

ProShare has been the voice of employee share ownership since 1992 when we were established by HM Government, a group of FTSE 100 companies and the London Stock Exchange to promote wider share ownership. Today, we focus solely on helping to promote employee share ownership in the UK and ProShare is the voice of over 1,750 employee share plan practitioners and professionals, representing 150 companies and providers.

ProShare is a part of The Chartered Governance Institute UK & Ireland, the professional body for governance, with members in all sectors and a Royal Charter purpose to lead 'effective governance and efficient administration of commerce, industry and public affairs'. With more than 125 years' experience, we work with regulators and policy makers to champion high standards of governance and provide qualifications, training and guidance. The Institute is the professional body that qualifies Chartered Secretaries, which includes company secretaries and governance professionals of all kinds. Our members are, therefore, well placed to understand the importance of stakeholders in organisations and, within companies, of employee share ownership.

In preparing this submission, we have consulted with, amongst others, our members, representing companies and share scheme providers across the market. However, the views expressed in this response are not necessarily those of any individual members, nor of the companies they represent.

Effectiveness and suitability of SAYE and SIP

8. To what extent do you agree/disagree that SAYE and SIP are fulfilling their policy objectives?

As the call for evidence indicates, "Tax-advantaged share schemes aim to:

- ***Align employee and shareholder interests:*** with the ability to benefit directly from company growth and with generous tax treatment alongside, the employee is encouraged to take a proactive part in increasing the employer's value.
- ***Support recruitment and retention efforts:*** the schemes help businesses attract and retain high-productivity workers. The tax advantages are an incentive to stay with the employer and help it grow so they benefit from the maximum reward available.
- ***Encourage financial planning:*** the schemes promote savings and investing habits amongst employees, enabling investment opportunities which may not have otherwise existed."

We believe that SAYE and SIP are, generally, meeting these policy objectives. Specifically:

- ***Align employee and shareholder interests:*** with the ability to benefit directly from company growth and with generous tax treatment alongside, the employee is encouraged to take a proactive part in increasing the employer's value.
- ***Encourage financial planning:*** employees participating in ESO plans are significantly better off compared to non-participants in the same income bracket. The Social Market Foundation has calculated this 'employee share ownership premium' and found that for those in the lowest income quartile (the 25% poorest households), the median net financial wealth of employee shareholder households is an average of £10,900 higher than non-shareholder households. Increasing employees' financial independence and resilience, and promoting saving, as these plans do, helps people to avoid debt and save for retirement, thereby decreasing reliance on the state. More generally, in their latest report 'Deadline to the Breadline', Legal & General note that financial resilience has shrunk by 21% since 2020, and the report found that the average UK employee could last just 19 days financially if they lost their main source of income. The case for building financial resilience via employee share plans has never been higher.
- ***Support recruitment and retention efforts:*** giving workers a stake in their employer enhances their commitment and motivation. It aligns the interests of employees with those of shareholders. The MacLeod Review said it was a 'profound and distinctive enabler of high engagement'. However, there is a concern that, although valued by employees, plans are not driving recruitment and retention, especially because of the 5-year holding requirements. This is particularly pertinent at present when, with the cost-of-living crisis, employees do not want to have money tied up for such a long time. While SAYE has a positive correlation with productivity, the majority of our plan issuer members see SIP and SAYE as an employee benefit not a retention tool.

There is a further benefit to employee share plans which we do not believe is given enough weight as a policy objective, and that is improving productivity. An *Oxera* study for HMRC found that: 'the effect of tax-advantaged share schemes is significant and increases productivity by 2.5% in the long run'... [and] 'there is a **4.1%** long-run improvement in performance for companies using SAYE schemes.'

9. If you offer SAYE or SIP to your employees, why did you choose to do so? If you are responding as a representative body, please specify your members' main reasons for offering SAYE or SIP to their employees.

