Inter-University Centre Split/Berlin, Institute for Eastern European Studies, Free University of Berlin

The PEPPER IV Report:

Benchmarking of Employee Participation in Profits and Enterprise Results in the Member and Candidate Countries of the European Union

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The PEPPER IV Report: Benchmarking of Employee Participation in Profits and Enterprise Results in the Member and Candidate Countries of the European Union

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Berlin
May 2008

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Preface

This Report summarises and updates the previous PEPPER reports. It is the result of the Commission-funded Project "Assessing and Benchmarking Financial Participation in the EU-27".

Complying with the concept of the PEPPER reports and building on them it provides a solid basis for leveraging the development of Financial Participation in the European Union in the context of the current reform process triggered by the European Commission and Parliament.

The Project closes the gap between PEPPER I/II (1991, EU-12 / 1997, EU-15) and PEPPER III (2006, 10 new EU Member States /4 Candidate Countries). Furthermore it implements benchmarking indicators developed by the European Foundation for the Improvement of Working and Living Conditions in all 27 EU Member States and Candidate Countries.

The PEPPER IV Report has been edited by Jens Lowitzsch (Inter-University Centre), Iraj Hashi (Staffordshire University) and Richard Woodward (CASE Foundation, Poland / University of Edinburgh) and written in cooperation with a core-team of experts in the field of Financial Participation, i.e., Milica Uvalić (Perugia University) and Daniel Vaughan-Whitehead (International Labour Organisation). The European Commission's Directorate General Employment, Industrial Relations and Social Affairs and the Kelso Institute have supported the Benchmarking Project. The editing of the country reports was supervised by Patricia Hetter Kelso. For individual countries' chapters of the PEPPER IV Report, an extensive use was made of the country chapters of the previous PEPPER I-III Reports. The mini survey complementing the CRANET survey was conducted by:

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The Report is divided into three parts. The first part consists of an overview chapter which provides a summary of the Benchmarking Project and the current situation of employee financial participation in countries under consideration, as well as chapters presenting and discussing the benchmarking results, as well as a chapter on the fiscal framework and tax incentives in the EU-27. The second part consists of country profiles, each covering four main issues: (1) a short introductory summary; (2) the general environment for employee financial participation, highlighting the background, the attitudes of social partners as well as government policies; (3) the legal foundations for different PEPPER schemes, including the incentives for application of those; and (4) a brief synopsis of participation in decision-making. The third part of the Report summarises the experience of employee financial participation in Western and Eastern Europe, its role in the changing world of work in the 21st century and its relevance in the context of the European integration process. Finally recommendations and suggestions for further initiatives are made.

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Part 1 – Benchmarking of Financial Participation

I. The Benchmarking Project, the Indicators Employed and the Current Situation in the EU-27

Jens Lowitzsch

1. Introduction

The PEPPER IV Report presents conclusive evidence, regardless of data source, that the past decade has seen a significant expansion of employee financial participation in Europe. This is true of both profit-sharing and employee share ownership, although profit-sharing is more widespread (for details, see Part 1, Chapters II and III). Throughout the European Union, the percentage of enterprises offering various PEPPER schemes is on the rise. Between 1999 and 2005, broad-based share ownership schemes increased from an average of 19% to 26% (unweighted country averages). The percentage of company employees taking advantage of these schemes also is growing.

On the other hand, – despite of this positive trend – it seems that financial participation has been extended to a significant proportion of the working population in only a handful of countries. The increase in all aspects of non-standard employment contracts may exacerbate this problem in future (for details, see Part 3, Chapter II). In order to guarantee the basic Commission principle that financial participation should cover all workers and not only the core labour force, further concrete policy actions to extend broad-based schemes are called for.

A review of the more than 30 years covered by PEPPER Reports indicates that employee financial participation (EFP), though slow to take off, has picked up surprising momentum. Reflecting the two main dimensions of European policy development in this period, i.e., integration and enlargement, the reports document several important advances. (1) Economic

research has empirically confirmed the positive effects of EFP. (2) The principles and definitions of PEPPER schemes were formally incorporated in the 1992 Commission Recommendation. (3) Studies by the European Foundation for the Improvement of Working and Living Conditions from 2000-2004 analysed in depth various aspects of EFP over the course of its evolution and developed the benchmarking indicators. Although the particularly dynamic upturn in some countries (Austria, UK, Ireland) has specific causes, we surmise that the most recent, more general stimulus for the rise of EFP has been the prior Commission activities, i.e., the PEPPER Reports as well as the reviewed strategy for growth and jobs in the EU, the Lisbon-Strategy, and the reform of the labour markets.

The different data sources of the PEPPER IV Report, each confirming the positive trend over time, show that companies offer more opportunities for financial participation (CRANET) than employees actually utilize (ECWS). The shortfall can only partly be explained by the fact that naturally not all eligible employees participate or that schemes are not well communicated. This discrepancy in the different sets of cross country data can be explained by different definitions and methodology as well as diverse perspectives. None of these surveys specifically dealt with the subject of financial participation per se. It should be clearly understood that in this respect the PEPPER IV benchmarking represents a compromise to cope with the existing data deficit without undertaking a new survey.

How should policy makers implement that part of the Lisbon Strategy calling for broadened employee financial participation? The road to these goals has three clearly marked lanes: Construct a legal framework. Promote. Research.

- Utilize optional tax incentives to encourage employee financial participation.

While not a prerequisite for EFP, tax incentives clearly have a positive influence in countries which offer them. Making them optional avoids conflict with national law.

- Legislate EFP at the EU level with a Council Recommendation on a European Platform utilising the Building Block Approach

Resting on the principle of voluntariness, the trans-national Building Block Approach reflects the diversity of schemes, while opening national practise to new forms.

- Research the current state of EFP in the EU with a comparative, focused survey.

No cross country data targeting financial participation exists to date. This data vacume needs to be filled. Policy makers need a clear and precise overview of the *status quo* in order to work towards the goals of the Lisbon Strategy.

a) Recent Initiatives

Both the European Commission and the European Parliament recently launched a new initiative, manifested in the opinion of the Economic and Social Committee of 26 February 2003,[1] on the Commission communication ‘on a framework for the promotion of employee financial participation’.[2] The European Parliament called on the Commission to submit studies on the issues raised in its Resolution of 5 June 2003[3]. Among these were the feasibility of financial

1 SOCI 115, Employee Financial Participation, CESE 284/2003.

2 COM (2002) 364 Final.

3 P5-TA (2003) 0253.

participation in small and medium-sized enterprises and the possibility of implementing in other EU Member States share ownership schemes based on the ESOP (Employee Stock Ownership Plans). In his foreword to the study published in response to this request[4], the President of the European Parliament, Hans-Gert Pöttering, stresses the value of the suggested 'Building Block Approach' therein proposed. This approach provides a broad incentive system made up of diverse and flexible alternative components, which correspond to existing national systems, thereby introducing a flexible European concept.

In the European Reform Treaty signed on 13 December 2007 in Lisbon, the EU for the first time expressly commits itself to the European Social Model as one of the pillars of its policy. Thus, Art. 3 III states that the Union 'shall work for the sustainable development of Europe based on […] a highly competitive social market economy, aiming at full employment and social progress' and that '[…] It shall combat social exclusion and discrimination, and shall promote social justice and protection […].' In 2006, in his foreword to the PEPPER III Report[5], the Commission's Vice-President Günther Verheugen postulated a stronger link between pay and performance as one possible way to reform the labour markets. Further, in September 2007, Mrs. Christine Lagarde, the French Minister for Economy, Finances and Labour, announced that on assuming the Presidency of the European Union in July 2008, France wishes to launch a European Model of financial participation supported by the Member States.[6]

In the light of these remarkable political initiatives and against the background of the positive dynamic of Financial Participation, we surmise that the conditions for further developing employees' financial participation are now especially favourable. Nevertheless, important challenges remain, both old and new, most urgently, the lack of a European legal framework for Financial Participation but also hardening global competition and the strain it is exerting on Europe's enterprises. While the former is familiar and has been addressed in recent initiatives[7] the latter has been fundamentally changing the 'world of work' (see below Part 3, Chapter II) leading to a growing demand for flexibility at the level of the individual firm.

b) To Address Both Challenges…

Both challenges call for implementation of a European platform for Financial Participation while the role of Financial Participation in the reviewed 'Lisbon strategy' needs to be more precisely formulated. The framework conditions set by legislators are an important factor in enhancing the growth of PEPPER schemes, but only a well formulated policy can fully unleash their potential to boost motivation, productivity, and ultimately economic growth and jobs (see below Part 3, Chapter I). To achieve their proclaimed goal of making 'the EU a more attractive place to invest and work in' European policy makers should ensure that the working

4 'Financial Participation for a New Social Europe' by *J. Lowitzsch et al.*, Berlin/Paris/Brussels 2008; the book was distributed in the European Parliament in French, German and English language.

5 *J. Lowitzsch* , 'The PEPPER III Report – Promotion of Employee Participation in Profits and Enterprise Results in the New Member and Candidate Countries of the European Union', Berlin 2006.

6 Speech on 12 September 2007 at the occasion of the 40th anniversary of FONDACT in the French Senate.

7 The European Commission's Directorate General Employment, Social Affairs and Equal Opportunities has supported the project 'A European Platform for Financial Participation' which sets forth both a policy and a detailed proposal for a European concept of employee ownership and profit-sharing; for the project report see 'Financial Participation for a New Social Europe' by *J. Lowitzsch et al.,* Berlin/Paris/Brussels 2008.

people who are to bring about these changes also participate in the fruits of this process, i.e., in profits and ownership stakes in European enterprises.

This is the context in which the question of internal versus external flexibility becomes of crucial importance. In addition to improving employee motivation and productivity, and thus the competitiveness of European companies, financial participation can play an important role in achieving internal flexibility. Flexibility no longer applies only to the options available to companies for production or other needs.[8] The Commission's new Flexicurity approach[9] also looks at flexibility in terms of enhanced mobility in the labour market and in work organisation. Table 1 contains a typology of work flexibility. Locational flexibility (or flexibility of place)[10] was added to the classical types of flexibility[11], i.e., working time, contractual arrangements, variable pay and financial participation as well as functional dispositions. They are grouped into external and internal types; by the internal types of flexibility we mean those that the firm applies to workers within the firm without changing the basic employment relationship, while we use the term external to refer to the interaction between the firm and the external labour market; that is, either to the firm's access to workers outside the firm (as, e.g., in the case of outsourcing) or to its ability to 'expel' workers and thereby 'externalise' them.

Table 1. A typology of work flexibility

Flexibility Category	**Internal**	**External**
Numerical	Working Time (Temporal) ➢ Part time / leave / flexible hours ➢ Overtime / shift / annualisation	Contractual (Employment) ➢ Temporary / Fix-term / Agency ➢ Relaxed hiring/dismissal regulations
Functional (work organisation)	➢ Job rotation / Team work / Task rotation ➢ Workers training/options to bring change	➢ Outsourcing ➢ Restructuring
Locational (spatial)	➢ Tele work / Home work ➢ Out-workers /Relocation within company	➢ Relocation ➢ Off-shoring
Financial / Wage	➢ Variable pay (individual/team related) ➢ Profit Sharing / Share- Option schemes	➢ Downsizing ➢ Financial restructuring

Source: compilation by the author.

It seems that at the national policy level, up to now, contractual flexibility (external / numerical) has been considered the most important aspect of labour market flexibility. Financial participation as a means of providing internal financial flexibility, on the other hand, has received

8 The European commission in its Joint Employment Report addresses this issue of flexibility, calling for an adequate flexibility for both workers and employers (EC, 2006).

9 As defined in the recent EC Communication 'Towards Common Principles of Flexicurity: More and better jobs through flexibility and security', COM (2007) Final (27 June 2007).

10 See C. Wallace 'Work flexibility in eight European countries: A cross national comparison", Sociological Series 60, Vienna, Institute for Advanced Studies, 2003.

11 The definition of flexibility proposed by *J. Atkinson* and *N. Meager* in 1986 distinguishes external numerical flexibility (contractual), internal numerical flexibility (working time), functional flexibility (organisational) and financial flexibility (wages).

much less attention. Moreover, in general, most of the flexibility discussion has been focused on specific arrangements or a specific category of flexibility despite the fact that flexibility is multi-dimensional. There are substitutional as well as complementary effects and the type of flexibility that is developed is just as important as its extent.[12] Increasing internal financial flexibility through financial participation would help to alleviate the pressure on contractual flexibility. This also is in line with many of the general principles of flexicurity held by the heads of states and governments of EU Member States, such as 'a better balance between external and internal flexibility', 'a climate of trust and dialogue', 'a better workers' adaptability capacity', etc. (see below Part 3, Chapter II).

What gives legitimacy to the current discussion of new forms of financial participation is the fact that the radical reforms of the European legal and economic order in the process of the EU's eastward enlargement, together with privatisation and globalisation, have led not only to economic progress but also to widening social fissures. While enterprise profits have been on a steep rise for more than a decade, wages have been stagnant and the economic lives of many have been rendered insecure. The 'society of owners' must be simultaneously understood as the 'society of non-owners'. The growing discrepancy between the few who are rich and the many others who are 'working poor' needs to be addressed.

c) …In the Context of the Current Situation in the EU-27

In the EU–15, more than 19% of employees in the private sector currently participate financially in the enterprise for which they work. These existing schemes constitute a pillar of the European Social Model. In spite of the unsatisfactory results of the PEPPER II Report which followed up the Council Recommendation of 1992, the number of share ownership schemes has seen a strong increase during the last decade (see below Part 1, Chapter II and III). Furthermore, for example in France, the country where PEPPER schemes have had the longest tradition, there has been a gradual increase in the share of variable pay in recent years.[13] This suggests a tendency in some countries to increase workers' income more and more through variable forms of remuneration. On the whole, a generally favourable attitude within a given country has usually led to some supportive legislation for PEPPER schemes, which in turn has spread their practice. This suggests a clear link between national attitudes, legislation and diffusion (see below Part 3, Chapter II). Nevertheless, the European Union still lacks a unified legal foundation on which to build a European system of financial participation.

A quite different situation obtains in the new EU Member States and Candidate Countries[14] (see the PEPPER III Report). Very few laws specifically address employee financial participation, and these refer almost exclusively to employee share ownership[15]; legislation on profit-

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12 *H. Chung, M. Kerkhoffs, P. Ester*, 'Working time flexibility in European companies' European Foundation for the Improvement of Working and Living Conditions, Dublin 2007.

13 Profit-sharing bonuses have increased from 3.1% in 1996 to 4.5% in 2003 of total pay, while 'participation' schemes from 3.8% to 4.6%.

14 Cyprus, Czech Republic, Estonia, Hungary, Lithuania, Latvia, Malta, Poland, Slovakia and Slovenia which joined the EU on May 1st 2004, Bulgaria, Romania on January 1st 2007 and Croatia, and Turkey as Candidate Countries.

15 Employee share ownership has largely developed in the course of recent privatisations, with different methods including sales of enterprise shares to insiders on privileged terms; employee-management buy-outs; leasing; mass privatisation, and ESOPs and ESOP-type schemes.

sharing is rare[16]. Although employees were frequently offered privileged conditions for buying shares of their employer companies, the purpose was not to motivate employees to become more efficient and productive. Nor was there more than mild concern for social justice. Rather, this method was simply an expedient for privatising state-owned enterprises for which at the time there were no buyers. Essentially it was a decision made by default. Given the limited incidence of PEPPER schemes, it is not surprising that empirical evidence on the effects of schemes is available for only some countries – the Baltic States, Hungary, Poland, and Slovenia. Although much of the evidence is preliminary and refers primarily to the 1990s, when employee ownership played a different role than today, these studies suggest that enterprises with employee ownership frequently performed no worse than firms with other ownership forms. The comparative analysis of the general attitude of governments and social partners shows the lack of concrete policy measures supporting PEPPER schemes, as well as limited interest of both trade unions and employer organisations.[17] Rather than being actively promoted as in some old EU Member States, employee financial participation has most frequently not even been considered, or is viewed with suspicion.

2. Responding to the Data Deficit: The Benchmarking Project

The PEPPER IV Report is an interdisciplinary legal and economic comparative study. It provides a Comparative Assessment of Financial Participation in the EU-27 and in the Candidate Countries based on coherent and thus for the first time comparable indicators.

a) Aims

The Project closes the gap between PEPPER I (1991, EU-12), PEPPER II (1997, EU-15) and PEPPER III (2006, 10 New Member States /4 Candidate Countries), and utilizes the benchmarking indicators developed by the Dublin Foundation in all 27 EU Member States and Candidate Countries. It consists of three complementary basic components that build on each other:

- Description of the legal environment, fiscal or other incentives and links to participation in decision-making with a specific focus on schemes for SMEs;
- Benchmarking financial participation, i.e., the scope and nature of financial participation schemes;
- Comparative analysis of the national policies and characteristics that affect the environment for financial participation.

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16 Despite the fact that company laws in several countries do refer to the possibility of employees having a share of company profits, Romania is the only country that has specifically legislated a general scheme for cash-based profit-sharing in state owned companies (though implemented in a small number of firms). Among the non-transition countries, only Turkey has legislation on profit-sharing.

17 Only occasionally have trade unions been supportive of employee ownership, but they remain rather critical of profit-sharing. The employers have been generally indifferent towards financial participation, despite a few cases of active support (as in the case of ESOPs in Hungary).

The final recommendations derived from the comparative analysis, best practise in the Member States and, in the context of the development of ESOPs, that in the United States, set forth both a policy and a proposal for promoting Financial Participation at the European and the National level.

b) Approach

The Benchmarking exercise continues the projects 'Financial Participation of Employees in the New Member and Candidate Countries' and 'A European Platform for Financial Participation' (both successfully concluded) funded under the same budget line and building on the PEPPER reports. It digests their results and data from previous studies (EWCS, EIRO, CRANET, EFES).[18] The purpose of the project is fourfold:

- To systematically assess similarities and compatibility of the laws and practices governing financial participation in the EU-27 and Candidate Countries;
- To close information gaps (i.e., between PEPPER I, II and III) that currently prevent a full profiling of financial participation policy and practice;
- To discuss individual country's scores on the indicators against the background of comparable scores for the other EU Member States, providing a contextual frame of reference for each single profile;
- To further promote a common platform for financial participation within the European Union, in the context of comparative analysis.

An interdisciplinary conference, with key EU experts presenting preliminary project results, took place in October 2007 in Berlin; the PEPPER IV Report was presented in Brussels and in Strasbourg to the European Commission and Parliament in May 2008.

c) Specific Difficulties to be Dealt with

In 2004, the European Foundation commissioned a report that developed 16 specific indicators of financial participation policy and practice facilitating like-for-like comparisons of the financial participation situation in each Member State. The second stage of the process, to 'road test' these indicators, was undertaken in 2005. While nine of the European Foundation's 16 benchmarking indicators were supported by existing data, seven of the measures were not supported at all. The Benchmarking project addressed this data shortage not by undertaking a new study dedicated to financial participation; instead, as recommended by the pilot benchmarking study of Slovenia commissioned by the European Foundation, it referred to existing upgraded surveys (i.e. by the European Foundations 'EIRO Comparative Study on Financial Participation in the New Member States', to whose questionnaire our team contributed input).

Furthermore, the Pilot Study by the European Foundation clearly demonstrated how the Foundation's nine supported indicators can be practically employed to produce a partial profile (in the test case of Slovenia). In order to be independent of new EU-wide surveys, the

[18] EWCS: European Working Conditions Survey and EIRO Comparative Study on Financial participation in the New Member States (both European Foundation for the Improvement of Working and Living Conditions); CRANET E: Cranfield Survey on International HRM (Cranfield School of Management); EFES: Employee Ownership Top 100 (European Federation of Employee Ownership).

work programme initially aimed at such a partial profile using those nine indicators. Including the results of the 'mini survey' of our project partners, additional indicators were added. For individual country's National Sources (see below Part 2, Country Profiles) and 'blank spots' (in some cases for single countries and single indicators), our team provided the necessary supplementary information using our EU-wide network from the previous projects.

The Commission and Parliament identified transnational obstacles to the development of a European model for financial participation, which a High Level Group of independent experts had classified at the end of 2003. Our assessment of the legal environment investigates the possibilities for creating a European legal framework for financial participation. In so doing, the project, as recommended in PEPPER III, builds on the 'Building Block Approach' to combine established schemes in a single program with alternative options and to keep the different elements complementary.

3. The Benchmarking Indicators

a) Sources

There are five main sources for the Benchmarking exercise:

(1) Country Profiles[19]: All 29 target countries (EU-27 + HR, TR) are briefly described in respect to Evolution of financial participation schemes, Social Partners' Attitudes, Current Government Policy and Legal framework. These profiles are supplemented by input from the team of experts.

(2a) The CRANET Survey[20]: As an e-survey of the human resource departments of companies having at least 200 employees, the survey of 2003/2005 covered 18 of our target countries (17 EU + TR) and the 1999 survey 14 EU countries.

(2b) Mini Survey: Our project survey closed the CRANET gap (PT, IE, and PL, LT, LV, MT, RO, HR) with a mini survey; as a result the data embraces 28 target countries (EU-26 + HR, TR) and enables a comparison with data from the 1999 CRANET survey for 14 EU countries.

(3) The European Working Conditions Survey (EWCS)[21]: A household survey in all 29 target countries (EU-27 + HR and TR) covering in the 3rd and 4th survey rounds nearly 30,000 workers, facilitates a comparison between data from 2000/2001 and 2005.

(4) The European Employee Ownership Top 100 Index[22]: Information from all EU-27, from the largest 2300 listed and 200 unlisted companies, providing comparative data from 2006 and 2007.

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19 Sources: PEPPER I, II, III Reports, EIRO Survey and our Project Expert Network in the field.

20 Collected by the Cranfield School of Management

21 Collected by the European Foundation for the Improvement of Working and Living Conditions.

22 Collected by the European Federation of Employed Shareholders (EFES)

b) The Indicators and their Link to the Commission Principles

Each of the Benchmarking Indicators selected complies with one of the essential principles of financial participation schemes set forth by the Commission in its communication seeking 'a framework for the promotion of employee financial participation'[23]. (Nevertheless, sufficient data for all of the chosen indicators for the screening was not available.)

- Principle 1: Participation must be voluntary for both enterprises and employees.
- Indicator: Legislative and fiscal support for financial participation.

The Country Profiles provide detailed information on whether specific legislation concerning financial participation exists and whether tax relief is given. Furthermore, the overview of taxation systems and tax incentives distinguishes between incentives for firms and employees, on the one hand, and for profit-sharing and share-schemes on the other.

- Principle 2: Access to financial participation schemes should in principle be open to all employees (no discrimination against part-time workers or women).
- Indicators: Percentage of enterprises offering broad-based financial participation schemes to employees and percentage of employees covered by financial participation.

CRANET measured this as the percentage of organisations offering financial participation to each of the three occupational non-managerial grades. In terms of the all-employees criterion, the assumption is that organisations that offer financial participation to a particular grade do so for all employees within that grade. Furthermore, CRANET indicates whether financial participation is offered to four separate occupational grades and the percentage of each organisation's workforce that falls into each occupational grade. Putting the two pieces of information together, it is possible to calculate the percentage of employees in each organisation that are offered financial participation.

- Principle 3: Schemes should be set up and managed in a clear and comprehensible manner with emphasis on transparency for employees.
- Indicator: Percentage of employees participating in financial participation.

The 4th EWCS asks whether the remuneration includes payments based on the overall performance of the company (profit-sharing scheme) and/or income from shares in the company the respondent works for.

- Principle 4: Share ownership schemes especially will almost inevitably involve a certain complexity, and in this case it is important to provide adequate training for employees so as to enable them to assess the nature and particulars of the scheme in question.
- Indicator: Countries with direct/indirect and consultative/delegative participation in decision-making.

The Country Profiles give an overview of the different types of participation in decision-making practised in different countries. Unfortunately, sufficient data for the screening of this indicator was not accessible. The available empirical evidence suggests that incentive effects of financial participation are much greater when accompanied by greater worker participation in decision-making.

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[23] COM (2002) 364 Final, 5 July 2002, pp. 3, 10.

- Principle 5: Rules on financial participation in companies should be based on a predefined formula clearly linked to enterprise results.
- Indicators: Percentage of employees whose financial participation is calculated on a predefined formula and the percentage participating in regular ongoing schemes.

The 4th EWCS asks whether payments are calculated on a predefined formula and whether these payments are received on a regular basis.

- Principle 6: Unreasonable risks for employees must be avoided or, at the very least, employees must be warned of the risks of financial participation arising from fluctuations in income or from limited diversification of investments.
- Indicator: European Employee Ownership Top 100 Index.

Sufficient empirical data for the screening of this indicator was not available. However, the information from the European Employee Ownership Top 100 Index permits an assessment of one dimension of risk through matching financial participation in quoted companies with their performance on the stock markets.

- Principle 7: Scheme must be a complement to, not a substitute for, the existing pay system.
- Indicator: Percentage of enterprises in which financial participation and regular salary are kept separate and distinct.

Sufficient empirical data for the screening of this indicator was not available.[24] Nevertheless, a good test for this indicator is to examine whether negotiations on the two issues take place separately and at different times; however, there is a danger of respondent bias (employers may be reluctant to give any information which could suggest salary substitution).

- Principle 8: Financial participation schemes should be developed in a way that is compatible with worker mobility both internationally and between enterprises.
- Indicator: Legislative and fiscal support for financial participation.

The Country Profiles look at specific financial participation schemes that are suitable for cross border use. The overview of taxation systems and tax incentives provide complementary information about this dimension of financial participation.

[24] The 2008 European Establishment Survey of the European Foundation for the Improvement of Working and Living Conditions envisages to include questions that could permit an assessment of this indicator.

4. Overview of Financial Participation in the EU-27

Table 2. The old Member States of the EU

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Belgium	**[A] TU** opposed, but relatively more support for profit-sharing; **EA** in favour; **[B]** Since 1982, legislation for ESO; amendment 1991; since 1999 legislation for stock options; since 2001 new law on ESO and PS.	**All plans:** EmpC max.20% of after tax profit / year; max.10% of total gross salary; **ESO:** NCL - discounted ES in JSC, financing by firm possible; in capital increases: max. 20% of equity capital, ES discount limit 20%; NTL - (restricted stock grant) value reduced by 16.7%, taxation deferred if 2 years not transferable, 15% tax on benefit, no SSC; (stock purchase plan) benefit tax base 83.33% of fair market value; **SO:** NTL - since 1999 taxed at grant on a lump sum basis, no SSC; **PS:** NTL - tax 15% for PS in an investment savings plan, 25% for other plans.	2005 Cranet: **ESO** 21%, **PS** 3.7%; 2005 EWCS: **ESO** 4.3%, **PS** 5.9%; firms involved mainly from financial sector, large firms and multinationals; **SO** 2005 Cranet: 2%; EU Report 2003: 75,000 employees' benefit; most of 20 largest Belgian firms operate plans; 40% of firms with more than 50 employees.
Den-mark	**[A] TU** indifferent to FP; **EA** opposed to any extension of employee participation; **[B]** Employee Funds discussed in 70s/80s, PS popular; later support for ESO and SO; in 2000s Government support for share-based schemes.	**ESO:** NCL - ES in JSC: discounted, max. 10% of salary/year, 7-year holding period, free max. 8,000 DKK/year; financing by firm possible if qualified plan; in capital increases deviation from subscription / pre-emption rights possible; NTL - deferred taxation of benefit,; EmplC: discount tax deductible; **PS:** NCL - SPS; NTL - max. 10% of annual salary; **SO:** NTL - broad-based max. DKK 8,000, 5-year holding period; individual max. 10% of annual salary or max. 15% difference exercise price / market price.	2005 Cranet: **ESO** 36%, **PS** 7.3%; 2005 EWCS: **ESO** 2.4%, **PS** 6.4%; **SO** 2005 Cranet: 2%; EU Report 2003: 20% of 500 largest firms by 1999, 1/3 of quoted firms 2000.
Germany	**[A] TU** sceptical / partly hostile because of 'double risk'; **EA** support individual firms **[B]** Traditional focus on savings plans (total capital higher than that of ES-firm plans); FP	**ESO:** NCL - discounted ES in JSC, financing by firm possible; state savings bonus of 18% of max. 400 EUR (72 EUR/year) invested in employer stock; no tax / SSC on max. 135 EUR /	2005 Cranet: **ESO** 11%; **PS** 45%; 2005 EWCS: **ESO** 0.8%,**PS** 5.3%; 2005 IAB: **ESO** 3%, **PS** 12%; 2003 WSI: **PS** in 1/3 of firms;

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
	since 2006 on political agenda of all parties.	year employer matching contribution; **PS:** None **SO:** NCL - in capital increase, nominal amount restricted to 10%, that of increase to 50% of equity capital.	**ESO:** 2006 AGP, 3,000 firms, 2.3 mln. empl., 19 bln. EUR; **SO:** EU Report 2003, in over 2/3 of DAX-listed firms.
Greece	**[A] TU** moved from scepticism to support in 1980s; **EA** indifferent, low priority not a current topic; **[B]** Some regulations on CPS (1984) and ESO (1987); since 1999 more attention on SO; not a current issue.	**ESO:** NCL – ES in JSC discounted or free; within capital increase for 3years not transferable, up to 20% of annual profit; NTL -no PIT/SSC on benefit; **SO:** NCL - free/discounted; NTL - taxable at exercise; tax exempt if qualified plan; **PS:** NTL - max 15% of company profits, 25% of employees' gross salary; no PIT, but SSC.	2005 Cranet: **ESO** 23,6%; **PS** 9.4%; 2005 EWCS: **ESO** 1%, **PS** 2.8%; **SO:** 2005 Cranet 2%; **SO** EU Report 2003: only a limited number of firms.
Spain	**[A]** Low priority: **TU** oppose income flexibility; **EA** ambivalent, fear information disclosure requirements; **[B]** Long tradition of social eco-nomy: COOPs (new law 1997) and **EBO**; **PS** supported in 1994 then shift to **ESO/SO**; active support.	**ESO:** NCL - ES/SO in JSC, financing by firm possible; NTL - tax benefits on PIT after 3year holding period; **PS:** NLL; **SO**: NTL - after 2 year holding period 40% reduction of taxed plan benefit; **EBO:** 'Workers Companies' with more than 51% ESO, 10-25% of profits in Reserve Fund; NTL - if 25% reserve, tax exempt from capital transfer tax; tax on formation/capital increase, notary fees.	2005 Cranet: **ESO** 5.7%, **PS** 17%; 2005 EWCS: **ESO** 0.5%, **PS** 6.4%; **ESO**: 2003 CNMV 20% of large firms with share purchase plans; **SO:** 2005 Cranet: 19%; EU Report 2003: plans in 40 firms of which 1/2 in IBEX 35; **EBO:** 2003 Heissmann, appr. 15.000 'Workers Companies'.
France	**[A] TU** show mixed attitudes: sceptical but actively involved, favour if not substitute to pay; **EA** generally in favour, esp. if voluntary; **[B] PS/ESO** strong continuous support since 1959; also in privatisations; climate FP-friendly, focused policy.	**ESO:** PrivL - 5% ES-reserve, max.20% dis-count; NCL - discounted ES in JSC, financing by firm possible, also capital increase; Save-as-you-earn schemes; NTL - flat rate tax of 7.6% and 10% on returns, no SSC; **SO:** NCL - capital increase; NTL - tax on exer-cise gain 26-30% after 4year holding period **ESOP/EBO:** Law on Trusteeship 2007; NCL - special reserve for EBO possible; **PS:** DPS compulsory/CPS voluntary; NTL - flat rate tax	2005 Cranet: **ESO** 34%, **PS** 92%; 2005EWCS: **ESO** 5.3%,**PS** 12%; 2004 FONDACT: DPS covered 53% of non-agriculture private sector firms employees (i.e. 6.3 million); **SO:** 2005 Cranet 3%; **SO** EU Report 2003: approx. 50% of quoted firms and 28% of limited companies, total approx. 30,000 employees.

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
		7.6-10% if paid to firm savings-scheme/fund after 5 year holding period.	
Ireland	**[A] EA** strong support; **TU** support if financial and intrinsic reward to employees; managers / employees pragmatically motivated; Lobby groups / Institutions e.g. banks for **ESO;** **[B]** Support in privatisation; improvements in 1995 and 1997; promoting voluntary adoption of SPS, e.g. Approved Profit-Sharing Scheme (APSS).	**ESO:** PrivL - 14.9% ESOT-stock paid for by loan/by state; NCL - ES/SPS in JSC, financing by firm possible; NTL - New Shares: limi-ted PIT tax base deduction for Empl., no SSC; **SO:** Savings-Plan: bonus/ interest on savings tax-free, no PIT on grant/exercise, no SSC; Approved-Plan: no PIT at exercise, no SSC; **ESOP:** Trust Act - taxed 15% interest / 10% investment; NTL - ESOT: tax incentives as for APSS if ESOT part of APSS; **PS:** NTL - APSS: at transfer no PIT, no SSC up to limit, salary foregone - up to 7.5% of gross salary deductible.	1999 Cranet: **ESO** 14%, **PS** 15%; 2005 EWCS: **ESO** 5.3%, **PS**,9.2%; **SO:** 2002 IBEC: 90 firms with SAYE schemes, 15 firms with Approved Share Option Schemes; **PS:** 2002 IBEC: 400 firms with APPS; **ESOP:** n.a.
Italy	**[A] TU** mixed attitudes, recent-ly interested in topic **/ EA** mostly supportive; **[B]** Trilateral agreement 1993 supported **PS**; then shift to support **ESO/SO**; recently discussed on political agenda.	**ESO:** CivC - discounted ES in JSC, financing by firm possible; in capital increases deviation from pre-emption rights and preferential 'ES' possible; NTL - PIT exemption up to max 2,065 EUR after 3-year holding period; **PS:** NCL- no SSC on max. 5% of total pay; **SO:** NTL - PIT exemption up to max 2,065 EUR after 3-year holding period.	2005 Cranet: **ESO** 13,7%, **PS** 6.2%; 2005 EWCS: **ESO** 1.4%, **PS** 3.1%; **SO:** 2005 Cranet 1%; EU Report 2003, approx. 6% of employees involved.
Luxem-burg	**[A] TU/EA** growing interest in 1990s, not supportive of share schemes; **EA** support profit-sharing; **[B]** FP not a current issue.	**ESO:** NCL - ES in JSC, financing by firm possible; **SO:** NTL – 'Tradable Option Plans' reduced tax burden; **PS:** None.	2005 EWCS: **ESO** 3.7%, **PS** 13.5%; **PS:** PEPPER II, 1995 CPS in 25% of firms, mainly banks; **SO:** EU Report 2003, estimates 25% of firms - mainly financial sector; **ESO:** n. a.
Nether-lands	**[A] TU/EA** generally in favour; **TU** support if supplement to pay, prefer PS to ESO; **[B]** Traditional focus on savings plans; support for SO in 2003.	**ESO:** NCL - ES in JSC, financing by firm possible; NTL - up to EUR 1,226 from pre-tax salary after 4 years in a savings plan 15% flat tax, no SSC; **PS:** NTL - up to EUR	2005 Cranet: **ESO** 20%, **PS** 44.8%; 2005 EWCS: **ESO** 1.5%, **PS** 13.8%; **PS:** 3 Mln. participants in 2000; **SO:** 2005 Cranet 4%; EU Re-

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
		613 from pre-tax salary after 4 years in a savings plan 15% flat tax, no SSC; **SO:** NTL – specific tax incentives abolished; **IEnt:** Qualified Savings Funds.	port 2003, more than 80% of all listed firms.
Austria	**[A] TU/EA** currently support FP and cooperate; diffe-rent views about participation in decision-making **[B]** Legislation since 1974; first tax incentives since 1993; more active support since 2001.	**ESO:** NCL - discounted ES in JSC; financing by firm possible; NTL - PIT/SSC allowance for benefit; CGT or ½PIT for dividends; tax exemption for share sale gain; **IEnt:** NCL - Empl. Foundation: EmpC buys own stock, sheltered in IEnt, dividends paid out; NTL - EmpC: contribution to IEnt, setting-up/ operation cost deductible; IEnt: tax allowance on contributions; Empl.: CGT on dividend s; **SO:** NCL - capital increase: nominal amount max. 10%, increase max.50% of equity capital; max.20% of equity capital for total amount of shares receivable; NTL - 10% of benefit/year, but max.50% of total benefit tax-free and carry forward of taxation for the remaining amount; **PS:** None	2005 Cranet: **ESO** 12%, **PS** 32.8%; 2005 EWCS: **ESO** 1.2%, **PS** 5.4%; 2005 WKÖ/BAK: **ESO** 8%, **PS** 25%; **SO:** 2005 Cranet: 2%; 2005 WKÖ/BAK: 1%
Portugal	**[A] TU/EA** Indifferent, low priority: **TU** prefer PS to SO; **[B] ESO** mainly supported in Privatisation, esp. around 1997; not on the Agenda; FP is generally ignored.	**ESO:** PrivL - discounted ES; NCL - ES in JSC, financing by firm possible; in capital increase: suspension of pre-emptive right of shareholders for 'social reasons' possible; **PS:** NLL - not remuneration, no SSC; **SO**: NTL – 50% of share sale gain liable to PIT.	2008 PEPPERIV: **ESO** 5.3%, **PS** 28% 2005 EWCS: **ESO** 0.9%, **PS** 1.9%; **SO:** EU Report 2003, from 60 firms listed at Euronext Lisbon Stock Exchange, about 22% have implemented SO.
Finland	**[A] TU / EA** generally support FP, especially desire to improve the environment for personnel funds; other forms not discussed; **[B]** Discussions on FP since the 1970s; 1989 law on Personnel Funds (the major form until now).	**ESO:** NTL - discount tax-free, no SSC; tax relief for dividends; **SO:** None; **PS:** Cash-based none; NCL - share-based 'Personnel funds': in firms with more than 30 employees, if all participate, registration with Ministry of Labour, after 5 year blocking period up to 15%/year can be	2005 Cranet: **ESO** 14%, **PS** 66%; 2005 EWCS: **ESO** 0.7%, **PS** 11%; **PS:** 2007 54 Personnel Funds with 126,000 members; **SO:** 2005 Cranet 5%; 2003 EU Report: 84% of companies listed at Helsinki Stock Exchange.

