CO-OPERATIVES UK

Budget 2017 Submission

Broadening ownership in an Inclusive Economy

January 2017

In this Budget 2017 submission Co-operatives UK makes the following recommendations to government, aimed at creating a more inclusive and democratic policy for ownership in our economy:

- Abolish two very expensive and highly exclusive employee shareholding tax reliefs, Company Share Option Plans and Enterprise Management Incentive, which together award £220 million a year in tax breaks to just 40,000 high earners
- Reallocate the hundreds of millions of pounds saved each year to create an Employee Buyout Investment Fund
- Reinvest the millions of pounds projected to be saved each year through the already announced abolition of Employee Shareholder Status in a Co-operative Entrepreneurs Programme, specifically designed to help entrepreneurial people on low and middle incomes own and control their own livelihoods through co-operatives
- Commit to a continuous assessment of the Share Incentive Plan and Save As Your Earn tax breaks to ensure these continue to make a strong positive contribution to a more inclusive economy

1 Background

1.1 In Autumn Statement 2016 the Chancellor announced that the tax reliefs attached to Employee Shareholder Status (ESS) would be withdrawn for entrants from December 2016, with plans to legislate to abolish ESS itself at the earliest legislative opportunity.[1]

1.2 The Chancellor gave the following explanation for this decision:

“We will abolish the tax advantages linked to Employee Shareholder Status in response to evidence it is primarily being used for tax-planning purposes by high-earning individuals.” [2]

1.3 As supporters of the Prime Minister’s agenda for an Inclusive Economy, we welcome the decision to scrap ESS on this basis. But we believe this move and the reasoning behind it should now lead to an evaluation of the UK’s other employee shareholding tax reliefs, to determine the degree to which they

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[1] See paragraph 4.31 of Autumn Statement 2016

[2] Chancellor’s speech

contribute to a more inclusive economy.

1.4 Using HMRC's own assessment of the four main tax reliefs, we have concluded that their impact in this regard is not as positive as it could be. Proportionally very large sums are spent each year providing tax breaks to small and in some cases shrinking numbers of people.[3] That is not something we would expect to see in an 'Inclusive Economy that works for everyone'.

1.5 In our view an Inclusive Economy is one where more people have a greater share in ownership, decision-making and wealth, especially when it comes to their livelihoods. Crucially we argue there is a vital link between inclusivity and productivity which should be reflected more strongly in government policy. A robust body of evidence suggests that there are productivity gains to be made by giving more workers a stake and a say.[4] Thus a more Inclusive Economy should be more productive as well. Inclusive Economy and Industrial Strategy are thus two government priorities that must be more aligned. Through its budget decisions HM Treasury has a decisive role in making this happen.

1.6 In **part 2** below we make a brief assessment of the two 'all employee' schemes, while in **part 3** we assess the two 'discretionary' schemes, through the lens of an Inclusive Economy. In **part 4** we argue that the public money spent on the discretionary schemes could do more to create an Inclusive Economy, in ways that particularly benefit workers on low and middle incomes. In **part 5** we propose the creation of a Co-operative Entrepreneurs Programme. In **part 6** we propose the establishment of an Employee Buyout Investment Fund. In **part 7** we make concluding remarks and reiterate our recommendations to government.

2 'All employee' schemes

2.1 The UK offers two tax-advantaged employee shareholding schemes which participating employers must open to all their employees: Share Incentive Plans (SIPs) and Save As Your Earn (SAYE). These schemes are intended to support broad-based employee shareholding and are often seen as key policy tools encouraging greater employee ownership across the economy.

2.2 HMRC analysis shows that these schemes spread the Exchequer's generosity over a fairly wide population of workers: in 2013-14 SAYE gave £320 million in tax breaks [5] to 170,000 workers exercising their options,[6] while SIPs gave £520 million [7] to an estimated 316,000 workers granted shares tax free. [8]

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[3] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/464263/ESS_National_Statistics_Commentary_Document.pdf

[4] http://employeeownership.co.uk/what-is-employee-ownership/employee-ownership-benefits/

[5] https://www.gov.uk/government/statistics/table-61-estimated-costs-of-income-tax-and-nics-relief

[6] https://www.gov.uk/government/statistics/save-as-you-earn-share-option-schemes

[7] https://www.gov.uk/government/statistics/table-61-estimated-costs-of-income-tax-and-nics-relief

While from a co-operative perspective these schemes are not perfect - they mainly support atomised undemocratic ownership after all – we believe they do spend public money in a way which promotes a more Inclusive Economy.

2.3 However government should be more mindful of the degree to which these schemes enhance inclusivity for people on low and middle incomes. It should commit to continuous assessment of SIPs and SAYE through an Inclusive Economy lens.

3 'Discretionary' schemes

3.1 Government also awards tax breaks through two 'discretionary' schemes: Company Share Option Plans (CSOPs) and Enterprise Management Incentives (EMIs), through which firms limit tax-advantaged share options to select employees as part of their remuneration packages.

