Chambers Ireland's Submission to the Department of Finance on the Taxation of Share Based Remuneration
30/06/2016

Chambers Ireland is the largest business network in the State. With members in every geographic region and economic sector in Ireland, we are well positioned to understand the concerns of Irish businesses and represent their views. Chambers Ireland welcomes the work of the Department of Finance and this consultation on the taxation of Employee Share Based Remuneration Schemes. We are pleased to have the opportunity to inform this consultation process and look forward to further engagement with the Department in the future. This submission has been formulated in correspondence with our Chamber Network and national policy councils, which represent the Chambers and their member companies across a variety of industry sectors in all regions, and including businesses of all sizes.

Consultation Questions

Interested parties are invited to make submissions regarding the following questions. It is not necessary for each submission to address every question, and other issues relevant to the taxation of share-based remuneration may also be raised.

1. **What aspects of the current system of taxation of share based remuneration are working effectively and why?**

Chambers Ireland recognises that approved share schemes have been beneficial and have facilitated a cost effective means of rewarding employees. However we believe that with the appropriate adjustments to their application and administration such schemes have the potential to benefit more companies in more substantial ways. The mandatory application of such schemes to all employees makes them less attractive for employers' who may wish to recognise and support productivity within certain business operations or high performing teams. We believe that increased flexibility in the application of approved shares should be considered. This would allow businesses to drive productivity and support the retention of highly skilled staff.

2. **What aspects of the current taxation of share based remuneration are not working effectively and why?**

The 2011 changes to the tax rules, with the imposition of employee PRSI and the USC on Employee Share Schemes, have lessened the attractiveness of Employee Share Schemes while also increasing the administrative complexity of their implementation. This increased complexity coupled with lower returns means that such schemes are far less accessible and attractive, especially to SMEs. The changes to the taxation of ESSs have curtailed the take-up levels of such schemes at a time when increasing our productivity, competitiveness and attracting and retaining highly skilled employees are of the utmost importance to our economy.

The tax treatment of share schemes in Ireland is now considerably less attractive than in competitor countries. In the wake of recent the recent British referendum we must ensure that the Irish economy is an attractive as possible destination for indigenous businesses, and in order to attract potential new FDI.

The current tax treatment of employee share options makes them unattractive to employees. The fact that the liability for income tax, PRSI and USC arises upon exercising of the option requires employees to have immediate access to cash in order to meet this liability and in advance of any potential income from the sale of shares. If and when shares are eventually sold by an employee, they are then liable for CGT at 33%.

The Irish Tax Institute identifies the UK Enterprise Management Incentive Scheme as a potential exemplar of a scheme that could be applied in the Irish context. No income tax or National Insurance Contribution is due when the share options are exercised (unless the price is less than the market price at the date of granting of the option). The employee is liable for capital gains tax upon selling of the shares. Chambers Ireland believes that a scheme such as this would prove far more attractive to small and medium companies and would incentivise the uptake of employee ownership.

3. Evidence has shown that companies with Employee Financial Performance perform better. If this is the case, is there a policy rationale for the tax system to support share based remuneration?

There is a clear policy rationale in having a tax system which supports and encourages better performance and productivity in business. Increasing the uptake of these schemes among Irish business has the potential to greatly benefit the wider economy. Employee Share Schemes are an effective way to boost the productivity of Irish SMEs which have been shown to lag behind MNCs in terms of productivity. The NCC 2015 Scorecard emphasised that "productivity performance is the crucial determinant of Ireland's international competitiveness"[1], and stated that "improved productivity performance offers the best pathway to prosperity."Incentivising greater uptake of ESSs is a very cost effective way to boost productivity among the Irish workforce. Linking employee remuneration directly with increased company productivity and performance has been proven to boost productivity.

According to the European Commission's 2014 study on Employee Ownership and Participation[2], employee financial participation leads to higher productivity and, therefore, higher competitiveness and growth, as well as strategic stabilisation of ownership. The study also highlights that at company level schemes such as ESSs contribute to solving problems such as absenteeism, labour turnover and the retention of key employees as well as business succession and funding, especially for SMEs and micro-enterprises. Productivity growth allows us to increase employment sustainably over a longer time period and offers an alternative to rises in wages which benefit both employer and employee. There is a risk that a general upward pressure on wages throughout the economy will lead to an erosion of Ireland's international competitiveness. Ireland already has high wage costs relative to our competitor nations and further increases to companies' wage costs will ultimately hinder Ireland's competitiveness and ongoing economic growth.

4. Does the rationale for use of share-based remuneration vary based on the size and/or age of the company? If so, what factors are relevant to

i. Start-up companies
ii. Established small to medium enterprises
iii. Large established enterprises

Chambers Ireland believes that the relative benefits of share-based remuneration vary depending on the size of the company. In the first instance, their complexity and additional administrative overhead cost to operate make them less attractive to SMEs than standard wage based remuneration system. We would like to see changes to the current models of ESS offered in order to increase their accessibility to SMEs and start ups. The current models work better for companies with greater resources to access external expertise, while SMEs find such schemes difficult to

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[1] http://www.competitiveness.ie/Publications/2015/Ireland%20s%20Competitiveness%20Scorecard%202015.pdf

[2] http://ec.europa.eu/internal_market/company/docs/modern/141028-study-for-dg-markt_en.pdf

implement owing to the administrative burdens and complexity involved. The schemes should better take into account the limited resources of SMEs and the Department should consider the introduction of a tailor-made scheme for SMEs to implement ESSs themselves. This would increase uptake and would see the benefits of such initiatives reach more businesses.

Increased uptake of Employee Share Schemes has the potential to offer Irish SMEs and start-ups in particular a comparative advantage in appealing to prospective employees. Especially for start-ups, there is a need to attract talented and dedicated staff, yet they may not have the finances as an early stage business for market rate wages. ESSs should be made more accessible for start-ups and small businesses as a means for them to attract talent in place of high wages. This is one way which the Department can foster and encourage entrepreneurship and facilitate new businesses expansion.

The attraction and retention of talented people is necessary for Ireland's economy and such Employee Share Schemes are also an effective way to retain staff. Such schemes are an excellent way for employers to encourage employee participation, productivity and loyalty, while employees benefit from tax savings and can also enjoy the positive impacts of their company performing well directly. This supports increasing the productivity of Irish companies, as rewards are linked to company performance.

Increased uptake of these initiatives also has the potential to mitigate the erosion of competitiveness arising from general increases to wages which would be a welcome relief to SMEs struggling with increasing wage demands.

5. Is the existing exemption from Employer PRSI for share-based remuneration an efficient use of the State's resources, or could this expenditure be more profitably employed in other forms of support for employment and/ or enterprise?

Chambers Ireland supports the retention of the exemption from employer PRSI for share-based remuneration. This exemption is an incentive to employers to introduce ESSs given the cost saving it allows for, which makes these schemes more appealing in light of the administration burden of their implementation. Given the benefits of such initiatives for companies and the wider economy the tax structures should encourage and facilitate their take-up as amongst both employers and employees.