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
		withdrawn; NTL - 20% of payments to employee tax-free; earnings of fund tax-free.	
Sweden	**[A] TU** neutral / opposed, advocated Wage Earners' Funds; **EA** favour PS for wage flexibility, but no active support; **[B]** From 1992 – 1997 tax incentives for PS in firms; since then no support.	**ESO:** NCL - ES in JSC, financing by firm possible; in capital increase suspension of pre-emptive right of shareholders possible; **PS:** Cash-based none; NCL - share-based 'Profit-Sharing Foundations': 1/3 of employees on similar terms, after dissolution assets to be distributed; NTL - for the employer 24.26% payroll tax instead of 32.28% SSC; **SO:** None.	2005 Cranet: **ESO** 16%, **PS** 26%; 2005 EWCS: **ESO** 1.6%, **PS** 15%; **PS:** 2003 Heissmann: 15%; Wage Earners' Funds created in 1983 were abolished in 1991.
UK	**[A]** Climate FP friendly and supportive; **TU** involved, but reservations: prefer SO to PS; **EA** positive, favour flexibility with regard to form of schemes; employees interested; **[B]** Long tradition of FP, esp. ESO and ESOP; now more active support for SO i.e. SAYE and Sharesave; 2000 new of Enterprise Management Incentives EMI; very little participation in decision-making.	**ESO:** NTL - Share Incentive Plan (SIP) discounted: no PIT/SSC; no dividend tax if dividends reinvested in shares, generally no SSC; no CGT if sale immediately after taking shares out of the plan; **SO:** NTL - Savings-Related SO-Plan, Firm SO-Plan: generally no PIT at grant or exercise, no SSC; SAYE: tax bonus on savings; EMI: no PIT, no SSC at grant or exercise; (NCL - Empl. Benefit Trust used); **ESOP:** NCL - max. £ 125/month shares for pre-tax salary in Trust, EmpC max.2 matching shares / share worth max. £ 3,000/year; NTL - shares exempt from income tax and SSC after 5 years; EmpC contribution to trust tax deductible; **PS:** NTL - approved PS; tax benefits abolished in 2002.	2005 Cranet: **ESO** 19%, **PS** 13%; 2005 EWCS: **ESO** 1.9%, **PS** 6.4%; 2006 ifsProShare: **ESO/ SO** approved plans in 5,000 firms, some with **ESOP**s; SIP in 830 firms; **SPS:** 2002 1 Mln. empl. under approved schemes, average/ head less than £ 700; **SO:** 2005 Cranet: 2%; 2006 ifsProShare: Savings-Related Plans in 1,300 firms, 2.6 mln. empl.; Company Plans in 3,000 firms; EMI in 3,000 firms.

Table 3. The new EU Member States and Candidate Countries

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Empl.
Bulgaria	**[A] TU** open to FP, **EA** indifferent; not a current topic on either of their agendas; **[B] ESO** strong support 1997-2000 since then ignored; in 2002 PrivL incentives abolished; FP generally ignored	**ESO:** None; NTL - Uniform 7% dividend tax; **PS:** None; NTL - SPS personal income tax exempt.	2005 Cranet: **ESO** 38%, **PS** 5%; 2005 EWCS: **ESO** 1.8%,**PS** 6.3%; **ESO:** 10% Mass-Priv, 4-5% Cash-Priv; low, decreasing; **MEBO:** 1,436, 28% privatisations; managers took over most; **PS:** AI, few cases survey evidence; **SO:** 2005 Cranet 14%.
Cyprus	**[A]** FP not an issue on **TU** / **EA** agendas; **[B]** FP so far ignored.	**ESO:** NCL - discounted ES in JSC; financing ES by firm possible; NTL - dividends/gains from share sale tax-free; **PS:** None.	2005 Cranet: **ESO** 10%, **PS** 7.7%; 2005 EWCS: **ESO** 1.2%, **PS** 2.7%; **SO:** 2005 Cranet: 4%; **ESO/PS:** AI, insignificant.
Czech Republic	**[A] TU / EA** indifferent to FP, not a current topic on their agendas; **[B] ESOP** discussed in 1990; FP ignored after introduction of voucher concept.	**ESO:** NCL - discounted ES/SPS in JSC; not considered public offering; ES discount limit: 5% of equity capital, financing by firm possible; NTL - uniform 15% dividend tax; **PS:** NCL - CPS/SPS in JSC; NLL: negotiable in collective bargaining agreements.	2005 Cranet: **ESO** 14%, **PS** 27%; 2005 EWCS: **ESO** 1.6%,**PS** 11%; **SO:** 2005 Cranet: 3%; **ESO:** Insignificant; 0.31% of the privatised assets; **PS:** AI, insignificant.
Estonia	**[A] TU** indifferent to FP, **EA** opposed to any extension of employee participation; **[B]** PrivL supported **ESO** until 1992; after 1993 FP ignored.	**ESO:** NCL rights attached to shares issued before 1 Sept.1995 remain valid; no public prospectus for ES needed; NTL Emp.: no income tax on dividends from resident firms; EmpC: 22% on distributed profit, only 'bonus issue' in capital increase exempt; **PS:** None.	2005 Cranet: **ESO** 9.6%, **PS** 11%; 2005 EWCS: **ESO** 2%,**PS** 11%; **ESO:** 2005 2% (1995 after privatisation 20%) of firms majority employee owned, 20% minority; **PS:** AI, survey evidence, very few cases.
Hungary	**[A]** FP for managers means to avoid external control, for employees to preserve workplace; **TU** lobbied **ES/ESO** in privatisation, recently passive; **EA** indifferent; **[B] ESOP/ES** strong support in PrivL until 1996; climate FP friendly but lack of concrete economic policy decisions.	**ESO:** PrivL - preferential sale; discount max. 10% firms assets and 150% of annual min. pay, instalments; Decree '*Egzisztencia*' Credit; NCL - specific 'ES' in JSC, discounted / free, max. 15% of equity capital, financing by firm possible; since 2003 tax-qualified stock plans, first 0.5 mln. HUF free, then 20% tax, 3-year holding period; **SO:** NTL – PIT base is value at exercise;	2005 Cranet: **ESO** 15%, **PS** 15%; 2005 EWCS: **ESO** 1%,**PS** 3%; **ESO:** 1998 1% of assets privatised; preferential privatisation in 540 firms; CS strong decline; now AI, 30% of firms (70% SO, 30% ES), mostly foreign; **ESOP:** initially 287 employing 80,000, in 2005 151 left; 1.2% of employment by private firms;

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Empl.
		ESOP: ESOP-Law 1992; preferential credit; corporate tax exempt until end 1996; contribution to Plan max. 20% tax deductible; tax base lowered; **PS:** None.	**PS:** AI, 20% of firms, mostly fo-reign, only 10%of entitled recei-ve profit; **SO:** 2005Cranet 27%.
Latvia	**[A] TU / EA** indifferent to FP, not a current topic on their agendas; **[B]** Little support for **ESO** in PrivL; FP so far ignored.	**ESO:** PrivL - max. 20% ES; specific 'ES' in state / public firms; NCL - preferential ES in JSC free / dis-counted, in capital in-creases max. 10% of equity capital non-voting stock; **PS:** None.	2005 EWCS: **ESO** 0.6%,**PS** 8.5%; **ESO:** PrivL 110.6 mln. vouch-ers to 2.5 mln. people; AI, 1999 16% of 915 firms domi-nant ESO but falling over time; **PS:** AI, 7% of firms; mostly IT, consulting, real estate.
Lithua-nia	**[A]** Climate FP friendly; **TU** interested, lack of actions; **EA** support indi-vidual firms; **[B] ESOP/ES** strong support in PrivL until 1996; now FP not on po-litical agenda of Parliament and Government.	**ESO:** PrivL - 5%ES deferred paym. max.5 years; NCL - in corporations ES for 3 years non transferable/non voting, financing by firm possible; NTL - uniform 15% dividend tax; after holding period profits from sale of shares not taxed; **PS:** None.	2008 PEPPERIV: **ESO** 4%, **PS** 36%; 2005EWCS: **ESO** 0.9%, **PS** 4%; **ESO:** low and decreasing; AI, 2000 36% (1995 92%) priva-tised firms dominant ESO, falling over time; **PS:** AI; CPS mostly foreign (IT, consulting, advertising, etc); DPS few cases 2005 linked to employee savings plan.
Malta	**[A] TU** support schemes in practice; FP not a cur-rent topic in national tri-partite dialogue; **[B]** FP collateral effect of nationalisation (1980's) and privatisation (1990's) not a current issue.	**ESO:** NCL – ES in corporations, exempt from prospectus/investment rules; max. 10% discount, financing by firm possible; NTL - SO only taxable at exercise; **ESOP:** Trust Act refers to FP; taxed 15% interest / 10% investment; **PS:** mentioned in NLL.	2005 EWCS: **ESO** 0.7%,**PS** 3.9%; **ESO:** AI; banking sector: ES, SAYE scheme, SO; **ESOP:** AI, Trust Funds in Bank of Valetta / Malta Tele-com; **PS:** AI; 2004 public sector (Shipyard 1,761 employees); private (foreign) firms, mostly reserved for management.
Romania	**[A] TU** support indiv. cases; **EA** avoid topic; Tripartite council tackled FP sporadically; **[B] ESO** supported until 1997 esp. **MEBO**; then support declined; current government gives little support and has other priorities.	**ESO:** PrivL - aim 30% of privatised assets Vouchers/ES; Vouchers free; 10% discount ES; NCL - ES in JSC, financing by firm possible; NTL - 10% dividend tax; **ESOP:** PrivL on Empl. Associations; leveraged transaction, preferential credit, max. interest rate 10%; **PS:** Ordinance – CPS compulsory in State/Municipal firms.	2008 PEPPERIV: **ESO** 6%, **PS** 42%: 2005EWCS: **ESO** 1.6%, **PS** 5%; **ESO:** ES 10% of shares issued at privatisation, decreasing; **ESOP:** 1998 1/3 priv., most frequently used single method 2000: 2,632 firms, average 65% ESO, 1,652 majority ESO; **PS:** estimated 1.2 mln. empl in

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Empl.
			public sector covered.
Poland	**[A] TU/EA** indifferent to FP; managers / employees pragmatically motivated; Lobby groups / Institutions e.g. banks for **ESO;** **[B]** FP Supported in early privatisation period; **ESO** in most privatisations, since mid-1990's more and more ignored; **PS** increased emphasis in the context of collective bargaining agreements.	**ESO:** PrivL - 15% ES for free, 2 years non transferable, max. value 18 month min. pay, *National Investment Funds* 1995 (NIF), shares for symbolic fee; NCL - ES/SPS in JSC, financing by firm possible; NTL - uniform 15% dividend tax; **EBO:** PrivL - *Leverage Lease Buy-Out (LLBO)*, anticipated ownership transfer possible; interest 50% of refinance rate; interest part of lease payments are costs; Insolvency Law - buy-out right; **PS:** NCL - CPS/SPS in JSC.	2008 PEPPERIV: **ESO** 40%, **PS** 26%; 2005EWCS: **ESO** 0.7%, **PS** 5%; **ESO:** low and declining; AI in privatised firms, 2000 ca. 11.4% (1998 12.7%); NIF adult citizens 1 share in 15 funds; **EBO:** LLBO 2002 1/3 of privatisations, most frequently used sin-gle method, 1,335 firms employing 162,000, 14% over 250 empl; **PS:** AI, limited to management.
Slovakia	**[A] TU / EA** indifferent to FP, not a current topic on their agendas; **[B] ESOP** discussed in 1990; **EBO** concept failed 1995; FP now generally ignored.	**ESO:** NCL - discounted ES and SPS in JSC; max.70% discount/ financing by firm possible; **PS:** NCL - CPS/SPS in JSC.	2005 Cranet: **ESO** 12.7%, **PS** 17%; 2005 EWCS: **ESO** 2.3%, **PS** 28%; **SO:** 2005 Cranet 10%; **ESO:** Insignificant; AI, banking sector / new privatisations; **EBO:** AI, in privatisation, usually management-led.
Slovenia	**[A] TU/EA** very supportive to FP; Employee Ownership Ass. lobbies legislation; active support by Works Councils / Managers Ass.; **[B]** Strong political support to FP; draft laws 1997/2005 in parliament rejected; new Law on FP in 2008.	**All Schemes:** since 2008 70% tax relief for PS and ESO with 1-year holding period (100% relief with >3-year); max. 20% profits or 10% total salaries/year and max. 5,000 EUR / employee; **ESO:** PrivL - max. 20% ES for Vouchers; Vouchers free, shares for overdue claims; NCL - ES/SPS in corporations; discount / financing by firm possible; **EBO:** max. 40%, shares 4 years non-transferable; Worker association proxy organisation under Takeover Law; **PS:** PrivL - SPS in internal buy-out.	2005 Cranet: **ESO** 14%, **PS** 20%; 2005 EWCS: **ESO** 2.6%,**PS** 18%; **ESO/EBO:** 90% of privatised firms; CS 1998 60% majority. ESO while only 23% of capital (2004 18% strong decline); **PS:** CS, in statutes of 32% of firms, but unexploited in 22%; for board members 20% of listed firms; **SO:** 2005 Cranet 4%.
Croatia	**[A] TU** recently promote **ESO** in revision of privatisation; **EA** indifferent to FP; long tradition of Self-management; **[B] ESO** supported until 1995, since then FP ig-	**ESO:** NCL - ES in JSC financing by firm possible; NTL - Dividends tax exempt; profits from sale of shares not taxed; **ESOP:** general rules of NCL apply; **PS:** None.	2008 PEPPERIV: **ESO** 34%, **PS** 29%; **ESO:** 2005 more than 10% of value of privatised firms (1996 20%); 2004 12% firms with majority ESO; **ESOP:** Survey evidence,

Country	**General attitude** [A] Social Partners [B] Government	**Legislation and Fiscal or other Incentives**	**Schemes and their Incidence** CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Empl.
	nored; ESOPs planned in new PrivL.		ESOP elements in 9,4% of firms (52 out of 552), completed ESOP approx. in 1/4 of them; **PS:** AI.
Turkey	**[A]** Climate FP friendly; **TU** supportive, **EA** undecided, split; employees interested; **[B]** FP issue 1968 in Tax Reform Commission; some attention in individual privatisations; 2002 program, lack of concrete measures.	**ESO:** PrivL decrees for individual firms; discount / instalments; NTL - after 1 year share-sale profits not taxed; for SO limited tax on dividends/profits from sale; **IntE:** NCL / CivC 'welfare/mutual assistance funds' of firms; financing by firm profits/contributions; **PS:** NCL / CivC both CPS and SPS; max. 10% prior reserve.	2005 EWCS: **ESO** 1.3%,**PS** 2.4%; 2005 Cranet: **ESO** 4.4%, **PS** 8.9%, **SO**, 1%; **ESO:** AI, PrivL 12 cases 9-37% ESO, 1case majority, up to 15%discount; SO/ESO private firms mostly foreign (26 registered 35 applications) 2007 survey evidence: 3-4% of publicly traded companies; **IntE:** N.A.; **PS:** AI, retained profits as dividends widespread; CS 38 out of 50 listed firms; 2007 survey evidence: 20% of publicly traded companies.

Source: PEPPER I-IV and: CNMV 2003; CRANET 2005/1999 (firms with more than 200 empl.); EU Stock Options Report 2003; EWCS 2005 (take-up rate); FONDACT 2004; Heissmann 2003; IAB 2005; IBEC 2002; ifsProShare 2006; WKÖ/BAK 2005; WSI 2003; please note that the country data of the different surveys is incoherent due to inconsistencies in methodology and definitions. *Excluded from studies*: Management Buy-out, General Savings Plans, Consumer and Housing Cooperatives;

Abbreviations: AI = Anecdotal Information only; CGT = Capital Gains Tax; CivC = Civil Code; CPS = Cash-based Profit-sharing; CS = Case Studies; DPS = Deferred Profit-sharing; EA = Employer Associations; EBO = Employee Buy-out; EmpC = Employer Company; ES = Employee Shares; ESO = Employee Share Ownership; ESOP = Employee Share Ownership Plan; FP = Financial Participation; IEnt = Intermediary Entities; JSC = Joint Stock Companies; MEBO = Management-Employee Buy-out; NCL = National Company Law; NLL = National Labour Legislation; NTL = National Tax Legislation; PIT = Personal Income Tax; PrivL = Privatisation Legislation; PS = Profit-sharing; SO = Stock Options; SPS = Share-based Profit-sharing; SSC = Social Security Contributions; TU = Trade Unions.

II. Availability of Financial Participation Schemes in EU Companies

Iraj Hashi and Richard Woodward

Any benchmarking exercise, especially one involving a large number of countries, relies on the availability of comparable and consistent data. While there are a large number of studies on the impact of employee participation on firm performance[25], there are very few sources of information on the availability and take up of financial participation schemes across countries. There are three main sources of information on FP schemes in European countries on which the discussion of this chapter and country reports are based. These three sources, briefly described below, are very different from each other and need careful interpretation.

(I) CRANET Survey - This is a survey of companies with more than 200 employees[26] undertaken by the Cranfield School of Management (Cranfield University, U.K.) approximately every four or five years since 1992. It is largely a postal survey, sent to the Human Resources departments of companies with the main aim of investigating the human resources characteristics and practices of these companies. One section of the questionnaire is concerned with employees' remuneration and its components. In this section there are questions on whether the company offers any FP scheme (specifically, share ownership, profit-sharing or stock option schemes) to various occupational groups of employees (management, professional and technical, administrative, and manual workers). In 2005, the Survey covered xxx companies in 32 EU and non-EU countries (except Croatia, Ireland, Latvia, Lithuania, Luxembourg, Poland, Portugal and Romania). Because of the postal nature of the survey, the response rate is rather low (15% in 2005). The CRANET sample is selected randomly from the population of companies with more than 200 employees and is designed to represent the size and sectoral distribution of companies in the population.[27] The companies included in the sample are selected separately in each round of the Survey, thus the data is no in the form of a panel. In order to have a complete picture of all Member and Candidate Countries of the European Union, we undertook a mini-survey in five of the missing countries (Croatia, Latvia, Lithuania, Poland, Portugal and Romania).[28] The mini-surveys covered only those parts of the CRANET questionnaire related to remuneration and the general information about the company, thus

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25 These studies are usually concerned with individual or a small number of countries and use different methodologies in pursuing their objectives.

26 The 2000 Survey covered companies with 100 or more employees. The unit of investigation in CRANET is an 'organisation' or a 'business unit'. While this may include a self-contained subsidiary of a larger company, in general they coincide with the boundaries of 'companies'. For the sake of simplicity, therefore, we refer to them as companies.

27 For more detailed information on the CRANET Survey, see CRANET (2005) and Pendleton, et al. (2001).

28 Another survey is currently underway in Ireland (expected to produce comparable information); the mini-survey was also undertaken in Latvia but it showed no financial participation scheme. Luxembourg has been excluded from the benchmarking exercise.

were comparable to the CRANET survey. It is essential to note that the CRANET Survey does not indicate the incidence of FP schemes in companies but only their availability. Furthermore, for the purpose of this research, we have been concerned with broad-based FP schemes (i.e., schemes covering more than 50% of employees) in private companies only as profit-sharing or share ownership are largely not applicable to publicly owned companies (which do not make 'profit' as such and do not always have shares to distribute to employees).

(II) European Working Condition Survey - This is a large survey of individuals undertaken by the European Foundation every four or five years. The 2005 Survey covered some 30,000 individuals in 31 countries (including all EU Member States and Candidate Countries as well as some non-EU countries). As with the CRANET Survey, this survey is concerned with all aspects of working conditions and the subjects are randomly selected individuals. These surveys are conducted by face-to-face interviews and consequently the response rate is higher (48% in 2005). One section of the questionnaire deals with remuneration and sources of income, asking the respondent whether they receive any income in the form of profit-sharing or any income from the ownership of shares in the companies for which they work. Given that individual subjects may be employed, unemployed, self-employed or retired, the present survey is only concerned with the individuals who are in employment. The survey does not always distinguish between employees of the public or private sector. Unlike the CRANET survey which only shows the availability of FP schemes to employees, the EWCS represents the actual take up of these schemes. However the data applies to all employees, irrespective of the size or ownership of their companies.

(III) European Federation of Employee Share-ownership (EFES) data - For many years, EFES has been collecting data on the scale of employee share-ownership in large European companies. The population of this data consists of companies traded on the stock exchange of European countries and a number of large non-quoted companies. The emphasis of this dataset is not on financial participation schemes in general but only on share ownership and only in large companies.

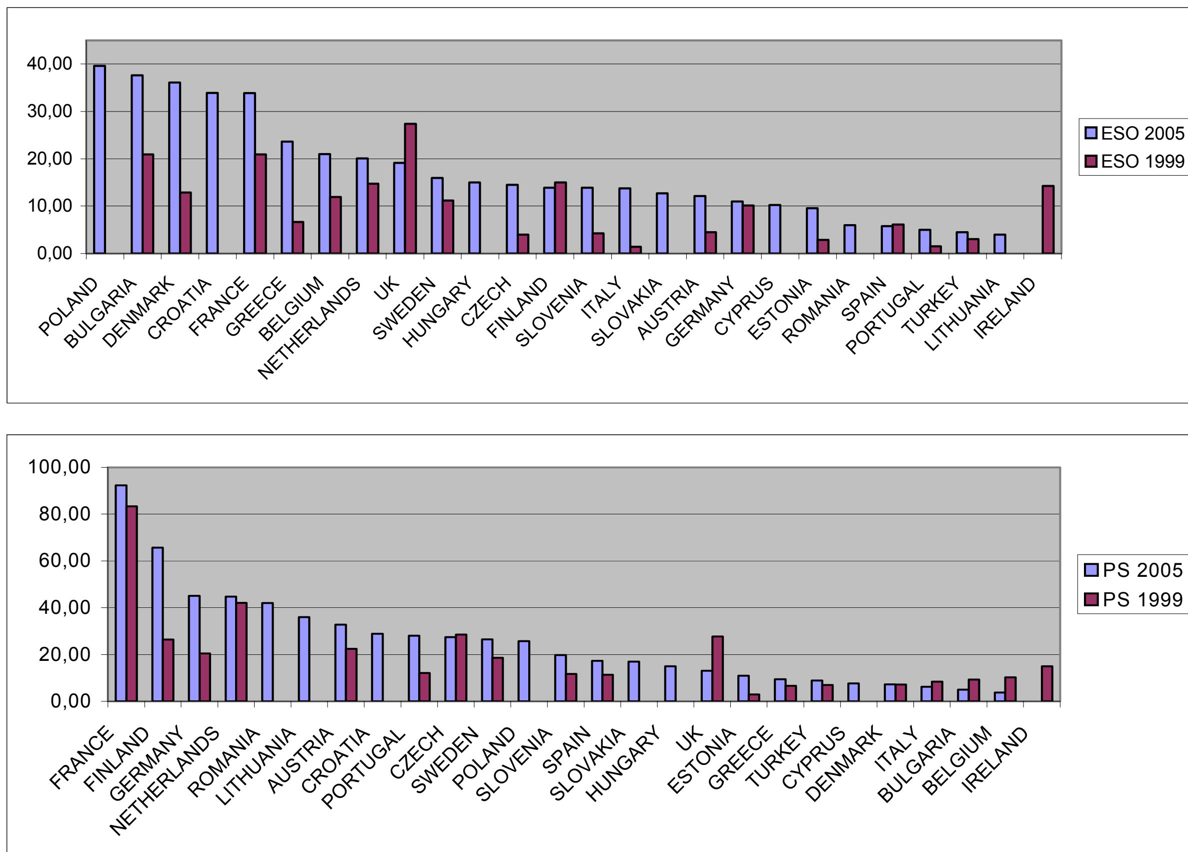
To sum up, it is clear that the three sets datasets are not comparable to each other as they refer to different indicators of financial participation. They should be seen as complementary, each highlighting different feature(s) of the development of employee financial participation.

1. Percentage of Firms Offering Broad-Based Financial Participation to Employees

We begin with a look at broad-based employee share ownership (ESO) plans on the basis of data from the CRANET survey of companies (supplemented with data we collected in an independent mini-survey). Figure 1 shows the percentages of companies with broad-based ESO and profit-sharing plans in 1999 and 2005 in 26 European countries (including five from our mini-survey). As we see in Figure 1, between 1999 and 2005, ESO grew in almost every country except the UK and marginally in Spain and Finland (the unweighted country average grew from 10 to 18%). If we look at the five leading countries in 2005 (ranging from 33 to 40%), we see that three of them (Poland, Bulgaria, and Croatia) are transition countries (indeed, the absence of Slovenia from this group is surprising, as the country's privatization pro-

gram generated a large amount of employee ownership); Denmark and France are the other two. The three lowest-ranked countries are Portugal, Turkey, and Lithuania (Latvia, covered in our mini-survey, is omitted, as the survey carried out there showed 0% for all measures of employee financial participation; we should also note that there are no observations for Ireland for 2005). Estonia is also one of the last-ranked countries, indicating the low incidence of ESO in the Baltic States generally. Spain's low ranking, combined with Portugal's, also indicates the low level of coverage in the Iberian Peninsula. It is interesting that Denmark is far ahead of other two Nordic countries (Sweden and Finland), which might indicate a divergence of that country from at least some aspects of the 'Scandinavian model.' We note that Finland was ahead of Denmark on this measure in 1999, and that Denmark's leadership is thus a recent development owing to what seems to be extremely strong growth of ESO there in recent years. Finally, it is also interesting to note that Hungary, the Czech Republic and Slovenia have such similar levels of coverage (all are middle-ranked) in spite of the very different privatization methods used in those countries. This is possibly an indicator of convergence of ownership structures in the transition countries.

Figure 1. Incidence of broad based profit-sharing and employee share ownership schemes in European countries, 1999 and 2005



Sources: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania).

Figure 1 also shows us how broad-based profit-sharing has developed between 1999 and 2005. Again we generally see growth, except in the UK, the Czech Republic, and the last-ranked countries (Belgium, Bulgaria, and Italy); the unweighted country average grew from 19 to 25%. We see a much wider range of results than in the case of ESO (for ESO, coverage ranges from 4 to 40%; for PS from under 4 to over 92%). It is not surprising that France is the leading country, far ahead of all others, as deferred PS is mandatory there. The second-ranked country is Finland. Germany, the Netherlands and Romania are fairly similar, with coverage between 40 and 50%. The lowest-ranked countries (with coverage under 10%), in ascending order, are Belgium, Bulgaria, Italy, Denmark, Cyprus, and Turkey.

It is interesting to note that two of the countries among the highest-ranked for ESO – Bulgaria and Denmark – are among the lowest-ranked for PS.

2. Percentage of Employees Covered[29]

Next, we look at the percentage of employees in the sample covered by ESO and PS plans. This is an indicator of the extent to which broad-based employee financial participation plans have been adopted in each country. We present data on this subject in Figure 2.

Looking at employee share ownership, we see that, as with the rise in the number of companies offering ESO plans, the coverage of employees by these plans is also growing in a large majority of countries (the unweighted country average grew from 12 to 18% between 1999 and 2005). The three leaders (with employee coverage averaging over 50%) are the UK, France and Poland. There is a fairly long tail of low-ranked countries (with coverage averaging under 10%). In ascending order starting from lowest, these are: Spain, Lithuania, Hungary, Italy, Czech, Turkey, Estonia, Slovenia, and Germany. Again, Slovenia's position here is surprising, given its privatization history. It is also interesting to note that Portuguese companies seldom offer a plan, but those that do are large, with many employees (see Figure 3 below).

Turning to PS, we see growth, albeit slower and from a higher starting point (the unweighted country average rose from 19 to 24% between 1999 and 2005). Here again we have a much wider range, from 100% in France down to under 1% in Cyprus, and again we have a long tail of low-ranked countries. After France, other leading countries (with over 50%) are (in descending order): Finland, Germany, the Netherlands, and Portugal (Romania is just under 50%).

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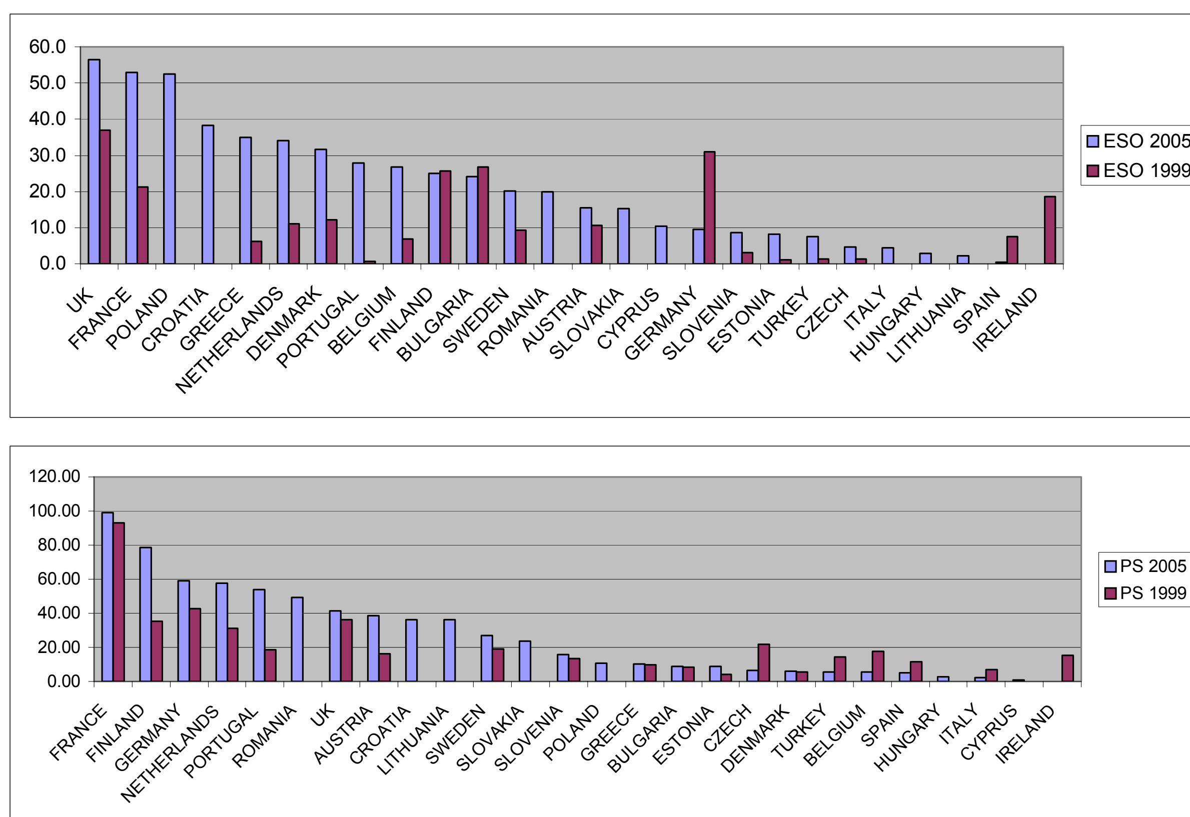
[29] The questionnaire contains questions on the proportion of different categories of employees (managers, professionals, administrative and manual) to whom FP plans are offered and on the share of these different categories in the total workforce of the company. This allows us to calculate the number of employees in each company to whom FP plans are offered (and their share in the total no. of employees in the sample for each country).

scending order): Finland, Germany, the Netherlands, and Portugal (Romania is just under 50%).

Figure 2. Coverage of employees by profit-sharing and employee share ownership, 1999 and 2005



Source: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania).

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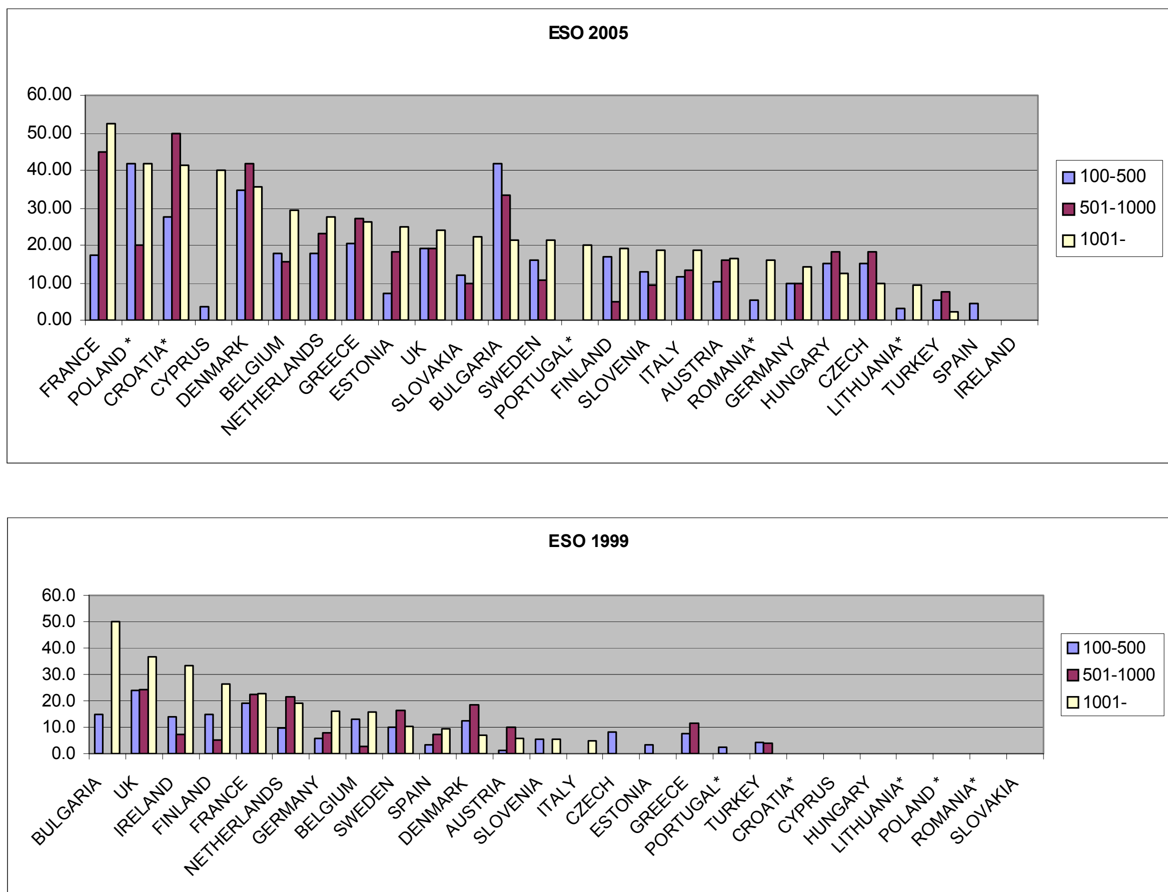
We are also interested in how employee financial participation might differ across firms with respect to firm size and sector of business activity.

The breakdown according to size is shown in Figures 3 and 4. The size categories can be described as medium (100-500 employees), large (501-1,000 employees) and very large (1,001 or more employees). On the average both forms of employee participation are found in the largest percentage of very large companies, with comparable (and lower) percentages being found in medium and large companies.

Figure 3 shows data regarding ESO. While the highest incidence is generally in the largest firms, we see notable exceptions in Poland, Bulgaria, Denmark, and Croatia, which have high percentages of medium-sized firms with ESO, though in the case of Denmark and Croatia it is the middle group of large companies that has the highest rate of incidence.

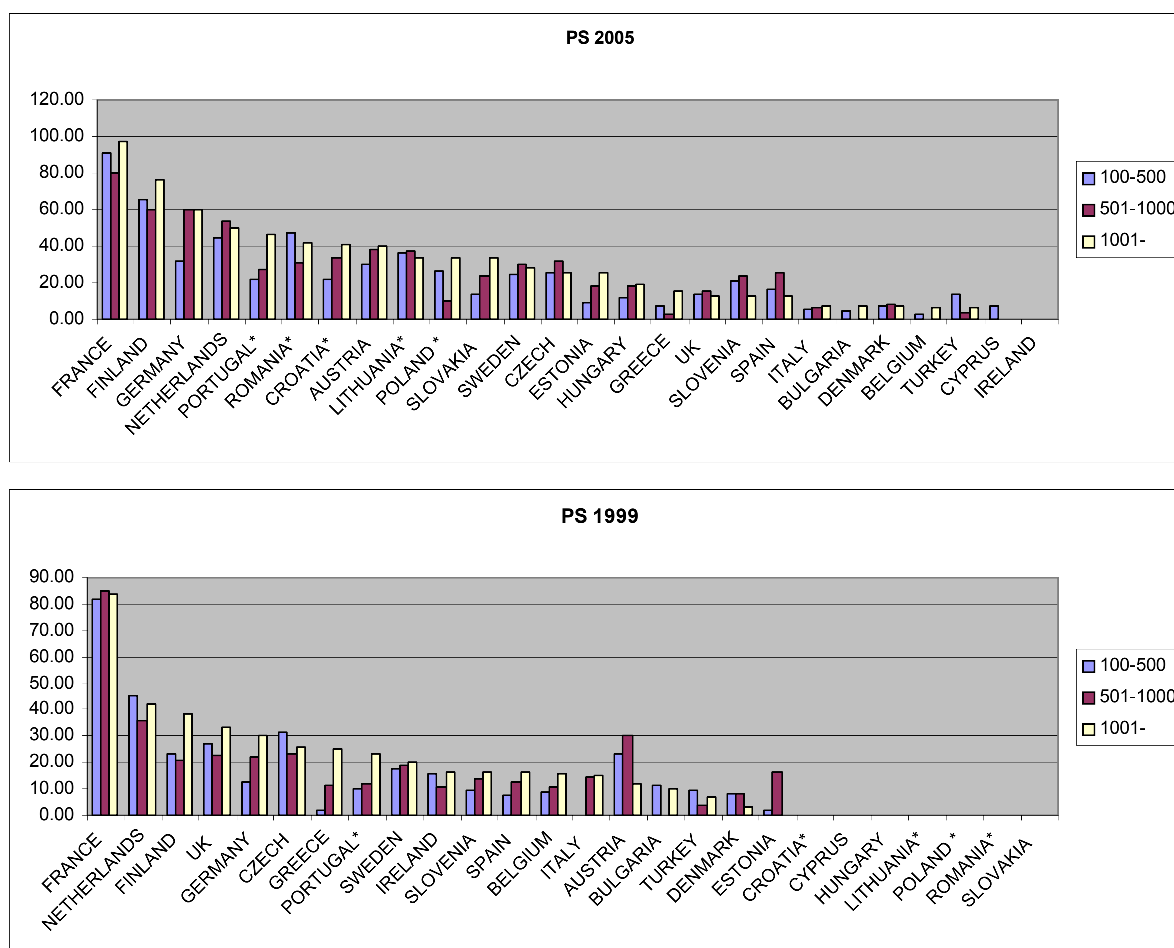
Figure 3. Employee share ownership by firm size, 1999 and 2005 (%)



Source: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania - for 2005).