3.2 In contrast to SIPs and SAYE, the discretionary schemes benefit a much smaller number of workers. According to HMRC, in 2013-14 CSOPs gave £110 million in tax breaks [9] to just 35,000 people.[10] And in the same year EMI gave £110 million[11] to just 5,000 people.[12] That is an average of £5,500 per head. Furthermore, HMRC calculates that through EMI government gives away an average of £15,400 a year per employee,[13] more than the annual income of someone working 35 hours week for minimum wage.

3.3 Given that these schemes are almost always used to advantage high earning employees at senior levels, it is much less clear that they contribute to a more Inclusive Economy.

4 Making better use of public funds

4.1 In this time of growing difficulty for people of low and middle incomes, and as realisation grows that we need to do more create an Inclusive Economy that works for everyone, we argue it is not an effective use of scarce public money to award £220 million a year in tax breaks to just 40,000 high earners.

4.2 We recognise that some smaller fast-growing firms have cash flow problems and so in order to attract and retain key talent augment wages with share options. As co-operatives who understand the benefits of sharing ownership

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[8] HMRC provides no estimate for the number of workers benefiting from SIPs each year. To arrive at our very rough estimate we have used the average number of workers per firm exercising SAYE options in a year, 386 workers, and multiplied this by the number of firms granting SIPs, 820 firms. For the data on firm numbers see HMRC table 6.2

[9] https://www.gov.uk/government/statistics/table-61-estimated-costs-of-income-tax-and-nics-relief

[10] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/464155/Table6-4.pdf

[11] https://www.gov.uk/government/statistics/table-61-estimated-costs-of-income-tax-and-nics-relief

[12] https://www.gov.uk/government/statistics/enterprise-management-incentives-share-option-schemes

[13] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/464263/ESS_National_Statistics_Commentary_Document.pdf

we are not opposed to this, though of course we would prefer ownership and control to be shared among all employees. Rather we question whether in the current climate the generosity of the Exchequer in further enhancing these elite remuneration packages can really be justified.

4.3 There are better ways to create an Inclusive Economy that is more productive for more people, including models that can do more to benefit workers on low and middle incomes. We believe SIPs and SAYE continue to play a positive role here, but tax-advantaged employee shareholding is not the only means by which progress can be made. Co-operatives offer another means by which workers can own and control their livelihoods. This model does not rely on tax-advantaged shareholdings but rather on supporting new forms of entrepreneurship, rooted in local needs and capacities and underpinned by a combination of pragmatism, solidarity and enterprise.

5 Co-operative Entrepreneurs Programme

5.1 Government expects to save £115 million by 2022 by scrapping ESS.[14] We believe this money could make a strong positive contribution to a more inclusive and productive economy by funding a programme that supports groups of entrepreneurial people on low and middle incomes to establish their own co-operative businesses.

5.2 While there are many examples of people successfully starting and growing their own business, it is not easy going it alone, especially if opportunities and resources are scarce in the local area. Through a range of tried and tested co-operative approaches, these entrepreneurs could pool talents and energies, share costs, access opportunities and benefit from solidarity and mutual support, all while taking control of their livelihoods. This would include supporting the creation of co-operatives of sole traders as well as new employee-owned firms. This approach would increase the likelihood of a successful outcome for more people. Notably, ONS data suggests twice as many co-operatives survive the difficult first five years than other businesses.[15]

5.3 The Co-operative Entrepreneurs Programme would add new businesses in local economies in which all workers have a stake and a say. The potential productivity gains from such conditions are well evidenced.

5.4 Furthermore, due to the way beneficial ownership works in co-operatives, the programme would create opportunities for communities to not only create more wealth locally, but crucially to keep more wealth locally too.

5.5 All this would also enhance the inclusivity and productivity of local economies and contribute to much needed social capital and cohesion.

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[14] Autumn Statement 2016: Policy costings

[15] https://www.uk.coop/sites/default/files/uploads/attachments/co-op_economy_2015.pdf

5.6 The Co-operative Entrepreneurs Programme would need to be delivered in a way that complemented Start-Up Loans, the New Enterprise Allowance and related business support at a very local level. This would reduce administrative costs and ensure effectiveness. There is a wealth of co-operative development expertise across the country that could augment existing capacity among Start-Up Loan Providers and other enterprise agencies. Co-operatives UK is also in the process of developing a practical business development strategy which could inform this work.

5.7 To a degree this about extending the range of publicly funded business support schemes already available through local channels to include a co-operative focus. But government can also look to examples of support for co-operative entrepreneurship provided with local government involvement in places as diverse as Glasgow[16] and Preston[17] in the UK and Cleveland[18] and New York City[19] in the USA. The Cleveland example is particularly noteworthy as the programme has raised significant social investment, and working with the city's 'anchor institutions', has been able to lever in $3 billion annual procurement power.[20]

5.8 Co-operatives UK is also managing a nationwide programme for the Department for Communities and Local Government to develop best practice in community economic development.[21] Our interim findings will provide practical learning on how the needs, aspirations and capacities of people and places can be better understood and utilised for local economic benefit.