Our members tell us that they offer SIP and SAYE to their members for all the above reasons, particularly helping employees to develop savings habits and encourage financial planning. Both SIP and SAYE create and drive a culture of financial savings by setting aside part of an employee's salary each month. Households that engage with employee share plans are more financially resilient. However, a concentration of savings in one company's shares may have a negative impact if share prices plunge. Some of our members noted that, whilst share ownership is almost instant with a SIP, both plans encourage financial planning.

Most issuers no longer see share plans as a retention tool. In the modern employment world, where an increasing number of companies offer share plans, they are rarely a point of differentiation between an employee leaving or staying. In circumstances where they might be, companies are often prepared to 'compensate' a prospective employee for any plan-related benefit that they might forego by leaving their current employer.

10. If you have chosen to offer only SIP or SAYE, what were the deciding factors of choosing one over the other? What do you see as the advantages of one over the other?

Some companies back SIP, others SAYE and many both – it depends on the economic position of the company.

The advantages of SAYE plans include:

- SAYE plans pose fewer barriers to entry and are generally favoured by potential participants over SIP.
- Employees can save from as little as £5 per month meaning even the lowest paid can participate.
- SAYE comms are typically issued annually which ensures new staff are engaged and can take advantage of the company scheme.
- SAYE plans are risk free and are more easily explainable to employees.
- SAYE encourages participants to save money from their salary each month which builds financial resilience.
- SAYE participants who retain shares at maturity also benefit from any dividends the company issues.

Conversely, SAYE plans are disadvantaged by recent tax changes, in particular to CGT, which will bring a significant number of employees into a tax net that they have previously escaped.

The advantages of SIPs include:

- SIP is a complex but, consequently, flexible model.
- SIP allows employees to build a stake in the company for which they work.
- Employees can save from as little as £5 per month meaning even the lowest paid can participate.
- Some employees see SIP as a long-term investment opportunity which can increase their tenure.
- Employees can typically start their participation in a SIP from the moment they join a company, and as most plans purchase shares on a monthly basis, they become shareholders very quickly after joining.
- A SIP allows companies to issue Free shares to their employees, thus aligning the entire workforce with shareholders.
- SIP participants also benefit from any dividends the company issues.

Conversely, however, the complexity and time commitment of SIPs can be a barrier to entry and, unlike SAYE, the element of committing your own money means that employees are exposed to potential loss. Furthermore, the complexity around the tax rules makes SIP appear less beneficial and it is significantly harder to convey the benefits of the plan to the workforce.

Our members believe that there should be a reduction in SIP holding periods from 5 to 2 years and the tax requirements should be simplified.

Finally, an issue common to both plans is that:

- Lower earners have a higher turn-over rate of employment, so the plans are too long term even for those employees who *can* afford to participate.

One ProShare member, a global employer in the Financial Services sector with 35,000 employees in the UK, has an average tenure of 13 years for mid-level grades, but just 4.5 years for the lowest grade. With the tenure so much shorter for this category of employee, the current 5 year SIP holding period makes the plan far less relevant and attractive to the majority of them.

Company and employee participation

11. The number of companies using SAYE and SIP has not increased in recent years. In your view, what barriers exist that may impact a company's decision to offer an employee share scheme? These could be barriers related to specific schemes or wider concerns.

Our members suggested to us a number of barriers to companies deciding to offer an employee share scheme. These include the following:

- Companies are not all aware of the different plans, their benefits and tax saving opportunities and, in particular, of the advantage (beyond the tax benefits) of employees having shares in the business. The London Stock Exchange used to maintain an index which showed that companies which had a certain percentage of employee participating in employee share ownership schemes outperformed companies that did not. https://www.equityprojectuk.com/uk-employee-ownership-index
- Complexity of the plans both increases operational costs and puts some companies off considering introducing SAYE or SIP.
- Some companies will be aware of bad experiences where a SAYE or SIP has not gone well, for example,
    - 'underwater' SAYE options - where the price to be paid for the share is more than its current market value - and employees not benefitting and becoming disillusioned with the plan
    - poor participation rates and not being seen to be worth the cost and effort, although this will often be due to poor plan communications.

