Employee Ownership
Australia *Making it your business*

ABN 40 152 310 256
a: GPO Box 2649, Sydney NSW 2001
e: info@employeeownership.com.au
w: www.employeeownership.com.au

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Email: IRconsultation@ag.gov.au

The Hon Christian Porter MP
Attorney-General of Australia

Dear Attorney-General

1 Introduction

Employee Ownership Australia ("**EOA**") welcomes the opportunity to make a submission on Cooperative Workplaces and how Australia can capture productivity improvements from more harmonious workplace relations.

EOA was formed in July 2011 to ensure ongoing advocacy for broad based employee ownership and dynamic workplace participation in Australian companies. It engages with and assists companies that have or aim to implement employee ownership or employee share plans, whilst also being a key advocacy body for broad based employee ownership. EOA is independent and entirely member funded, and is the only independent, dedicated advocacy and education group in this space in Australia.

As the discussion paper identifies, Australia's current industrial relations system suffers from conflict and adversarial behaviour that result in detriments to both employees and employers. The provision of employee equity can help solve these problems. Our submission focusses on employee ownership as a model for creating more engaged and cooperative workplaces and illustrates the range of mutual gains it generates for both employees and employers.

We also advocate for tax and corporate regimes that promote, not prevent, the ability of business to engage in employee ownership. We believe appropriate tax and corporate law reform would help to further encourage the use of employee equity to foster more cooperative and productive workplaces. We also provide our comments on the key impediments to offering employee equity below.

We are preparing a separate submission to the recently announced Inquiry into the Tax Treatment of Employee Share Schemes, which will be available in due course.

We would be happy to discuss if you have any questions regarding our submissions.

2 Submissions

2.1 Employee ownership is a critical tool for creating mutually beneficial and cooperative workplaces

We believe that the provision of employee equity is a critical tool for producing mutually beneficial and productive work places for employees and employers. This has been identified through numerous studies associated with the provision of employee equity which have found resulting improvements in company performance and resilience, together with improvements in employee commitment, engagement and wellbeing.

Most recently, the Office of the Chief Economist made a number of findings associated with the provision of employee equity in their research paper, *The performance and characteristics of Australian firms with Employee Share Schemes* ("**Office of the Chief Economist Report**").[1] The findings include that firms with employee equity have lower employee churn, higher sales, higher value added, higher labour productivity and higher value added growth when compared with their non-employee ownership counterparts.[2]

The greatest benefits associated with the provision of employee ownership policy incentives are to small business. The positive correlation between employee ownership and performance weakens as firms get larger and older.

Despite the stronger correlation with small business performance, large mature firms are significantly more likely to use employee equity compared with young small and medium enterprises in Australia due to the cost to set up and administer these arrangements and the burden imposed by regulatory complexity.

2.2 Specific benefits of employee ownership

There is a substantial body of evidence demonstrating the benefits of employee ownership to both business performance and employee well-being. Importantly, these benefits are best realised when integrated with ensuring more general employee engagement.

Two critical points can be made about employee ownership:

1. The concepts of employee ownership / employee equity are interlinked and mutually reinforcing with employee engagement. As the *Sharing Success: The Nuttall Review of Employee Ownership* ("**Nuttall Review**") identifies, there is a strong correlation between employee engagement and the provision of employee equity. [3] That employee owners are more likely to be engaged with their company via employee ownership can enshrine employee engagement into a company.[4]

   David MacLeod and Nita Clarke's report, *Engaging for success: enhancing performance through employee engagement* ("**MacLeod Report**"), demonstrates the benefits of increased

[1] *The performance and characteristics of Australian firms with Employee Share Schemes Research paper*, Hendrickson et al., Office of the Chief Economist (April 2017).
[2] See page 1 of the Office of the Chief Economist Report.
[3] *Sharing Success: The Nuttall Review of Employee Ownership* (July 2012). See, in particular, page 14.
[4] See paragraph 1.10 of the Nuttall Review.

engagement: workplaces with high employee engagement have greater staff commitment, well-being and reduced staff turnover.[5]

2. Employee ownership creates benefits that can be shared between both employees and employers. For employees, employee ownership is linked to increased financial and non-financial well-being and higher performance. For employers, it is linked to increased business performance, resilience and innovation. These benefits are similarly mutually reinforcing: greater employee well-being is associated with greater productivity and gains for the company, while gains for the company will flow back to employees.