Figure 4 shows data regarding PS. There is a much more even distribution across size classes here than in the case of ESO, although here again we see a dominance (albeit a mild one) of the largest firms. This situation appears to have changed little over time.

Figure 4. Profit-sharing by firm size, 1999 and 2005 (%)



Source: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania - for 2005).

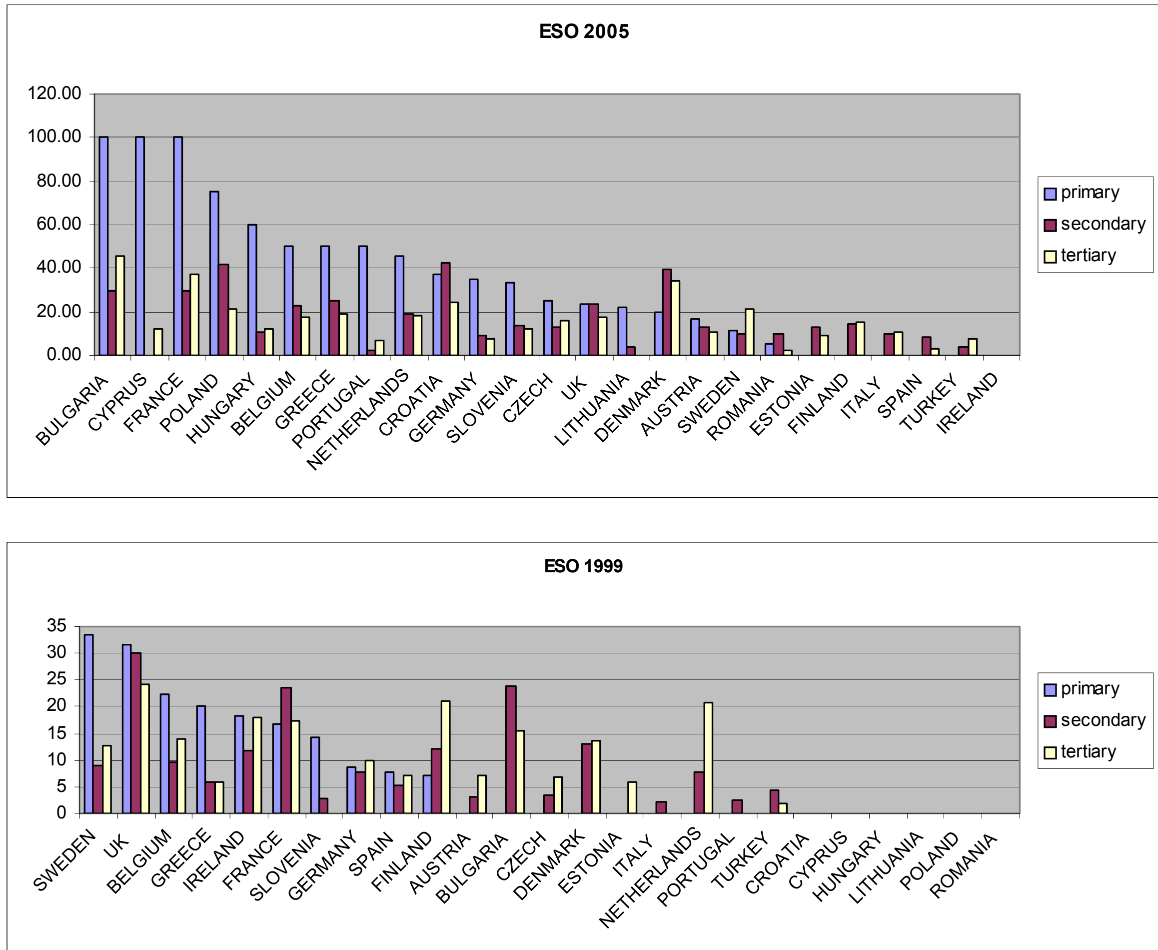
We present sectoral breakdowns in Figures 5 and 6, classifying firms into one of three sectors: primary (basically, agriculture and extractive industries), secondary (manufacturing), and tertiary (services). For 2005, we see a high average rate of incidence of both ESO and PS in the primary sector. However, this is mostly likely a statistical artifact due to the very small percentage of firms in the sample from that sector, and we see no such pattern for the 1999 data. The really interesting differences would be between the service (tertiary) and manufacturing (secondary) sectors in which the vast bulk of the workforce in a modern economy is found.

With respect to ESO, based on the information contained in Figure 5, there is little differentiation between these two sectors on the whole. In Poland and Croatia (countries for which we lack 1999 data), we see significantly more ESO in the secondary sector, while in there is significantly more ESO in the tertiary sector in Bulgaria and Sweden[30]. In others, the tertiary and secondary sectors are close, with one of the two slightly dominating, or virtually identical. In 1999, we see strong secondary sector dominance in France and Bulgaria, and strong tertiary sector dominance in the Netherlands, Finland and Ireland. It is, however, difficult to say

[30] This appears to be the case for Cyprus as well, but only because there are no secondary sector companies in the Cypriot sample.

whether the changes between 1999 and 2005 reflect only changes in the sample or broader trends (especially given the generally much lower rates of incidence in 1999). It is perhaps worth noting the significant drops in the UK (which can also be seen in Figure 1).

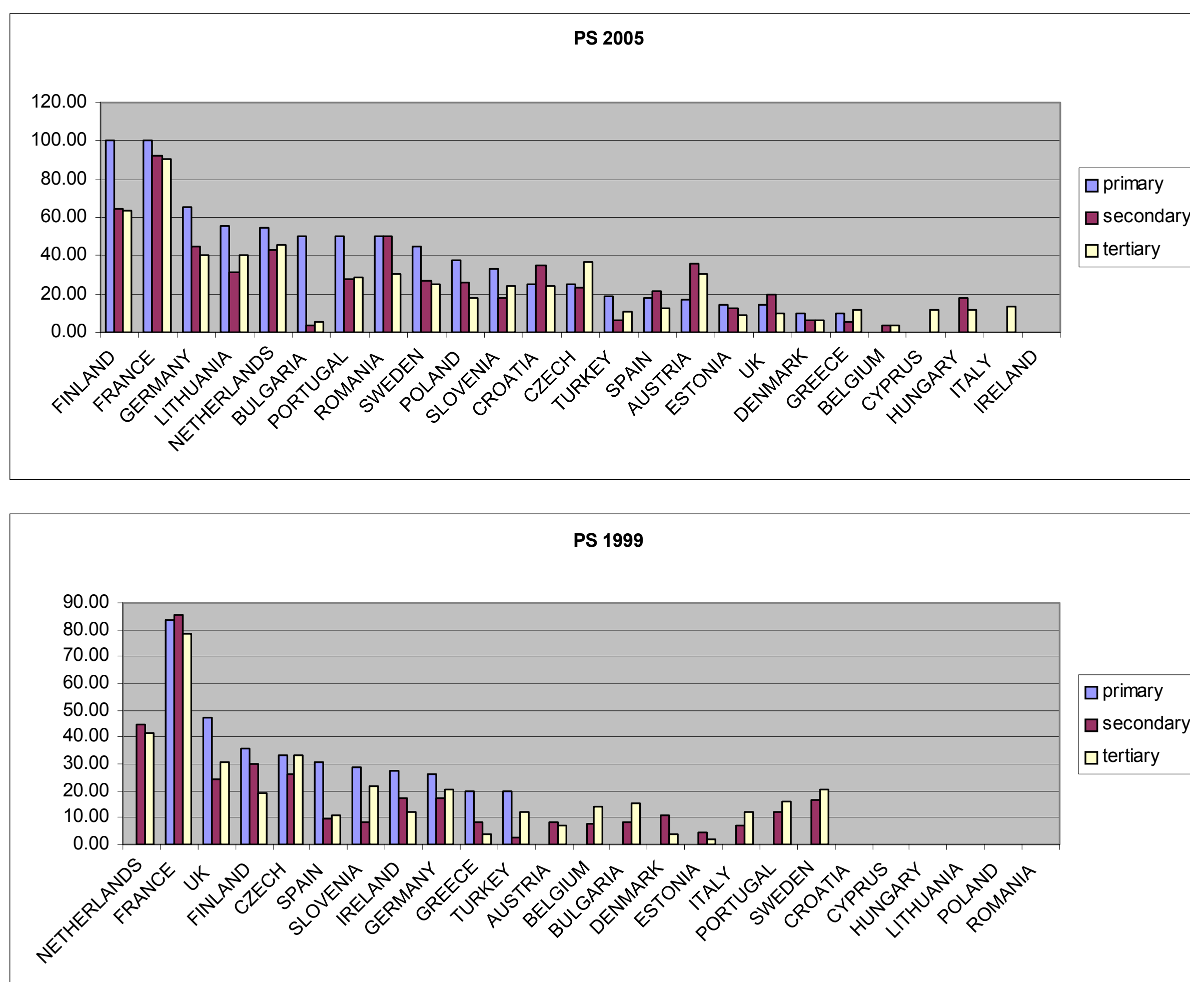
Figure 5. Employee share ownership by sector, 1999 and 2005



Source: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania – for 2005).

Figure 6 contains information on PS. Again, we generally observe a higher incidence in the secondary than tertiary sector, though for the most part the rates of incidence in the two sectors are quite similar. This was also largely the case in 1999, when overall incidence was lower across the board.

Figure 6. Profit-sharing by sector, 1999 and 2005



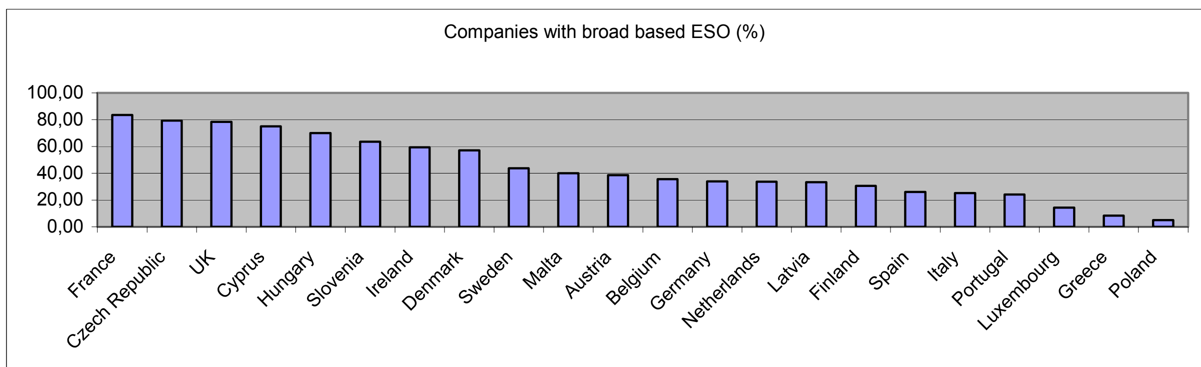
Source: CRANET data and own survey (Croatia, Lithuania, Poland, Portugal, Romania – for 2005).

3. Percentage of Large (Listed) Firms with Employee Share Plans

The European Federation of Employee Share Ownership (EFES) has a database covering almost 2,500 companies, including over 2,200 of the largest publicly traded corporations and roughly 200 large, privately held companies in 29 European countries (these are the 27 EU Member States with the addition of Switzerland and Norway; we ignore the latter two in our discussion). The data on broad-based ESO in those companies presented in Figure 7 were gathered in 2006 and 2007. On the basis of the data contained therein, we arrive at a quite up-to-date picture of the incidence of broad-based ESO schemes in the largest European companies, which we can contrast with the picture emerging from the CRANET survey. (Note that five countries – Bulgaria, Estonia, Lithuania, Romania and Slovakia – have values of 0% and are therefore not included in the figure.)

While it is not surprising to find France, the United Kingdom and Ireland with high rates of incidence of broad-based ESO plans among large companies, the presence of the Czech Republic (represented by 34 companies in the sample), Cyprus (only four companies) and Hungary (20 companies) among the group of leaders is quite surprising. Denmark ranks high, which is consistent with the CRANET data, and so does Slovenia, which is what we expected, but did *not* find in the CRANET data. Poland and Bulgaria, which were leaders in the CRANET data, are in the rear here. (If the CRANET and mini-survey data for these countries is reasonably representative, this would tend to indicate that ESO plans are concentrated in smaller and mid-sized companies in those countries, which would be quite unusual, although perhaps consistent with the Polish privatization program's emphasis on restricting management-employee buyouts to SMEs.) However, the relatively low positions of Romania and the Iberian and Baltic countries in the CRANET data are replicated here and thus seem to provide quite strong corroboration for the CRANET picture of those countries. The high ranking of Hungary and the Czech Republic here and their mid-level ranking in the CRANET data seem to indicate that something is going on with respect to the dissemination of employee ownership in those two countries which has thus far eluded the attention of researchers, probably due to the low level of employee participation in the privatization programs of those countries. It would seem that, contrary to the experience of a number of other transition countries, post-privatization ownership structure evolution has brought more, rather than less, employee ownership to those countries (possibly because of the policies of foreign investors?).

Figure 7. Proportion of large EU companies with broad-based ESO schemes, 2006-2007



Source: EFES.

III. Take-Up Rate of Financial Participation Schemes in the Workforce

Iraj Hashi and Richard Woodward

1. Percentage of Employees Participating in Financial Participation Schemes

The data from the EWCS survey presented in Figure 8 should give us a picture of the extent of employee financial participation in the population of employed persons, as this is a survey of individuals rather than firms. As in the case of CRANET, it covers both ESO and PS schemes, and gives us figures for two years (2000/2001 and 2005), allowing us to draw some conclusions about the rate of diffusion of these schemes in recent years.[31]

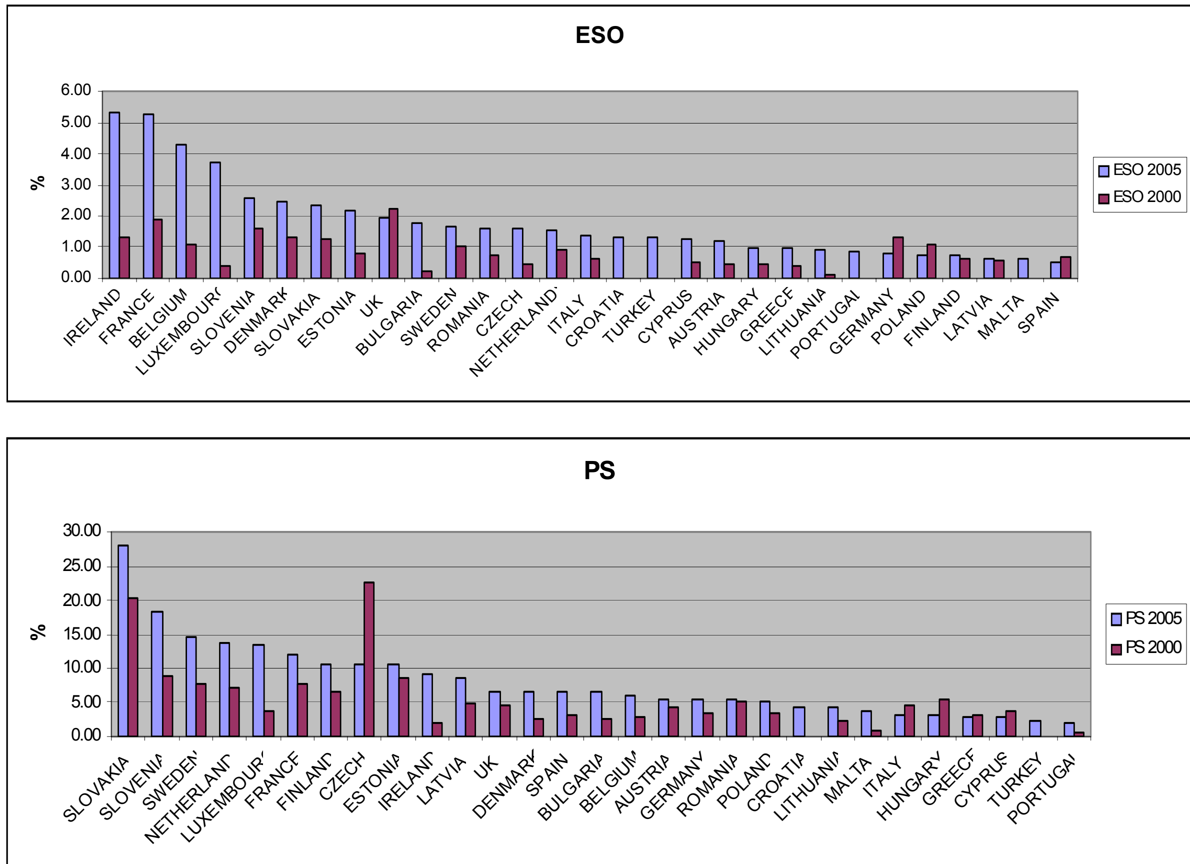
For ESO schemes, as in the case of the CRANET, we see growth in almost all countries (the country unweighted average rose from 0.8% to 1.8%). The exceptions were the UK, Germany, Poland, and Spain (the UK and Spain saw declines in both the CRANET and EWCS surveys). The top countries (with participation rates over 3%) were Ireland, France, Belgium, and Luxembourg (France is the only one of these in both the CRANET and EWCS top country lists, although Ireland also does well in the EFES survey). The lowest-ranked countries (with participation rates under 1%), in ascending order, were: Spain, Malta, Latvia, Finland, Poland, Germany, Portugal, Lithuania, Greece, and Hungary (Portugal, Spain and Lithuania ranked similarly low in both surveys; the low ranking of Latvia and Lithuania again confirms the low incidence of ESO in the Baltic countries). We see strongly contrasting figures for Poland, which ranks highest in the mini-survey data and lowest in the EWCS survey (and also very low in the EFES survey).

Turning to PS schemes, again as in CRANET, we see a much higher incidence than in the case of ESO (for ESO, the 2005 country unweighted average was 1.8%, for PS 8.0, and the range for ESO was 0.5-5.3, whereas for PS it was 1.9-28.0). As in CRANET, we see growth in almost all countries (the country unweighted average rose from 5.6% to 8.0%). The exceptions were the Czech Republic, Italy, Hungary, and Cyprus (Czech Republic and Italy saw declines in both CRANET and EWCS). The top countries (with participation rates of over 10%), in descending order, were: Slovakia, Slovenia, Sweden, Netherlands, Luxembourg, France, Finland, the Czech Republic, and Estonia (with France, the Netherlands and Finland ranking high in both the CRANET and EWCS surveys). The last-ranked countries (with participation rates under 3.5%), in ascending order, were: Portugal, Turkey, Cyprus, Greece, Hungary, and Italy (Turkey, Cyprus and Italy ranked poorly in both CRANET and EWCS). The high ranking of Slovakia is very surprising, and we suspect that this may be due to misunderstandings about the types of bonuses which can actually be considered to be forms of profit-sharing.

[31] The earlier survey was done in two stages: EU-15 in 2000 and accession and other countries in 2001.

We also see high rates of ESO and PS for two countries for which recent CRANET data were not available: Luxembourg and Ireland.

Figure 8. Profit-sharing and employee share ownership 2000-2005



Source: EWCS.

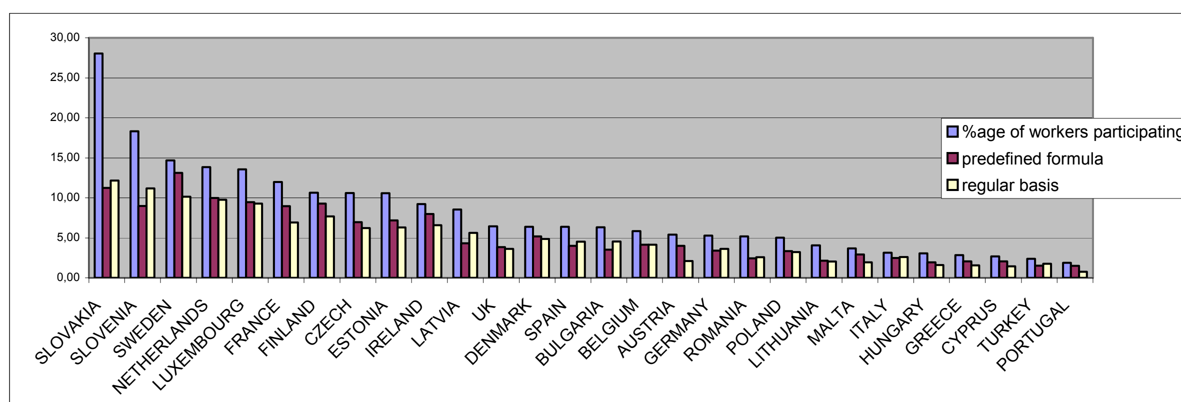
2. Percentage of Employees Participating in Profit-Sharing Schemes with Pre-Defined Formulas on a Regular, Ongoing Basis

To refine our picture of profit-sharing somewhat, we wish to distinguish profit-sharing schemes run according to pre-defined formulas and providing payments to employees on a regular, ongoing basis from those that are dependent on the discretion of employees' superiors and thus do not provide any ex ante incentives to employees to improve their performance at work. To do this, in Figure 9 we present EWCS data for the year 2005 showing the total extent of profit-sharing schemes (that is, the percentage of the workforce that participates in such a scheme), of those which are run according to pre-defined formulas, and of those under which payments occur on a regular, ongoing basis. In all cases we see that profit-sharing schemes operating with high-powered incentives cover a smaller proportion of employees than those covered by schemes referred to (possibly incorrectly) as profit-sharing.

Regardless of which of the three categories is used to rank the countries, there is little difference in the rankings. So although we speculated in section 1 that the high ranking of Slovakia might have been due to a misunderstanding of what exactly constitutes profit-sharing, this point of view is weakened by the country's strong showing when the question is asked more precisely. Using a strict definition of profit-sharing, we see that in the best cases approximately 10% of the workforce is covered.

The leading countries, independent of the category used to rank them, clearly include Slovakia, Slovenia, Sweden, the Netherlands, and Luxembourg. (It is strange to see France coming in behind these countries.) In the rear are, equally as clearly: Portugal, Turkey, Cyprus, Greece, and Hungary. Given the similarity of results for more precisely defined types of profit-sharing and the general results presented in section 1, the comparison with the results from the CRANET survey and our mini-survey here is basically the same as it was there.

Figure 9. Profit-sharing in 2005: A closer look



Source: EWCS.

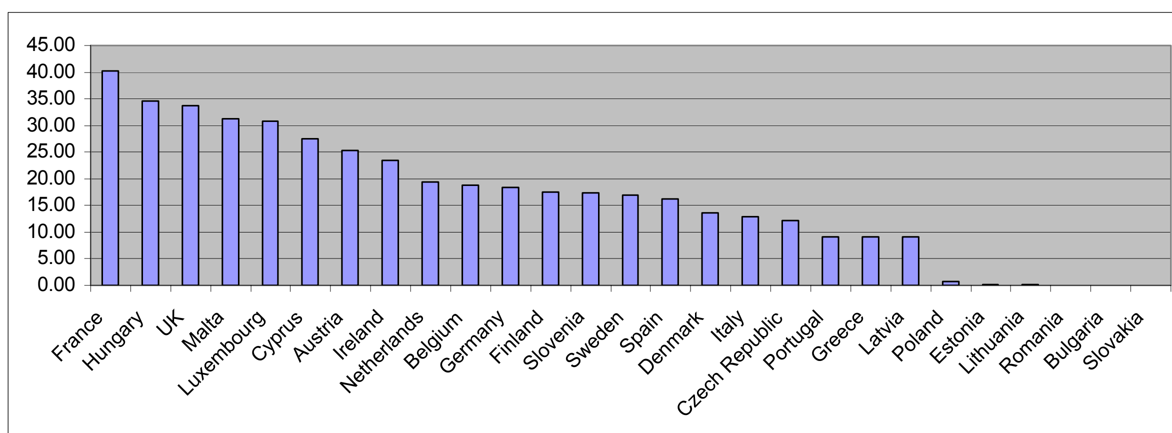
3. Percentage of Employees Holding Shares in Largest (Listed) Firms

Returning to the EFES survey of large European companies, we turn now to the question of take-up of ESO schemes by employees – i.e., how many employees have actually become owners as a result of the schemes. Figure 10 provides us with information on employee owners as a percentage of the total number of employees in the companies surveyed by EFES. For the entire sample, 26.17% of the total workforce is actually participating in ESO plans (15.05% for the 12 new EU Member States). We can, to some extent, compare this with the CRANET-based information on ESO coverage in Figure 2, although take-up is not the same thing as coverage.

Again, as in Figure 3, France is in the lead, and Hungary and the UK also rank very high (the leading positions of France and the UK are consistent with the CRANET information presented in Figure 2, though Hungary's high position here is in stark contrast to its low position there). Given the small number of Maltese and Luxembourg companies in the sample (5 and 7 respectively), the leading positions those two countries have here can perhaps not be considered representative (although the high ranking of Luxembourg is consistent with the EWCS survey

results). Czech companies do not do as well with respect to take-up as they do in offering schemes, and rank among the last countries here. In Denmark we see a similar discrepancy, though not as large as in the case of the Czech Republic (in Denmark's case this may be due to the rapid diffusion of ESO plans in very recent times, as noted in section 1 – take-up may not have caught up with the rate of introduction of schemes). Not surprisingly, we again see Romania and the Baltic and Iberian countries in the rear (although Romania was mid-ranked in Figure 2).

Figure 10. Proportion of employees participating in ESO schemes in large EU companies, 2006-2007



Source: EFES.

4. Conclusions

Regardless of the data source used, the evidence presented here shows conclusively that Europe has seen extensive growth of employee financial participation in recent years. This is true for both profit-sharing and employee share ownership, although profit-sharing is more widespread than employee ownership (although Figure 9 suggests that the difference between the two may diminish or even disappear if we adopt a very strict definition of profit-sharing). The percentage of companies with EFP schemes of various sorts in operation is growing steadily almost everywhere in the European Union, and the percentage of company employees covered by, and taking up, these schemes is also increasing. On the other hand, on the basis of both company surveys (like those of CRANET and EFES) and surveys of individuals in the workforce (like the EWCS survey), it seems that EFP has extended to a significant proportion of the working population in only a handful of countries. It is therefore clear that, while much has been accomplished, much remains to be done.

There are some discrepancies between data sources with regard to certain countries; however, the overall picture is quite clear. While for most individual countries it would be rather risky to make definitive assertions about the degree of advancement of dissemination of EFP on the basis of the data we have examined, we can identify what seem to be some regional trends. For example, we can state with a great deal of confidence that a few regions seem to be much less advanced in the dissemination of EFP than others, notably the Iberian Peninsula, the Bal-

tic States, and the southeastern corner of Europe (including Greece, Turkey and Cyprus). On the other hand, the data examined here do not seem to indicate the existence of a West-East divide (i.e., significant differences between the 15 states former members of the EU (prior to May 2004) on the one hand, and the 10 post-Communist states that have joined the EU since 2004). There seems to be much more variation within those two groups than between them.

IV. Fiscal and Tax Incentives in the EU-27

Jens Lowitzsch and Natalia Spitsa

1. The Problem

At the national level, taxation can either inhibit or support the spread of employee financial participation. At the EU level, cross-border migration of employees partaking in financial participation plans, as well as the transfer of such plans by multinational companies to subsidiaries in different Member States, may involve problems caused by conflicting tax regimes.[32] Generally, attention is centered on tax incentives, often considered the State's main instrument for promoting employee financial participation. Tax incentives, however, are relative; they need to be analysed in the context of the general taxation system in the given country. National tax systems are not easily compared; it is even more difficult to compare taxation laws governing national financial participation schemes.[33] Moreover, compulsory social security contributions must be taken into account since they add substantially to the overall burden of state levies, especially on labour; also, in many countries, they influence the tax base of the main income taxes. A systematic overview of the situation in the EU-27 shows, on the one hand, the impact and, on the other hand, the limits of tax incentives in encouraging employee financial participation.[34]

The objectives here are:

- To outline general systems of direct taxes as they affect employee financial participation in the EU. National tax systems will be classified as unfavourable, neutral or favourable for employee financial participation schemes.
- To review specific tax incentives for employee financial participation in order to determine whether specific tax incentives are a prerequisite for employee financial participation and whether some tax incentives are more effective than others irrespective of the country where they are offered.

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32 Report of the High Level Group of Independent Experts on cross-border obstacles to financial participation of employees for companies having a transnational dimension, Brussels, December 2003, p. 43 et seq. on obstacles to exportation.

33 For the comparison of general tax systems, different types of taxes, different systems of individual taxes, different tax rates, tax bases and taxation moments all must be considered. Tax rates are only comparable if effective tax rates are calculated. However, that is only possible for a specific tax and for a specific personal status and situation. Since most major direct taxes should be examined to determine their effect on employee financial participation plans, effective tax rates cannot be calculated for every possible status or situation.

34 Due to the complexity of the issue, a discussion on comparability of individual country tax rates of EU Member States cannot be covered in this publication.

A useful criterion for measuring the efficiency of tax incentives is the increase in the number of a specific form of employee financial participation immediately after a certain tax incentive is introduced.

2. General Taxation of PEPPER Schemes in the EU

The following direct taxes are relevant to employee financial participation:

- corporate income tax (CIT),
- personal income tax (PIT),
- taxes on dividends at shareholder level (special rates of personal income tax, 'investment tax', 'dividend tax', 'share income tax', etc.)
- taxes on sale of shares at shareholder level (special rate of personal income tax, capital gains tax, 'investment tax', etc.).

According to Art. 3 (1) h) ECT, an EU priority is to prevent the diversity of national tax systems from negatively affecting the development of the Common Market by harmonising national legal codes. As a special case of Art. 3 (1) h) ECT, Art. 93 ECT stipulates that indirect taxes (VAT and excises) must be made consistent. Prompted by this provision, numerous directives have been issued and indirect taxation has already been harmonised to a great extent. However, there is no special provision on harmonisation of direct taxes.[35] Moreover, potential harmonisation in this area is restricted by Art. 5 (2) ECT. On the one hand, the European Commission supports competition of direct taxes[36], regarding tax autonomy as the core component of state sovereignty, closely related to country-specific economic, social and cultural structures. On the other hand, it recognizes the importance of preventing unfair tax competition, especially in the area of corporate taxation.[37] Since there is neither a legal basis nor political support for harmonisation of corporate tax rates, the European Commission currently favours the development of the Common Consolidated Corporate Tax Base (CCCTB).[38] However, even if the CCCTB should be introduced in all Member States, it will not apply to enterprises having no cross-border activities.[39]

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35 Only more general provisions of Art. 94, 96 and 97 ECT on prevention of market distortions and, in cases of substantial discrimination, Art. 87 ECT on prevention of state subsidies, Art. 39, 43, 49, 56 ECT (basic freedoms) and Art. 12 ECT (general anti-discrimination provision) apply. However, these aim at non-discriminatory taxation of physical persons and legal entities from other EU Member States as compared with domestic physical persons and legal entities and at prevention of double taxation. They do not lead to a higher degree of harmonisation.

36 See COM (1980), 139; H. Weber-Grellet (2005): Europäisches Steuerrecht, München, p. 28, 152.

37 Whereas the issue of unfair tax competition was originally connected with such traditional tax havens as the Channel Islands and Monaco, it has gained even more importance with the accession of new Member States having generally much lower corporate and partially also personal income taxes than Western European EU Member States, except Ireland. See Weber-Grellet, Heinrich (2005): Europäisches Steuerrecht, München, p. 163.

38 See COM (2001) 582 of 23.10.2001; COM (2003) 726 of 24.11.2003; CCCTB/WP/046 of 12.12.2006; COM/2007/223 of 02.05.2007; the proposal, due in 2008, has not yet been completed, but it seems probable that the CCCTB could be introduced in several years. Seven Member States with relatively low tax ra-

Nevertheless, international tax competition is exerting considerable pressure, especially on corporate income tax rates, since the U.S. tax reform of 1986. This is responsible for two persistent tendencies observable worldwide. Firstly, the tax burden has been shifted from direct to indirect taxes[40] (with some exceptions, e.g., France), and from capital to labour.[41] Thus taxation of share-based plans may become more favourable over time than that of cash-based plans, since the tax burden on dividends and capital gains is lower than on employment income. Secondly, tax rates are lowered while the tax base is broadened.[42] Although this might lead to the abolishment of specific tax incentives, it does not necessarily mean less favourable taxation: if the rates become sufficiently lower, this may compensate for the loss of tax incentives. The general characteristics of national systems of direct taxes are illustrated in Figure 11 below.

A common feature of all direct tax systems of EU Member and Candidate States is that only income and not expenditure is taxable.[43] Accordingly, as affecting the relationship between the respective tax burden on capital and labour, income tax systems can be divided into flat tax, dual tax and differentiated tax systems; all these systems have advantages and drawbacks from an economic standpoint and are currently present in different EU Member States. In a genuine flat tax system, represented by Romania and Slovakia, the tax burden falls equally on all sources of income, flat and relatively low, since the basic tax rate to which other tax rates are adapted is the tax on capital income. This system is generally equally favourable to all forms of employee financial participation. The same is true of tax systems which impose different tax rates on labour and capital income, but levy a flat personal income tax (Estonia, Latvia, Lithuania).[44] Dual tax systems represented, e.g., by Sweden and Finland, are characterised by a highly progressive personal income tax as opposed to a flat tax on capital income. This combination is, theoretically, negative for cash-based profit-sharing and positive for share-based schemes. Most EU Member States have a differentiated tax system which generally favours employee share ownership if taxes on capital are flat and relatively low. As far as tax systems are concerned, no common tendencies can be observed. Taxation traditions and

tes are opposed to the idea, but no unanimous decision is required in this case. The EU Tax Commissioner declared that the initiative can, if necessary, be implemented by eight Member States through enhanced cooperation.

39 Moreover, the usefulness of this instrument for harmonisation of corporate taxation is considered to be questionable if no limits for corporate tax rates are set at the same time. See Bundes-ministerium der Finanzen (2007): Einheitliche Bemessungsgrundlage der Körperschaftssteuer in der Europäischen Union, in: Monatsbericht des BMF, April 2007, p. 73.

40 See OECD (2005): Tax Policy Reform Conclusions, OECD Centre for Tax Policy and Administration, p. 6.

41 See Weber-Grellet, Heinrich (2005): Europäisches Steuerrecht, München, p. 30. There is no theoretical basis and/or empirical evidence for the assumption that the tax burden on capital should be lower than on labour, although the practice is based on it (see Ganghoff, Steffen (2004): Wer regiert in der Steuerpolitik?, Frankfurt am Main, New York, p. 35).

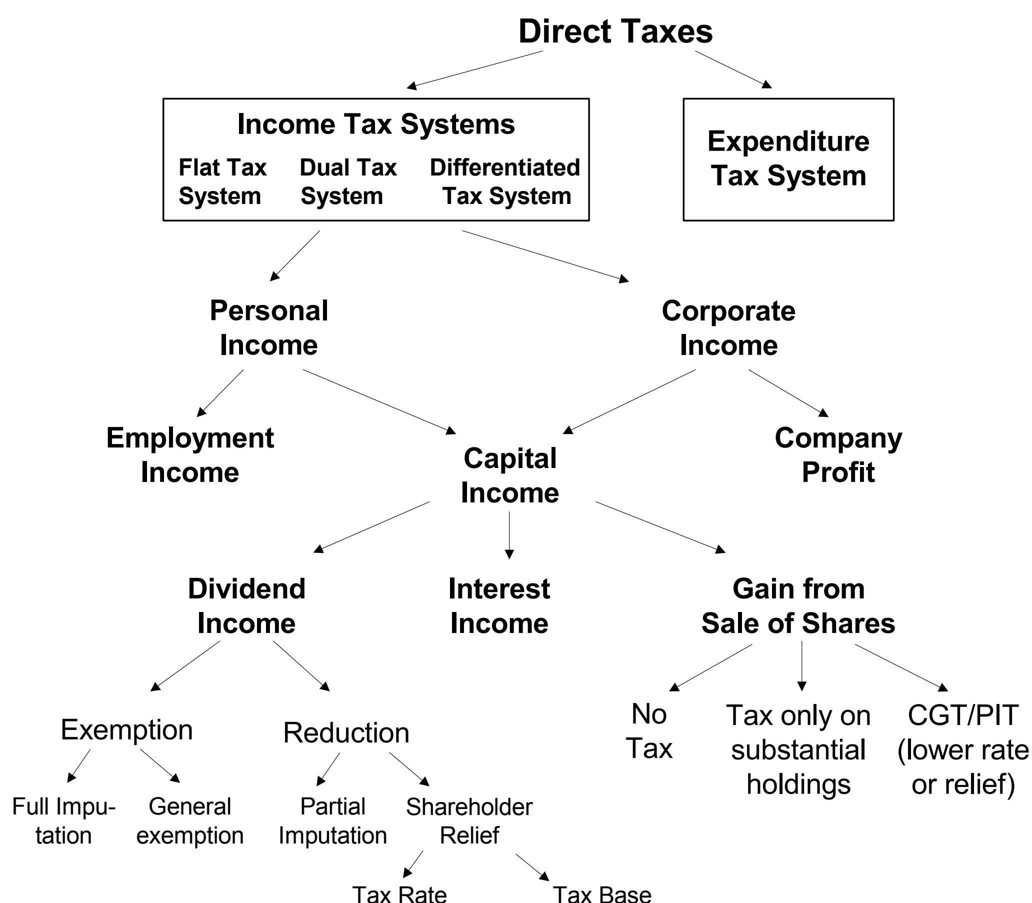
42 See OECD (2005): Tax Policy Reform Conclusions, OECD Centre for Tax Policy and Administration, p. 6.