- Many companies are keen to promote SAYE and SIP plans to their younger workforce, but the need to hold shares for at least 5 years to realise the full tax advantage (in SIP), is seen as a deterrent and does not meet the companies' needs to provide an attractive benefit for their younger workers.
- Companies not being able to afford to provide benefits of a SAYE (i.e. the accounting costs of the options) or the Free or Matching shares in a SIP (not that either are mandatory).
- Cost for private companies was regarded as a particular issue, especially for small companies where the cost to establish and then maintain a plan was not considered to deliver value for money. Our members suggest that companies with small workforces would find a SIP or SAYE scheme cost prohibitive. Key costs for private companies were the cost of the legal, accounting and valuation advice and the ongoing administration costs, particularly to obtain regular valuations.

However, these barriers are not the only reasons for the fall in the number of companies offering employee share schemes. Other reasons include the following:

- There has been a reduction in the number of plans because of the change of companies in the FTSE with companies being taken over by:
  - overseas companies who have not chosen to re-establish a UK tax-advantaged plan, particularly where the target company has had an SAYE as they tend not to sit well where a global company is already operating a plan globally.
  - private equity, where:
    - the company will no longer meet requirements to have a tax-advantaged plan, or
    - the PE firm will want to introduce plans with more flexibility, or
    - the PE firm will not want plans that will vest and have shares held by employees before their liquidity event, they want flexibility to defer vesting to a liquidity event and therefore use non-tax advantaged plans.
- Some listed companies have seen their share price fall in recent years, or become more volatile. SAYE options may have been 'underwater' at maturity and the employees have seen no benefit.
- There is concern that some companies are already stopping their UK tax-advantaged plans in favour of non-tax advantaged plans to give them the flexibility for their younger and agile workforce.
- Accounting treatment for SAYE, especially where the employee does not take up their options and the option is cancelled. In these instances, the company incurs a cost but has not delivered financial benefit to the employee. The result is a misalignment of cost to the company when there is no benefit to the employee.
  - Government support particularly focussed on supporting private companies to introduce the two plans would be welcomed.

Regardless of any barriers , it is important to note that SAYE and SIP are predominantly used by the listed sector (albeit some overseas listed companies in the case of SIP), but the UK listed sector is in decline. In terms of company numbers, the sector has declined by around one-third in the last fifteen years. This will clearly have an impact on the number of companies using these plans .

12. The number of employees using SAYE or SIP has declined in recent years, what do you think has caused that decline? Do you have evidence to support this?

In general, our members believe that this decline is largely explained by three fundamental factors:

- Changes in workforce behaviours and expectations which mean that the long-term commitment of 3 to 5 years in a plan to get benefit is seen as unattractive.
- The complexity of the plans, especially around tax.
- Where the plans are contributory, financial pressures and affordability.

One of the consistent themes of this response is that some of the design features of SAYE and SIP are very much a product of their respective times. But times change, and so do workforces, workplaces and the nature of work itself, rendering some of these features irrelevant or even counter-productive. We are increasingly seeing societal change too – changes in worker demographic, in worker attitudes and in the way in which society looks at companies.

A key feature of that societal change is the changing attitude to career development. Historically, and certainly 43 years ago when SAYE was introduced, there was the concept of a 'job for life'. Many employees joined a business from school or further education and expected to retire from that same company. This is no longer the reality, with three to five years now often being seen as a long time at any individual company. People move on far more regularly in the interests of career progression - at the cost of losing their shares. Consequently, SIP and SAYE are perceived as less valuable to employees, especially for a younger workforce which is more agile than ever, and many of whom have shorter time horizons: they are not getting enough value back because their anticipated length of service is not sufficient to do so. This is exacerbated in the modern workplace by the prevalence of the 'gig economy'.