6 Employee Buyout Investment Fund

6.1 As the Chancellor highlighted in Autumn Statement 2016, the UK has a growing problem with business succession. Too many home grown firms get to a certain size only to be brought out by foreign investors, with increased risk that capital and employment will end up being offshored.[22] There are also concerns that the successful succession of thousands of 'family businesses' in the coming decade is far from assured.[23] If we don't have a plan to deal with these issues we will see more jobs and capital move abroad. With proper public and private backing, employee buyouts could be a viable succession

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16 https://www.glasgow.gov.uk/CHttpHandler.ashx?id=36459&p=0

17 http://www.preston.gov.uk/businesses/co-operatives/preston-co-operative-initiative/

18 http://www.evgoh.com/about-us/

19 https://drive.google.com/file/d/0B24IaEIz1aPFeTN4aXNvWGkwQmc/view

20 http://www.evgoh.com/about-us/

21 http://mycommunity.org.uk/take-action/community-economic-development/

22 http://www.telegraph.co.uk/business/2016/12/06/foreign-firms-spend-100bn-buying-british-businesses-far-2016/

23 http://www.pwc.co.uk/private-business-private-clients/insights/family-business-survey-succession-tax-and-legislation.html

route in the UK, as they are elsewhere in the world.[24] Since evidence shows that employee ownership boosts productivity, the economic gains from this would extend beyond the retention of capital, jobs and skills.

6.2 Abolishing ESS was the right thing to do. But we think a government serious about creating a more Inclusive Economy could be bolder and go further, by ending the discretionary tax breaks - CSOPs and EMI - and investing the money saved in further measures to promote genuine broad-based employee ownership in the economy.

6.3 In 2013-14 the government spent £220 million in tax breaks through those schemes. If £220 million a year could be placed in an investment fund to support employee buyouts of viable business during succession, this would crowd-in private finance and give more business owners confidence in this option. This would prepare the UK for the looming succession crisis while at the same time making a significant contribution to a genuinely Inclusive Economy.

6.4 Great efforts must be made to ensure financial support is only given on the basis of commercial viability. And the very real limitations of using government policy and state support to create effective worker-owned firms must be recognised. Around the world the best frameworks supporting employee buyouts tend to combine statutory frameworks and specialised financing mechanisms with a patient long term commitment to co-operative development, led by an autonomous and mutually supportive co-operative sector.[25]

6.5 To reduce administrative costs and ensure effectiveness and independence, the Employee Buyout Investment Fund could be held and administered by the British Business Bank. It would have to operate alongside specialised business development support. Government should look to Co-operative Development Scotland (part of Scottish Enterprise) for an example of successful public sector activity in this area.[26] There is also a wealth of expertise and capacity government could draw on from the UK's already strong co-operative and employee owned sectors.

7 Concluding remarks

7.1 We applauded the Chancellor's decision to scrap ESS. But by his own logic we think there is a lot further to go before we get an employee ownership policy, let alone an economy, that might actually work for everyone.

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[24] http://www.cecop.coop/IMG/pdf/bussiness_transfers_to_employees_under_the_form_of_a_cooperative_in_europe_cecop-4.pdf

[25] Ibid

[26] https://www.scottish-enterprise.com/services/develop-your-organisation/co-operative-development-scotland/overview

7.2 In particular we believe CSOPs and EMI should be evaluated to see how well they contribute to an Inclusive Economy. As part of this government should seriously consider whether the hundreds of millions spent each year on these tax breaks for a small number of high earners could be better spent in other ways which focus more on inclusivity for workers on low and middle incomes.

7.3 Our recommendations ahead of Budget 2017 are as follows:

- Invest the money saved by scrapping ESS in a Co-operative Entrepreneurs Programme, specifically designed to help entrepreneurial people on low and middle incomes own and control their own livelihoods through co-operatives
- Abolish CSOP and EMI and reinvest the hundreds of millions saved each year in an Employee Buyout Investment Fund
- Commit to monitoring the ‘inclusivity impact’ of SIP and SAYE, to ensure these reliefs continue making a strong positive contribution to a more Inclusive Economy, with a particular focus on the benefits for low and middle income workers

7.4 Our proposals do not call for additional public spending but rather the reallocation of existing resource. There are administrative costs to be considered for both the Co-operative Entrepreneurs Programme and the Employee Buyout Investment Fund but these would be mitigated to a significant extent by virtue of being attached to existing institutional and operational arrangements.

7.5 The proposed reallocation of funds would benefit a broader population of workers, across a wider range of incomes, at the expense of a small number of individuals who are already motivated, productive and highly paid.

7.6 Reallocating public funds in this way would spread ownership, save jobs, boost productivity, create opportunity, lower inequality and enhance social capital in places across the UK, just as any policy for a genuinely Inclusive Economy surely must.

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About Co-operatives UK

Co-operatives UK is the network for Britain’s thousands of co-ops. We work to promote, develop and unite member owned businesses across the economy. From high street retailers to community owned pubs, fan owned football clubs to farmer controlled businesses, co-ops are everywhere and together they are worth £34.1 billion to the British economy.