43 However, Croatia has had an expenditure tax system from 1994 till 2000. I. a. Bulgaria, Estonia and Hungary have an expenditure tax on fringe benefits payable by the employing company. The quite unusual Estonian corporation tax system (replacement of corporate income tax by the tax on distributed profits) could also be connected with the idea of expenditure tax.

44 These systems give more leeway to share ownership since tax rates on capital income are usually lower than those on labour. However, in practice the advantage of flat tax systems may not be so substantial since often relatively high compulsory social security contributions will be levied additionally.

goals of EU Member States are different and none of the prevailling systems can be considered the best objectively.[45]

Figure 11. General characteristics of national systems of direct taxes



As far as the system of corporate income tax (taxation of dividends at the corporate and shareholder level) is concerned, no EU Member State provides relief for corporations, but many mitigate double taxation by providing relief for shareholders. Within the EU, classical, imputation, shareholder-relief and exemption systems are all represented. From the point of view of employee financial participation, classical systems (double taxation of dividend income, e.g., Ireland, Latvia, Romania) are generally unfavourable.[46] Partial imputation generally leads to a higher tax burden at shareholder level than full imputation and shareholder-relief[47] and is, therefore, relatively unfavourable. Most countries presently offer shareholder-relief, but

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45 Most Western European countries cannot introduce a flat tax system because of the potential loss of revenue (see for Italy OECD (2005): Tax Policy Reforms in Italy, OECD Centre for Tax Policy and Administration, p. 4).

46 However, it depends on the personal income tax rate. I. a. the income tax rates in Ireland, Latvia and Romania are relatively low.

47 See Spengel, Christoph (2003): Internationale Unternehmensbesteuerung in der Europäischen Union, Düsseldorf, p. 23.

it is difficult to assess the effect on employee financial participation without comparing effective tax rates.[48] The best system for share-based plans is undoubtedly one that exempts dividend income from taxation by law (e.g., Croatia, Cyprus, Estonia, Greece, Slovakia) or through full imputation (e.g., Finland).

Taxation of capital gains from sale of shares is of great importance for employee share ownership. In this context, three concepts can be distinguished within the EU: exemption from taxation (e.g., Belgium, Portugal, Cyprus, partially Bulgaria, Malta); taxation only on substantial holdings (defined differently in different countries, e.g., Austria, Germany, Italy, Luxembourg, Netherlands) and taxation by capital gains tax or by personal income tax at a lower (and usually flat) rate. Obviously, tax exemption is the most advantageous for employee financial participation. Taxation of substantial holdings is also favourable, since employee shareholdings are usually small. There is no common tendency for the taxation of capital gains.

Compulsory social security contributions[49] can either reduce the tax base of corporate and personal income tax or be calculated on after tax income (e.g., Latvia). Otherwise, they impose an additional burden on gross income and are thus very unfavourable for cash-based profit-sharing, even when general taxes are low as in Slovakia. Further, social security contributions can be levied on capital income as in France (this would have had negative consequences for share-based schemes had France not introduced specific tax incentives). Generally, no common tendency in the development of social security is discernable, since in most countries contributions are connected to long-term insurance and thus are not as easily altered by the state as are taxes.

Tax and social security rates and deductions are interdependent within a national tax system, therefore each national system has to be analysed separately as a whole; details are presented in Table 4 below.

48 Due to globalisation of business and to the requirements of the EU law, there is a tendency to exchange imputation for shareholder relief systems. See Spengel, Christoph (2003): Internationale Unternehmensbesteuerung in der Europäischen Union, Düsseldorf, p. 25.

49 Whether social security is levied as a tax, e.g., as in Denmark and Estonia, or takes the form of social insurance contributions merely means that in the case of taxes there is no corresponding claim against a social insurance institution.

Table 4. General taxation and compulsory social security contributions

	Type of dividend treatment	CIT[50]	Taxation of dividends at shareholder level[51]	Taxation of share sale at shareholder level[52]	PIT[53]	Compulsory SSC[54]
Belgium	Shareholder Relief: reduced tax rate	34%	15%	generally 0%	progressive 25 - 50% central + 0-9% sub-central; SSC deductible	Emp.: overall rate 13,07% EmpC: overall rate 35%
Bulgaria	Shareholder Relief: reduced tax rate	10%	7%,	shares of public companies listed at Bulgarian Stock Exchange 0%	progressive 20-24%, voluntary SSC deductible	Emp.: (cumulative) 12.43-25.74% EmpC: (cumulative) 23.34-25.74 %
Croatia	Dividend tax exemption for shareholders	20%	0%	0%	progressive 15-45% + city surtaxes 0-18%; SSC deductible	Emp.: 20% to pension fund EmpC: 17.2% to the health, unemployment, injury funds
Cyprus	Dividend tax exemption for shareholders	10%	generally 0%	generally 0%	progressive 20-30%; SSC deductible	Emp.: overall rate 6.3% EmpC: overall rate 6.3% + 2% to Social Cohesion Fund
Czech Republic	Shareholder Relief: reduced tax rate	24%	15% withholding tax at source	general PIT for sale of shares within 6 months	progressive 12-32%; SSC deductible	Emp.: (cumulative) 12.5% EmpC: (cumulative) 35%
Denmark	Shareholder Relief: reduced tax rate	28%	28% Share Income Tax up to DKK 44,300, 43% above; not for professional traders	28-43%	progressive 5-26.5% central + 29-35% sub-central; ceiling 59%	Emp.: 8% labour market tax EmpC: 0%
Germany	Shareholder Relief: re-	38.7%	general PIT + solidarity	0% for small long-term	progressive 15-45.4% + solidar-	Emp.: (average) 13-21.4%

[50] Data on corporate tax for 2007 are presented in the report of the German Federal Ministry of Finance of April 2007, p. 68, Table 1. The generic term ‘corporate tax" includes in this context all central and sub-central statutory taxes and surcharges on corporation profits.

[51] Data on dividend taxation from the database at <http://www.deloittetaxguides.com>, Log-in: 20.07.2007.

[52] Data on capital gains taxation from the database at <http://www.deloittetaxguides.com>, Log-in: 20.07.2007.

[53] Data on personal income tax rates for 2006 are generally downloaded from the database of the European Union <http://ec.europa.eu/taxation_customs/taxinv>, Log-in: 20.06.2007.

[54] Data on social security contributions for 2006 are downloaded from the homepage of MISSOC <http://ec.europa.eu/employment_social/missoc/2006>, Log-in: 20.06.2007.

	Type of dividend treatment	CIT[50]	Taxation of dividends at shareholder level[51]	Taxation of share sale at shareholder level[52]	PIT[53]	Compulsory SSC[54]
	duced tax base		surcharge 5.5%; tax base reduced to 50% of the dividend income (half-income system); no SSC	holdings; for substantial shareholdings general PIT on difference between 50% of proceeds and 50% of acquisition costs	ity surcharge 5.5%; limited by an absolute amount; pension and health care contributions partly deductible	EmpC: (average) 20.5% Both limited by an absolute amount
Estonia	Tax exemption for shareholders; exemption of retained profits from corporate tax	22% on distributed profits	0%	general PIT	flat 22%; mandatory SSC deductible	Emp: contribution to the unemployment fund 0.6% EmpC: 'social tax' 33% + contribution to the unemployment fund 0.3 %
Greece	Dividend tax exemption for shareholders	25%	0%	generally 0%; 20% on sale of shares of LLC or partnerships	progressive 15-40%; SSC deductible	Emp.: 11.55% (16%) EmpC: 23.1% (28.06%); both limited by an absolute amount
Spain	Partial Imputation	32.5%	15%; imputation credit	15% if held more than 1 year, otherwise general PIT	15-45% savings income deductible	Emp.: 16.35% EmpC: 30.6%
France	Partial Imputation	34.4%	general PIT with tax credit of 40% + social levies (CRDS, CSG) - 11%	CGT 16%; on stock options 30-40%	progressive 5,5-40%	Emp.: (cumulative) 10.6-17.8%; limited by an absolute amount EmpC: (aggregated) 29.72-34.22%
Hungary	Shareholder Relief: reduced tax rate	17,5%	25% for dividends on up to 30% of equity; 35% above +14% health care contribution	25%; on up to 30% of equity; 35% above	progressive 18-36%; voluntary SSC deductible	Emp: 17% limited by an absolute amount EmpC: 32% + health care contribution
Ireland	Classical system	12.5%	20%	20%	progressive 20-42%; voluntary SSC deductible	Emp.: 2-6% EmpC: 8.5-10.75%

	Type of dividend treatment	CIT[50]	Taxation of dividends at shareholder level[51]	Taxation of share sale at shareholder level[52]	PIT[53]	Compulsory SSC[54]
Italy	Shareholder Relief: reduced tax base	37,3%	general PIT; tax base reduced to 5% of dividend income; below 5% (or 2% of voting rights) 12.5%	12.5% for small shareholdings; 27% on substantial; tax base reduced to 40% of gain	progressive 23-43%+ surcharge 0.9-1.4%; SSC deductible	Emp.: (cumulative) 9.2-10.2% EmpC: (cumulative) 32.08%
Latvia	Classical system	15%	general PIT	general PIT	Flat 25%	Emp.: overall rate 9% EmpC: overall rate 24.09%, both from after-tax income
Lithuania	Shareholder Relief: reduced tax rate	15%	15%	generally 15%; 0% if held more than 1yer and no substantial shareholding for last 3 years	Flat 27%	Emp.: 3% EmpC: 30.7%
Luxembourg	Shareholder Relief: tax base reduced	29.6%	15%; tax base reduced to 50% of the dividend income;	General PIT for short-term holdings; high allowance and 50% of PIT rate for long-term holdings	progressive 8-38%	Emp.: 11.8-14.05% EmpC: 13.15-20.75%
Malta	Full imputation	35%	general PIT and tax credit for CIT	stamp duty; shares quoted on Malta stock exchange tax exempt	progressive 15-35%	Emp.: overall rate MTL 2.84-13.38 weekly EmpC: overall rate MTL 2.84-13.38 weekly
Netherlands	Shareholder Relief: reduced tax rate	25.5%	15% for small, 25% for substantial holdings	0% for small, 25% for substantial shareholdings	progressive 33.65-52%	Emp.: 5.2-31.7% EmpC: 6.5-11.31%
Austria	Shareholder Relief: reduced tax rate	25%	25%; optional: general PIT at a half rate; generally no SSC	0% for small long-term holdings; for substantial shareholdings 25%	progressive 23-50%; statutory and voluntary pension contributions partly deductible	Emp.: (cumulative) 16.85-17.2% EmpC: (cumulative) 20.5-20.7% deductible; both limited by an absolute amount
Poland	Shareholder Relief: re-	19%	19%	19%	progressive 19-40%	Emp.: average 22.2%

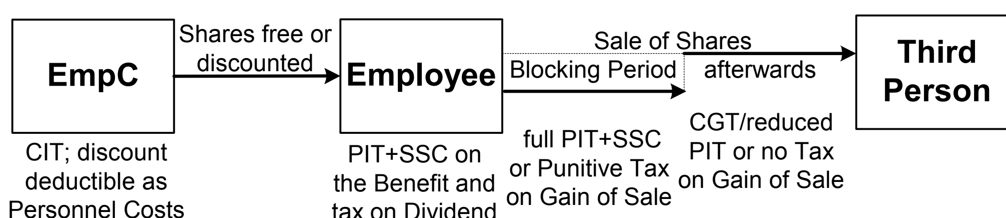
	Type of dividend treatment	CIT[50]	Taxation of dividends at shareholder level[51]	Taxation of share sale at shareholder level[52]	PIT[53]	Compulsory SSC[54]
	duced tax rate					EmpC: average 20.6%
Portugal	Partial Imputation	27.5%	20%; imputation credit of 50%	generally 10%; tax exemption if shares are held more than 12 months	progressive 10.5-42%	Emp.: overall rate 11% EmpC: overall rate 23.75%
Romania	Classical system	16%	'Investment Tax' 16%	'Investment Tax' 16%; 1% for long-term investment	Flat 16%; voluntary contributions to private pension funds deductible	Emp.: (cumulative) 17% EmpC: (cumulative) 30.35-31.35%
Slovakia	Dividend tax exemption for shareholders	19%	0%	general PIT	Flat 19%	Emp.: 13.4% EmpC: 28.4%
Slovenia	Shareholder Relief: reduced tax rate	23%	20%	0-20% according to the holding term	progressive 16-41% contributions to private pension funds deductible	Emp.: 22,1% EmpC: 16.1%
Finland	Full Imputation	26%	'Investment Tax' 28%; generally no SSC	28%	progressive 9-32% central + 18,46% (average) sub-central; SSC deductible	Emp.: (cumulative) 6.61-7.18%; EmpC: (cumulative) 20.69-32.69%; both limited by an absolute amount
Sweden	Shareholder Relief: reduced tax rate	28%	'Individual Capital Income Tax' 30%	30%	progressive 20-25% central + 31.6% sub-central	Emp.: 7% EmpC: 32.28%
Turkey	Partial imputation	20%	15%; imputation credit of 50%	0% if held more than 4 years, otherwise general PIT	progressive 15-35%	Emp.: 15%; EmpC: 21.5%; both limited by an absolute amount
UK	Partial imputation	30%	10% up to the basic rate limit; 32.5% above; imputation credit	CGT 40%; taper relief	progressive 10-40%	Emp.: overall rate 11% EmpC: overall rate 12.8%

Abbreviations: CIT - Corporation Tax, PIT - Personal Income Tax, CGT - Capital Gains Tax, SSC - Social Security Contributions, EmpC - Employing Company, Empl. - Employee, IntE - Intermediary Entities.

In the context of taxation, it is only relevant whether a financial participation scheme is cash-based or share-based and whether an 'intermediary entity'[55] is used as a vehicle. The same taxation rules apply to employee share ownership schemes and share-based profit-sharing schemes, both direct and deferred.

a) Employee Share Ownership

Employee Shares



The benefit in value from transfer of discounted shares is generally deemed employment income and correspondingly subject to full personal income tax and compulsory social security contributions at the employee level. The employer company can generally deduct the discount as a personnel cost. However, valuation rules, especially for non-quoted shares, differ considerably between countries.[56] Taxation of dividends depends on the country-specific type of dividend treatment. Since there is no tax relief for the employing company in any EU Member State, full corporate tax generally is to be paid by the employer company on the entire profit, including the part to be distributed.[57] The different systems of dividend taxation at shareholder level are explained above (see Table 4). Taxation of gains from sale of shares depends on whether the shares are sold during or after the end of the blocking period. If the shares are sold during the blocking period, there are no major differences between EU countries: either full personal income tax and social security contributions or a special (high) punitive tax will be imposed. If the shares are sold after the end of the blocking period, taxation depends on the system of taxation of capital gains presented above (see Figure 11). If there is no general exemption, or exemption for small shareholdings, other forms of tax relief usually apply.

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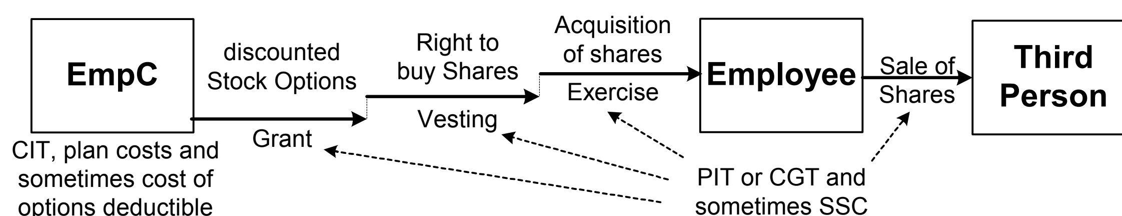
55 The generic term used for intermediary companies, funds with a separate legal personality and trusts (in common law countries UK, Ireland and Malta), which accumulate distributed profits, hold, allocate and transfer shares, options or certificates of the employer company for employees, sometimes pay out dividends or returns, administrate dividends, and make investments.

56 The valuation of the same shares for the purpose of taxation of employees or employers may follow different rules and lead to different taxable amounts as in Austria. The moment of valuation of shares may also be different in different countries and lead to differences in value and in the tax base derived from it.

57 However, in one EU Member State, Estonia, corporate tax is replaced by the tax on distributed profits. This original system may have a positive economic effect on accumulation of funds, but it constitutes a strong disincentive for the employer company in relation to share-based employee participation plans as well as to cash-based profit-sharing.

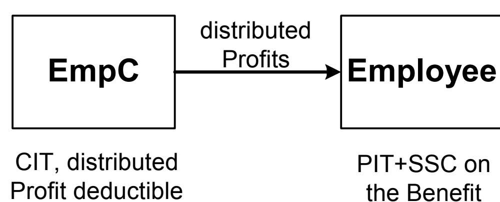
Stock Options

Taxation of employee stock options is complex due to differences in the taxation moment and valuation methods which depend on the taxation moment. In most EU Member States, taxes are imposed at exercise; taxation at grant or optionally at grant or exercise, as well as taxation at sale of shares, are also practiced.



Upfront taxation at grant is connected with considerable risks, so that special tax relief such as reduced tax rate or tax base and exemption from social security contributions are necessary as compensation. Although it could be argued that stock option benefits should be considered as capital gains, it is deemed to be employment income in most EU Member States; as such it is usually charged as personal income tax and partly also subject to social security contributions. The employer company can generally deduct setting up and operating costs of the plan as well as cost of options if the shares are repurchased (with the exception of, e.g., Belgium). In some countries (e.g., Denmark, Ireland, Luxembourg, Portugal), both the employer company and the employee are exempted from social security contributions.[58]

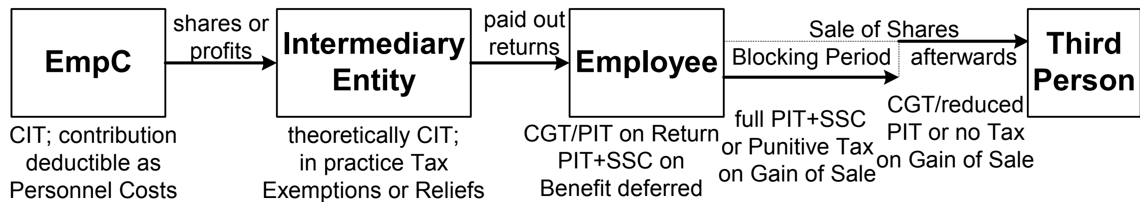
b) Profit-Sharing



As far as cash-based profit-sharing is concerned, no major discrepancies exist between different EU Member States. Distributed profit is generally deductible for the employer company as a personnel cost (with the exception of Estonia, where it is instead subject to the tax on distributed profits), and it is subject to full personal income tax and social security contributions for the employees. The same taxation rules as for employee share ownership apply to share-based profit-sharing (see above).

[58] For details see EC (2003), Stock Options; PriceWaterhouseCoopers (2002): Employee Stock Options in the EU and the USA, London.

c) Intermediary Entities



Share ownership plans and profit-sharing plans using a vehicle for the holding of shares and the investment of accumulated funds exist in many varieties in different EU Member States, especially because of substantial differences in company law. However, there is a similar basic logic: the employer company can usually deduct contributions to the intermediary entity, as well as set up and operating costs, from the tax base of the corporate income tax; the intermediary entity is usually established in a tax-friendly form. Taxation of employees would be the same as for simple share-based plans (see 1. above) if it were not for specific tax incentives (e.g., deferred taxation of the benefit), which in most cases are granted.

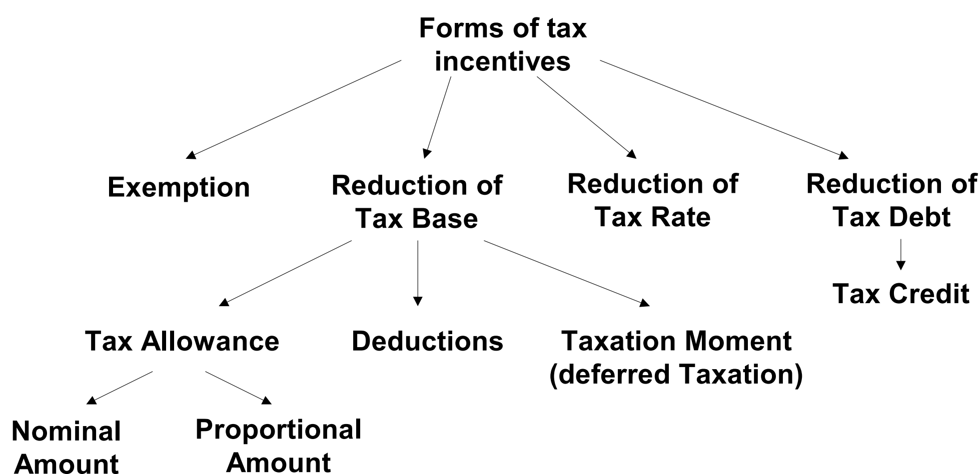
3. Specific Tax Incentives for PEPPER Schemes in the EU

Aside from specific tax incentives, most national taxation systems are more or less favourable to financial participation. The only tax system which actually hinders the development of financial participation is that of Estonia, due to taxation of distributed profits at company level instead of general corporate income tax.[59] National taxation systems which exempt dividends and capital gains from taxation and social security contributions are especially advantageous to share-based schemes. Although details differ, generally in most countries the same taxes apply to similar plans so that the important difference is the general level of the tax burden of standard income taxes and compulsory social security contributions determined by tax rates and tax bases. As mentioned above, comparable effective rates cannot be calculated for all possible situations. Nevertheless, a substantial difference in tax rates implies a difference in tax burden. Thus it can be argued that low-tax countries generally have more favourable tax regimes for financial participation so that specific tax incentives are not necessary. The example of Ireland, however, shows that the government of a low-tax country can have a strong political interest in promoting employee financial participation; it can offer additional tax incentives even though the low level of general taxation limits their impact.[60] Therefore the different instruments used to create specific tax incentives are important. Incentives may take the different forms diagrammed below.

59 For this reason, it is contrary to the financial interests of the employing company to distribute profit to employees in cash-based profit-sharing schemes or as dividends to employees who have become shareholders. However, the Estonian tax system is to be changed in 2009 to comply with the EU Parent-subsidiary Directive. See KPMG (2007), Corporate and Indirect Tax Rate Survey 2007, p. 15.

60 See Irish Department of Finance, TSG 98/12.

Figure 12. Forms of tax incentives



Tax rate reductions and exemptions, although most effective because they are based on law rather than arbitrary judgments of tax authorities, and confer the same advantages to all categories of income, are seldom utilised.[61] One reason for this neglect is that such tax incentives result in heavier losses of revenue; also tax authorities have virtually no discretionary power over their use.[62] Deductions favour higher incomes under a progressive system of taxation, like the personal income tax in most EU Member States; tax credits (direct reduction of tax liability), on the other hand, are non-discriminatory and usually more valuable than an equivalent tax deduction or tax allowance.[63] Tax allowances benefit lower incomes whereas nominal tax allowances benefit the taxpayer less and therefore involve smaller revenue loss than would a proportional determination of the tax allowance. Deferred taxation favours share ownership schemes avoiding otherwise necessary additional liquidity at the moment of acquisition. Specific tax incentives for employee financial participation are currently in effect in 15 (mainly Western) countries out of the 29 Member and Candidate States; these differ substantially in type and size. Details are presented in Table 5 below.

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61 See Spengel, Christoph (2003): Internationale Unternehmensbesteuerung in der Europäischen Union, Düsseldorf, p. 28.

62 To compensate for revenue losses caused by lowering the tax rate, either rates of other taxes are increased or the tax base is broadened. Thus a lower tax rate does not necessarily lower the total tax burden. It is not surprising that countries with low statutory tax rates like Ireland have fewer tax concessions than countries with high statutory tax rates like France, Italy and Spain. See Spengel, Christoph (2003): Internationale Unternehmensbesteuerung in der Europäischen Union, Düsseldorf, p. 29.

63 However, more value for taxpayers means higher revenue losses for the state. In addition, tax credits generally cause higher tax administration costs. Recently, tax credit systems have been replaced by tax allowances in France and Italy. See Tipke, Klaus, Lang, Joachim (eds.) (2005): Steuerrecht, 18. Aufl., Köln, p. 799, p. 802.

Table 5. Tax incentives for employee financial participation

Country	Employee	Employer Company
Belgium **ESO**	**ES:** Since 2001: 15% tax on benefit, no SSC if 2-5 years blocking period; tax base: quoted shares market value-costs, non-quoted shares purchase price-net asset value of shares; Sale of shares: tax-free up to 25% of equity; sale during blocking period 23.29% punitive tax; **SO:** Since 1999: taxation moment – at grant; taxation base: lump sum value = 15% of stock value at grant + 1% for each year before exercise, value reduced by half (7.5% + 0.5%) if options cannot be exercised within 3 years from grant, exercise period within 10 years from grant, no guarantee against fall in value, strike price determined at option offer; no SSC; **IntE:** Do not exist.	**ES:** Discount deductible from tax base of CIT; **SO:** Difference between market price of stock and exercise price of options deductible from tax base of CIT only if not EmpC, but a foreign company provides shares for employees at exercise and cross-charges the cost to EmpC; **IntE:** Do not exist.
PS	**General:** Since 2001: 15% tax for participation in the framework of an investment savings plan; 25% tax in other cases; but full SSC; **IntE:** Do not exist.	**General:** No SSC; **IntE:** Do not exist.
Denmark **ESO**	**ES:** Since 1987 (broad-based plan): no PIT, no SSC on discount, if value does not exceed 10% of annual salary, 5 years blocking period and shares deposited on trust with a bank; **SO:** (1) Broad-based plan (since 1987): no PIT, no SSC if value of options does not exceed 10% of annual salary and 5 years blocking period; (2) Individual plan under § 7H (since 2003): no PIT, no SSC if value of options does not exceed 10% of annual salary or exercise price less than 15% lower than market price of underlying shares; (3) Individual plan under § 28: no incentives; **IntE:** Do not exist.	**ES:** Discount deductible from tax base of CIT; **SO:** (1) Option costs deductible from tax base of CIT; (2) No; (3) Option costs deductible from tax base of CIT; **IntE:** Do not exist.
PS	**General:** (1) Broad-based plan (since 1987): up to DKK 8,000 tax-free if blocking period 7 years and shares deposited on trust with a bank (2) Individual plan under § 7H (since 2003): no PIT, no SSC on benefit if value does not exceed 10% of annual salary; **IntE:** Do not exist.	**General:** (1) Costs of shares deductible from tax base of CIT; (2) No; **IntE:** Do not exist.
Germany **ESO**	**ES:** No PIT, no SSC on benefit, if not exceeding 50% of the share value and EUR 135 annually; savings bonus of 18% on investment up to EUR 400 annually if annual income up to EUR 17,900 and 6 years blocking period; **SO:** No; **IntE:** Do not exist	**ES:** No; **SO:** No; **IntE:** Do not exist
PS	**General:** No; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.

Country	Employee	Employer Company
Greece **ESO**	**ES:** Since 1987: (only for JSC) no PIT, no SSC on benefit – if shares issued in a capital increase 3 years blocking period; Dividends: tax on movable assets (10%); **SO:** (1) Since 1999 'Qualified plans': no PIT, no SSC at grant or exercise; (2) Since 1988 'Non-qualified plans': gift tax can be applied instead of PIT at discretion of tax authorities; **IntE:** Do not exist.	**ES:** Discount deductible from tax base of CIT, no SSC; **SO:** (1) No; (2) Costs of distributed shares deductible from tax base of CIT; **IntE:** Do not exist.
PS	**General:** (only for JSC, usually cash-based) no PIT, but SSC on benefit if not exceeding 25% of annual gross salary; **IntE:** Do not exist.	**General:** Distributed amount deductible from tax base of CIT, but SSC; **IntE:** Do not exist.
Spain **ESO**	**ES:** (1) Since 2003: no PIT, no SSC on benefit up to EUR 12,000, if plan regular, each employee and his family own not more than 5% of equity capital, 3 years blocking period; (2) Since 1997 Sociedades Laborales: no tax on company formation and tax credit of 99% on transfer tax, levies for notarial deeds on transfers to the company, debts, bonds and debenture bonds, if reserve for loss compensation 25% of annual profits; **SO:** 80% tax relief on up to 2 x (annual medium wage x number of years before vesting), if vesting period not exceeding 2 years, options granted not annually, 3 years between option grant and share sale, plan broad-based; **IntE:** Do not exist.	**ES:** No; **SO:** No; **IntE:** Do not exist.
PS	**General:** No; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.
France **ESO**	**ES:** No; **SO:** No; **IntE:** Do not exist.	**ES:** Training of employees on EFP: tax relief EUR 75 per hour p. p. up to EUR 5,000 per company for 2 years (2007); **SO:** No; **IntE:** Do not exist.
PS	**General:** Since 1986/1994 (intéressement – gain sharing): no SSC, but full PIT, if transferred immediately; tax incentives only if combined with savings funds (PEE, PPESV); Since 1967/1986/1994 (participation – profit-sharing): no PIT, no SSC, special flat tax of 7.6% on benefit if blocking period 5 years, the amount does not exceed 25% of gross salary up to EUR 14,592; returns tax-free if accumulated, 10% special flat tax if paid out during blocking period; **IntE:** Since 1986/1994 (PEE - short-term savings plan): no PIT, no SSC, flat tax of 7.6% if blocking period 5 years and EmpC match does not exceed the ceiling; Since 2001: (PPESV - long-term savings plan): like short-term, but blocking period 10 years; if	**General:** Since 1986/1994 (intéressement – gain sharing): no SSC; tax incentives only if combined with savings funds (PEE, PPESV); Since 1967/1986/1994 (participation – profit-sharing): no CIT, no SSC, special flat tax of 7.6% on benefit if blocking period 5 years, the amount does not exceed 25% of gross salary up to EUR 14,592; returns tax-free if accumulated, 10% special flat tax if paid out during blocking period; **IntE:** Since 1986/1994 (PEE - short-term savings plan): no CIT, no SSC, flat tax of 7.6% if blocking period 5 years and EmpC match does not exceed the ceiling; Since 2001: (PPESV - long-term savings plan): like short-term, but blocking period 10 years; if EmpC match exceeds the ceiling for short-term, but is

Country	Employee	Employer Company
	EmpC match exceeds the ceiling for short-term, but is under the ceiling for long-term - flat tax of 8.2%; Returns: flat tax of 10%.	under the ceiling for long-term - flat tax of 8.2%; Returns: flat tax of 10%.
Hungary **ESO**	**ES:** Since 2003 'Approved Employee Securities Benefit Programme': no PIT and tax relief for voluntary insurance on benefit, if not exceeding HUF 50,000 annually and programme approved; **SO:** Since 2003 'Approved Employee Securities Benefit Programme': incentives as for **ES**; **IntE:** Since 1992 ESOP: no PIT on shares transferred via ESOP; contributions to ESOP deductible from tax base of PIT.	**ES:** No; **SO:** No; **IntE:** Contributions to ESOP deductible from tax base of CIT.
PS	**General:** No; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.
Ireland **ESO**	**ES:** (1) Purchase of new shares: at sale of shares no PIT, no SSC, only CGT on issue price, if full price paid, 3 years blocking period and not exceeding lifetime ceiling of EUR 6,350; (2) Restricted Stock Scheme: deduction from tax base of PIT on benefit from 10% for 1 year blocking period to 55% for 5 years blocking period; **SO:** (1) Since 1999 SAYE: no PIT, no SSC at grant or exercise, if plan broad-based, SAYE contract with a bank for 3, 5 or 7 years, exercise price of shares up to 25% under the market value of underlying shares at option grant, plan approved by tax authorities; (2) Since 2001 APOS: no PIT, no SSC at grant or exercise, if plan broad-based, 3 years blocking period, plan approved by tax authorities; **IntE:** ESOT enjoy incentives only if combined with APPS (see below).	**ES:** (1) No SSC; (2) No; **SO:** (1) No SSC; (2) No SSC; **IntE:** ESOT enjoy incentives only if combined with APPS (see below).
PS	**General:** No; **IntE:** (1) Since 1986 APSS: no PIT, no SSC on benefit not exceeding EUR 12,700, if plan broad-based, 3 years blocking period in trust, plan approved by tax authorities Sale of shares: CGT; sale during blocking period PIT at top rate on proceeds of sale less market value and CGT on increase in value; (2) Since 1997 ESOT: incentives only if combined with APSS trust.	**General:** No; **IntE:** (1) Costs of setting up and operating the plan deductible from tax base of CIT, no SSC; (2) EmpC: incentives only if combined with APSS trust; IntE: no tax on dividends if dividends used for qualifying purposes.
Italy **ESO**	**ES:** Since 1999: no PIT, no SSC on benefit up to EUR 2,066; no SSC (since 2006) if 3 years blocking period **SO:** Since 1999: no PIT, no SSC up to EUR 2,066, if 5 years blocking period between option grant and sale of shares, unless proceeds of the share sale invested in securities with the value equal to the difference of shares value at option	**ES:** Discount deductible from tax base of CIT; **SO:** No; **IntE:** Do not exist.

Country	Employee	Employer Company
	grant minus share purchase price; **IntE:** Do not exist.	
PS	**General:** Since 2007: 23% deduction of PIT up to EUR 350 annually, no SSC; **IntE:** Do not exist.	**General:** Since 1997/2007: 5% tax exemption for contributions distributed to employees, 25% deduction of SSC; **IntE:** Do not exist.
Nether-lands ESO	**ES:** Since 1994, usually JSC: tax incentives only in combination with a savings plan – no PIT, no SSC, instead 15% flat tax, if plan broad-based, 4 years blocking period, annual ceiling of the savings plan EUR 1,226; **SO:** No; **IntE:** Since 1994, usually LLC: regulation of tax incentives as for direct employee share ownership.	**ES:** No; **SO:** No; **IntE:** No.
PS	**General:** Since 1994/2003: tax incentives only in combination with a savings plan – no PIT, no SSC, instead 15% flat tax, if plan broad-based, 4 years blocking period, annual ceiling of the savings plan EUR 613; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.
Austria ESO	**ES:** Since 2001: Amount free of taxes and SSC up to EUR 1,453.46 annually, if 5 years blocking period, plan broad-based, shares deposited with a domestic credit institution; **SO:** Since 1999: tax allowance (10% of the benefit per year, but not more than 50% of the total benefit tax-free) if options non-tradable, plan broad-based, value of underly-ing share at option grant not exceeding EUR 36,400 + carry forward of taxation for the remaining amount (taxation optionally at sale or at termination of employment, but at the latest at the end of the 7th year after grant) if options deposited with a domestic credit institution; **IntE:** Since 2001: up to EUR 1,453.46 annu-ally CGT; if more PIT; no SSC.	**ES:** The book value of transferred shares deductible as personnel costs; **SO:** Costs of share purchase or the amount not contributed to the equity in the case of capital increase deductible from CIT; **IntE:** payments to IntE and costs for IntE deductible from CIT; up to EUR 1,453.46 annually p. p. tax-free; if more CGT; dividends on shares tax-free.
PS	**General:** No; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.
Portugal ESO	**ES:** No; **SO:** No SSC; **IntE:** Do not exist.	**ES:** No; **SO:** No SSC; **IntE:** Do not exist.
PS	**General:** Since 1969 (usually cash-based): no PIT, no SSC, if individual agreement con-cluded and effective; **IntE:** Do not exist.	**General:** Profit distributed to employees de-ductible from tax base of CIT; **IntE:** Do not exist.
Slovenia ESO	**ES:** Since 2008: 70% deduction from PIT on benefit not exceeding EUR 5,000 annually per employee, if 1 year blocking period, 100% deduction, if 3 years blocking period;	**ES:** Value of distributed shares deductible from tax base of CIT in the year, when the blocking period ends; **SO:** No;

Country	Employee	Employer Company
	SO: No; **IntE:** Do not exist.	**IntE:** Do not exist.
PS	**General:** Since 2008 (for share-based PS): same as for ES; **IntE:** Do not exist.	**General:** same as ES; **IntE:** Do not exist.
Finland **ESO**	**ES:** Since 1992: no PIT, no SSC on discount, if it does not exceed 10% and plan broad-based; Dividends: in public companies 30% tax-free; in private companies 100% tax-free if earnings per share less than 9% and the total amount less than EUR 90,000; **SO:** No; **IntE:** Do not exist.	**ES:** Discount deductible from tax base of CIT; **SO:** No; **IntE:** Do not exist.
PS	**General:** No; **IntE:** Since 1989/1997: Personnel Funds no PIT, no SSC on 20% of pay-outs from the Fund, if 5 years blocking period.	**General:** No; **IntE:** EmpC: no CIT, no SSC on profits transferred to IntE; IntE: earnings tax-free.
UK **ESO**	**ES:** No; **SO:** (1) Since 1980 SAYE: no PIT, no SSC at grant or exercise, if plan broad-based, exercise price of shares up to 20% under market value of underlying shares at option grant, SAYE contract with a bank, plan approved by tax authorities; (2) Since 1984/1996 CSOP: no PIT, no SSC at grant or exercise, if value of outstanding options up to GBP 30,000 per employee, exercise price not lower than market value at grant, exercise period 3 to 10 years after grant, plan approved by tax authorities; (3) Since 2000 EMI: no PIT, no SSC at grant or exercise, if value of options granted annually not exceeding GBP 100,000 per employee and GBP 3 million per company, tax authorities notified; **IntE:** Since 2000 SIP: no PIT, no SSC on benefit, if plan broad-based, 5 years blocking period in trust, value of shares up to GBP 3,000 (free shares), up to GBP 1,500 (partnership and dividend shares) annually per employee, plan approved by tax authorities; Sale of shares: no tax, no SSC if sold immediately after withdrawal.	**ES:** No; **SO:** (1)-(3) Costs of setting up and operating the plan; since 2003: costs of providing shares to the plan deductible from tax base of CIT, generally no SSC; **IntE:** Costs of setting up and operating the plan; since 2003: costs of providing shares to the plan deductible from tax base of CIT, generally no SSC.
PS	**General:** No; **IntE:** Do not exist.	**General:** No; **IntE:** Do not exist.