This is a key issue for companies – indeed, one member talked about their client with a predominantly young workforce establishing an all-employee plan that operates in the UK and globally, where there is vesting every three <u>months</u>. This is now a common approach for many American companies.

For those employees who do expect to remain with a company for sufficient time to derive benefit from SAYE and SIP, our members tell us that the feedback they have received is that, in spite of considerable efforts, many employees simply don't understand the plans. This is particularly the case with SIP with the tapering of the availability of the tax benefits from 3 to 5 years; it is confusing and difficult to administer. It would be better if there was one date when shares could be transferred without income tax liability. The recently announced changes to the CGT regime – which will bring many employees into scope who have never previously been subject to this liability and reporting requirement only exacerbates the problem.

Finally, there is the issue of affordability where there is a contributory requirement. This is a particular issue at present, when the cost-of-living crisis is making it difficult for employees to save and, of course, lower income earners being more affected by the cost-of-living crisis than others.

Our recommendations to address these issues are:

- reducing the time horizon for tax advantaged plans from five years to two
- making resignation a 'good leaver' status
- simplification of the tax treatment of SIP to create a single applicable date
- optional company SAYE contributions on behalf of employees
- exempting some gains from Non-Discretionary Tax Advantaged Share Schemes from the CGT regime

13. What proportion of employees participate in the share scheme(s) your company offers?

Not applicable, but see the ProShare's 2022 SAYE and SIP report for detailed analysis of take-up levels etc.

14. In your view, what are the reasons your employees give for choosing to participate in the scheme? If you are responding as a representative body, please specify what you think are the main reasons employees choose to participate in a share scheme.

The reasons that our members have been given for their employees choosing to participate in a SIP or SAYE plan vary between companies and, to some degree at least, are driven by how the plan has been positioned with and communicated to employees. For example, SAYE is portrayed by many companies as a savings tool, and it is popular for that reason, with employees wanting to be part of the company but also realising a gain and building financial resilience.

Some companies have emphasised that employee share plans are a great way to introduce employees to investing in shares, by showing them how to invest in their employer's shares. There are also no brokerage fees for them to acquire the shares. This is particularly beneficial for employees on low income as it's a cost-free way of them acquiring shares and the 'good news' stories about employees who have been able to save and build up a nest-egg are popular. Two examples of 'good news' stories are those from Pets at Home and CVS Group.

15. What changes, if any, would increase participation amongst employees or change the way your company uses or offers the schemes?

Our members recommendations to increase participation amongst employees or change the way their company uses or offers the schemes are:

- reducing the time horizon for tax advantaged plans from five years to two
- making resignation a 'good leaver' status, allowing companies to enable SAYE options to be exercised when an employee leaves a company for any reason (other than dismissal) before the normal exercise period. For SIP, where shares are not forfeited, shares should be released with good leaver status, incurring no income tax/NIC deductions
- simplification of the tax treatment of SIP to create a single applicable date
- exempting some gains from Non-Discretionary Tax Advantaged Share Schemes from the CGT regime via an increased threshold. The inclusion of gains from these Tax Advantaged schemes is widely viewed as an 'unintended consequence'.
- emphasising that an employee has the right to transfer their SIP or exercised SAYE entitlement to an ISA or SIPP without tax penalty on leaving a company.
- develop a government portal with standard downloadable company documents, and an app for employee participation.

16. In your view, is awareness of the benefits of SAYE and SIP low? How could the government and other groups raise awareness?

We were struck by the fact that, as the Call for Evidence states (paragraph 2.18), 'The share schemes evaluation published alongside this Call for Evidence suggested that while the schemes are generally well targeted, awareness is low. This in turn may affect uptake.' We do not agree. Typically, in companies where plans are operated, they are communicated well and there is a good level of awareness amongst employees.

