

Nice little sweetener for the stockpot

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'Penetration of SMEs is well behind many other countries like the US and UK," says the president of the Australian Employee Ownership Association, Tim Mitchell.

Figures are not available on the number of small and medium enterprises with employee share-ownership schemes, but it's generally accepted that the bigger companies have most of them.

The latest data from the Australian Bureau of Statistics shows that only 5.5 per cent of employees received shares as a benefit of employment in 1999 (compared with 2.4per cent 10years earlier). That's low by international standards, which is one reason why the federal government wants to double employee share ownership to 11per cent by 2009.

Part of the reason for the slow take-up is the cost and complexity of setting up the plans. Mitchell estimates that establishment costs can be between \$30,000 and \$50,000.

Lowering the costs associated with setting up share ownership schemes is included in the aims of the government's employee share plans project. Launched in February by the one-year-old employee share ownership development unit within the Department of Employment and Workplace Relations, the unit will test different employee share plan templates in a range of businesses.

Mid-year, those templates are expected to be made available to businesses to help them implement share schemes and reduce costs.

The initiative is a response by the federal government to the Nelson report on employee share ownership in Australia. Already, the unit has developed a free CD ROM and video for employers and human resource specialists to promote employee share ownership.

In the wider business community, employee share-ownership schemes are considered part of a broader package to reward and motivate staff. PricewaterhouseCoopers' Business Insights survey, released this week, shows that people quality and people performance are the leading drivers of Australian mid-sized companies' success.

The survey of 400 companies with profits of between \$20million and \$500million a year finds that 60per cent expect to increase profits in 2004. Moreover, that group is 30per cent more likely to focus on people quality than companies that do not expect higher profits.

They are also 44 per cent more likely to nominate people performance as the major driver of better business performance in the next 12 months. "It's all about getting the human resource package right," says PwC partner Allan Watson, who included employee share plans in that package.

The trend to reward loyal staff coincides with concerns by SMEs that they can't get enough of the right kind of staff when there's strong economic growth. The February Sensis business index for SMEs found that the most important business concern was finding quality staff. Some SMEs are adopting a more ambitious "catch 'em and keep 'em" philosophy. One of the tools to achieve that objective is share schemes.

John Savina, who owns three pharmacies in Townsville, has been looking at introducing an employee share ownership scheme for his team. Like many professionals, he is unable to sell ownership in his partnership directly to staff.

Traditionally, pharmacies, medical surgeries, lawyers, accountants and architects had limited opportunities to give real ownership in their businesses to other staff for several reasons. For instance, professional requirements allow only practicing and registered pharmacists, lawyers or accountants to be owners of the business.

Savina has discussed alternatives to regular share schemes with Melbourne-based Remunerations Strategies Group, which works extensively with the SME sector. RSG director John Day says the solution is to satisfy those interests through notional equity provided under a share replicator plan.

These plans replicate real employee share-ownership plans, but without issuing real shares or options. Replicator plans are often used where the company does not want to use real shares, for reasons including control, minority interest problems or lack of a market.

Replicators provide incentive-based benefits based on the growth and profitability of the organisation. The benefits are provided by participation rights in either funded or unfunded plans. They can be subject to performance and other vesting conditions.

For example, an employee might have to wait until the shares are valued at specific times before receiving the benefit. On vesting, employees can redeem and cash in their performance rights according to their prevailing value, which is measured by reference to the growth and profitability of the employer organisation over the period that the participation rights are held by the employee.

Any type of organisation, listed or unlisted, private or public sector, profit making and non-profit making, can use an unfunded plan. Once established, business owners can invite selected employees to apply for performance rights, for no consideration. "These rights must be issued as a long-term incentive, in addition to any existing fixed remuneration or incentive entitlements," Day says.

The funded replicator plan suits any type of organisation, but it is particularly suited to listed and unlisted, private or public sector non-profit making organisations such as clubs, local, state or federal government departments.

Selected employees are invited to apply for performance rights, funded by way of an interest-free loan of monies to the participating employee. Performance rights may be issued through salary sacrifice, or as matching offers (buy one, get one free), bonus rights or restricted rights that are subject to vesting conditions and/or performance hurdles.

The loan is structured as a non-recourse loan, which means that where the value of the share investments fall below the amount of the loan, employees will be able to surrender their funded performance rights in full and final satisfaction of the debt outstanding on the loan.

Not all replicator funds get the thumbs-up from employers. Privately owned CEATechnologies' 16-year-old fund is no longer issuing shares, although 82per cent of its 180 employees hold shares.

CEA president David Gaul says it was very complex to administer. "People find it hard to get their head around valuing that share," he says.

Last year, CEA started an options scheme that attracted 82per cent of employees. Gaul expected a higher take-up because there was no risk involved, and says he was disappointed. Some employees said the scheme's complexity and their lack of interest in learning about it were the reasons for their non-participation.

There is some upside. Gaul says the company's share plans partly contributed to the firm's high retention rates.

Anecdotal information from consultants who are members of the Australian Employee Ownership Association reveal strong growth where the consultant specialises in servicing SMEs. Consultants like RSG, for example, have had annual growth of 20per cent in the past four years. Not surprisingly, much of that comes from SMEs because, unlike many bigger firms, they are not listed and therefore have no underlying shares to trade.

However, most of the AEOA's membership who were contacted for this article service large listed companies. Rather than predicting share plans being started from scratch, they say existing schemes will probably review their position on options in the lead-up to the change in accounting standards.