Abbreviations: APOS - Approved Share Option Scheme, APSS - Approved Profit-Sharing Scheme, CIT - Corporate Income Tax, CGT - Capital Gains Tax, CSOP - Company Share Option Plan, EMI - Enterprise Management Incentives, EmpC - Employing Company, ESOP - Employee Share Ownership Plan, ESOT - Employee Share Ownership Trust, IntE - Intermediary Entities, JSC - Joint Stock Company, LLC - Limited Liability Companies, PIT - Personal Income Tax, SAYE - Approved Savings-Related Share Option Scheme, SIP - Share Incentive Plan, SSC - Social Security Contributions.

Although at first impression, the table seems to suggest unbridgeable diversity, the analysis of the data leads to the conclusion that pre-conditions as well as forms of tax incentives are generally similar, but differ substantially in size. The table columns correspond to the classification of employee financial participation forms in country profiles, but, as explained above, a different classification should be used for purposes of tax analysis: employee share ownership plans and share-based profit-sharing plans belong to the first category (with certain specific features of leveraged plans), stock option plans to the second category, and cash-based profit-sharing plans to the third category.

a) Share-Based Plans

Tax incentives in most countries apply to non-leveraged share-based plans, share-ownership as well as profit-sharing. The most common pre-condition is a blocking period between one and seven years, the most common being 5 years (e.g., Austria, Belgium, Denmark, France and Italy for some plans). A blocking period can be combined with an obligation to deposit shares with a bank. In leveraged share-based plans, shares must be deposited with an intermediary entity (intermediary company, fund or trust) and cannot be withdrawn within a certain period of time (up to 10 years), which practically corresponds to the 'voluntary' blocking period in non-leveraged plans (e.g., Austria, Finland, France, Ireland, UK). In some cases, tax incentives apply only if the primary plan is linked to a savings contract or scheme (e.g., France, the Netherlands). In many countries, tax incentives apply only if the plan is broad-based (e.g. Austria, Denmark, Finland, Hungary, the Netherlands, Ireland, UK, France). However, some countries introduced broad-based as well as individual plans with partly different pre-conditions and tax incentives (e.g. Denmark). In some countries, where the plans are pre-defined in the law, approval of tax authorities is necessary (e.g. Hungary, Ireland, UK).

The most common form of tax incentives for employees on the benefit in share-based plans (excluding stock option plans) is an allowance of tax and social security contributions, but the absolute amount differs significantly, from EUR 135 per employee annually in Germany to EUR 12,700 in Ireland. In Finland and Denmark, where the amount is given as a percentage of annual salary, the allowance might be even higher (10% in Denmark and in Finland for non-leveraged share ownership plans and 20% in Finland for leveraged share-based profit-sharing). The tax-free amount in leveraged plans is often larger than in non-leveraged plans. Another possibility is a special, relatively low flat tax instead of personal income tax and social security contributions (e.g., 15% in Belgium, 7.6% in France). In France, the special tax is imposed on the employees as well as on the employing companies. Relatively rare tax incentives for employees are deduction from the tax base of personal income tax (Ireland for restricted stock schemes, Slovenia for a short blocking period) and a savings bonus (Germany for very low incomes). Tax incentives on dividends are also applied quite seldom (e.g., Finland, France), since taxation of dividends is always lower, and social security contributions are not levied. Since the employer companies usually can deduct the value of distributed shares as personnel costs under general taxation rules and are not subject to social security contributions on that amount, special incentives are not required. However, in France the employer companies were exempted from social security contributions, which are usually imposed, and a special flat tax of 7.6% on the benefit and of 10% on the dividends was introduced, which also applies to employees. Specific tax incentives exist for intermediary entities in leveraged plans: all earnings (e.g., Finland) or at least a certain amount of contributions and dividends (e.g., Austria, Ireland, France, UK) are either tax exempt or levied by a special low tax.

b) Stock Options

The greatest variety of tax incentives occur in connection with stock option plans. In addition, it is difficult to compare pre-conditions and incentive forms in different countries, since several stock option plans often exist in a single country. At a higher level of abstraction, the most common pre-conditions are blocking and exercise periods (e.g., Belgium, UK, Ireland); restrictions on the difference between the market price of underlying shares and the exercise price (e.g., Belgium, Denmark, Ireland, UK, Austria); the existence of a broad-based plan (e.g., Austria, Denmark, Ireland, UK), and approval by the tax authorities (e.g., Hungary, Ireland, UK). In the so-called SAYE plans in Ireland and UK, combination with a savings contract is required. As far as tax incentives for employer companies are concerned, eligibility often depends on whether the shares are to be purchased on the market or issued in the course of capital increase (e.g., Austria, Greece).

The most common tax incentive forms for employees are an allowance of personal income tax and social security contributions, whereby the amounts are either the same as for shares, e.g., Denmark, Hungary, or much higher, e.g., CSOP (GBP 30,000) and EMI (GBP 100,000!) in the UK. Such forms as deferred taxation (e.g. Austria) or taxation at grant (e.g. Belgium) are country-specific. Tax incentives for employer companies is the deductibility of costs of share purchase or option costs from the tax base of the corporate income tax.

c) Cash-Based Profit-Sharing

Only two countries (Greece and Portugal) have tax incentives for cash-based profit-sharing; in both cases these were introduced several decades ago. These tax incentives were obviously inefficient, the incidence of employee financial participation in Greece and Portugal is still the lowest among Western European countries. A possible reason for this inefficiency is restricted eligibility of – otherwise quite generous – tax incentives: in Portugal, tax incentives become applicable only on the basis of an individual contract limited in time; in Greece, tax incentives are applicable only to joint-stock companies.

Two general principles and several conclusions may be drawn from the combined data on tax incentives and the incidence of financial participation from the various countries:

➢ **Tax incentives are not a prerequisite to financial participation**

Financial participation schemes without tax incentives (e.g., profit-sharing plans in Austria and Germany) sometimes have a higher incidence than those with tax incentives (e.g., share ownership plans in Austria and Germany).[64] Therefore tax incentives are not to be considered a prerequisite to the development of financial participation. Furthermore, in low-tax countries

[64] In Austria, only 8% of enterprises and 6% of the workforce participated in employee share ownership plans in 2005, tax incentives for which were introduced in 2001, whereas 25% of enterprises operated profit-sharing plans without tax incentives (see Kronberger, Ralf, Leitsmüller, Heinz, Rauner, Alexander (eds.) (2007): Mitarbeiterbeteiligung in Österreich, Wien, pp. 11, 17, 162). In Germany, 2.4% of enterprises had an employee share ownership plan in 2001, supported by (marginal) tax incentives, whereas at the same time 8.7% of enterprises operated profit-sharing plans without tax incentives (see Würz, Stefan (ed.) (2003): European Stock-Taking on Models of Employee Financial Participation, Results of ten European Case Studies, Wiesbaden, p. 59).

(e.g., Ireland), tax incentives are less important and, in any case, cannot be as large as in high-tax countries.[65]

➢ **Tax incentives effectively promote the spread of financial participation**

Countries with a long tradition of employee financial participation (e.g., UK, France)[66] universally confirm this experience, but so do countries where tax incentives are quite recent, e.g., Austria,[67] where a substantial increase has been observed, even though total numbers are still relatively low.

According to the above graph by EFES representing the increase in the number of European widest companies offering financial participation plans from 1945 to 2007, introduction of tax incentives in most Western European countries has led to a significant increase in the number of plans in the short-term and a steady growth in the long-term. In most countries, the angle of the graph representing increase becomes steeper following the years in which tax incentives were introduced (e.g. Denmark 1987 and 2003; Finland 1996; France 1986 and 1994; Ireland 1986 and 2001; the Netherlands 1994 and 2003; UK 1980, 1984 and 2000). However, in some countries there is no correspondence between the introduction of tax incentives and the increase in the number of plans (e.g. Greece (increase since 1999, although tax incentives since 1987; Portugal (increase 1993 until 2000, although tax incentives since 1969); Austria (increase since 1997, although tax incentives since 2001). In each deviating case it can be explained by country-specific circumstances. It is common to all deviating countries that they have (or have had until recently) only insignificant tax incentives and a small number of financial participation plans. In Portugal, a vast majority of plans emerged as a result of privatisation in the 1990s, because in this procedure substantial incentives, not only concerning taxes, were granted to the workers of privatised enterprises; all these incentives were abolished after privatisation procedures were completed at the end of the 1990s. In Greece, complexity of regulation and lack of information about financial participation prevented the companies from introducing broad-based plans, although tax incentives were introduced quite early; since 1999, tax incentives for stock options were introduced and utilised generally by executives. In Austria, profit-sharing, although not linked to tax incentives, traditionally makes up the major part of financial participation plans. However, the increase of originally almost non-existent share

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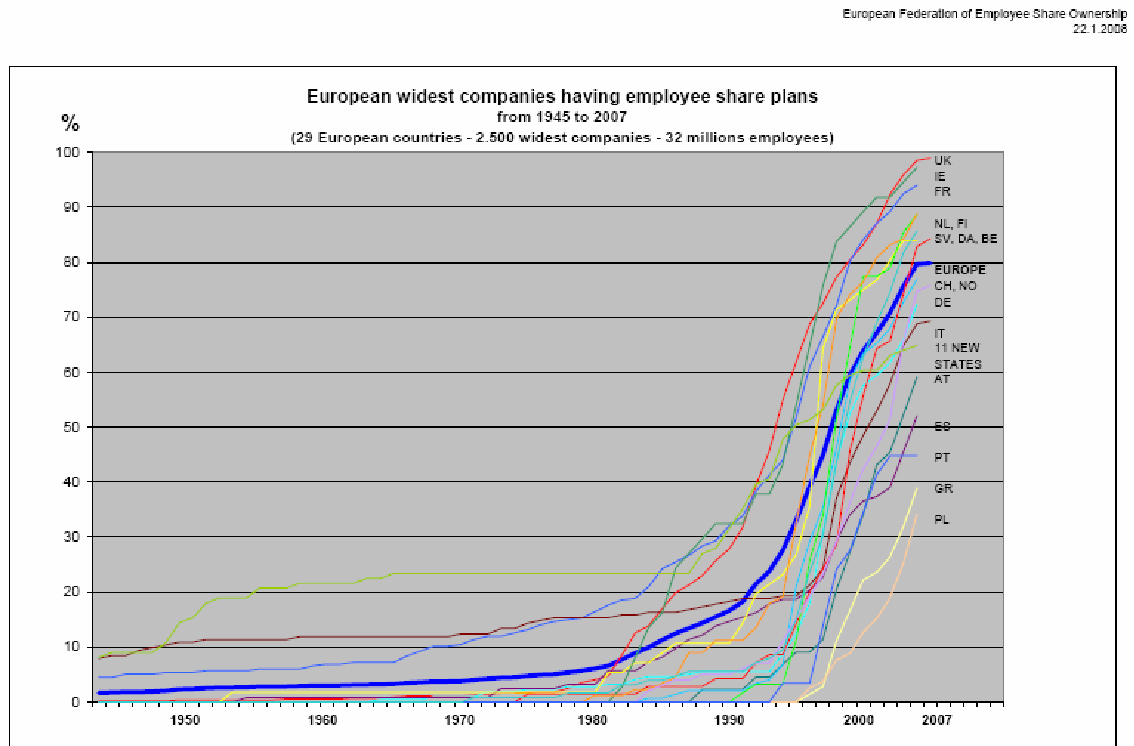
65 It should be noted that in countries which are considered low-tax, not all statutory taxes are necessarily low; the statement refers only to low statutory taxes. For example, in Ireland, corporate income tax is exceptionally low (12.5%), whereas personal income tax is close to the EU average (20-42%). Therefore, most tax incentives for employee financial participation in Ireland concern employees and not employer companies. The Irish Government declared that no tax relief which reduced the revenue from corporate income tax can be introduced because the low tax rate leaves very little leeway (Irish Department of Finance, TSG 98/12).

66 In France, legislation on voluntary employee financial participation without tax incentives of 1959 and even legislation on compulsory employee financial participation without tax incentives of 1967 did not lead to a significant number of plans in operation. Only in 1986 when the first tax incentives were introduced did the number of plans increase rapidly; this upward tendency has been supported by the introduction of new tax incentives (see Würz (2003), p. 39). In the UK, although profit-sharing has existed since the 19th century and share ownership since the early 1950s, the number of plans remained small until the first tax incentives were introduced in 1978. Since then, the system of tax incentives and economic efficiency of incentives and plans are regularly reviewed by the government, and the number of plans is steadily increasing, especially Revenue Approved plans (see Würz (2003), p. 130; <http://www.ifsproshare.org>, Log-in: 20.07.2007.

67 In Austria, only 8% of employee financial participation plans were implemented before first tax incentives were introduced in 1993, while 45% of plans were introduced in four years after more substantial tax incentives became effective in 2001 (see Kronberger, Ralf, Leitsmüller, Heinz, Rauner, Alexander (eds.) (2007): Mitarbeiterbeteiligung in Österreich, Wien, p. 32).

ownership plans was substantial after the introduction of tax incentives in 2001 according to national statistics; it can only not be seen on the graph due to the still low percentage of share ownership as compared to profit-sharing plans.

Figure 13. European largest companies having employee share plans



4. Conclusions

Firstly, tax incentives should (and in most countries actually do) target those taxes which constitute the heaviest burden in the national taxation system. Usually (with the exception of countries with flat tax systems which at present do not offer specific tax incentives) these are the progressive personal income tax and social security. Many countries therefore provide:

- exemptions from social security contributions for certain plans (e.g., France, Belgium, UK, Ireland, Finland),
- levying a capital gains tax (e.g., UK, for dividends Belgium),
- levying a special low tax (e.g., France) in lieu of personal income tax, and
- tax allowances for personal income tax (e.g., Austria, Finland, Ireland).

Secondly, tax incentives should be provided for both employees and the employer company, inasmuch as participation is voluntary for both parties in all EU Member States except France.

However, this requirement is relative: in most countries the employer company has already been granted tax incentives in the form of deductions under general taxation law and only tax incentives for taxes involving the cost of shares and stock options are needed. In most countries, the only important incentive for the employer company is the exemption from social security contributions; this has actually been introduced in many countries (e.g., France, Ireland, Finland, Belgium). The employee is usually more in need of direct incentives as the heaviest burden of progressive taxes falls on him or her.

Thirdly, even substantial tax incentives may prove inefficient when the pre-conditions of eligibility are too restrictive, complex or inflexible. This is the case (e.g., in Greece) for cash-based profit-sharing and in Germany and Belgium for schemes of all types.[68] The flexibility problem can be solved, as in Ireland and the UK, by allowing the employer company to choose between less flexible approved schemes combined with substantial tax incentives and more flexible unapproved schemes combined with minor tax incentives. Another interesting approach was presented in the EC Report on Stock Options[69]: Since direct taxes cannot be harmonised under the effective EU Treaty, as shown above, it might be reasonable to harmonise the pre-conditions for the application of tax incentives where they exist in a particular country. National legislators would be authorised to introduce additional national plans and to decide the size and the form of tax incentives for these as well as for those plans encompassing all of Europe. Harmonisation can only be accomplished if the existing pre-conditions in different EU Member States are at least comparable for all types of employee financial participation schemes, as is apparently the case for stock options. This comparison will be made in the forthcoming PEPPER IV report.

Fourth, some forms of tax incentives are more favourable for certain types of plans and also lead to higher efficiency:

- For share ownership and stock options as far as benefit taxation is concerned: generous valuation rules combined with a favourable taxation moment (often linked to holding period), and, if possible, exemption from SSC for both the employer company and the employee.
- For dividends and sale of shares: a special tax rate or capital gains tax in lieu of personal income tax and, if necessary, exemption from SSC.
- For ESOPs and Intermediary Entities: exemptions from income tax on share acquisition[70] or on share sale if the profit is realised after a holding period or within a retirement program; the company may qualify for tax relief on both interest and principal payments on the loan; sale of stock to an ESOP on a tax-deferred basis if the proceeds of the sale are reinvested in securities of other domestic corporations (tax-free rollover).
- For profit-sharing: a special tax rate in lieu of the progressive personal income tax as well as exemption from SSC for both the employer company and the employee.

However, the most effective forms of tax incentives do cause revenue losses. Therefore, efficiency should be weighed against the revenue requirements of each country independently. Should a government wish to introduce specific tax incentives, it might well begin with 'soft'

68 See EC (2003), Cross-border obstacles, p. 17, 24.

69 See EC (2003), Stock Options, p. 42, 43.

70 In Ireland this is the case only where the ESOP comprises an ESOT working in tandem with an Approved Profit Sharing Scheme.

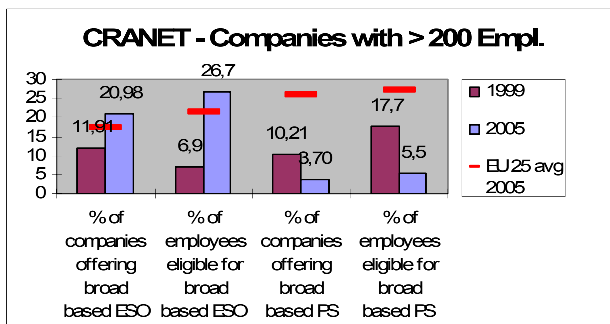
tax incentives which do not cause substantial revenue losses, e.g., tax allowances defined by nominal amount (as in Austria). Later, depending on revenue needs and the political climate, it may proceed to more effective measures: tax allowance as a proportional amount, deductions, tax credits, introduction of special low tax rates, and, finally, full exemption from taxation.

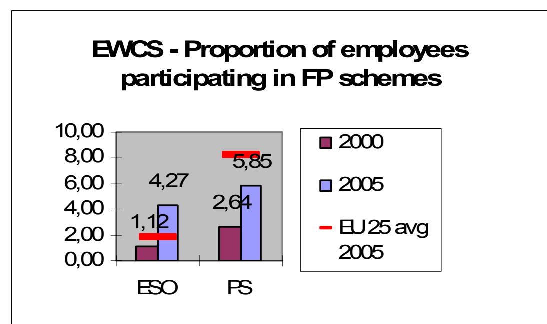
Fifth, in spite of the difficulty of their implementation at the European level (because of the exclusive jurisdiction of national legislation over tax law), tax incentives remain powerful tools for enhancing and broadening financial participation. This is especially true when they remain optional for the Member States and not subject to a unanimous vote of approval. Countries could voluntarily offer tax incentives singly or in groups. Such a step would create an increasingly favourable environment in which countries having an advanced tradition, such as France or the United Kingdom, would encourage emulation. Optional preferential treatment as part of the Building Block Approach requires distinguishing between profit-sharing schemes, share ownership schemes and employee stock ownership plans.

Part 2 – Country Profiles

I. Belgium

Some forms of employee financial participation began to emerge at the end of the 19th century; the number of plans, however, remained very small, especially between 1945 and 1990. The Belgian government introduced the first incentives for employee share ownership in King's Arrest 'Monory-De Clerq' on 9 March 1982. These provisions were primarily intended to support the stock exchange in the wake of a financial crisis; among them was share ownership, submitted in a proposal by the Liberal Party. Still applicable, these provisions have proved efficient. Additional incentives were introduced in 1991 by the Law on Equity Capital Incentives. The Law on Incentives for Stock Options of 26 March 1999 and the Law on Promotion of Employee Financial Participation of 22 May 2001 followed. Both of the latter laws introduced tax incentives for profit-sharing and employee share ownership schemes. However, the number of plans continues to be relatively small. Approximately 10% of large, primarily multinational companies in the financial sector had employee share ownership plans in 1999.[71] Stock option plans have become relatively widespread. Over 40% of enterprises with more than 50 employees offered stock option plans in 2002.[72] Many of these, however, are limited to management.





71 Priewe/Havinghorst (1999), FES-Wirtschaftspolitische Diskurse Nr. 123.

72 PriceWaterhouseCoopers (2002).

1. General Attitude

Especially since the end of the 1990s, the government has supported employee financial participation, regarding it as a pillar of the social security system. However, legislative proposals have been introduced into Parliament from the beginning of the 1970s. These were mainly sponsored by the Liberal Party, although until 1999 the Socialist Party blocked all such proposals. At the end of the 1990s, the government announced a new employee financial participation promotion campaign intended to spread financial participation to 25% of all employees. The employers' associations (e.g., Federation of the Belgian Enterprises, National Federation of Small Firms and Traders) had given support to employee financial participation even earlier, seeking to influence the government through campaigns in the mass media which were obviously successful. The employers' associations, however, mainly favour financial participation only for executives and higher management. The trade unions (especially the largest, the Christian Unions and the Socialist Unions) generally oppose any form of employee financial participation on the grounds that employees are powerless to influence competitiveness or profitability. To a certain extent, they do support employee share ownership plans not financed from the wages or salaries of employees.

2. Legal and Fiscal Framework

The Law on Promotion of Employee Participation of 22 May 2001 regulates in detail the procedure for establishing employee financial participation plans, especially cash-based and share-based profit-sharing. Terms and conditions prescribed by law (e.g., rules for calculating length of employment, duration, mandatory or non-mandatory participation of employees, and blocking period) must be introduced by a collective agreement or, in companies without union representation, by a collective agreement or an act of accession. Terms and conditions not prescribed by law can be introduced by the employer company upon consultation with the workers' council; in companies without a workers' council, with the committee for prevention and protection at work; in companies without such a committee, with the union delegation, and in companies without union representation, with all individual employees. For group level plans, it is sufficient that the company which first proposed the plan within the group concludes the collective agreement and the other companies consult with their employee representatives. Moreover, the bodies representing employees must be informed of how the plan relates to the company's employment development and employment policies before the plan is introduced. Plans must include all employees, with the possible exception of employees with less than one year of service; different classes of employees may be treated differently under the plan if this is the industry-wide collective agreement or a Royal decree. Plans are generally voluntary, unless the collective agreement or the act of accession provide otherwise. The size of the plan is limited by a double ceiling; the total annual amount of transfers under the plan cannot exceed 10% of the payroll and 20% of the annual profit after taxes.

a) Share Ownership

Employees may be granted shares, share certificates or stock options under an employee share ownership plan. If the shares are held two to five years, the special tax of 15% on the benefit (if shares are transferred free or at a discount) applies. The blocking period terminates earlier if the employee is dismissed, resigns for serious cause, retires or dies, or if the plan shares are publicly offered, if control of the company has been changed by the transaction, or if the employee is transferred to a non-affiliated company under the collective agreement 32bis. Shares sold during the blocking period are subject to an additional punitive tax of 23.29%. Stock option plans are governed by a special law.

Share Ownership Plans – If restricted stock is granted free, the benefit can be taxed at grant or, if ownership is transferred later,[73] at vesting. The tax base is the market value of publicly traded stock. If ownership is transferred later, the tax base is reduced to the market value less 20/120 (i.e., 16.7%) to compensate for market risk.

On common stock granted free or at a discount, the benefit corresponds to the fair market value of shares or so-called net asset value[74] of privately held shares. The tax base can be reduced to 100/120 (i.e. 83.33%) if the company grants a 'substantial' number of shares. This is the case if the purchase of shares by the company on the stock market may be expected to be followed by a drop in price. However, this might be difficult to prove if the stock is traded at a large stock exchange and there is a liquid market. The employer company can deduct the discount from the tax base of the corporate income tax if the stock is purchased and sold by a foreign company which charges the discount back to a Belgian company. If a Belgian company purchases and sells the stock, the deduction is subject to debate: if the discount is regarded as capital loss, it is not deductible, but if it is regarded as personnel costs, it can be deductible. However, it is probable that the tax authorities will generally favor the more restrictive option.

Stock Option Plans – Stock option plans to which tax incentives apply are governed by the Law on Incentives for Stock Options of 26 May 1999. This law applies to stock options granted as of 1 January 1999. Stock options are taxed at grant. If the employee does not notify the tax authority within 60 days after grant, the option is considered refused.[75] Since employee stock options are usually not tradable, the tax base is generally a lump sum value equal to 15% of the underlying stock value at grant plus one percent for each year or part of the year beyond the initial five years from grant to expiration. The tax base can be reduced by half (i.e., to 7.5% plus 0.5% for each year or part of the year) if options cannot be exercised until three years from the date of issue; if the exercise period does not extend beyond the tenth year following the year of issue, options are transferable only upon death of the employee; the underlying shares are of the employer company, its parent or grandparent company, no guarantee was issued by the employer company or an affiliated company against fall in value of the underlying share after its grant, and the strike price was determined at the time of offer. No compulsory social security contributions need by paid on the lump sum benefit. The employer company can deduct the difference between the market value of the underlying stock and the

[73] A criterion of a later ownership transfer is that no dividends are paid to the employee during the blocking period.

[74] The net asset value defined as the amount of company net equity and reserves divided by the total number of shares.

[75] Until 24 December 2002 it was considered as acceptance of the stock option.

exercise price of the option if the employee obtains shares from another company upon exercise and the costs are charged back to the Belgian company. Stock option plans and the prospectus must be approved by the Bank and Finance Commission prior to the introduction.

b) Profit-Sharing

Profit-sharing plans are usually cash-based. For small enterprises, defined in the Company Code, the so-called investments savings plan was introduced. Under these, an employee immediately loans his share of the annual profit to the company; the loan must be repaid within two to five years with interest. Tax incentives and pre-conditions for interruption of the blocking period for these plans are the same as for share ownership plans. All profit-sharing plans are subject to special tax rates on the attributed profit share: 15% for investment savings plans and 25% for other profit-sharing plans. No social security contributions are imposed. The employer company cannot deduct the profit attributed to employees from its corporate income tax base.

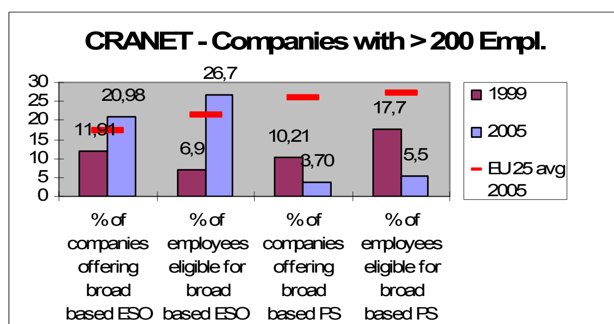
c) Participation in Decision-Making

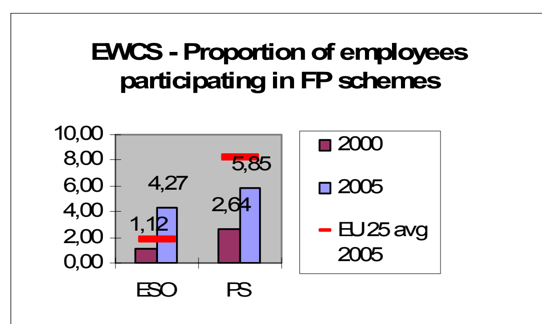
Participation in decision-making has no connection with financial participation; financial participation plans are specifically forbidden to extend existing decision-making rights. However, the plan can only be introduced when a collective agreement or an act of accession and consultation with employees' representatives is prescribed for the remaining part of the plan so that terms and conditions are negotiated with employees' representatives; thus some elements of participation in decision-making may be included in the financial participation plan.

There is no system of board level representation in the private sector in Belgium, except of employee representatives on the boards of a few state-owned companies. Workplace representation in Belgium runs through two separate channels. The works council represents the whole workforce, although it is only elected in larger workplaces (above 100 employees, see Law on the organisation of the economy, first passed in 1948 and subsequently amended). The trade union delegation represents trade unionists (regulated by a series of legally binding collective agreements covering the vast majority of employers, with the national level agreement signed in 1971 and agreements for individual industrial sectors reached later). The two bodies have different functions, but generally it is the union delegation which negotiates key issues with management, although the works council has extensive information and consultation rights, and although it is a joint body with an employee majority, it has decision-making powers in some areas. The employer must consult the works council on cases of mergers, closures, business transfers, large scale redundancies, training plans and the introduction of new technology, as well as other major developments likely to have an impact on employment. The trade union delegation also deals with disputes between the employer and the workforce, both on an individual and collective basis. The decision-making power of the works council includes introducing or changing works regulations; the general criteria for redundancy and re-hiring; the timing of annual and other holidays; and the management of social benefits, including pension funds etc.

II. Bulgaria

The development of PEPPER schemes in Bulgaria has been influenced, on the one hand, by the historical commitment to a strong cooperative movement (percentage of coops among industrial enterprises ranging from 8.5% to 10.4% between 1980 and 1988, corresponding numbers for personnel – 6.8% and 6.7%, Source: NSI) and, on the other hand, by the special circumstances accompanying the transition to a market economy. The main form of employee financial participation became employee share ownership, with the voucher system being the prevailing privatisation method at the beginning of transition 1992-1994 (however, the proportion of enterprises privatised this way was low, approx. 4-5%) and the management employee buy-out (MEBO) method gaining support from 1994 until 2000 (1,436 or 28% of 5,165 deals, Source: Minchev, 2004). Almost half of the enterprises were privatised by insiders, but employee ownership has decreased over time. Although no data on the sales of shares by employees after privatisation are available, it can be fairly estimated that about 10% of enterprises privatised by MEBO may still be under majority employee ownership. According to the Centre for Mass Privatisation, shares immediately at the close of mass privatisation in 1998 were distributed as follows (Miller and Petranov, 2000): 40.8% state property; 6.4% employees; 12.9% individual shareholders, and 39.9% privatisation funds. Subsequently, however, these employees' shares were transferred to managers and outside owners. Profit-sharing has developed only very recently as the private sector began to stabilise and human capital became a major factor in company success.





1. General Attitude

Three trade union organisations are recognised as representative at the national level: the Confederation of Independent Trade Unions in Bulgaria (CITUB), the Confederation of Labour Podkrepa (Podkrepa) and Promiana. From early transition on, CITUB has been in favour to the development of financial participation, with its leader Kastriot Petkov writing books on the issue, including concrete proposals on how to help the workers to get more involved in

the capital, profits and decisions of their company. The transition period has brought about a significant change in the power relationship between social partners. In the beginning, trade unions dominated the social dialogue. The newly emerged trade unions, with tremendous popularity and influence in the society, made 'green' investments at the beginning of the transition period.[76] For example, CL 'Podkrepa' established an insurance company and made unsuccessful attempt to register a bank. One of the most effective trade union associations making investments was CITUB participation in the Privatisation Fund 'Labour and Capital'. Through that successful fund, CITUB indirectly acquired a high percentage of shares of many enterprises. Thus, the trade union activists were directly involved in the management of those enterprises, although CITUB sold its shares to other owners later. The end of the privatisation process saw their power and influence drastically decrease. In recent years, the employers' associations have grown more powerful than the trade unions. Until 2005, employers have been represented by a couple of national associations.[77] Employers' organisations currently do not consider employee financial participation an important issue in either their policy or practice.

The 39th Bulgarian Parliament which vested power in the national government under Prime Minister Simeon Sakskoburggotski (2001-2005) did exhibit interest in the questions of financial and decision-making participation of employees. Under the guidance of Prof. Dr. Ognyan Gerdzhikov, at that point President of Parliament, a comparative legal survey on the national solutions within the European Union and some adjacent states was conducted. The survey, focussing on joint-stock companies, identified a number of national regulatory mechanisms[78] and possibly contributed to the popularity of the ideas behind them. However, the survey resulted in no relevant act of law. The new government (since 2005) under Prime Minister Sergey Stanishev is sceptical of the concept of Financial Participation. Furthermore, this issue has not been on the political agenda of Parliament nor has any political party currently addressed it.

2. Legal and Fiscal Framework

There is no specific legal regulation of any PEPPER scheme but the legal framework provides neither incentives nor restrictions concerning employee financial participation.

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76 Trade unions inherited property from the former state trade union, which was transferred to trade companies controlled by the trade unions at the beginning of transition. Some of these companies were very profitable, e.g. the company issuing Trud newspaper (one of the most popular national newspapers) and managing holiday houses.

77 I.a. the Bulgarian Industrial Association (BIA) - 2,481 affiliated employers, the Bulgarian Chamber of Commerce and Industry (BCCI) - 2,262 affiliated employers, the Union of Private Bulgarian Entrepreneurs Vazrazhdane (UPBE) - 873 affiliated employers, the Union for Private Economic Enterprise (UPEE) - 660 affiliated employers, the Employers' Association of Bulgaria (EABG) - 828 affiliated employers and the Bulgarian Industrial Capital Association (BICA) - 862 affiliated employers; all according to the most recent census data.

78 The summary is available in Bulgarian under <http://www1.parliament.bg/students/95_bg.htm>.

a) Share Ownership

Privatisation (1992, 1997, abolished in 2002) – In the course of privatisation pursuant to the Law on the Reorganisation and Privatisation of State and Municipal Enterprises of 7 May 1992[79] (hereinafter referred to as LRP) prior to 2002 employees with Bulgarian citizenship and permanent residency in Bulgaria were entitled to one of two methods of preferential (free or discount) share acquisition. If the privatisation organ had included the target enterprise in the list of public-owned merchant entities to be privatised by the means of voucher (mass) privatisation, each eligible individual could obtain free shares. The total value of the free shares distributed could not exceed 10% of the nominal stock of the target entity. This privilege was abolished in 1998 when voucher privatisation was virtually abandoned. If the privatisation entity had chosen the stock-sales method, eligible individuals were entitled to acquire up to 20% of the nominal stock at 50% of the assessed price. This privilege was abolished on January 2002. The share acquisition[80] itself had no tax relevance. Subsequently, dividends received were subject to the general rule on dividend taxation.

Following the respective LRP-sections came three separate entitlement provisions, hereinafter referred to as 'the 25-rule', 'the 30-rule' and 'the 35-rule'. All three are based on the so called 'MEBO-company'[81], a legal entity established by individuals of a designated status for the sole purpose of participating in the privatisation process. A general incentive for a MEBO-company was the stock exemption provided by Par. 6 Subsection 1 of the Temporary Arrangements of the amendment of the Commercial Act from 1997[82]. MEBO-companies were then permitted to maintain stock of only 10% of the minimum stock generally required for stock corporations or limited liability companies under the Bulgarian Act. A further incentive from which a MEBO company could generally benefit was the VAT exemption of the privatisation deal. Yet another incentive was provided by Section 58 of the abolished Profit Tax Law[83]. As long as the chosen privatisation mechanism (this was the case with the 25-rule) allowed the public hand to keep a minority share in a target company it was possible for this target company to receive a 100% profit tax exemption for three years after concluding the privatisation contract. For the following two years the exemption was 50%. The '25-rule' provided for preferential payment conditions applicable to the privatisation of a state or municipal enterprise that had previously been commercialised into a merchant entity under the Commercial Law. At least 20% of the target company's employees had to be members, shareholders or partners in the MEBO-company. The '30-rule' contained an identical payment privilege applicable in cases of privatisation of state and municipal enterprises (or integrated substructures) that had not previously been commercialised. At least 30% of the employees of the target enterprise had to be members, shareholders or partners in the MEBO-company. Further issues were resolved in compliance with the '25-rule'. It is the '35-rule' that provided for both immediate transfer of property and preferential payment conditions. It applied to enterprises (or integrated substructures) of minor value that had not previously

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79 DV 1992, 38, abolished DV 2001, 42.

80 The number of free shares obtainable was defined in each case by the ratio between the individual share price as assessed by the Council of State Secretaries, on the one hand, and the sum of the latest 24 indexed gross salaries of the eligible individual on the other hand.

81 In Bulgarian: 'rabotničesko-medidžărsko družestvo'.

82 Zakon za izmenenie i dopălnenie na tărgovskija zakon, DV No. 100/1997.

83 Zakon za danăk vărhu pečalbata, DV No. 59/1996.

been commercialised. Thus, until March 2000, MEBO companies had significant advantages, especially concerning the acquisition price being about 36% less than for other buyers.[84]

The effective Law on Privatisation and Post-Privatisation Control of 19 March 2002 proclaims in Art. 7 the equality of privatisation candidates as a general principle of Privatisation Law. The law establishes no privileges based on the status of the applicants. In particular, there are no provisions in favour of employees. The current privatisation legislation is a negation of the former LRP which provided a number of preferential measures to facilitate employee participation. These were intended to narrow the social gap between capital owners and the labour force that the liberalisation of the Bulgarian economy opened during the post-communist era.