In the 500 or so companies that regularly operate SAYE or SIP, our members believe that there is good awareness of the plans' benefits. There should be too, not least because companies spend significant sums of money on raising awareness and we see the hard work they put in when judging our annual ProShare Awards. However, there are tens of thousands of companies – both listed and private – which could have employee share plans, but do not. Among listed companies, we believe that there is reasonable awareness of the existence of SAYE and SIP plans, but perhaps less awareness of the benefits shown by research demonstrating the beneficial impact on productivity and employee engagement, or the additional benefits to companies like the NI savings. For private companies, many would not know about the benefits of tax-advantaged plans, and if they did, would consider the cost and complexity of operating them a barrier.

Our members suggested the following solutions:

- additional corporate tax relief for companies, particularly private companies, offering a SIP or SAYE
- government provision to allow companies to make an SAYE contribution for all employees, e.g. £10 a month, to help employees get into the habit of saving

- government support for the portability of shareholdings, so when employees leave a company they retain shares in a tax-efficient way.
- more flexibility in allowing the employer contribution into a stakeholder pension to give the company or employees the choice to invest some of that employer contribution into a SAYE or SIP. This way the employer is still helping the employee to save for the future, but for a shorter term (through a SIP or SAYE) rather than only through a pension plan
- creation of a bank of experts available within HMT, DBT or another government department to be available to advise on the benefits of, and the types of employee share ownership and tax-advantaged plans available to companies. The Welsh Government have experts in employee share ownership available to advise Welsh companies on establishing both SIP and SAYE as well as becoming employee-owned. They offer a 'fully funded' appraisal of suitability for employee share plans and employee ownership: https://employeeownershipwales.co.uk/about-us/
- support the development of SAYE to be operated in a way that would attract more favourable accounting treatment under the Accounting for Share-based Payments rules
- under the FSCS protection rules, allow the SAYE savings contract to be treated separately under the rules. It is a significant issue for banks offering SAYE to check who has other accounts with them.

SAYE and SIP rules and flexibility

17. In your view, how easy or difficult is it to operate or administer SAYE and SIP? Please explain your answer and specify any ways in which the schemes could be simplified.

Feedback from our members is that SIP is significantly the more complicated of the two, and harder to run than SAYE. SAYE is more straight forward and rules are more generally understood amongst companies and administrators. SIP, on the other hand, can trip companies up. There are a host of technicalities, not all of which seem necessary, but which have to be understood by companies. For example, the 10% limit which is probably no longer needed in light of minimum wage legislation and is particularly confusing for those who go on long-term leave. The SIP taxation table is very confusing for participants, particularly the two-tier taxation between 3 and 5 years. This means that employees do not feel able to calculate how much they will make/how much tax they will pay at any stage of a plan.

Although at first sight SIP looks more similar than SAYE to schemes which are operated globally, SIP performance conditions are too complicated (companies generally do not operate these) and there is a large up-front set-up cost, not to mention the cost of providing a Matching element. Conversely, SAYE is less costly to implement and administer and, because of the annual nature of SAYE, there is an annual focus on communicating with employees. SIP has an evergreen 'rolling' nature, so no automatic annual relaunch or annual reminders to help employees better understand the plan (although we are aware of some members who do issue ad hoc reminders to non-participating employees). SAYE is an incredibly popular plan amongst those who participate, it is long-standing and resilient, despite macroeconomic headwinds in recent years.

18. Do you feel SAYE and SIP offer enough flexibility to adapt to individual companies' circumstances? If not, please state why.

No. SAYE was introduced in the Finance Act of 1980, with the first plans being approved by shareholders at plan issuer companies' AGMs the following Spring. The SIP came into force in 2000. For legitimate reasons, both were introduced supported by a package of rules that were appropriate to the time, but the world of work has changed beyond all recognition since 2000, let alone since 1980 and the rules need to be updated to reflect those changes.