The benefits from employee ownership are usefully described in the Nuttall Review and we elaborate on them further below.[6] While these benefits should translate to greater opportunities for small business, they are not confined to that area.

Greater employee commitment, engagement and collaboration

This is regarded as the clearest benefit of employee ownership and there are a series of empirical studies which examine and illustrate it.

A survey of UK employee owned businesses by Burns (2006)[7] revealed that these businesses widely hold the view that greater employee commitment is the biggest advantage of an employee ownership model – 90.6% of the businesses surveyed felt they gained extra staff commitment from employee ownership. The broader literature on employee ownership and commitment also supports this link (see, for example, the Matrix Evidence Review 2010).[8]

Further research by Blasi et al. (2015)[9] found that workers at an employee ownership business were more likely to say their company had a collaborative management culture and that it was an excellent place to work.

The MacLeod Report specifically identified employee ownership as also having a profound and distinctive effect in facilitating employee high-performance.[10]

Enhanced employee well-being

Employee ownership and enhanced engagement have been associated with benefits to employee well-being. Research conducted by the Napier Business School found that a majority of workers at an employee owned company were more satisfied compared to when they had worked for non-employee owned companies.[11]

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[5] *Engaging for success: enhancing performance through employee engagement*, report to Government by David MacLeod and Nita Clarke (2009).
[6] See page 22 of the Nuttall Review.
[7] *Good business: the employee ownership experience,* Burns (2006).
[8] *The employee ownership effect: a review of the evidence*, prepared by Matrix Evidence (2010).
[9] *Do broad-based employee ownership, profit sharing and stock options help the best firms do even better?* Blasi et al. (2015).
[10] See for example the discussion of engagement's effect on performance from page 11 of the MacLeod Report.
[11] See the *Health and wellbeing of employees in employee owned businesses* report prepared for the John Lewis Partnership and Employee Ownership Association by McQuaid et al. (2012).

The Nuttall Review also suggests well-being improves when employees are provided with a greater stake and involvement in long-term collaborative goals, a key feature of employee ownership.

Financial benefits for employees

Benefits to employees extend to enhanced financial well-being. US research has illustrated this gain sharing aspect of employee ownership: it is correlated with increased employee retirement savings; greater actual and perceived job stability; and higher median hourly wages. These benefits for employees can be substantial – a 2018 survey by the National Centre for Employee Ownership found US workers in companies with employee ownership had over twice the retirement savings than the national average.[12]

In the Australian context, the Office of the Chief Economist Report found significantly higher wages per employee in firms that had employee ownership structures in place.[13] Again, these gains can be substantial: mature, large firms with employee equity plans had 38% higher wages than their counterparts.

Reduced absenteeism

A number of empirical studies have examined the effect of employee ownership on absenteeism.

Research by Peel and Wilson (1991)[14] found that companies that implemented share option plans experienced rates of absenteeism 13% lower on average than those without share plans.

Improved business performance

Employee ownership also provides significant benefits to business. The Nuttall Review found that companies with employee ownership outperform other companies, while the Office of the Chief Economist Report found that growth and productivity was significantly higher in small firms with employee equity plans compared to their counterparts.[15]

The Employee Ownership Australia Index ("**EOA Index**"), which compares the performance of companies with employee ownership schemes open to their whole workforce to the performance of the ASX200, supports these claims.

The EOA Index shows that firms with employee ownership consistently outperformed the ASX200 across June 2011 – June 2017, shown in Figure 1 below.

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[12] *S Corporation ESOPs and retirement security*, Wiefek and Nicholson (December 2018).

[13] See, in particular, pages 1 and 11 of the Office of the Chief Economist Report.

[14] *The impact on absenteeism and quits of profit-sharing and other forms of employee compensation,* Peel and Wilson (1991).

[15] See also: *Model growth: do employee-owned business deliver sustainable performance,* Lampel et al (2010).