Private Companies – Commercial Law[85] (hereinafter CL) and company law in general contain no specific regulations pertaining to employee share ownership. In the absence of statutory regulation, therefore, certain general provisions[86] will be examined here. There are no general squeeze-out and sell-out rules concerning the minority shareholders of a joint stock company. However, the Law on Public Offers of Securities obliges a shareholder who has acquired 50% of the stock of a public joint stock company and wishes to keep this majority position to make an economically justifiable public offer to acquire the remaining shareholders shares (Art. 149). The majority shareholder does not have the right to vote in the General Assembly until that offer. This public offer is the only legitimate means of capital concentration available to the majority shareholder. Upon its expiration, he may acquire an additional 3% of the stock per year. Also, where a shareholder of a limited liability company or a joint stock company has voted against a Mergers and Acquisitions deal (Art. 263c CL) or a joint-venture project (Art. 126e Law on Public Offers of Securities) he/she has the right to have his/her shares bought by the company.

b) Profit-Sharing

Bulgarian employers do not usually link employee bonuses to the company's financial success. While not forbidden, employers generally derive no benefits from such schemes under Bulgarian tax law. However, under Bulgarian Law it is possible to offer profit-sharing solutions on an individual contract basis.[87] These may be cash-based or share-based.

c) Participation in Decision-Making

In the majority of cases employee ownership did not lead to participation in management. Currently, most employees are minority shareholders without notable influence. The rights of employees to participate in decision-making under the Labour Code[88] are extremely limited and have no significant influence on management. While the workers' meeting composed of

84 See Ivanova and Keremidchiev, Extended report Financial Participation in Bulgaria, p. 29, according to the calculations of the authors.

85 DV 1991, 48 as amended in DV 2005, 66.

86 Since associations limited by shares are extremely rare in Bulgaria the examination will disregard them and concentrate on limited liability companies and joint-stock companies only.

87 Joint stock company offers of any of these incentives to a Council or Board member, must be approved by the general meeting for every beneficiary on an annual basis.

88 Labour Code of 1986, DV 1986, 26 as amended in DV 2005, 83.

all employees of a given business once accounted for more than 20 sections[89] of the socialist version of the Labour Code, only two relevant provisions are presently in force. These empower the workers' meeting to choose between two or more drafts of a collective bargaining agreement when the trade union organisations at the enterprise level cannot agree on a single version (Art. 51a (3) Labour Code). Also, the workers' meeting can decide the disposition of the company's social fund (Art. 293 (1) Labour Code). The employer, however, is not obliged to establish such a fund. The Commercial Law provides that an employees' representative must be chosen in corporations[90] employing more than fifty persons. This representative must be given an advisory vote at the shareholders' meeting. The company is under no obligation to recognise more than one representative as its work force grows. Also, the number of employees has no effect on the form or the force of employee representation. Thus the Commercial Law establishes a model friendly to the employer.

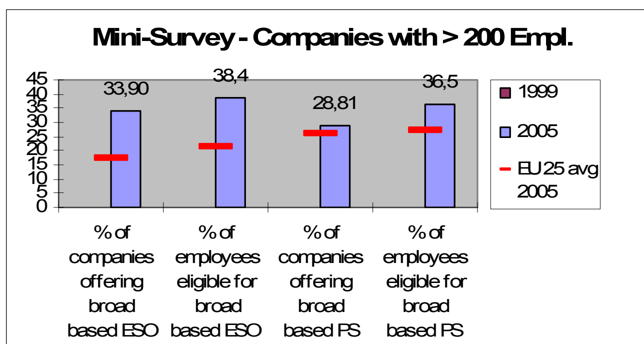
89 Art. Art. 12-32 Labour Code were abolished in 1992.

90 Commercial Law: Art. 136 (3) (for limited liability company), Art. 220 (3) (for joint stock company) and Art. 253 (2) (for a partnership limited by shares).

III. Croatia

Despite the fact that the economic and political system of Croatia, while it was a part of the former Yugoslavia, was based on employee participation for more than 40 years, today its role is relatively minor. Employee stock ownership created in the early stages of privatisation is steadily diminishing; the position of employees, previously strong, has weakened. By 1995, small shareholders owned (bought or subscribed) about 20% of the nominal value of the enterprises privatised during this first stage (Jelušić and Perić, 1999; Tipurić, ed., 2004). During the second (1995-1999) and third (1999-2002) stages of privatisation, support for employee participation ceased and employee ownership gradually declined and that share had fallen to only 12% in 1998 with the decline continuing up to the present moment. There is little public support for measures which would reverse this decline. ESOP models, defined as any organised programme involving large numbers of employees as shareholders in the enterprise, is almost the only form of employee financial participation that has been developed and gains momentum after privatisation; but ESOPs are rare and lack broad support. In a study from end-2003 (Tipurić et al., 2004) 'organized programmes of larger involvement of employees in the enterprise ownership' were found in 9.4% of enterprises (52 out of the 552 total surveyed)[91]. Employees owned 10% of shares in 68% of enterprises reporting; in only 5% of firms did employees own more than 90%. Employees held a majority share (over 50%) in 12% of enterprises.[92]

Profit-sharing is rare – no mention of it is found in legislation, legal documents or collective agreements.



[91] In many cases analysed in the study, ESOP programmes were stopped or completed, and some programmes had only a few ESOP characteristics in their design.

[92] See also PEPPER III, pp. 118 f., 123 (Table 1).

1. General Attitude

Trade unions had no part in the design of the privatisation models, nor did they promote a stronger position for employees.[93] Not until the first two stages of privatisation had been completed did some unions and union leaders begin to advocate employee ownership as a means of privatising remaining state-owned assets, as well as for restructuring distressed enterprises, and to propose models for doing this. Employees are represented by numerous trade unions organised at different levels for various purposes. At present there are four major trade union confederations, as well as a number of smaller associations and independent trade unions. After declining at the beginning of the 1990s, union membership has remained stable. While there are no statistics on this issue, a rough estimate of trade union membership ranges from 20% to 50%. Employers, represented by the Croatian Association of Employers, have a stronger position in most issues involving the interests of employers and employees. The fact that employers are represented by a single organisation and employees by many only partly explains this disparity in power. On the issue of employee financial participation, employers and their organisation remain publicly non-committal – neither positively in favour nor adamantly opposed.

Croatian governments did not support employee privatisation beyond the first stage; instead, they focused their efforts on attracting outside investors, even at the price of lower output, less employment, diminished assets and worse business results in general. While this policy was entirely consistent with the ideological orientation of the right-wing governments in power during the first decade of transition, it is less easy to explain why the Social Democratic governments, in office from 2000-2004, made virtually no changes in the area of employee participation. Nor has the present government shown any serious intention of introducing measures to promote or at least to regulate employee financial participation. Some business spokesmen, representing firms that already have employee ownership in some form, have publicly advocated greater employee participation in the privatisation of the remaining state shares. They have also requested clearer regulation and support of existing schemes. These requests are currently being discussed but a concrete feedback on these proposals either by the government or political parties is still pending.

2. Legal and Fiscal Framework

Employee financial participation is at present not explicitly regulated. Privatisation legislation in the past, however, has supported employee share ownership. Various schemes of financial

[93] The Statute of Parliament 2000 authorizes social partners to participate in the work of Parliamentary committees, thus giving them direct influence over the drafting of laws dealing with such matters as employment and industrial relations.

participation, including profit-sharing and ESOPs,[94] occur in individual firms despite the absence of state regulation. Amendments to the Privatisation Law, now being drafted, are expected to bring ESOPs into the regulatory fold.

a) Share Ownership

Privatisation (1991, 1996) – The Croatian Law on the Transformation of Enterprises Under Social Ownership 1991[95] (hereinafter referred to as the 'Transformation Law') gave employees (including managers and former employees) the right to buy shares at a discount proportional to their years of employment, starting at 20% and adding one percent for every working year up to a maximum of 60%. Employees who paid for their shares in cash were given an additional discount of 10%. Payment could also be made in instalments spread over five years.[96] After having paid 5% of the total price, the employee received all his or her discounted shares outright. Amendments to the Transformation Law in 1993 entitled employees to buy no more than 50% of total shares with a value not to exceed 1 mln. EUR. One-third of the remaining shares were transferred to state pension funds and two-thirds to the state Privatisation Fund with the purpose to be publicly tendered at market value.

After most enterprises had been privatised under the provisions of the Transformation Law in 1996, a new act, the Privatisation Law (PL)[97], was adopted, which provided no special provisions or preferential conditions to employees.[98] The Transformation Law, however, was not repealed, and after 1996, some enterprises were still utilizing it. In companies where small shareholders owned a significant amount of stock, so-called small shareholder associations were established. Although these did not take the form of registered associations and their membership was unstable, they did gain some influence in some enterprises because of a close relationship with trade unions. Since privatisation was partly reversed in 1999, many shares of state enterprises still remain to be privatised.[99] After the bankruptcy of 22.2% of all privatised firms, the remaining assets were transferred back to the state Privatisation Fund. By 1999, 379,030 out of 641,152 sales contracts of employees who were buying discounted shares in instalments had been broken. Recognizing that the objectives of privatisation had not been achieved, a new law, the Law on Revision and Transformation and Privatisation, went into effect on 16 May 2005. The privatisation of 1,556 enterprises was investigated under this law; procedural irregularities were discovered in all but 75.

Private Companies (2003) – According to Art. 233 (2) of the new Company Law[100] from 2003 (hereinafter referred to as CL), a company can issue special employee stock with a value

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94 In this context, the term ESOP is applicable to all schemes where employees make an offer to buy shares of the company, the purchase is funded by special credit, and a new company is formed in order to administer the shares.

95 Of 23 April 1991, Official Gazette of the Republic of Croatia, No. 19/91, as amended.

96 This period was later prolonged to 20 years.

97 Of 14 March 1996, Official Gazette of the Republic of Croatia No. 21/96, as amended;

98 Instead Vouchers were distributed to 230,000 persons who had suffered under the former socialist regime: refugees, displaced persons, war veterans, war invalids, families of dead or missing soldiers, and political prisoners; these, together with employees, made up the category of small shareholders.

99 Privatisation is presently regulated by the Transformation Law of 23 April 1991, the Privatisation Law of 19 March 1996 and the Law on Takeover of Joint-Stock Companies of 17 July 2002.

100 Of 23 December 1993, Official Gazette of the Republic of Croatia No. 111/93, as amended.

not exceeding 10% of registered capital. Employee shares are non-voting until fully paid for. Further, Art. 313 CL stipulates a 'conditional capital increase' for the purpose of fulfilling the employee' acquisition right. In order to facilitate employee acquisition, Art. 234 CL exempts the company from the general prohibition against borrowing in order to acquire its own stock. This exemption is granted on condition that a reserve is created so as not to endanger equity capital by the sale of shares to employees. Since employees – including those who became shareholders during the course of privatisation – are usually minority shareholders, provisions protecting this class are also relevant. A 3/4 majority of votes representing equity capital is required to change the Articles of Association. Shareholders holding at least 10% of the equity capital have a voice in decisions made by the General Meeting on liability of members of the Board of Directors or of the Supervisory Board (Art. 273 CL); they can also lodge a claim at court to remove a board member for cause. Shareholders owning at least 5% of shares can call the general meeting. A majority shareholder who holds at least 95% of total shares can buy-out minority shareholders, at fair compensation, if the general meeting so resolves (Art. 300 CL).

Draft Legislation (2005/2006) – Amendments to the PL are planned to provide several different schemes for selling shares to employees on preferential terms.[101] According to the present draft, the State Privatisation Fund would be authorized to sell shares to a joint stock company on condition that the latter offer these shares to employees on the same or better terms. The ESOP model is an additional option. The management and employees of a joint stock company could form a new company ESOP limited liability company. The new company will take a credit from the bank, based on the pledged shares and pay off the shares to the Privatisation Fund as a single payment. If none of these schemes suit, the Privatisation Fund can sell shares directly to employees; shares thus acquired are voting shares. Enterprises that at the time of privatisation were not under social ownership, but administered by their managers and work force, according to 'rights to administer' are a special case. They can transfer these rights back to the company, which – according to the draft – would increase the company's capitalisation. The new shares created would be assigned to the Privatisation Fund, which would then offer them for sale to those employees who were with the company at the time of privatisation. Although the draft was withdrawn in 2007 from Parliament it is still referred to in the ongoing discussion.

b) Profit-Sharing

There is no legal regulation of profit-sharing and hence no incentives. Although individual enterprises offer monetary incentives, especially to managers, bonuses are usually not linked to company profit. They are regarded as wage compensation and taxed accordingly.

[101] The draft law is prepared by the legislative committee of Parliament in the course of harmonisation with the EU law and is supported by trade unions and employers' associations; see the website of the Parliament <http://www.sabor.hr/default.asp?mode=1&gl=200309170000001_&jezik=1&sid=>, Log-in: 12 December 2005 (in Croatian).

c) Participation in Decision-Making

Participation in decision-making is expressly regulated by both the CL and by the Labour Law[102]. These laws almost completely correspond with counterpart EU legislation. Employees of a private company employing at least 20 regular employees have the right to a voice in decisions which affect their economic and social rights and interests, under conditions and procedures prescribed by the Labour Law. Employees of such companies are entitled to elect one or more representatives to the employees' council by means of a free, direct and secret ballot. The function of the council is to protect and promote the interests of employees vis à vis the employer.[103] If no employee's council has been established, the trade union assumes its powers. According to Art. 158 of the Labour Law, at least one[104] employee representative is to be a member of the Supervisory Board in companies employing an annual average of more than 200; also in companies which are public institutions, or in which the state owns at least 25% of shares. It should be noted that this provision is in conflict with a company law regulation on the establishment of a supervisory board.[105]

102 Of 8 June 1995, Official Gazette of the Republic of Croatia No. 38/95, as amended.

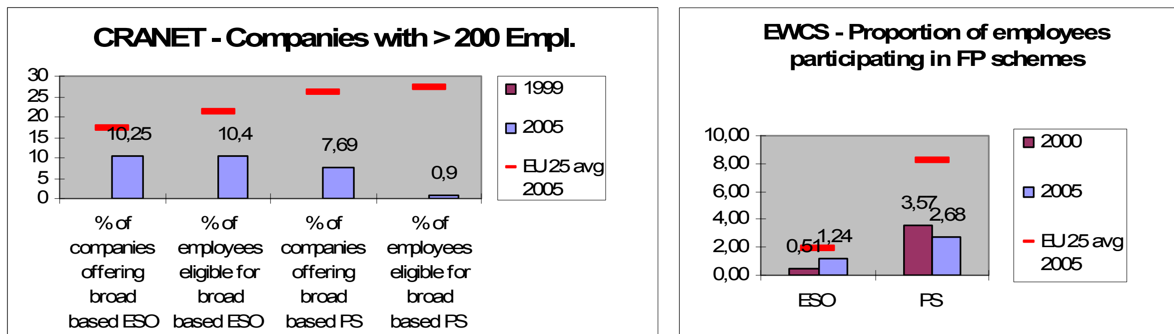
103 The employer has to inform the employees' council of the companies' results, amount of overtime work, protection and safety measures, etc. (Art. 144 of the Labour Law). He has to consult the employees' council on labour regulations, employment plans, reassignment of employees and dismissals, introduction of new technology and organizational modifications, annual leave plans, schedules of working hours, planned night shift work, compensation for inventions and technical innovations, and programmes for surplus work force (Art. 145 of the Labour Law). Furthermore, the employer needs the approval of the employees' council for decisions on the dismissal of an employee whose working ability is reduced or who is directly in danger of becoming disabled, the dismissal of an employee who is a representative of the employees on the Supervisory Board, the dismissal of a male older then 60 years of age or a female over 55, decisions on the collection, use and delivery of information concerning employees to third parties, and the appointment of a person authorized to supervise the collection of personal information concerning employees (Art. 146 of the Labour Law).

104 A higher number of representatives can be stipulated by a special law, e.g., Art. 17 of the Railway Law prescribes that three out of nine members of the Supervisory Board of the Croatian Railway Company must be elected by employees.

105 For details see Barbić (2003), p. 212.

IV. Cyprus

Neither employee ownership nor profit-sharing is present in the economy of Cyprus. The country has developed financial institutions, with more than 50% of households holding shares as financial assets, and a well developed cooperative sector with more than 50% of the population being cooperative members. The industrial relations system, based largely on voluntary regulations that allow room for joint initiatives, is at the same time characterised by relatively high union density. Nevertheless, employee participation, either in the form of financial or decision-making, has not been on the agenda of the government or social partners.



1. General Attitude

The long tradition of tight regulation of financial markets, capital controls, and limited financial assets available to households has changed since the mid-1990s. A modern capital market has evolved through the Cyprus Stock Exchange (CSE), which launched its official operations in March 1996 in accordance with the Cyprus Stock Exchange Laws and Regulations passed by the House of Representatives in 1993 and 1995. Nevertheless, the existing scepticism of the population towards financial markets is mainly rooted in the boom and crisis of the CSE.[106] With regard to the average size of enterprises and units, in 2000 only 70 companies in Cyprus employed more that 250 employees.[107] Self-employment has been a permanent feature

[106] By October 2001, the market was approaching the 100 level, having fallen from 800 at the peak of a short-lived boom in 1999. During 2002 and 2003 the market continued a long-term decline, with brief turns to growth, reaching a level of 80 in late 2003. In 2004 and 2005 the market remained calm, with the index unable to break out of the range 80 - 90.

[107] 58% of the enterprises employed one person, 37% 2-9 persons, 4% 10-49 persons and only 1% exceeded the limit of 50 employees (this amounts to 99.9%), see Census of Enterprises 2000 (Statistical Service of the Republic of Cyprus, 2001).

with self-employed persons accounting for 20% of the active labour force.[108] Voluntarism has been developed through the Industrial Relations Code and operates via National Tripartite Bodies such as, amongst others, the Labour Advisory Board, which deals with the main issues of industrial relations, and an equally important Economic Advisory Committee which deals with economic policy issues. The tripartite bodies work as integrated functions of the Ministries.[109] The voluntarism in industrial relations is coupled with relatively high union density estimated at 65-70%, and similarly high levels of coverage by collective agreements.[110]

Social partners in Cyprus are well organised and play an active role in the development and implementation of social and economic policy. Trade Unions are mainly organised at industry level and belong to strong federations or confederations, the most important being the Cyprus Workers Confederation (SEK, affiliated to the ETUC) the Pancyprian Federation of Labour (PEO) and the Democratic Labour Federation (DEOK).[111] Employers are also organised into industry or branch level associations, most of which are members of the Cyprus Employers' and Industrialists' Federation[112] and the Cyprus Chamber of Commerce and Industry. While the social partners shape the evolution of industrial relations, employee financial participation has not been an issue on their agendas. During the 1990s only SEK initiated a stance in favour of employee representatives' participation in decision-making through the participation of labour representatives at the board level of public sector and semi-public sector institutions and organisations, but without success.

The aims of the economic policy of the government in the last decade have not embraced the idea of financial participation of employees, favouring voluntary arrangements in industrial relations. In the context of the pre-accession period national policy makers have focused on priorities related to the compulsory transposition of the *acquis communautaire*, thus leaving aside issues such as the development of PEPPER schemes. The process of harmonising national with European law has recently led to debates concerning the evolution of the voluntary-based system of industrial relations, but has not yet touched upon issues of employee financial participation. With the minor exceptions of the Laws transposing the directives on the Involvement of Employees in the Activities of EC-scale Undertakings, EC-scale Groups of Undertakings and European Companies transforming EC directives 94/45/EC and 2001/86/EC this is also true for participation in decision-making.[113] Neither the government nor the social partners have included the issue of promoting financial participation schemes in their agendas. Political forces and the trade unions, which could have promoted the idea of employee par-

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108 It has also been observed that salary and wage earners undertake small-scale entrepreneurial activity, and are thus 'multiple-jobholders' - especially with regard to the development of the services sector.

109 A Redundancy Board and a Central Board for Annual Holidays with Pay complete the set of national tripartite bodies.

110 According to Ministry of Labour estimates 41% of employees have their pay and working conditions defined by sectoral collective agreements (approx. 74,000 employees), 6% of employees have their pay and working conditions defined by agreements in the semi-governmental sector (approx. 10,000 employees), 25% of employees have their pay and working conditions defined by company collective agreements (45,000 employees) and 17% of employees have their pay defined by agreements in the public sector (approx. 33,000 employees). The government set the minimum wage and the minimum standards to cover segments of the remaining 11% of employees (approx. 20,000) who are not covered by collective agreements.

111 There are also other powerful individual unions, such as the Public Employees' Union (PASYDY), the Bank Employees' Union (ETYK) and the Teachers' Unions (POED and OELMEK). Nearly 98% of white-collar civil servants are members of PASYDY.

112 Founded in 1960 OEBE is a Pancyprian independent Organisation and member of UNICE.

113 However, at the moment there is no European Company registered in Cyprus.

ticipation, may first have to implement the idea of employee participation in decision-making and then - or in parallel - consider the issue of financial participation. However, the process of the transposition of EU directives suggests the issue may gain further momentum.

2. Legal and Fiscal Framework

The Cypriot legal system is based upon the same principles as those applicable in the United Kingdom and all laws regulating business matters and procedures are based essentially on English Common Law.[114] The institutional and legal framework generally does not - at least intentionally - create incentives for, but neither do they prevent, the development of PEPPER schemes.

a) Share Ownership

Registered companies in Cyprus are governed in the main by the Cyprus Company's Law (hereinafter referred to as CL), Chapter 113 of the Laws of Cyprus, as amended, which is identical to the UK's former Companies Act 1948. Under the CL, companies can be divided into companies limited by shares and companies limited by guarantee[115]. Companies which are limited by shares can be subdivided into private companies and public companies. There is no law in Cyprus on share option schemes for employees but these may be included in private employment contracts or may be decided upon by the company so as to give these options to employees as part of an incentives scheme. The CL does not contain special rules on employee profit-sharing and contains only a mere notion of employee share ownership: The provisions of the Second Council Directive 77/91/EEC of 13 December 1976 were adopted by the national legislation and specifically in the CL. Therefore, in deviation from the general prohibition to acquire own stock, Art. 57a CL permits a company to acquire its own shares without requiring a special resolution of the general shareholders assembly[116], if the shares are acquired for the purpose of being transferred to the company's employees[117] or to the employees of an associate company. In order to facilitate the acquisition of shares by employees Art. 53 CL permits that the company may advance funds, make loans, or provide security, with a view to acquisition by employees of the company or employees of an associate company.

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114 English case law is cited in the Cypriot Courts and is of persuasive authority.

115 In the majority of cases, companies of this nature are incorporated as non-profit making organisations. Companies limited by guarantee can be registered with or without share capital and the liability of each member is limited to the amount agreed on in the memorandum of association to be contributed in the event of the company going into liquidation.

116 As the general provision for a company acquiring its own shares stipulate.

117 The term 'employee' also includes directors holding salaried employment or office in the company.

b) Profit-Sharing

There is no prohibition in the Cypriot legal system with regard to profit-sharing by companies with their employees. However, there is no explicit regulation linked to that either.[118]

c) Participation in Decision-Making

Industrial relations in Cyprus are based upon the Industrial Relations Code, which is a joint agreement between the two major labour confederations (PEO and SEK) and the Cyprus Employers' and Industrialists, signed in April 1977. The CL does not contain any special provisions concerning employee participation in control and decision-making in corporations. With regard to board-level representation the practice in state and semi-state companies has been for the government to appoint from time to time high-level trade union officials, mainly from the confederations, to the administrative boards of state-controlled organisations, although this is not required by law, but is rather a legacy of state management. A new and emerging influence comes from the European Union, i.e. employee participation in decision-making at a Community level has to some extent been safeguarded by the implementation into Cypriot national law[119] of Council Directive 2001/86/EC on supplementing the Statute for a European company with regard to the involvement of employees. Other social and labour legislation issues, such as employee rights concerning information and consultation as regulated in Member States, are within the scope of existing national provisions, as these apply to public limited-liability companies.

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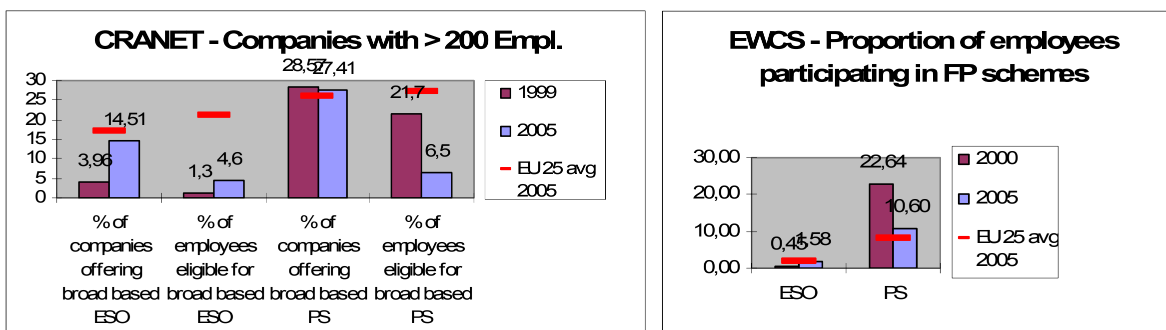
118 There is, however, the possibility that a company may agree to implement bonus schemes with its employees according to their performance or for percentages (commissions) according to the sales that their department has made.

119 By virtue of Law No. 277(I)/2004.

V. Czech Republic

The country which has granted far the fewest concessions to insiders through privatisation is the Czech Republic. Despite some tradition[120] of both financial participation of employees and employee participation in decision-making, the Czech privatisation framework did not anticipate any special price reductions, credit facilities, or pre-emptive rights for employees. In contrast to the comprehensive approaches of, for example, Poland, Czech policy favoured the voucher concept; no specific schemes for employees were developed. After the split with Slovakia in 1993, the corporate governance and enterprise structures were – and still are – unfavourable to the evolution of employee participation in general. Out of 1,688 state enterprises transformed into joint-stock companies, 480 proposed and received approval to privatise part of their shares as employee shares, but only 171 eventually gave shares to their employees. Employee share ownership remained insignificant, representing only 0.31% of privatised assets (Kotrba, 1995). In the framework of voucher privatisation the portion of shares allocated to employees was only about 1.5% of the total shares under consideration. Currently, most of the rare profit-sharing plans which exist are found in foreign companies. Of the existing, rather restrictive, regulations on employee share ownership and (share-based) profit-sharing, only the former have been implemented, although to a very limited extent. Nor have they so far been accompanied by a comprehensive incentive system.



1. General Attitude

Trade unions do not actively promote employee participation, nor do they consider doing so in future.[121] After the outcome of voucher privatisation the confidence of the general public in share ownership and similar programmes is negligible, if not non-existent. They see em-

120 Concerning historical development see Kotrba (1997, reprinted 1999).

121 Such was the basic line in an interview with Ing. Fassman, a representative of ČMKOSs (Českomoravská komora odborových svazů), the leading association of major trade unions.

ployee financial participation in the near future as extremely limited in both scale and scope. A similar picture is given in the case of the Czech Association of Employers/ Entrepreneurs SPČR (Svaz podnikatelů ČR)[122]: they have no official stand regarding employee participation models and neither possess data nor investigate how frequent it is or what its scope is amongst their members. Nowadays the involvement of employees in decision-making within the Czech economy takes place through tripartite negotiations rather than through direct participation by individuals or groups of employees in company management. There is a group representing workers' interests within the labour union network, as well as a group representing employers. These groups are concerned with both the sectoral and macro-economic levels. They meet with the government regularly in tripartite negotiations of crucial issues of economic policy. While participation in decision-making – as part of the *acquis communautaire* – has been put on the agenda, financial participation of employees has not.

Today employee participation is no longer a political issue – none of the democratic parliamentary political parties includes this issue in their programmes. The last time it was raised as a political issue was at the end of the 1990s, when Social Democratic Prime Minister Miloš Zeman was trying to push forward the agenda of increasing employee financial participation. Since that time, politicians have been silent about the issue.

2. Legal and Fiscal Framework

The Czech legal framework does not contain any specific employee financial participation measures or any particular law or regulation designed to regulate specific issues pertaining to PEPPER schemes, as in some other countries. The only form of corporate ownership the law makes available to employees are – to a limited extent – regulations on share acquisition by employees and profit-sharing in joint-stock companies.

a) Share Ownership

Privatisation (1990) – Mass privatisation, in principle, allowed employee shares and ownership to emerge. For each firm assigned to the mass privatisation, the firm's management had to submit a privatisation plan depicting for how the firm could be privatised. This proposal could involve any combination of all available methods of privatisation (e.g. voucher scheme, domestic direct sale, foreign direct sale, public auction or tender, free transfer, or employees' shares). It was possible for anyone other than the firm management to submit a competing privatisation plan for all or part of each enterprise. The supervising ministry and the Ministry of Privatisation decided on the winning project (foreign sales had to be approved by the government). Finally voucher privatisation itself provided another way of creating employee ownership within the privatisation process. In the design a small portion of shares was offered to and reserved for employees.

122 The opinion given in an interview with JUDr. Hejduková, a representative of SPČR.

Private Companies (2000, 2004) – In 2000,[123] Art. 158 of the Commercial Code (herein referred to as CC)[124] was revised in line with the *aquis* to abolish any type of special share; it also eliminated 'employee shares' as a special type of share. Instead, from now on, joint-stock companies could add to their Articles of Association provisions allowing their employees to buy company shares at a discount. Previously issued 'employee shares' had to be converted into regular shares by decision of the general shareholders assembly by January 2003.[125] Since, according to Art. 186a para. 3 ff. CC, dissenting shareholders must be bought out in a public offering, employed shareholders were given the de facto opportunity to cash-out their shares (Štenglová et al., 2004, § 158). Acquisition of shares on preferential conditions according to Art. 158 CC – introduced into the Commercial Code and replacing 'employee shares' – is limited to current or retired employees.

As an exception to the general prohibition against acquiring its own stock, Art. 161a para. 3 CC, introduced in 2004, permits a company to acquire its own shares in order to sell them – in accordance with the Articles of Association[126] – to company employees of the company. In this case the shares must be transferred on preferential conditions to the employees within twelve months of acquisition. If the transfer is not carried out within the stipulated time period, Art. 161c CC requires that the shares be sold or the share capital will be decreased accordingly; if the company does not comply, a court can order its liquidation (Art. 161c para. 2 CC). Furthermore, current legislation permits joint stock companies to issue new shares granting employees favourable conditions in the context of so-called mixed capital increases, i.e. the capital increase of a company issuing new stock financed by the company's own capital. According to Art. 209a para. 3 CC, 50% of the purchase price must be paid before registration of the increased capital in the commercial register, while the remaining 50% may be paid for by instalments. According to Art. 203 para. 3, 209 para. 2 lit. d) CC, shares issued to be acquired by employees shall not be considered to constitute a public offering, provided that the relevant employees are identified in the decision of the general shareholders assembly on the capital increase. In order to facilitate the acquisition of shares by employees, the legislation also permits the company to fully pay for the stock acquired by its own employees. The restrictions of the preferential conditions for the purchase of shares by employees are enumerated in Art. 158 para. 2 CC. As in the previous regulation, the overall value of the granted discount for the issued shares may not exceed 5% of the enterprise's equity capital and must be covered by the company's own resources (Eliáš et al., 2004, § 158). In addition, Art. 161e para. 3 of the Czech Commercial Code contains a regulation excepting a company from the general prohibition against leveraging the acquisition of its own stock if these shares are to be sold – in accordance with the Articles of Association[127] – to its own employees (Štenglová et al., 2004, § 161e). Thus share acquisition by the employees of a particular company may be leveraged by the company's discounting the purchase price within the aforementioned limits, by credit financing, by providing collateral, or by a combination of these three preferential methods.

123 Law No. 370, effective as of January 1, 2001.

124 CC of 5 November 1991, Sb. 1991 No. 513; last amended by the Law of 3 April, 2005, Sb. 2005, No. 216.

125 According to Part VIII No. 25 of the amending Law No. 370.

126 As required by Art. 158 CC.

127 As required by Art. 158 CC.

b) Profit-Sharing

Nothing in the Czech legal system prohibits profit-sharing. The only explicit regulation provided is Art. 178 para. 4 of the Commercial Code which states that in accordance with the Articles of Association employees may be entitled to a share of company profit (cash-based profit-sharing). According to Art. 158 CC, the Articles of Association may also stipulate that profits allocated to employees be used exclusively to purchase shares on preferential conditions or to offset the discount granted to employees for this purpose (share-based profit-sharing) (Štenglová et al., 2004, § 178; Eliáš et al., 2004, § 158). Share-based profit-sharing is also mentioned in the context of capital increases. A capital increase generally requires the approval of the general shareholders assembly. However, Art. 210 CC – in accordance with the Articles of Association – assumes that this decision will be delegated to the management board. Art. 210 para. 4 CC regulates a capital increase by the issuing of shares to be transferred on preferential terms to employees. It emphasizes that this option is especially suitable in cases where the general shareholders assembly has previously directed that profits allocated to employees be used exclusively to purchase these shares. These benefits are all taxable at the progressive personal income rate of 15% to 32%. Therefore as personal income rises, the incentive to provide additional benefits progressively decreases. Benefits from profit-sharing, for example, may be as much as 17% less than the same amount in dividends paid to shareholders.

According to Law No. 1/1992 Sb. on Wages, Remuneration for Work Readiness and on Average Earnings, as amended, basic areas that can be negotiated in collective bargaining agreements are the amount and the conditions for providing incentive wages (bonuses, rewards etc.), which includes participation in company profit as well.

c) Participation in Decision-Making

Art. 200 CC requires joint-stock companies with more than 50 employees to have one-third of its supervisory board composed of employee-delegated members. There are no special rules on employee participation in decision-making with respect to PEPPER schemes or privatisation matters. With regard to employee shareholding the general rules of the CC concerning shareholders rights apply.[128]

The main structure for representing employees at the workplace is the local trade union grouping, which only needs three individuals to set it up. Until 2001 this was the only structure but since then it has been possible to set up a works council in companies with more than 25 employees where there is no trade union organisation and where at least one third of the workforce ask for such a body. Nevertheless the majority of companies have no representation at all. The most important level of collective bargaining in the Czech Republic is at company level, although in many companies there is no bargaining at all. Industry level agreements cover some industries and following legal changes in 2005 they can again be extended more widely.

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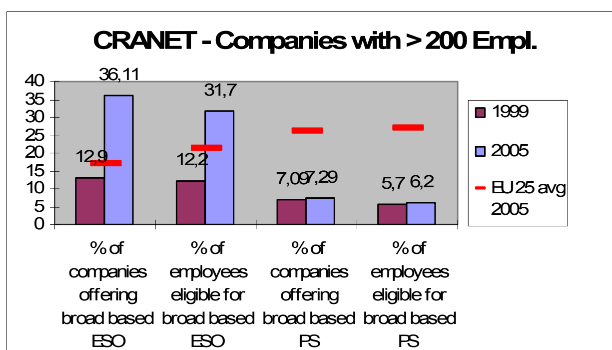
128 Stating that stocks as well as shares grant the right to shareholders to take part in the administration of the company, to receive dividends and, in the case of the liquidation of the company, a liquidation quota. For limited liability companies see Art. 114, 122, 123, 125 ff., for joint stock companies see Art. 178, 179, 180 ff. CC.

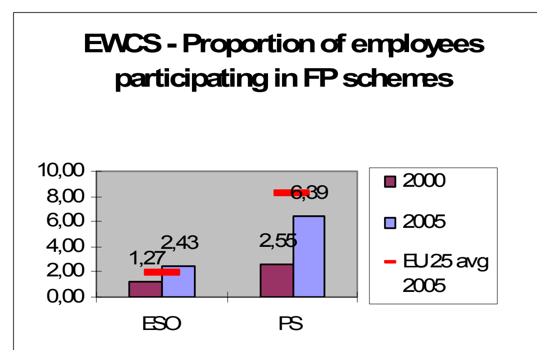
VI. Denmark

Employee financial participation began to be discussed at the end of the 1950s, in connection with an ideological debate on the concept of economic democracy. In the 1960s and 1970s, the Danish Trade Unions Federation and the Social Democratic Party submitted several proposals for compulsory collective funds, national and regional, in response to the wage earner fund (the Meidner Plan) of Sweden. These proposals were strongly opposed by both the Danish Employers Federation and the parties of the central and right political spectrum; they preferred tax incentives for voluntary plans at the enterprise level.

In 1987, the Liberal Conservative Government introduced the first tax incentives for certain forms of broad, voluntary, share-based plans at the enterprise level. Many firms implemented these plans with success. But then the issue of financial participation disappeared from the political agenda, remaining dormant until the beginning of the new century. In 2003, several new individual share-based plans as well as stock options were added. In 2005, these new plans were amended, in response to problems that had emerged in practice. All plans are based on employee shares or stock options. Currently recognized are the following basic forms: broad-based, share-based profit-sharing plans, including stock options; broad-based share ownership plans; individual share-based profit-sharing plans, including stock options, and individual stock option plans with no limitations.

The Tax Ministry now regularly reports to the Parliament on the progress of employee share ownership. According to the 2005 report, the number of employees participating in the various plans and the corresponding asset values were as follows: broad-based, share-based profit-sharing plans 10,000 employees, asset value DKK 163 million; broad-based profit-sharing plans based on stock options 1,000 employees, asset value DKK 10 million; individual stock option plans without limitations 4,047 employees, asset value DKK 388 million.





According to the 2006 report, the newly introduced individual profit-sharing plans based on shares and stock options (the so-called 10% and 15% plans under § 7H of the Tax Assessment Law) covered 1,326 employee participants in 77 enterprises. It should be noted that these numbers reflect the 'flow', i.e., the number of additional plan participants/shares in the

respective year. Data in absolute numbers were presented by the trade union Dansk Metal for 1999: estimated 160,000 employees were shareholders in their companies, while 13% of companies in high-growth industries and 25% of all IT companies operated a share-based plan for their employees.

1. General Attitude

Employee financial participation remained a highly controversial political issue until the late 1980s. Employers' associations advocated voluntary enterprise-level schemes; trade unions promoted compulsory schemes on a collective basis, while the government wanted to introduce additional tax incentives for existing schemes, but failed to get its draft law through Parliament. During the 1990s, little attention was paid to financial participation by either the government or social partners. Since the beginning of the present decade, the government has actively supported employee financial participation by introducing and adopting new individual share-based plans.

