

Abstract: Equity-Based Compensation in Start-Ups and Scale-Ups: A Comparative Regulatory Analysis of the USA, the UK, and Germany | Moritz Jim Tilgner (tilgner@law.eur.nl)

Author: Moritz Jim Tilgner, PhD Researcher at Erasmus University Rotterdam, PhD Candidate in the European Doctorate in Law & Economics (EDLE) program
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ABSTRACT

Equity-based compensation (EBC) is a crucial element in start-ups and scale-ups to attract employees in a competitive environment and to incentivize an entrepreneurial mindset focusing on the company's growth. Across jurisdictions, the regulation and taxation of EBC differs potentially contributing to differences in global highly skilled labor migration and the concentration of start-up and scale-up clusters. While the USA and the UK have long-standing EBC practice and corresponding regulation and taxation, Germany's government is pushing for changes to gain international market competitiveness – i.a. with the first and second Financing for the Future Acts.

The existing literature addressing EBC on a comparative level is incomprehensive given the coverage of only some compensation models and outdated given recent changes in regulation and taxation – especially considering changes in Germany. Furthermore, the policy setters' rationale and the examination of compatibility with rational-choice theory is mostly not considered in the analysis.

To create a comprehensive comparative and up-to-date overview and assessment of the relative theoretical attractiveness of the regulation and taxation of EBC at start-ups and scale-ups from an employee's and employer's perspective in the USA, the UK, and Germany.

The author analyzes the respective regulation and taxation using the comparative legal research (CLR) method and evaluates their attractiveness based on rational-choice theory while considering their respective non-legal context. Key assessment elements include the availability of types and corresponding requirements as well as taxation. The regulators' rationale is identified by analyzing commentary by regulators - e.g. in introductions to laws and drafts, in legislative discussions, and in public communication. The preliminary results show that Germany lags in terms of competitiveness – even when the latest amendments are considered. General EBC issues identified are information asymmetries and conflicts of interest, which will be addressed with an EBC contract optimization model to maximize joint surplus as well as a social welfare optimization model to maximize social welfare.

The findings are expected to be valuable bases for future policy setting and the corresponding cost-benefit analysis weighing economic benefits and tax income, as well as future studies (including a follow-up project by the author assessing the perceived attractiveness of EBC regulation by employees using a discrete choice experiment).