For example:

- Companies do not see employee share plans primarily as recruitment and retention tools, but rather as part of a wider employee benefits package. Their purpose is now aligning participants with shareholder interests, helping them to feel that they are actively participating in the success of the company, rather than aiding retention as the amounts involved are typically not significant enough. Employees are much more mobile, and consequently, leaver rules should be simplified with companies given the flexibility to set their own leavers rules. If share plans are not the retention/recruitment tools they used to be, then there should not be 'good' and 'bad' leavers and benefits should kick in earlier – without a commitment to three or five years.
- A significant proportion of the workforce is in informal contracts, working on zero-hour contracts or in the 'gig economy', or employed through third parties, many of these workers are paid on a weekly basis. Some companies would like the flexibility to treat these individuals as part of their workforce and include them within share plans.

19. Does your company make use of the current flexibility within the scheme rules? Do they vary the terms on which the employees participate? If so, in what ways?

"Probably not as much as we might," is a typical comment from our members. SIP can incentivise participation when Free Share awards are offered, and it is helpful that minimum contribution amounts are set low (£5) as this encourages participation. Some companies set lower maximum contribution limits for their SAYE e.g. £100 per month per annual invite, rather than £500, so that the plan is not perceived as a 'high earner' scheme. This also allows people to take-up an annual invitation each year.

Overall, however, our members felt that the rules need to be made more flexible (see some of the suggestions in our responses to other questions in this section) and there should be greater clarity about the flexibility that is allowed. For example, a number of companies and, more importantly, their advisers were unaware that the requirement that all employees must be invited to participate on the 'same' terms did not preclude the alteration of plans in the basis of remuneration so that they could favour the lower-paid. The call for evidence (paragraph

3.9) states that “plans can be altered based on remuneration, length of service or hours worked but they cannot contain features that are likely to have the effect of conferring benefits wholly or mainly on directors or higher paid employees.” This is not common knowledge in the market and it would be helpful were Government guidance to include a specific example of this.

It is beneficial that companies have flexibility to set the maximum contributions for SAYE per month – as stated above, setting a relatively low maximum amount can help to avoid the plan being viewed as a high earner scheme, and it also allows employees to pay into multiple schemes. It is also helpful to have the choice between automatic reinvestment of dividends, and automatic payments of dividend cash, although not all providers offer this flexibility.

Lower income earners: Questions

20. Does participation in SAYE or SIP amongst employees vary according to remuneration? If so, in what ways?

Yes: lower income earners are least likely to join a SIP where there is no Matching element. SAYE participation is somewhat more evenly spread across income bands.

Example: This can be illustrated by a ProShare member - a global employer in the Financial Services sector with 35,000 employees in the UK - which currently has 67% of employees participating in a Sharesave plan. The plan is popular across all employee grades with similar level of participation across all grades, except the most junior grade where average participation is still very high at 48%. The plan is also popular amongst all age groups and genders.

Their SIP (Partnership and Dividend shares, but no Match) has a lower participation rate of 21%. SIP Participation is significantly elevated at higher grades compared to lower grades: above 30% for middle/senior management, whereas the two lowest grades have participation rates of just 10% and 7%.

There are a number of reasons behind this disparity.

- Pressures on disposable income for those on lower levels of pay mean they are less inclined to participate; it is simply not affordable for many, and the level of contribution is often too low to see much gain. For example, contributing £5 per month to maybe realise a gain of £100 in three years’ time will simply not appeal to many. The benefits need to materialise more quickly and be higher in value.
- Tax relief also has a role to play: if a lower income earner contributes £150 to a share scheme, their take home goes down by £102. If a higher income earner contributes the same, their take home only goes down by £87.
- Lower income earners are, disproportionately, non-office-based staff, often working part time, with pro-rated salaries and contributions, or ‘gig workers’ in informal contracts. These employees may not have easy access to company emails, so communications about share plans needs to be handled differently – e.g. by having

employee advocates in warehouses, promotional posters in canteens and so on, and is thus more complicated. It takes more work on the part of the company, and costs more too, where a simple email campaign is not appropriate.