2. Legal and Fiscal Framework

The following employee financial participation plans are currently regulated: broad-based share-based profit-sharing plans, including stock options (§ 7A of the Tax and Assessment Law); broad-based share ownership plans (§ 7A of the Tax Assessment Law); individual share-based profit-sharing plans, including stock options (§ 7H of the Tax Assessment Law), and individual stock option plans without limitations (§ 28 of the Tax Assessment Law).

a) Share Ownership

Share Ownership Plan – Under the broad-based share ownership plan connected with tax incentives, shares of the employer company can be offered at discount to all employees; special rules may apply according to length of employment, working hours or seniority. The plan may not include management (e.g., members of the supervisory board). If the reduced price is paid in full at appropriation, the value of the shares does not exceed 10% of the annual salary, and the shares are placed with a bank for 5 years for five years, the employee is only liable to share income tax at sale while the employer company can deduct its costs from its corporate income tax base.

Stock Option Plan – The stock option plan under § 28 of the Tax Assessment Law is individual and may include members of the supervisory board. The number of options under this plan has no limits. However, it must be filed with the tax authorities. The employee is taxed at exercise of the option on the difference between the market price and the purchase price and again at the time of sale with the share income tax. The employer company can deduct the option costs from its corporate income tax base.

b) Profit-Sharing

Broad-based share-based profit-sharing plans linked to tax incentives, introduced in 1987, are based on share or stock options. They must include all employees, although special rules may pertain to length of employment, working hours or seniority; they must exclude management, e.g., members of the supervisory board. The plan must be approved by the tax authorities. If free shares are allotted within the plan, no tax need be paid by the employee at grant on total share values not exceeding DKK 8,000 (2006), and shares are placed in trust with a bank subject to a blocking period of seven years. In the case of stock options, the employee pays no tax at grant or exercise if the value does not exceed 10% of annual salary and the shares are placed in trust with a bank for a blocking period of five years. According to the 2005 amendment, the obligation of the employee to return shares to the issuing company under certain circumstances is not an obstacle to tax exemption. In both cases, general taxation rules in force at the time the shares are sold apply: if the income from sale of shares does not exceed DKK 44,300 (2006), the tax rate is 28%; otherwise 43%. The employer company can deduct from its corporate income tax base the value of shares or options transferred to employees.

Individual share-based profit-sharing plans, first introduced in 2003 under § 7H of the Tax Assessment Law, are based on shares and/or stock options. Only employees are eligible, and members of the supervisory board excluded. The employer company and the employee must conclude an agreement which is to be endorsed by an auditor or attorney and submitted to the tax authorities. Only common stock can be allocated; value may not exceed 10% of annual salary. The value of shares should not exceed 10% of the annual salary; the value of stock options should not exceed 10% of the annual salary or the exercise price should be less than 15% lower than the market price of underlying shares. This means that an employee is eligible for tax incentives if he acquires shares under the 10% rule and, additionally, stock options under the 15% rule, but not stock options under both rules. If the above pre-conditions are fulfilled, the employee is exempted from personal income tax and social security contributions at grant or exercise and is only liable to the share income tax at sale according to general taxation rules. However, the employer company cannot deduct costs from the tax base of the corporate income tax.

Cash-based profit-sharing plans are are not linked to tax incentives; their incidence is reputedly low.

c) Participation in Decision-Making

No direct connection exists between participation in decision-making and employee financial participation. Financial participation plans are specifically enjoined from extending the existing rights in connection with participation in decision-making. Financial participation is generally not a part of collective bargaining agreements.

Employee representation at board level is prescribed for companies with 35 or more employees, whereby the employees have one third of the seats. The one exception relates to board level representatives in a European Company – they must be elected by the workforce. Unions are central to workplace representation in Denmark. Local union representatives take up employees' concerns with management and are automatically members of the main information and consultation body – the cooperation committee. Bargaining at national level provides a framework for much of the Danish industrial relations system. Pay and conditions are negoti-

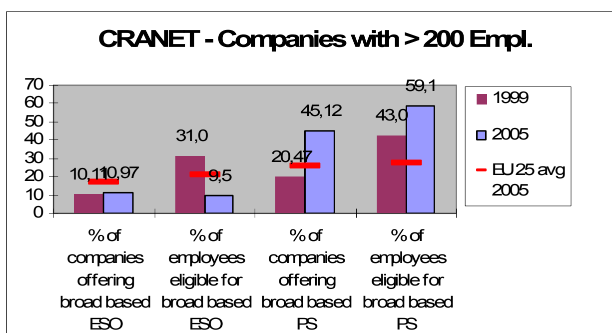
ated between ‘cartels’ of unions and the employers at industry level, but complementary negotiations at company level are becoming increasingly important.

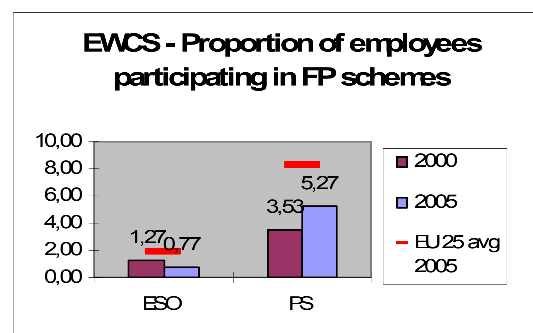
VII. Germany

Despite its generally positive effects on both productivity and job creation, employee financial participation is not widespread. Germany's lower standing in comparison to other countries may be attributed to insufficient government support. Only insignificant tax incentives for employee share ownership are offered under the Fifth Law on Wealth Creation, while profit-sharing is not supported by any tax incentives. Another reason is the traditional skepticism of both trade unions and employers' associations towards employee financial participation. A further possible reason is an underdeveloped shareholder culture; also the public social insurance system absorbs a large part of the employees' income, thus diminishing interest in alternative forms of investment.

In 2007, a number of government officials as well as representatives of major political parties declared that employee financial participation should be better promoted in the future. It remains to be seen whether this declaration of intent will be put into effect in the form of new, more supportive legislation considering the substantial differences that divide the two member parties of the Grand Coalition.

Although profit-sharing enjoys no tax incentives, it is more widespread than share ownership. In 2001, 8.7% of enterprises had profit-sharing schemes, while only 2.4% had share ownership schemes.[129] In 2005, 610 joint-stock companies maintained share ownership plans for 1,400,000 employees, and 230 limited liability companies for 7,000 employees; 17,000 employees of 340 cooperatives had membership status (AGP/GIZ of 1 January 2006).





1. General Attitude

Until recently, the attitude of the government and social partners towards employee financial participation has been generally indifferent or negative. In 2007, the Federal President Horst

129 Würz, Stefan (ed.) (2003): *European Stock-Taking on Models of Employee Financial Participation*, Wiesbaden, p. 59.

Köhler announced his support of the promotion of employee financial participation. In response to his speech, the Federal Chancellor Angela Merkel and a number of politicians of the Grand Coalition also made commitments to improve the legal framework. The two member parties of the Grand Coalition presented their concepts of employee financial participation in mid-2007. Unfortunately, the concepts contradict each other too drastically to combine. In the reports of the so-called Laumann Commission and Laumann-Huber Commission, the Christian Democratic Party proposed to support voluntary employee financial participation at the company level by introducing additional tax incentives for employee share ownership up to 1,000 EUR per employee annually. The Social Democratic Party proposed to create the so-called 'Germany fund' under state guarantee. The employees would invest their shares in the employing company in the fund, and the fund would invest this capital in German enterprises, especially in middle-sized companies. Existing tax incentives would be insignificantly increased to 240 EUR per employee per annum.

Trade unions continue to exercise enormous political power through workers' codetermination, despite declining union membership. They fear decentralization and desolidarisation of the wage policy along with a general loss of power. As an argument against profit-sharing, the labor unions cite the risk that employers could calculate a decrease in the amount of profit to the detriment of employees. Employee share ownership, they argue, imposes on employees the risk of losing both jobs and share income. Profit-dependent wage components are usually accepted only as auxiliary earnings in good times, while participation in loss is refused. Employee share ownership as a partial substitute for wages or in combination with wage reductions is generally rejected. Recently the employers' associations have paid more attention to employee financial participation. They favour voluntary company-level plans.

2. Legal and Fiscal Framework

No special law on employee financial participation exists. Only a few provisions in certain general laws address financial participation directly (e.g., the 5th Law on Wealth Creation), or apply to such plans (e.g., Income Tax Law and Law on Joint-Stock Companies).

a) Share Ownership

Share ownership is mostly practiced in joint-stock companies (Aktiengesellschaft) due to special peculiarities of German company law. In partnerships (OHG, KG), the concept of co-ownership precludes the development of employee share ownership. In limited liability companies (GmbH), employee share ownership is rare because of specific legal obstacles, e.g., the relatively strong position of a shareholder vis a vis management, the transfer of share ownership only by notarial deed, and an absolute prohibition against a company acquiring its own shares.

In joint-stock companies, stock can be distributed to employees in connection with a capital increase. The law provides for a conditional capital increase (§§ 192 et seq., Law on Joint-Stock Companies (JSCL)), a repurchase of its own shares (§ 71, para. 1, no. 8, JSCL), and a capital increase by authorized capital (§§ 202 et seq., JSCL). In the latter case, the board of

directors is authorized by the general meeting to increase capital up to a certain nominal value. Such an authorization, however, must be intended in the company statute. The general meeting's decision to authorize the board requires a majority of three quarters of the decision-making stock capital (§ 202, para. 2, JSCL).

If an employee receives stock from the employer company under his employment contract free of charge or at a reduced price, the difference between the market value and the subscription price is regarded as a part of salary. However, the benefit is tax-free if it does not exceed 50% of the share value, with a maximum of 135 EUR in a calendar year (§ 19a, para. 1, Income Tax Law). Under the 5th Law on Wealth Creation, an employee is granted a savings bonus of 18% on the investment (22% on investments in Eastern German federal states before 31 December 2004), but the amount is limited to 400 EUR (470 EUR annually on investments in Eastern Germany prior to 31 December 2004). However, only employees with an exceptionally low annual income (17,900 EUR) are eligible for this benefit. Additionally, there is a blocking period of six years. Proceeds from the share sale are not taxed if the period between the date of acquisition and sale is more than one year (§ 23, para. 1, no. 2, Income Tax Law).

Stock options are granted to management, and sometimes to other employees. The decision to adopt a stock option plan must contain a description of the allocation scheme (§ 193, para. 2, no. 2, JSCL). The plan itself must determine the strike price per share (§ 193, para. 2, no. 3, JSCL). In lieu of the strike price, the decision can state the basis for the calculation of the price. Details on the blocking period and vesting period shall be included in the decision on capital increase (§ 193, para. 2, no. 4, JSCL). The law stipulates a blocking period of at least two years.

b) Profit-Sharing

Profit-sharing, while not legally regulated or linked to tax incentives, is believed to be more widespread than employee share ownership; the latter enjoys at least some tax privileges. The statistical evidence on this issue might reflect the fact that indirect financial participation (e.g., employee loans, participation certificates and debenture bonds) is considered as profit-sharing. The only genuine form of profit-sharing actually practiced is cash-based profit-sharing within a bonus plan, which partly connects the share amount to the annual profit of the enterprise and partly to the individual performance of the employee.

c) Draft Legislation

A working group of the Coalition Government was charged with preparing a joint concept and a draft law by the beginning of 2008. The joint concept was presented on 16 April 2008. It has not changed the incentive system under § 19a of the Income Tax Law and the 5th Law on Wealth Creation, but merely increased the amounts, percentages and income ceilings to a certain extent: the tax-free benefit from free or reduced shares according to § 19a Income Tax Law is increased from EUR 135 to EUR 360 annually; savings bonus on investment is increased from 18% to 20% and income ceiling for eligibility from EUR 17,900 to EUR 20,000 annually. The draft on the amendments to the relevant laws will be based on the concept. The probability of the adoption of such draft law by the Parliament is very high, since the parties of the Grand Coalition have already accepted it.

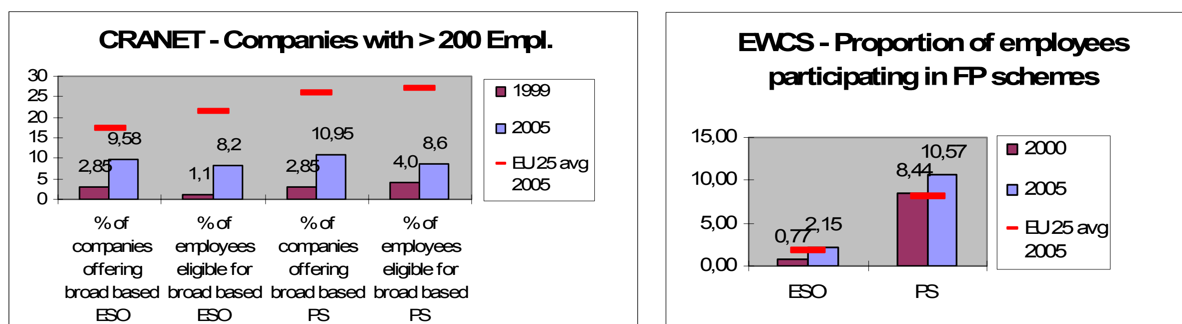
d) Participation in Decision-Making

Co-determination and participation rights of employees through their representatives are traditionally well developed under German labor law. Employees are represented in the supervisory board, and the workers' council protects their rights. There is no direct connection between participation in decision-making and financial participation of employees; in particular, financial participation plans cannot extend existing rights pertaining to decision-making.

An employee shareholder enjoys mandatory rights (right to control, right of participation, right to demand information). Examples of these rights are: the right of the limited partner in a limited partnership to demand information pursuant to § 166 Commercial Code; the right of a shareholder in a limited liability company (GmbH) to inspect and demand information pursuant to § 51a of the Law on Limited Liability Companies, and the right of the stockholder in a joint-stock company (AG) to demand information at the general meeting pursuant to § 131 of the Law on Joint-Stock Companies.

VIII. Estonia

Employee financial participation has made little progress in Estonia. PEPPER schemes did not develop during the period of independence between the two world wars or under the Soviet regime. Although employee participation in decision-making had some role in state enterprises during the Soviet era, it was later dismissed as a relic of that system. Employee ownership was briefly popular as a tool for privatising publicly owned assets in the early stages of privatisation, but this turned out to be a temporary expedient. Neither was employee financial participation considered relevant to the solution of employment and social problems. 29% of employees were estimated to be owners in 1995; this figure had fallen to around 25% in January 1997 (Jones and Mygind, 1998).[130] In January 2005, out of a sample of 722 firms 19 or 2.63% were (partly) employee-owned with a share varying from 20 to 100% (Jones, Kalmy and Mygind, 2005). Profit-sharing is not common in Estonia, but other forms of monetary incentive schemes are used in more than 50% of cases (Mygind, 2002). Some information on profit-sharing in Estonia was found in the Estonian management survey (1997/98),[131] with only 13 instances or 5.9% being reported out of a sample of 220 firms.



1. General Attitude

Currently, social partners are represented by the Confederation of Estonian Trade Unions (Eesti Ametiühingute Keskliit) and the Estonian Employers' Confederation (Eesti Tööandjate Keskliit). They do not have equal power; the trade unions traditionally are the weaker party. Recent debates between social partners on employee participation were triggered by the necessity to transform the *aquis communautaire* into Estonian law. The most recent debate between the social partners took place in connection with the draft law on the Involvement of Employees in the Activities of EC-scale Undertakings, EC-scale Groups of Undertakings, and

130 According to an overview of the distribution of ownership in a sample of 666 Estonian enterprises.

131 Done by Mygind in cooperation with the Estonian Statistical Office (ESA).

European Companies transforming EC directives 94/45/EC and 2001/86/EC. Since the government was not willing to play the role of arbitrator and the social partners could not agree upon a compromise solution, bipartite consultations ended without resolution. Nevertheless, Parliament adopted this law on 12 January 2005 to meet the deadline and thus avoid EU sanctions.

The government is passively waiting for the trade unions to produce an initiative to improve the situation, but the trade unions are not planning to address this issue either. PEPPER schemes have not been on the political agenda of Parliament. Only one political party has addressed this issue: the Social Democratic Party. These circumstances make it unlikely that Estonia will adopt new legal regulations on employee participation soon. However, as the discussion on transformation of EU directives shows, the issue will be addressed and even new legislation could be adopted if an EU legal act on financial participation of employees were issued.

2. Legal and Fiscal Framework

There is no specific legal regulation of any PEPPER scheme in Estonia at present. The legal framework generally does not – at least intentionally – create incentives for, but neither does it prevent the development of PEPPER schemes. More complicated forms of employee participation such as ESOPs would require new laws, regulations, and tax incentives.

a) Share Ownership

Privatisation (1990, abolished in 1993) – Semi-private forms of business ownership ('people's enterprises' and leased enterprises) introduced in the early stage of privatisation under Soviet law (and later legalised also according to Estonian law), in particular leased enterprises, are assumed to have been a major source of employee ownership in Estonia (Jones, Kalmi and Mygind, 2003, p. 10). In the privatisation of small and medium-sized enterprises, employees were given a pre-emptive right to buy the enterprise at the initial price.[132] When all privileges were abolished in 1993, small enterprise privatisation was almost completed; an estimated 80% of enterprises had been taken over by insiders (Mygind, 1996, p. 240). The privatisation programme for large enterprises, finally adopted in 1993, followed the German Treuhand model, and contained no preferential rights for employees. Employee ownership of shares in enterprises purchased during privatisation is decreasing. Although privatisation in Estonia can be considered as virtually complete, enterprises in the energy sector as well as public utilities are still partially state-owned; they could be put up for sale in the future.[133] The current Privatisation Law (as amended on 14 November 2001) offers no privileges to employees or other groups of potential buyers. It is based upon the provision for the termination of activities of

[132] According to the Law on Privatisation of State-Owned Service, Trade and Catering Enterprises from 29 December 1990.

[133] For this reason, the laws regulating privatisation (Privatisation Law of 17 June 1993 (herein referred to as PL), Law on Ownership Reform of 13 June 1991 (hereinafter referred to as LOR), and Law on Land Reform of 17 October 1991 (hereinafter referred to as LLR)) are still effective.

the Privatisation Agency, and thus on the termination of major privatisation proceedings, while the few privileges employees had under Estonian law were abolished as early as 1993.[134]

Private Companies – Estonian Commercial Law does not contain special rules on profit-sharing or on employee share ownership with respect to acquisition, limitations on the number of shares, or issuance of employee stock for any specific undertaking; therefore, general rules apply. Some employees still hold shares purchased during privatisation and thus have the rights attached to these securities according to company and securities law. In Estonia, company law is primarily laid down in the Commercial Code of 15 February 1995 (herein referred to as CC) and securities law in the Securities Market Law of 17 October 2001 (herein referred to as SML).

Most legal entities are corporations, of which limited liability companies are the most popular. Since employees who became shareholders often acquired minority shares in newly founded limited liability companies and joint-stock companies during early privatisation, provisions concerning the rights of minority shareholders and shares acquired during this period are of special importance. Pursuant to §§ 515 (1) and (2) CC, rights attached to shares issued before 1 September 1995 which do not comply with the provisions of the Commercial Code remain valid, whereas rights not attached to shares are void. Minority shareholders of a joint-stock company can be bought out by the majority shareholder holding at least 9/10ths of the shares upon resolution of the general meeting with at least 95% of the votes represented by all shares; a fair compensation to minority shareholders in this case is secured by the provisions regarding takeover bids (§§ 363 2 (2) and 363 7 (1) CC) and the right to lodge a claim with a court (§§ 363 8 (2) and (3) CC). Minority shareholders have no corresponding sell-out right, i.e. they cannot demand that the majority shareholder buys their shares if they wish to sell them.

If securities issued by a company are offered solely to the employees or managers of that company, the prospectus need not be made public and registered (§ 17 (1) 2) SML). This means that the employees and management are not entitled to compensation pursuant to § 25 SML if they suffer losses as a result of the volatility of acquired securities.[135] Furthermore, if a company provides investment services solely to its employees and management, it does not have to be registered as an investment firm (§ 42 (1) SML). Thus it can conduct investment activities without a licence (§§ 48 ff., SML). It is not obliged to report transactions (§ 91 SML) or to have additional reserve and risk funds (§§ 93 ff., SML), and there are no additional requirements for managers (§ 79 SML).

b) Profit-Sharing

Special legislation on profit-sharing with regard to employees does not exist; therefore, there are neither direct incentives nor direct restrictions. For employees it is preferable to receive distributed profits under a corresponding scheme rather than wages/salaries since they do not

[134] Initially, pre-emptive rights, which often also led to the possibility of buying assets or shares under value, were the most popular mechanism. With regard to privatisation in the industrial sector, most influential political forces were opposed to buy-outs by employees.

[135] This seems to be justified since management and employees might have insider knowledge, but it could be argued that employees, unlike managers, do not necessarily have full information as to the financial situation of the company. Notably, employees are not deemed insiders, but rather as third persons who could receive information from insiders, under the same law (§ 191 (1), (3) SML).

have to pay income tax on profits or dividends. Nevertheless, the resident company pays income tax at the rate of 22% on distributed profits (§ (4) ITL), whether the distribution is monetary or non-monetary (§ 50 ITL), which creates a disincentive for implementing profit-sharing schemes.

c) Participation in Decision-Making

Rights to participate in decision-making were granted to employees of EC-scale Undertakings, EC-scale Groups of Undertakings and European Companies,[136] as a result of EC directives 94/45/EC and 2001/86/EC.[137] In such companies, the nomination of employees' representatives onto the Special Commission for Negotiations, the European Work Council, the SE Special Commission for Negotiations, and the SE Council or Administrative Council is required. Although Estonian company law is so strongly influenced by German law that rulings by German courts can be used to interpret provisions of the Estonian CC (Klauberg, 2004, p. 1), special rules on the participation of employees in management and decision-making contained in a special German law (Betriebsverfassungsgesetz) were not considered by the Estonian law-makers.[138] If employees are also shareholders, they have voting rights in each company form, although they generally have no influence on resolutions of the general meeting since they are, in most cases, minority shareholders.[139]

136 According to the Law on Involvement of Employees in the Activities of EC-scale Undertakings, EC-scale Groups of Undertakings and European Companies which was adopted on 12 January 2005 after a long controversial debate between the social partners.

137 'On employee involvement required in the case of establishing a European company'.

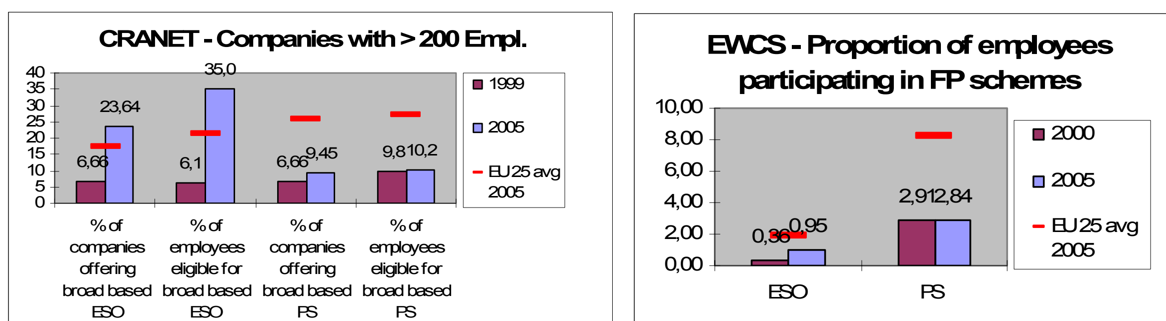
138 For details on participation in decision making in a European context see Tavits (2004).

139 Minority shareholders representing at least 10% of the share capital are entitled to demand a general meeting (§ 171 (2) 3 CC for limited liability companies and § 296 CC for joint-stock companies) and to lodge a claim with a court for the removal of members of the management board or supervisory board for good reason (§ 184 (5) CC for limited liability companies and § 319 (5) CC for joint-stock companies).

IX. Greece

The first tax incentives for employee financial participation plans were introduced as early as 1974. Legislation broadened tax incentives in 1980 and 1988. Currently in place are special regulatory laws and tax incentives covering cash-based profit-sharing, employee share ownership and certain types of stock option plans. Although employee financial participation plans are still not widespread, they have been on the increase since the beginning of the current decade, especially executive stock option plans. Thirteen percent (13%) of companies listed on the Athens Stock Exchange offered stock option plans in 2007, mainly to executives. Thirty thousand (30,000) persons (1.8% of employees) participated in these plans.[140]

The High Level Group of Experts found that the limited spread of employee financial participation plans, despite tax incentives, was attributable to the complexity and restrictions of the regulations. Tax incentives are indeed restricted to joint-stock companies (anonimes etairies). However, the number of such companies in Greece is quite high (16,767 companies in 2007), with the majority of them being SMEs. The regulation is complex only in so far as the regulation is fragmented and the provisions on tax incentives are contained in many different legal acts. Another important factor inhibiting the spread of employee financial participation is the reluctant attitude of social partners at the company level, although social partners at the national level view the issue more positively.



1. General Attitude

The government generally supports employee financial participation by initiating and implementing tax incentives for specific types of plans. Employers' associations were not initially interested in employee financial participation. Trade unions (i.e., the General Confederation of Greek Workers and public sector unions), originally strongly opposed, have accepted financial participation since the beginning of the 1990s. Attitudes of both social partners have become

140 Ioannou, Ch. (2008), Changing Payment Systems in Greece, in print.

more favourable since the beginning of the present decade. Facilitation of employee financial participation has been on the national collective bargaining agenda. In the current round of collective bargaining (2008), both social partners made facilitation of employee financial partnership an issue to be included in the agreement. However, this agreement requires government ratification to become applicable at the company level.

2. Legal and Fiscal Framework

Special legislation, including tax incentives, exists for cash-based profit-sharing, employee share ownership and stock option plans.

a) Share Ownership

Both share ownership and stock option plans enjoy tax incentives under certain conditions.

Share Ownership Plans – Since 1987, joint-stock companies have been allowed to acquire their own shares in order to distribute them to employees. If these shares are purchased on the public market, up to 10% of equity capital can be distributed; the distribution must be made within 12 months. If the shares for distribution are to be issued in the course of a capital increase, up to 20% of the annual profit can be distributed; the shares must be blocked for three years unless the general meeting provides otherwise. If these pre-conditions are satisfied, the employee is not subject to either personal income tax or social security contributions on the benefit, but is liable to the tax on movable assets (10%) on dividend or interest payments. The employer company can deduct the distributed amount from the tax base of the corporate income tax. According to the Circular of the Ministry of Finance of 2000, the gift tax can apply to the employee's benefit instead of the personal income tax. When the shares are sold, only the transfer tax is applicable; companies often offer shares to employees at a reduced price in order to overcome opposition to privatisation.

Stock Option Plans – Stock Option Plans are divided into qualified plans under the Law 2971/1999 and non-qualified plans under the Presidential Decree 30/1988. In qualified plans, the shares to satisfy the claims of option owners at exercise are issued in a qualified capital increase whereby the number of shares should not exceed 1/10th of shares already outstanding. In such plans, employees are not subject to taxation at grant or exercise or liable to social security contributions; the employer company, however, cannot deduct the cost of the shares. In non-qualified plans, shares to satisfy the claims of option owners at exercise are purchased on the public market. Under these plans, employees are generally subject to personal income tax and social security contributions, but the local tax office can levy a gift tax instead of the personal income tax if 'the benefit derived exceeded the proper measure'. The employer company can deduct the value of distributed shares as personnel costs. Because there has been a substantial increase in the number of executive stock option plans since the year 2000 and the benefit of the executives usually exceeded 50%, the government is considering much higher tax rates (40%) in such cases.

b) Profit-Sharing

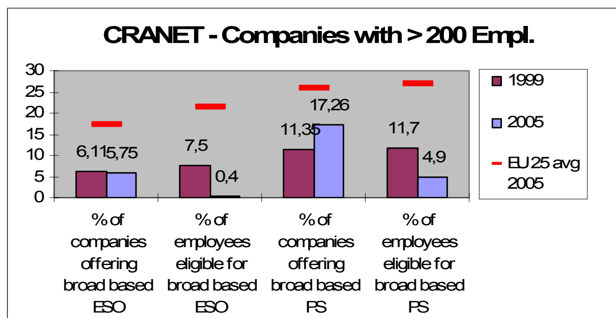
Profit-sharing plans are dominantly cash-based and linked to tax incentives. The company is allowed to distribute 15% of annual net profits to employees. Each employee can receive up to 25% of annual gross salary as his profit share. The company must submit a list of beneficiaries, with amounts payable to each individual employee, to the workers' council within one month of approval by the general meeting. However, it must be noted that only a small number of companies have workers' councils; when they exist, they must be informed, but their approval is not required. In practice, no case is known where this pre-condition became a problem. If these pre-conditions are met, the employee is exempt from income tax, but subject to social security contributions on the profit share amount. The employing company can deduct the distributed amount from the tax base of the corporate income tax, but is liable to social security contributions.

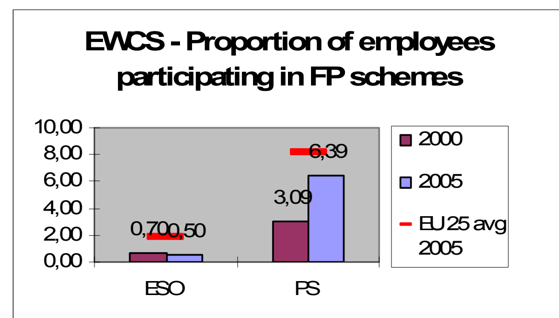
d) Participation in Decision-Making

There is no direct connection between participation in decision-making and financial participation of employees. In particular, financial participation plans cannot extend existing rights with regard to participation in decision-making. The employees in the 'socialized sector' (e.g., public utilities and transport), where two levels of employee representation are compulsory for companies under state control (representative assembly of social control setting broad policy objectives: 1/3rd employees, 1/3rd board of directors, 1/3rd elected by employees) might have influenced the introduction and design of financial participation plans but did not choose to do so.

X. Spain

The form of employee financial participation typical of Spain are on the one hand 'Workers Companies' (Sociedades Laborales), which combine employee share ownership with decision-making rights, and on the other hand profit-sharing. Although their number is relatively small (approx. 20.000 enterprises in 2007, employing 125.000 workers), in recent years the increase in both number and employment has been stable; its growth has been much higher than any other form of financial participation, so that the model can be considered as successful. Profit-sharing plans are prevailingly cash-based. According to a 2006 survey of the Ministry of Labour and Social Affairs 18.8% of private sector employees participate in some kind of participation in the profits of their workplace.[141] There are relatively few cases of employee share ownership and stock option plans, prevailingly in large multinational companies and often limited to the executives. However, tax incentives for share purchase plans were introduced in 2003 which could lead to a wider spread of employee share ownership.





1. General Attitude

Under the Constitution, the Government is obliged to take measures in order to facilitate the access of employees to the ownership of productive facilities. It generally supports employee financial participation by proposing and implementing tax incentives for workers' companies and employee share ownership schemes. The employers' associations are cautious not to promote executive plans, since the stock option plans for executives and their undesirable consequences for the financial markets have led to tensions and a negative image in the past. Nevertheless, they do not actively support broad-based plans. The trade unions accept financial participation plans only on the condition that they should be designed as an addition to the regular salary. Associations lobbying to protect the achievements of companies with financial par-

[141] The overall figure for Spanish employees, including management and cooperatives is 23.7 %. Genuine profit-sharing plans and performance-related pay not connected to financial indicators are not clearly differentiated, so that it is not clear whether this data reflects the incidence of profit-sharing correctly.

ticiaption exist on regional and on firm level (e.g., MCC, Confesal, CEPES, Federaciones de Cooperativas). In 2008 (following a proposal of Confesal) a modification of the Law on Workers' Companies eliminating some of the restrictive prerequisites and, in effect, turning this type of firms more into 'normal' firms with standard labour relations, is being considered.

2. Legal and Fiscal Framework

The workers' companies are governed by the Law on Workers' Companies of 1986 substantially amended in 1997. Tax incentives for employee share ownership and stock option plans were introduced by the Law on Stock Ownership Incentives 46/02 of 18 December 2002, in force since 1 January 2003. There is no special regulation of profit-sharing.

a) Share Ownership

Listed companies usually implement stock option plans, often only for the executives, whereas non-listed companies generally introduce share purchase plans. In addition, workers' companies constitute the typically Spanish form of employee share ownership. Specific tax incentives are applicable to all these forms of employee share ownership.

Workers' Companies (Sociedadas Laborales) can be founded as a workers' company or become a workers company by changing their corporate form. Since 1997, there are two forms of workers' companies: Sociedad Anónima Laboral (SAL) with the minimum equity capital of EUR 60,000 and Sociedad Limitada Laboral (SLL) with the minimum equity capital of EUR 3,000. The majority of shares must be held by the employees, whereby individual employees must not hold more than one-third of the capital. The articles of association must contain regulations on transfer of shares if an employee shareholder leaves the company. Each workers' company must establish a special fund for the compensation of losses amounting to 20% of its profits (compulsory 10% for normal companies and additional 10% for workers' companies). The remaining 805 of he profits can be distributed between the members of the workers' company or attributed to as a voluntary reserve to raise the company's own funds and hus the value of the shares. If the compensation fund amounts to 25% of annual profits, tax incentives apply. Workers' companies are exempted from taxes in connection with company formation and capital increases and have a tax credit of 99% in relation to taxes in connection with transfer of shares to employees, notarial deeds on transfers to the company and notarial deeds on debts, bonds and debenture bonds. These incentives only concern the setting up of the workers' company (i.e., they do not affect personal income tax liability etc.). The Law on Workers' Companies contains detailed special labour regulations (e.g. on allocation of working time between employee shareholders and other employees). The federal Labour Ministry and municipalities exercise control over the workers' cooperatives.

Share Ownership Plans (Share Purchase Plans) enjoy tax incentives under certain conditions since 2003. If the market value of the benefit at the time of acquisition does not exceed EUR 12,000 p.a., shares are offered within the framework of a regular compensation plan (but not necessarily of a broad-based plan), each employee and his family members own not more than 5% of the equity capital and the shares are blocked for 3 years, tax incentives apply. No tax

incentives apply to dividends, but at sale of shares a flat tax of 15% instead of the personal income tax is imposed on the employee.

Stock Option Plans are also linked to tax incentives since 2003. If the vesting period does not exceed 2 years and options are granted not annually, a 40% tax allowance limited by the annual medium wage determined by law multiplied by the number of years before vesting applies. If the shares cannot be sold within 3 years after the option has been granted and the plan extends to all employees on the same terms, the amount of the tax allowance and the ceiling are doubled. Approx. 40 listed companies operated stock option plans in 2003 (EU Report on Stock Option Plans, please note that these figures include executive plans).

b) Profit-Sharing

Both cash-based and share-based profit-sharing plans exist, but cash-based profit-sharing prevails. In many cases, profit-sharing plans contain financial indicators as well as performance-related indicators, so that they cannot be considered as genuine profit-sharing plans. Some share-based plans ('performance shares') are linked to financial indicators as BPA, RTA etc. Stock appreciation rights, i.e. payment in cash or transfer of shares connected to the increase in the share value at the end of a determined period, are sometimes granted, but such plans are rare.

c) Participation in Decision-Making

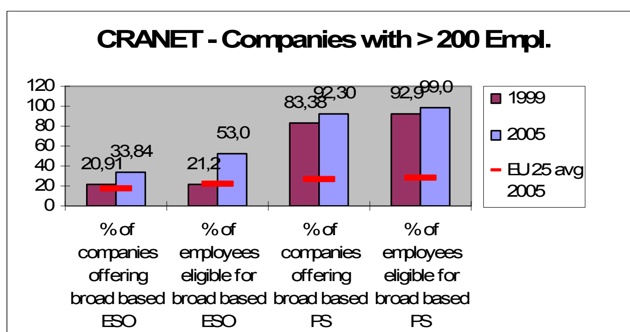
Employee share ownership in workers' companies is directly linked to participation in decision-making. The board of directors cannot decide about the liqiuidation, the increase or reduction of capital or the composition of the board without the consent of the general assembly. Each member of the workers' company has the right to candidate for election on the governing bodies of the company. In other plans, there is no direct connection between participation in decision-making and financial participation of employees; in particular, financial participation plans cannot extend the existing rights in connection with participation in decision-making.

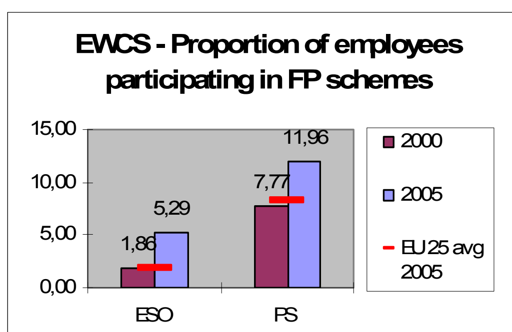
There is no overall right to employee board-level representation. However, there are a small number of employees on the boards of some public and recently privatised companies and savings banks. Elected works councils are the main channel of workplace representation for employees in Spain, although the law also gives a specific role to the unions at the workplace and in larger workplaces the trade union delegate may be the key figure. The works councils themselves are dominated by the unions and, as well as information and consultation rights, they also bargain on pay and conditions at company level. Negotiations take place at national, industry and company level in Spain, and since 2001 an annual national agreement has provided a framework for lower-level bargaining. The overall level of coverage is high at around 80%.