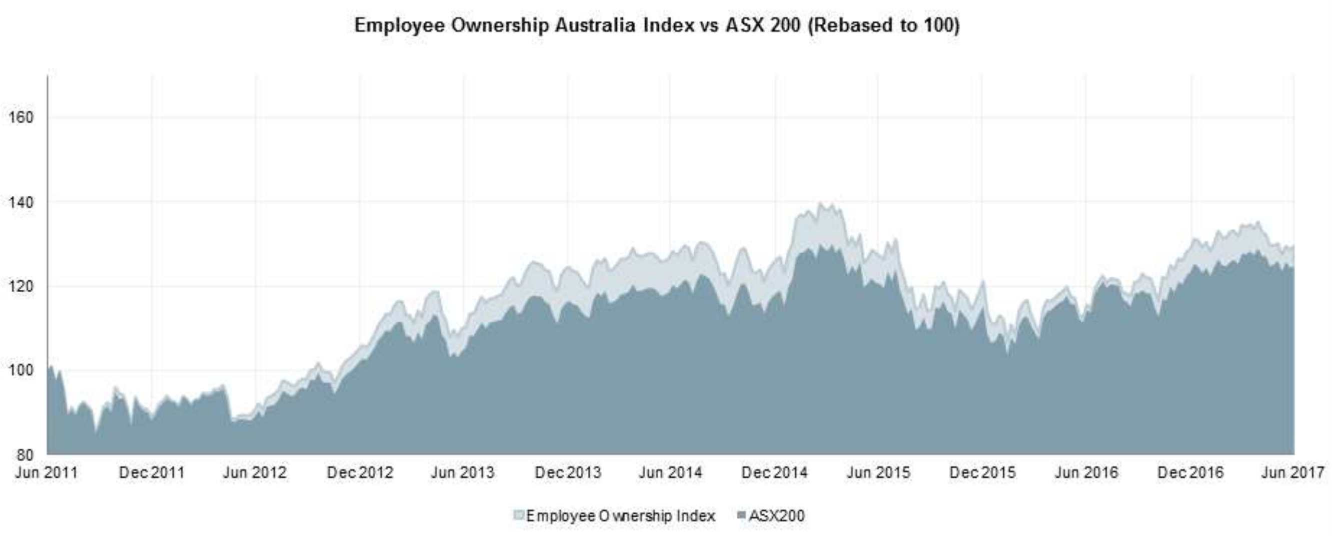

Figure 1

Employee-owned companies also outperform or match the ASX200 in 3 of 5 social sustainability factors, covering corporate risks; performance relating to employees; relationships with external stakeholders; and human rights. They are also twice as likely to show clear evidence of equal opportunity systems.[16]

Increased economic resilience

Firms with employee ownership have shown more resilience to economic downturns. UK research has found that employee owned firms demonstrated consistent sales growth during the 2008 – 2009 financial crisis compared to their non-employee owned competitors. [17]

Research in the US context by Kramer (2008)[18] found that the risk an employee owned company will not survive in a given year is 75% of the risk for a similar but non-employee owned company.

Driving innovation

UK research has found that employee ownership can drive innovation through a variety of mechanisms: [19]

- Employee owned companies perceive that they have a strong ability to attract and retain talented employees who then provide boosts to innovation.
- Employee ownership is a strong driver of employee engagement and involvement, both of which are associated with greater levels of innovation.

Benefits of employee ownership - international case studies

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[16] See https://employeeownership.com.au/employee-ownership-index/.

[17] *Model growth: do employee-owned business deliver sustainable performance,* Lampel et al (2010).

[18] *Employee ownership and participation effects on firm outcomes*, Kramer (2008).

[19] See, for example, page 15 of the Office of Chief Economist Report, page 10 of the Ownership Effect Inquiry literature review and page 22 of the Matrix Evidence Review.

The MacLeod Report and The Ownership Effect Inquiry Final Evidence Report[20] provide a series of helpful international case studies on the benefits associated with employee ownership and how it may be implemented. We draw your attention to these should you wish to examine concrete examples of employee ownership in practice.

3 What are the impediments to employers and employees currently providing employee equity arrangements in Australia?

The key impediments to providing employee equity arrangements can be broadly summarised as follows:

- The actual and perceived legal, tax, accounting and regulatory complexities of employee ownership.
- The lack of resources available to support employee ownership in a simple and cost-effective manner.
- The lack of awareness of the concept of employee ownership and its benefits.

These are the impediments identified in the Nuttall Review in the UK. We believe that the impediments in Australia are broadly equivalent. However, there is considerable emphasis and focus in the Australian market on the tax and legal complexities of employee ownership.

3.1 The actual and perceived legal, tax, accounting and regulatory complexities of employee ownership

We consider these elements to be a significant barrier to the provision of employee equity in Australia.

Unlisted entities face particular difficulties implementing employee ownership. The ability to provide employee equity for unlisted entities is more complicated not only because of the commercial structure associated with ownership of the entity but also the corporate and tax consequences associated with offering equity in unlisted vehicles.