- Lower income earners are also more likely to be receiving in-work benefits and may have concerns or questions about the impact of share schemes on their eligibility to receive these. A simple solution might be for income from employee share schemes to be excluded from welfare and benefit eligibility calculations.
- Finally, there is also a societal issue. There is some evidence that the younger generation (who are often, though not always, at lower levels of remuneration) are less likely to save than other generations – even in auto-enrolment pensions.

21. In your view, does employee motivation or the reasons for participating in a share scheme vary according to different levels of remuneration? If so, in what ways?

Yes, it does. At lower levels of remuneration, employees are less likely to see their own wealth building as being connected to that of their employer. Whilst the old 'job for life' model meant that an employee's wealth building was connected to their employer, this is no longer the case. Motivations amongst lower- or middle-income earners might include buying property or a vehicle, clearing debt, supporting retirement, or supporting family members. Also, motivations often differ more between generations than between different income brackets. For example, with SAYE, the youngest and oldest generations sell some or all of their shares at maturity (because they either need the cash, or to support their retirement), whilst generations in the middle tend to retain their shares at maturity.

Employee mobility also has an impact – this makes treatment of leavers a central issue and portability is important. Members with significant employee bases in the United States tell us that, in the US there is greater awareness with regard to holding shares, for example in a 401k plan. SAYE is seen as safer, but share ownership at maturity of an SAYE is lower because around 50% of participants immediately sell some or all of their shares.

The question for the government is, therefore, whether it is important or beneficial to encourage lower income earners to hold their shares – or whether, actually, it is not a problem if they want to sell and use the cash generated.

On balance, we believe that participation is probably far more important than long-term ownership, particularly as company shares represent a potentially volatile single equity if that is the only 'savings' for the individual. In such cases, a responsible employer may well make advice available to employee shareholders in whose best interest it is to sell some, or all, of their shares in the employing company to avoid over-exposure.

22. If you are a company or a scheme user, does your company currently make use of the flexibility of the rules and vary the terms on which your employees participate according to remuneration?

As per our response to question 15, our members experience is that companies probably do not use this flexibility as much as they might. SIP can incentivise participation when Free Share awards are offered, and it is helpful that minimum contribution amounts are set low (£5) as this encourages participation. Some companies set lower maximum contribution limits for their SAYE e.g. £100 per month per annual invite, rather than £500, so that the plan is not perceived as a 'high earner' scheme. This also allows people to join an annual invite every year.

When we consulted with members, a number of companies and, more importantly, their advisers were unaware that the requirement in the rules for SIP and SAYE schemes that all employees must be invited to participate on the 'same' terms did not preclude the alteration of plans in the basis of remuneration so that they could favour the lower-paid. The call for evidence (paragraph 3.9) states that "plans can be altered based on remuneration, length of service or hours worked but they cannot contain features that are likely to have the effect of conferring benefits wholly or mainly on directors or higher paid employees." This is not common knowledge in the market and it would be helpful were Government guidance to include a specific example of this.

23. In your view, are SAYE and SIP appropriately targeted towards lower- and middle-income earners?

Whilst SAYE and SIP are intended to be used by all, they are not always appropriately targeted and do not always work for lower- and middle-income earners. Longevity of holding period is an issue – workforce behaviours have changed and fewer people, particularly younger people, expect to stay in jobs for 3+ years. This is particularly pronounced in lower income bands.

We believe that the Government should address this issue by reducing the holding period to two years. This balances the need for shorter holding periods with awareness that equity is a medium- to long-term investment, subject to volatility; moving to a one-year holding period would mean exposure to increased volatility.

Some of our members argued that it should be possible to target SIP Free Shares at lower income earners only, or that share matching in SIPs should be leveraged to target lower- and middle-income earners. For example, a company could match shares up to the first £40 of a participant's monthly contribution. Of course, some companies do this already.

Other proposals included:

- abolish the 10% salary limit on employees' SIP contributions. With the minimum wage legislation, this restriction is no longer necessary and should be removed
- greater ShareSave discount – for example 30% or 40% rather than the current 20%.

24. In your view, what barriers exist that might prevent lower income earners from participating in an employee share scheme?

The simplest answer to this question is education to increase understanding of shares and investing generally, and of share schemes specifically. Employee share schemes are, and are perceived as being, complex and there is a lot of surrounding jargon that can deter participation. Evidence for this can be found in the number of organisations which exist to support the employee communications process, helping companies and their advisers to simplify the terminology and use plain English. This is a particular problem where employees may work part-time or be in receipt of benefits, which could be impacted by share scheme participation. Those at higher income levels are likely to be more attuned to effective tax planning, whereas the benefits of tax advantaged schemes might not be as immediately obvious to those at lower income levels.

The perception of a reduced 'upside' for employees also presents a potential barrier. There are two issues underlying this. The first is a concern that where schemes are underwater, only savings will be recovered and there is, in any event, a greater inclination amongst this group to save via traditional methods (e.g. savings accounts) or in places where government provides incentives (e.g. LISA, Help to Buy). Another challenge is an increasing awareness that changes to CGT will mean that many more employees will be liable and need to complete self-assessment tax returns, or report (and pay) via HMRC's 'real time' service. Once the CGT threshold is set at £3,000, this will impact many participants. This is likely to be a serious deterrent to participation, as many employees will not have sufficient understanding of CGT and the potential reporting requirements, and will be put off from participating in the plans.

Solutions that our members have suggested include:

- a lookback feature to guarantee a gain, and dissuade people from withdrawing and joining other schemes
- allowing share scheme contributions out of employees' pre-tax salaries – although this would have implications for National Insurance contributions
- use the market value of the shares on the date of exercise as the base cost for CGT, or the exemption from CGT of some gains through Non-Discretionary Tax Advantaged Share Schemes.

Other incentives

25. What other performance incentives does your company offer? How do these compare to SAYE and SIP?

Most companies offer a variety of performance incentives, many of them in the form of variable bonuses, so their purpose is very different from that of SAYE or SIP and their direct comparability is variable. That said, there was a suggestion that perhaps a more appealing option would be to offer employee shares as a part of a wider flexible benefits package – effectively giving employees a pot of money to divide as they see fit into e.g. pension, shares, healthcare and so on.

The major negative is cost, in terms both of actual cost – of the set-up and management of schemes, as well as, in the case of SAYE, the 'accounting hit' (the accelerated accounting charge should people come out of the scheme early) – and the opportunity cost. As one member observed, "To run a share plan costs us £100,000 a year, but we could give everybody in the company family medical insurance for less [than that]. Why would we not do that instead?"

There is a trade-off between other benefits - gym memberships, subscriptions, financial wellbeing etc., and a consciousness that, for the employee, a simpler cash bonus may be preferable.

26. In your view, how are SAYE and SIP valued by employees compared to other forms of remuneration or incentive?

For many employees it is important to feel that they are owners and part of the business for which they work, and these plans emphasise that. However, the complexity of the plans, especially SIP, means that the benefits are less well understood.

27. Would your company have granted options or awards to employees outside of SAYE or SIP in the absence of those schemes?

Not applicable.

28. Is there any other information you would like to share with us in relation to these schemes?

ProShare believes that the Government must provide strong support for ESO and widening rates of employee ownership, making it a key part of the economic agenda as part of its plans to address the UK economy's longstanding productivity challenge. This is particularly important in light of an expected recession, and to better support employees facing the cost-of-living crisis, and building financial resilience more generally.