Corporate restrictions on the provision of equity in unlisted vehicles through employee share schemes cause particular difficulty, primarily through the cost and complexity of complying with the relevant rules and the very limited exclusions available.

We have commented in detail on the corporate reform required in relation to employee share schemes in our submission to the Department of Treasury in response to Treasury's 2019 Consultation Paper on the proposed form of the regulation of employee share scheme offerings. (A copy of our previous submission is **attached**).

The essential elements of reform can be encapsulated as follows:

1. Ensure tax rules and corporate regulations work efficiently.
2. Harmonise the tax and corporate rules.
3. Remove cessation of employment as a tax trigger point.

[20] Lampel et al (June 2018). This report formed part of the broader *Ownership Effect Inquiry* – we have provided a link in the 'Key research material' section of this submission.

4. Facilitate “baby boomer” succession arrangements.

Our key observations on reform of the tax system is that it should be simplified to remove unnecessary complexity and ensure that it is globally competitive. It is critical that reform produces an appropriate tax outcome reflecting the timing and access of the economic benefits available to employees - in many cases this is not the outcome under the existing tax rules.

There is significant opportunity to expand employee ownership via reform of the employee share scheme rules insofar as they apply to the unlisted environment. This in particular facilitates start-up ventures and the succession of “baby boomer” businesses to employees.[21]

3.2 Lack of resources available to support employee ownership in a simple and cost-effective manner

One of the consequences of the complexity associated with the corporate and tax aspects of offering employee equity is the lack of simplicity and the resulting cost in providing employee equity.

The Australian Tax Office provides a very useful guide to the provision of employee equity through market value options. It includes detail of both the tax consequences and the corporate regulation of offering securities. We consider that it would be helpful to continue to expand the range of guidance provided.

If this is accompanied by a simplification of the corporate and tax rules, we consider that it should be possible to provide employee equity, even in unlisted entities, in a simple and cost-effective manner.

3.3 Lack of awareness of the concept of employee ownership

As we have noted, the current regulation of employee share equity derives from a combination of both tax rules and corporate rules. As a result it is administered by both the ATO and ASIC.

There would be benefits in establishing a single body which incorporates key stakeholders and promotes the regulation and benefits of employee ownership in Australia.

4 Conclusion

We believe widespread employee ownership will “discourage adversarial behaviour and foster an environment where the preference of the parties is to cooperate and avoid a conflict model.”

Our submission provides substantial “examples of the practices and techniques that foster and grow mutual benefits” and highlights what policy makers have already identified as the key issue - that “workplace culture is a critical area for improvement.”

[21] See the example provided on page 18 of the Nuttall Review.

The success of employee ownership around the world – as this submission indicates – can be shown to be positively measured against the three criteria identified in the discussion paper: driving jobs and wages growth, boosting productivity and strengthening the economy while ensuring protection of employees' rights.

Leadership, workplace culture and sharing positive commercial outcomes are all inherent in employee ownership, and all are key components underpinning the success of employee ownership businesses and their increased productivity, innovation and performance.

Employee owned businesses also prove that "it is a fundamental fact of successful market economies that when employers and employees collaborate and work together to improve the performance of their business they can jointly share the rewards from their efforts – including better job security, higher wages, prospects for career enhancement and better business performance."

We would welcome the opportunity to discuss each of these points with you. Please contact Andrew Clements, Deputy Chair, EOA [redacted]

Yours sincerely

Andrew Clements
Employee Ownership Australia

5 Key research material

The key research materials cited in this submission are listed below, together with links to access the relevant source documents and reports (all further research materials have been listed in the footnotes only):

Good business: the employee ownership experience, Burns (2006)

Engaging for Success: enhancing performance through employee engagement, report to Government by David MacLeod and Nita Clarke (2009)

The employee ownership effect: a review of the evidence, prepared by Matrix Evidence (2010)

Sharing Success, the Nuttall Review of employee ownership (2012)

The performance and characteristics of Australian firms with Employee Share Schemes, Hendrickson et al., Office of the Chief Economist (July 2017)

The *Ownership Effect Inquiry (*2019), including:

- *The Ownership Effect Inquiry – Final Evidence Report;*
- *The Ownership Dividend, the economic case for employee ownership* (the report itself); and
- *The Ownership Effect Literature Review*.