XI. France

France has a relatively long tradition of employee financial participation, especially of different forms of profit-sharing and collective savings plans. The first so-called gain-sharing (intéressement) plans were introduced in 1959, but they have not become wide-spread until first tax incentives were introduced and restrictions were abolished in 1986. The profit-sharing (participation) plans were introduced in 1967 as plans compulsory for all companies with more than 100 employees. This number was reduced to 50 employees in 1986. In addition, further tax incentives were introduced for profit-sharing. Also first short-term savings plans (Plan Partenarial d'Epargne d'Enterprise – PEE) were adopted. Important improvements were enacted in 1994 for all types of plans. The most recent employee financial participation plan is the long-term savings plan (Plan Partenarial d'Epargne Salarial Volontaire – PPESV) of 2001. Stock option plans were first introduced only for listed domestic companies in 1971 and extended to unlisted and foreign companies in 1987. Although the taxation of these plans has become more favourable in 1996, they are still prevailingly used by executives and seldom broad-based.

Currently, four basic plans are the most common: gain-sharing (intéressement), profit-sharing (participation), short term savings plans (Plan Partenarial d'Epargne d'Enterprise – PEE) and long-term savings plans (Plan Partenarial d'Epargne Salarial Volontaire – PPESV). Whereas the profit-sharing is compulsory for all companies with more than 50 employees, other plans are voluntary. All these plans are traditionally classified as profit-sharing plans, although gain-sharing can be linked to other indicators than profit and even to non-financial indicators and savings plans are rather a financial vehicle for profit-sharing and gain-sharing plans than genuine profit-sharing plans. The traditional classification is followed here with the above reservations. Shares can be transferred to employees directly for free or at a discount, but there are no distinctive share ownership plans. Employee share ownership prevailingly emerges within the profit-sharing plans if gain or profit shares, employee earnings or employers' matching amounts are invested in company shares. For that reason, statistical data are only available for the major profit-sharing plans and not for employee share ownership. Since the plans are generally not to be approved prior to introduction by tax authorities, no regular statistics on the number of companies or the number of employee participants are available.





According to the data of the Association Francaise de Gestion (AFG), 2/3 of large companies operated profit-sharing plans with 10.3 million beneficiaries in 2006. In this period, the total amount of assets in profit-sharing plans in the broader sense was EUR 82.4 billion (19% more than in 2005), of which EUR 5.8 billion were held in profit-sharing plans (participation), EUR 2.5 billion in gain-sharing plans (intéressement), EUR 2.9 billion were voluntary payments of employees and EUR 1.7 billion matching payment by the employing company to PEE and PPESV. In 2006, 52% of assets from funds were invested in company shares, so that the employee share ownership seems to be increasing, although the share of employees in most companies is still less than 3%.

1. General Attitude

The successive Governments have been developing employee financial participation schemes for the last 40 years. Legislation had to become more complex in order to prevent discrimination of lower-ranking employees in relation to the management, on the one hand, and to prevent the abuse of employee financial participation schemes for tax avoidance by employees, on the other hand. The main political goals are more equal distribution of wealth by participation in enterprise results and contribution to a solution of social security problems, especially of pension accumulation.

The employers' associations support voluntary plans as these plans allow more flexibility in the planning of labour costs, but are strongly opposed to compulsory schemes, although they have to implement them. The employers also support the development of savings plans and advocate the view that savings plans must be closely connected to or even replace pension plans.

The trade unions generally support all schemes if they do not lead to a reduction of cash pay. If the assets of employees are to be invested, the trade unions advocate diversification of investment rather than investment in company shares because it is associated with fewer risks. They are opposed to using the savings plans as future pension tools.

2. Legal and Fiscal Framework

The major employee financial participation plans (gain-sharing (intéressement), profit-sharing (participation), short term savings plans (Plan Partenarial d'Epargne d'Enterprise – PEE) and long-term savings plans (Plan Partenarial d'Epargne Salarial Volontaire – PPESV)) were introduced by laws (i.a. Law on Gain Sharing of 1959 as amended, Law on Compulsory Profit Sharing of 1967 as amended, Law on Shareholders Voluntary Employee Savings Plans of 2001 as amended) which have been amended many times, most recently by the Law of 31 December 2006. Irrespective of the type of plan, an employee starting to work for the company must be informed of the operated plans and the pre-conditions of participation. Training of employees on financial participation issues by the company is linked to tax incentives: the tax

relief for the employing company is EUR 75 for one hour training of the employee, but not more than EUR 5,000 per company for two years.

According to the amendment of 2006, plans can be approved by state authorities prior to introduction. If the state authority submits no objections within 4 months upon submission of the agreement by the employing company, the plan is deemed approved. However, this provision does not protect the employing company if the competent state authority contests the implementation of the plan.

a) Share Ownership

As explained above, no special share ownership plans are common; share ownership is generally acquired by means of profit-sharing plans. However, it is possible to transfer free shares to employees, since 2006 without a holding period and with a vesting period of 4 years. In privatisation, 5% of shares are reserved for employees and can be offered at a discount of up to 20% of the fair market value.

b) Profit-Sharing

As explained above, all major plans are regarded as profit-sharing plans in the broader sense. An employee can participate in different types of plans at the same time if several plans are operated by the company. The combination of different plans is advantageous from the viewpoint of taxation and, therefore, quite common: profit-sharing or gain-sharing amounts can be transferred to PEE or PPESV and afterwards also to a general Stock Savings Plan (SICAN/FCP Investment Fund) or to a Collective Retirement Savings Partnership Plan (PERCO). Since 2006, it is prescribed by law that the company must introduce PEE if it operates a profit-sharing plan (participation) and must introduce PERCO if it has been operating PEE for more than 5 years.

Profit-sharing plans (participation) are compulsory; the other three plans are voluntary. Profit-sharing, gain-sharing and PPESV can be introduced only on the basis of an agreement with employee representatives, whereas PEE can also be based on a unilateral decision of the employing company. All plans must be broad-based, i.e. apply to all employees, with the exception of those with less than 3 months of service. A blocking period of 5 years (profit-sharing, PEE) or 10 years (PPESV) is compulsory and linked to substantial tax incentives, which generally include exemption of personal income tax and social security contributions and imposition of a special flat tax of 7.6% for both employees and the employing company and a special flat tax on returns of 10%. The blocking period expires if certain personal circumstances of employees emerge (death, disability, cessation of employment, insolvency, marriage, birth of the third child, divorce while keeping custody of at least one child, purchase of a principal residence). The employee earnings and matching amounts of the employing company must and employee gain shares and profit shares can be transferred to mutual funds (FCPE), usually managed by banks or insurance companies, which invest the assets in shares or bonds of the employing company or of several different companies. If the employing company is not listed, the FCPE is obliged to invest 1/3 of assets in marketable shares or bonds, unless the company buys back 10% of own shares or all assets belong to employees planning to participate in a leveraged buy-out. After the blocking period expires, the accumulated assets are paid out as a

lump sum (all plans) or an annuity (only PEE, PPESV). In the following, individual plans are presented.

Profit-sharing plan (*participation*) is compulsory in all companies with more than 50 employees. However, not all such companies have introduced profit-sharing plans in practice, especially if they cannot pay the minimum amount of profit share according to the compulsory formula to all plan participants due to financial results. The compulsory formula is as follows: 50% x (profit – 5% of equity) x salaries/added value. Since 2006, the minimum amount calculated on the basis of the formula can be increased in relation to the annual increase in the price of a pre-determined number of shares. In addition, an additional bonus (the so-called 'working dividend') can be paid according to the general rules of the profit-sharing plan in the company if the profits are substantially higher than expected. The maximum annual amount per employee is 25% of the gross income, but not exceeding EUR 14,592 (2003). The plan can be introduced on the basis of an agreement with the trade unions or with the workers' council or of the approval by 2/3 majority of employees. Since 2006, profit-sharing should become a compulsory part of collective agreements of individual economic sectors applicable to individual companies on a voluntary basis. During the blocking period, the amount is transferred either to a deferred profit-sharing fund (RSP) or to a mutual fund (FCPE). The benefit is exempted from the personal income tax and social security contributions and a special flat tax of 7.6% is imposed instead. The interest or returns paid out during the blocking period are subject to a special flat tax of 10%; if the interest or returns are accumulated, they are exempted from taxation.

Gain-sharing (*intéressement*) is voluntary and its formula is free. It can be linked to different indicators, not necessarily profit or gain, but also reduction of losses, less injuries at work or other performance-related indicators, but is usually based on financial indicators. The maximum amount is the same as for the profit-sharing plan. It is introduced by a three-year agreement, which is not automatically renewable, with the trade unions or the workers' council or on the basis of the approval of 2/3 of all employees. The amount can be transferred to the employee immediately; it is then exempted from social security contributions, but subject to full personal income tax. However, the gain sharing amount can be invested for 5 or 10 years in a company savings plan (PEE, PPESV); in this case, the respective tax incentives apply.

Savings plans (*PEE, PPESV*) are voluntary and their formula is free. The holding period for PEE is 5 years, for PPESV 10 years. An employee can transfer 25% of the earnings or gain sharing amounts to the savings plan. The company is entitled (but not obliged) to match the amount of the employee contribution with an up to 3 times higher amount. The maximum matching amount (abondement) was originally expressed in absolute figures, but, since 2006, it is expressed as a proportion of the annual social security ceiling. The maximum matching amount is higher for the investment in company shares than for diversified investment and higher for PPESV than for PEE. The matching amount is generally exempted from personal income tax and social security contributions, but subject to a special flat tax of 7.6%. However, the amount exceeding the ceiling for PEE in PPESV is subject to 8.2% flat tax and the amount exceeding the ceiling for PPESV in PPESV is subject to full personal income tax and social security contributions for the employee and the employing company. The tax on returns is a flat tax of 10%. After the blocking period expires, the amount can be paid as a lump sum or an annuity or transferred to a Stock Savings Plan (SICAN/FCP Investment Fund) available to all citizens for further 3 years to increase the amount. In large companies, leveraged savings

plans are possible: employees can use an interest free bank loan in order to purchase up to 10 times more shares than with their own earnings.

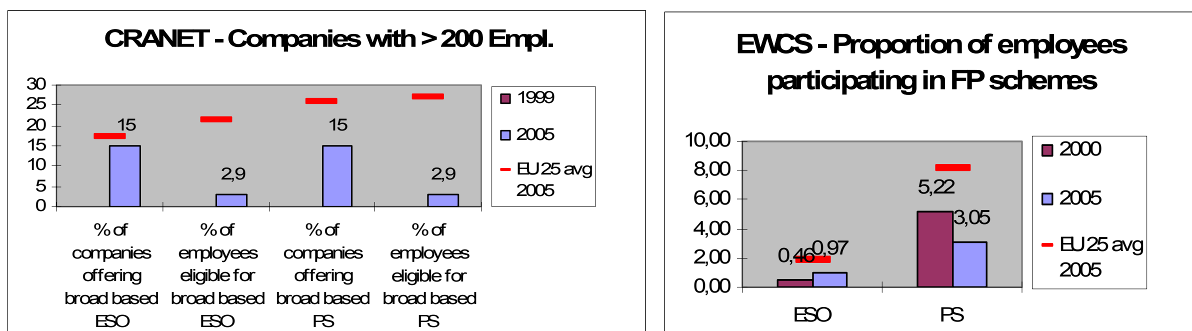
c) Participation in Decision-Making

The most major employee financial participation plans can be introduced only on the basis of an agreement with the trade unions or the workers' council, so that employee representatives generally participate in negotiations on the design of the plans. In addition, the workers' council must always be consulted before the agreement is signed and be regularly informed on the implementation of profit-sharing and gain-sharing plans; on savings plans, a special supervisory body elected by the workers' council must be consulted and informed. The mutual funds are managed by the supervisory board consisting of half employee representatives, elected by the workers' council for two years, and half employers' representatives. If the assets are invested in company shares, the chairman must be an employee representative. In practice, this body is not efficient, since the management decisions are taken by the bank or insurance company and generally accepted by the supervisory board. If employees own more than 3% of the equity capital of a listed company, they must have at least one representative on the company board who must be elected. The mandate of the representative ends upon cessation of employment. All companies have to amend their statutes accordingly at the first extraordinary meeting after the publication of the law. However, this provision does not play a major role in practice, since employees have a larger share in a very small number of companies.

XII. Hungary

In Hungary employee ownership has been the most frequent form of employee financial participation with the Hungarian Employee Share Ownership Programme (ESOP) still being prevalent. Although it spread quickly in the early phase of privatisation, the relative weight of this ownership form in the whole of the economy is not significant. With privatisation complete, the number of ESOP companies has been decreasing relatively quickly. Other PEPPER schemes in the context of privatisation as well as in the context of incentive plans, including profit-sharing, were implemented only to a limited extent. They did not receive any economic policy support – and consequently proper central registration systems do not exist. An exception is the 'Approved Employee Securities Benefit Programme' introduced by tax laws in 2003.

As for profit-sharing, according to Hewitt Associates, about 80% of the enterprises in Hungary use short-term incentive tools that go beyond the simple sales premium.[142] 20% of them use profit-sharing. In most cases (in 67% of companies) the basis of entitlement is one's position in the hierarchy, but many places (23% of the enterprises) set other criteria as well. According to the survey, however, only 10% of entitled employees receive a share of the profits.



1. General Attitude

Trade unions participated at a national level in the promotion of the various forms of employee ownership. Local unions, however, were often surprisingly passive and limited action

142 The incentive systems of 50 companies were surveyed in 2003, the majority of which were large ones in terms of sales and number of employees. The majority (66%) were foreign-owned, 20% were production, 27% were service providers and 27% were trading companies. In their systems, the contingent wage included short- and long-term incentives and social and other benefits. A similar study by the HayGroup analysed wage data of 201 mostly foreign-owned companies (82%). 84% of all companies give their employees some kind of contingent wage made up of bonuses/premiums, profit share, and turnover bonus in sales jobs.

to declaring their interest in employee buy-outs but did not play any role in organising the procedure; in other cases, however, local trade unions actively lobbied for preferential shares as well as for ESOP buy-outs. In addition to influencing privatisation decisions, unions usually had at least one of their leaders as a member of the organising committee and the ESOP trust. Subordinates saw ESOP and other durable buy-out schemes as a tool to preserve their workplace.

Since the end of privatisation in 1998 lobbyists have been fighting without any success for political support and financial encouragement for ESOPs 'outside privatisation' as well as to make the technique applicable in cases of liquidation. Furthermore, in contrast to the international trend of the individual account-based pension system, plans to encourage tying employee ownership to pension fund membership have so far gone unnoticed. Another important effort of lobbyists was to amend laws (ESOP and tax laws) to make sure that the unfavourable economic environment would not undermine the operation of existing ESOP enterprises.[143] The latest example is placing out-patient health care services and the organisation of ESOP companies on the privatisation agenda. Nevertheless, there is a great deal of uncertainty around the programme, not least because of the recent referendum on the ban on the privatisation of the health care system. On the whole, in Hungary there is no policy on employee ownership. While most of the political parties (both on the left and the right) declare their commitment to the issue, concrete economic policy decisions are still missing.

2. Legal and Fiscal Framework

The Hungarian Labour Code states that an employer may grant any benefit to its employees if it is provided in a non-discriminatory manner.[144] In Hungary, the legal framework of financial participation of employees embraces both profit-sharing and employee share ownership. However, specific (legal/tax) incentives for profit-sharing do not exist, neither for employees nor for employers. Company law regulates employee shares, including stock options, explicitly and recently an 'Approved Employee Securities Benefit Programme' including specific incentives have been introduced.

a) Share Ownership

Employee privatisation on preferential terms (1991, 1995) – The privatisation law of 1991 contained various preferential privatisation techniques. In 1995 a new Law on Privatisation[145], still in force, reduced some of the allowances for employees, but at the same time offered new forms and techniques, i.e. privatisation on deferred terms, employee privatisation on preferential terms, *'Egzisztencia'* credit and ESOPs. In the context of privatisation three financial techniques for acquiring employee ownership on preferential terms exist: (1) price reduction, (2) purchase by instalment and (3) purchase on credit. Thus it is possible to grant a discount of

143 Early regulations focused on asset acquisition, and questions of distributing and balancing power at that time did not allow the operational problems to be addressed.

144 Section 5 of Law XXII of 1992 on Labour Code.

145 Law XXXIX of 1995 on the Realisation of Entrepreneurial Property in State Ownership.

up to 150% of the annual minimum salary. However, the nominal value of shares acquired this way may not exceed 15% of the company's registered capital and the discount granted may not be above 50% of the purchase price. This allowance can be used either individually, or on a broad basis. Payments on deferred terms for privatised property may be granted for a maximum period of fifteen years. The interest rate on such credit cannot be less than 50% of the current official national bank interest rate while ownership passes to the buyer with the payment of the first instalment. Furthermore Hungarian citizens may take up to 50% of the property that they wish to acquire and as a maximum up to 50 million HUF as an *'Egzisztencia' credit*[146], regardless of the number of buyers.[147]

Employee stock ownership programme (1992) – In Hungary [148] the US ESOP system had a strong influence on the drafting of the law regulating the establishment and functioning of ESOPs. Basically the Hungarian ESOP followed the American 'trust' model (Luxne and Szucs, 1993, p. 9; Boda and Neumann, 1999, p. 45). However, there is a major difference between the two systems: while in Hungary the ESOP is a privatisation form with the organisation ceasing to exist as soon as all the securities are paid for and their ownership is transferred to the employees, in the United States, an ESOP continues to administer the securities of employees.[149] Hungarian literature distinguishes between so-called 'privatisation' and 'non-privatisation' ESOPs (Szakértői Munkaközösség: ESOP, 1990, pp. 49-50). In the case of the former, the ESOP organisation buys the property of the State Property Agency or of municipalities and there are incentives related to this form. In the case of the latter, shares or business shares that are not at the disposal of the State Property Agency are sold, e.g., already existing securities or securities issued in the case of capital increase also foreseen by the ESOP law. The only difference between both forms is that there are no specific incentives encouraging companies or employees to establish non-privatisation ESOPs.

Should the employees decide that the ESOP organisation remains in place, it is required to develop regulations for the period after repayment (e.g. rules for marketing shares).[150] The organisation has full liability for its obligations. Members of the organisation are not liable for the debts of the organisation except with the securities already allocated to them. Until the shares are transferred to the participants of the ESOP the organisation is the owner of the shares. With regard to the exercise of property rights, participants have voting rights in proportion to their registered shares, but up to a maximum of 5% of the property acquired by the ESOP organisation.

Tax exemptions for 'privatisation' ESOPs allow the company to offer tax allowances for the property sold to the ESOP organisation prescribed by the Corporate Tax Law (Lukács 2004, 9.5.2.5). Accordingly, up to 20% of the amount paid to the ESOP organisation can be de-

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146 Governmental Decree No. 28 of 1991 on 'Egzisztencia' Credit and Deferred Payments Benefits; see below.

147 Section 58 (3) of Law XXXIX of 1995 on Realisation of Entrepreneurial Property in State Ownership. This rule applies to ESOP credits as well.

148 Regulated by Law XLIV of 1992 on Employee Share Ownership Programme, which entered into force on July 14, 1992, amended with Law CXIX of 2003.

149 Another difference between the American and Hungarian regulation was that under the 1992 ESOP Law there were no 'fairness' rules (this led to disproportionately large manager ownership); however, this was changed with the 2003 Amendments. It should be also noted that the ESOP Law does not differentiate between employees and managers.

150 As a result of legal regulations, the overwhelming majority of ESOP organisations ceased to exist after the loans were repaid. Furthermore, the established forms of operating the asset (such as setting up a limited company) involve considerable costs (Boda, Neumann and Vig, 2005).

ducted from the company's tax base. ESOPs were not subject to corporate profit tax until December 31, 1996. However, following this date, the income of ESOP organisations falls under the rules of the Law on Corporate Tax and Dividend Tax, and accordingly 16% tax is paid on the taxable income of the organisation.[151] However, two special rules apply when calculating the tax base of ESOPs: (1) the tax base should be reduced by the amounts paid in by private persons as their own contribution to the ESOP organisation and by the amounts of subsidy paid in by other private or legal persons, or by the employer company (otherwise these amounts should have been accounted as income). (2) at the same time, the tax base has to be increased by the acquisition value of the shares given to the ownership of participants of the ESOP – on the pretence of transferring means without compensation, that amount is accounted among expenditures (reducing the profit) according to the rules of accounting.[152] According to Personal Income Tax Law, the securities transferred from the company to employees are tax-free, such securities are not considered as income.[153] However, at the time of sale of such securities by the employee, the income from this sale is considered a capital gain and taxable at a rate of 20%.[154]

Private Companies (1988) – Employees' shares were first introduced by the Law on Business Associations of 1988 and still exist under the current version of the law[155]. They are registered shares and can be issued free of charge or at a reduced price in accordance with the provisions of the Articles of Association of the joint-stock company, e.g. in the context of a Long-Term Incentive Plan or a broad-based Stock Option Plan. Employees' shares may be issued with a simultaneous share capital increase of the joint-stock company, up to a maximum of 15% of the increased share capital. A joint-stock company may pass a resolution on the issue of such employees' shares which entitles their holders to dividends from after-tax profits to be distributed amongst shareholders prior to the shares belonging to other categories or classes of shares, but following shares granting preferred dividends. In the event of the death of an employee or the termination of his/her employment relationship, excluding the case of retirement, his/her heir or former employer shall have the right to transfer the employees' shares in question to other employees of the company within a period of six months.[156] The company issuing such shares can distribute them for free or give discount for their purchase, which makes this form of financial participation very attractive for employees. However, there are no tax incentives related to this form of share acquisition (Lukács, 2004, 9.5.1.3). From January 1, 2003 income received in the form of securities is no longer regarded as an allowance in kind.[157] Thus, in case of employees' shares, the difference between the purchase price and the sale price falls under personal income tax.

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151 Section 2 (2) (e) and 19 (1) of Law LXXXI of 1996 on Corporate Tax and Dividend Tax.

152 See Földes, p. 573 (2005).

153 Section 18 (4) of Law XLIV of 1992 on Employee Share Ownership Programme.

154 Section 66 of Law CXVII of 1995 on Personal Income Tax; Securities acquired from already taxed personal income of the participant of the programme are not taxable.

155 Section 187 (1) of Law CXLIV of 1997 on Business Associations.

156 If this deadline expires without success, at the first shareholders' meeting thereafter the company shall withdraw the employees' shares in question with a corresponding reduction in its share capital, or shall decide to sell such shares after transforming them into ordinary, preference or interest-bearing shares.

157 The applicable rules of taxation are determined by the legal relationship between the private person and the provider. In the case of securities provided by employer to employee, such income is considered as income from employment, and the pertinent tax rules have to be applied. See Informant of the Tax and Financial

Approved Employee Securities Benefit Programme (2003) – At the beginning of 2003 new legislation[158] entered into force allowing companies to set up state-recognised, tax-qualified stock plans. The organiser of the Employee Securities Benefit Programme has to submit an application for the recognition of the programme as an approved programme to the Ministry of Finance which informs the competent Tax Authorities about its decision. To be approved, the programme must meet a catalogue of conditions, e.g., that only securities issued by the applicant company or by its majority shareholder may be offered in the programme and the statutory threshold levels of at least 10% employee participation and a management share of less than 25%, with less than 50% of the total share value. At the time of sale, the employee is subject to tax on the spread between the exercise price and the sale price. Such capital gain is taxed at 20%, separately from other income.[159] Companies have no withholding or reporting obligations in connection with employee stock option or purchase plans. The first HUF 500,000 of the shares that have met the vesting requirements are not taxable at exercise or vesting. Any shares deemed non-qualified are taxed as normal employment income.[160] Once employees exercise the shares, the shares must be held in a security account overseen by a custodian, and there is an obligatory three year vesting period which ends on December 31 of the second year subsequent to providing the securities.[161] Following this, they have the same rights as any other shareholder from the same class. The most recent amendment of the Law on Personal Income Tax (Act LXI of 2006) stipulates, that gains of all share purchasing and similar transactions should be added up in the given year and, that for the calculation of tax base instead of the nominal value at the time of allocating the share option, now the actual value at the time of purchase matters. At the same time, according to the interpretation of the officers at the Ministry of Finance, the amendment abolished the blocking period.

b) Profit-Sharing

Except for section 5 of Law XXII of 1992 on the Labour Code, which states that an employer may grant any benefit to its employees if it is provided in a non-discriminatory manner, no regulations exist. Specific incentives do not exist, neither for employees nor for employers. There is no tax allowance or other kind of state subsidy in the case of profit-sharing, every kind of benefit and allowance paid to employees falls under the Personal Income Tax Law and there is also no allowance for employers.

c) Participation in Decision-Making

Employee representatives make up one third of the members of the **supervisory board** in companies with more than 200 employees. In companies with a two tier board system – both

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Control Administration (APEH) on the Rules on Securities Allowance in Force from January 1, 2003. Source: Hungarian CD Jogtar (Feb. 28, 2005).

158 Law CXVII of 1995 on Personal Income Tax; Decree of the Ministry of Finance No. 5 of 2003 on the Procedure of Registration of Approved Employee Securities Benefit Programme, and on the Rate of Administration Service Fee for the Initiation of the Procedure.

159 While personal income tax is payable because the shares are regarded as earned income, no social security contribution must be paid (earlier share benefits were regarded as in-kind benefits, belonging to the highest income tax bracket (44%), and the social security contribution was also payable).

160 Personal income tax in Hungary is based on a progressive scale from 18% to 38%.

161 Section 77/A, 77/C of the Law CXVII of 1995 on Personal Income Tax.

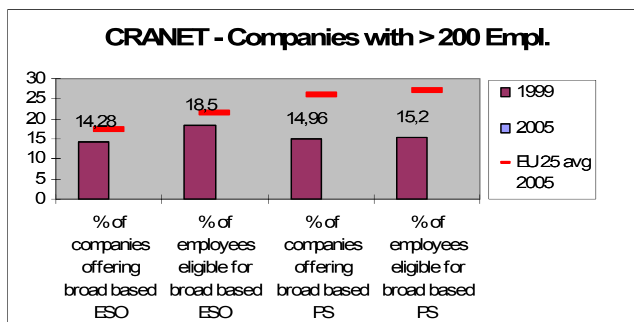
a supervisory and a management board – the works council has the right to nominate one third of the members of the supervisory board in companies with more than 200 employees. The one exception, introduced through new legislation, passed in 2006, is where there is an agreement between the works council and management to the contrary. In companies with a single tier board system – just a board of directors – employee participation at board level must be regulated by an agreement between the works council and the company. This is a new development – before the 2006 legislation only two tier board structures were possible – and it represents a potential weakening of employee representation at board level, as there are no minimum requirements.

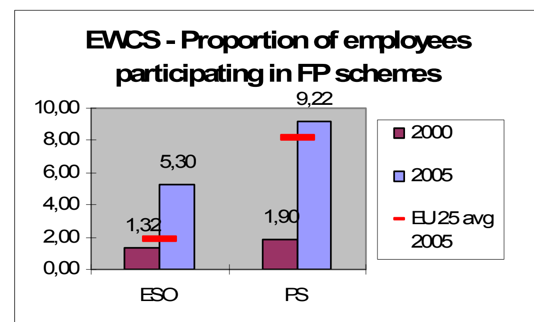
Workplace representation in Hungary is provided by both local trade unions and (since 1992) elected works councils with the balance between the two varying over time. After legal amendments initiated by the socialist government elected in 2002, only the union has the right to negotiate collective agreements. The union workplace representatives must be consulted over major issues affecting employment, including job cuts and changes. Works councils have information and consultation rights but in practice often find it difficult to influence company decisions.

XIII. Ireland

Although employee financial participation has been discussed in Ireland since the mid-1970s, not until 1982 was the first plan introduced (Approved Profit Sharing Scheme/APSS). The first tax incentives came in 1986. During the tax reform of 1997, additional plans (Approved Savings-Related Share Option Scheme/SAYE and Employee Share Ownership Trust/ESOT) were added. In 2001 another plan (Approved Share Option Scheme/APOS) was approved.

There are now six share-based plans linked to tax incentives — the four enumerated above plus the purchase of new shares and restricted stock schemes. In addition there is an unapproved stock option plan. According to statistics provided by the Irish Business and Employers Confederation (IBEC), in 2002 there were in operation 400 APSS plans, 90 SAYE plans with 140,000 employees, and 15 APOS plans. Although not the most numerous, SAYE plans seem to be the most popular judging by the number of participating employees. Many companies combine several approved plans and also operate unapproved ones (no statistics are available). The majority of plans are found in listed multinational companies.





1. General Attitude

Employee financial participation, especially share ownership, has been supported by successive governments, as a means of aligning the interests of employees with employers and making retirement more secure. But encouragement has not gone so far as to connect financial participation schemes with pension policy. Employee Financial Involvement (EFI) is addressed in national economic programmes and in national wage agreements, but is regulated only by local collective agreements or by in-house agreements.

Since the beginning of the 1980s, the Irish Business and Employers' Confederation (IBEC) has supported tax-efficient share schemes and regard them as a key element in recruiting and retaining personnel, but only if they remain voluntary. The Irish ProShare Association, which promotes and conducts research on employee financial participation, was founded by IBEC.

Trade unions also support those financial participation plans which provide explicit financial rewards as well as a sense of participation. Representatives of both employers and trade unions support partnership initiatives at the enterprise level.

2. Legal and Fiscal Framework

Employee financial participation plans fall into two categories: either they are approved or unapproved. Plans introduced under the annual finance acts and approved by and registered with the Inland Revenue enjoy tax advantages as well as exemption from PRSI (compulsory social security contributions), which especially benefit employees. Unapproved plans may be designed and introduced at the employer company's discretion but receive no specific tax advantages. Approved plans must be designed in accord with legal specifications whereas unapproved plans enjoy more flexibility. Under current legislation, all approved plans (and typically unapproved plans as well) are share-based, including profit-sharing, share ownership and stock option plans. Tax incentives for approved plans are governed by the Taxes Consolidation Act of 1997, as amended (Part 17, Schedules 11, 12, 12A, 12B and 12C). Unapproved plans are used for granting shares or options to individual employees which exceed the legal maximum or for granting shares, options or cash equivalents to employees not subject to Irish taxation. Unapproved plans are usually combined with approved plans.

a) Share Ownership

Two approved share ownership plans (purchase of new shares and restricted stock) and two stock option plans (SAYE and APOS) are supported by tax incentives. There is also an unapproved stock option plan which exempts employees from PRSI contributions but imposes the full personal income tax at exercise.

Share Ownership Plans – Purchase of New Shares: If employees pay full price for newly-issued shares and hold them for three years, the subscription cost (subject to a lifetime ceiling of 6,350 EUR (2006) is exempt from both personal income taxes and PRSI. A capital gains tax is based on the issue price. The employer company is also exempt from PRSI.

In a restricted stock scheme, participants are given a future interest in shares, subject to certain restrictions. On shares held for at least one year, the employee may deduct a specific percentage of the benefit from the personal income tax base (from 10% for one year to 55% for more than five years).

Approved Stock Option Plans – The Approved Savings-Related Share Option Scheme (SAYE), introduced by the Finance Act of 1999, is currently the most popular plan judging by the number of participants. It must be open to all employees on similar terms, with possible exception of employees with less than three years of service. The plan is structured as follows: the employee make a save-as-you-earn (SAYE) contract with a bank, agreeing to save a specified monthly amount (12 to 320 EUR) through deductions from after-tax remuneration for a period of three, five or seven years service, while the employer corporation grants him share options for the maximum number of shares his SAYE savings will be able to buy at the exercise price. The SAYE contract always includes a tax-free bonus to be awarded at completion,

the amount depending on the term. The exercise price may be up to 25% lower than the market value of the shares at the time of grant. At maturity of the SAYE contract, the employee may choose to exercise the option, selling or retaining the shares, or to receive the savings and bonus in cash. These requirements fulfilled, the employee is exempt from the personal income tax at the time of grant or exercise; the capital gains tax, however, is levied at the time of sale. Neither the employee nor employer must pay PRSI.

The Approved Share Option Scheme (APOS) was introduced in the Finance Act of 2001. Eligibility requirements are the same as for the share option scheme described above. It is further required that at least 70% of options are transferred to the broad-based plan; shares may not be sold within three years of grant. These requirements fulfilled, the employee is exempt from the personal income tax at grant or exercise; at sale, the capital gains tax must be paid on the difference between proceeds and option price. Neither the employer company nor the employee is liable for PRSI.

b) Profit-Sharing

The oldest form of financial participation is the Approved Profit-Sharing Scheme (APSS), introduced in 1982. It is a share-based leveraged profit-sharing plan. Cash-based and/or direct share-based profit-sharing plans are also possible, but have no tax advantages. Individual gain-sharing based on performance-related indicators, promoted by the government since 2000, may be more widespread than cash-based profit-sharing.

The APSS must apply to all employees on similar terms, with the possible exception of those having less than three years service. 'Similar terms' refers not only to other members of an employee group but to shareholders who are not employees. This provision is an obstacle to introducing employee financial participation plans in non-listed companies if the employees – unlike shareholders who are not employees – have to sell the shares to the company after leaving. Employee shares are held in trust and cannot be withdrawn for two years; not until the third year do tax incentives apply. The trust must appropriate the shares to the employees within 18 months and is then not liable to the tax on dividends. Employee benefits of up to 12,700 EUR (2006) are exempt from both income taxes and PRSI contributions. If the shares are sold during the blocking period, the employee is liable to personal income tax at the top rate on proceeds of sale less the market value and to capital gains tax on the increase in value. Shares sold after the blocking period are subject only to the capital gains tax.

Subsidiary schemes to APSS are salary foregone and the employer matching scheme (so-called BOGOF (Buy-one-get-one-free)). In the context of salary foregone, the employee can deduct up to 7.5% from his pre-tax basic salary to increase his share-based profit-sharing. In the context of BOGOF, the employee purchases shares from his after-tax income, and the employing company matches it on at least one for one basis. The employing company can deduct costs of setting up and operation of the plan and costs of providing shares to employees, and it is not liable to PRSI.

Since 1997 the APSS has been allowed to combine with an ESOT. In contrast to the APSS trust, the ESOT is empowered to hold shares for 20 years; it may also borrow funds and sell shares. The trust pays no tax on dividends used for specified purposes (e.g., acquiring shares, repaying loans, etc.). Shares transferred to the ESOT must be common shares, fully paid for and irredeemable. Employees must elect a majority of ESOT trustees. On shares not trans-

ferred directly to employees but first to the APSS trust, tax incentives for APSS apply. The ESOT is not subject to capital gains tax on disposal of shares.

The ESOT was widely used for privatization of state-owned enterprise. Usually 14.9% of the equity capital of the company undergoing privatization was accumulated in the ESOT for employees. Shares were typically acquired by a combination of loans and a direct state grant, in exchange for productivity concessions and the agreement of trade unions to privatize.

c) Participation in Decision-Making

Participation in decision-making and financial participation have no direct connection, nor can existing decision-making rights be extended by a financial participation plan. General provisions of labour law, such as equal pay and prohibition of discrimination, also apply.

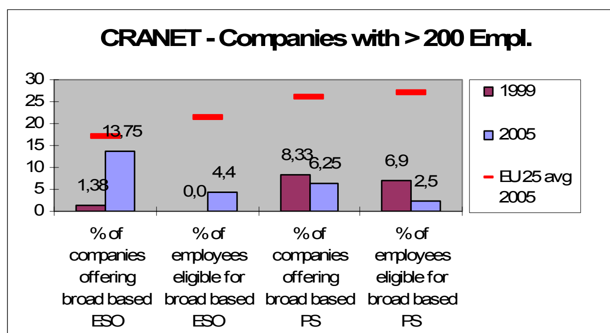
Employee representatives in Ireland's single-tier boards are only found in the state-owned sector, where they normally account for a third of the total. Privatisation has cut the number of companies covered and the process is continuing.

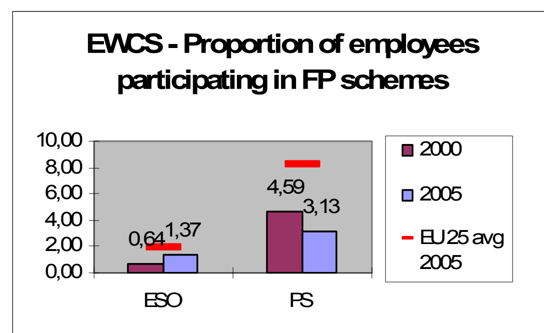
There is no statutory system for workplace representation in Ireland. Those who work in unionised workplaces – about half of the entire workforce – have representation through the union. New procedures have been introduced as a result of the EU directive on information and consultation, but they may not make much difference.

National pay pacts have provided a framework for bargaining in Ireland since 1987. Agreed between the unions, employers and government, they are not legally binding, but have been widely observed.

XIV. Italy

Financial participation in Italy has emerged especially in the second half of the 1980, with the development of firm level bargaining agreements. This was a phase where companies were restructuring production processes and were redesigning their human resource management, while unions tried to obtain more power and legitimacy thorough a high level of workers' representation in company level agreements. The most significant form of employee financial participation in Italy is profit-sharing, while employee ownership has a more limited diffusion. Even after the Italian privatisation processes, implemented in a massive way since the Nineties, there have not been significant impacts in terms of employees' ownership. On the other hand, workers' cooperatives, especially in the commercial sector, have a significant importance and a long historical tradition. Tax incentives for employee financial participation have been introduced after the 1993 tripartite agreement and in the late Nineties.





1. General Attitude

A reform of the wage setting system has been adopted in 1993; the tripartite agreement[162] has defined new setting rules to implement decentralised bargaining and new income policy rules. Although this had a positive effect on the introduction of PEPPER schemes, corresponding tax incentives to promote employee compensation schemes have not been introduced until 1997 with the main aims of obtaining *macro*-benefits expected from linking pay to firm performance, in particular limiting wage inflation. The promotion of a new participative climate at the *microeconomic* level had less relevance. A proper evaluation of the application of the new bargaining rules of the 1993 agreement and of the subsequent changes in the diffusion of fi-

162 '*Protocollo sulla politica dei redditi e dell'occupazione, sugli assetti contrattuali, sulle politiche del lavoro e sul sostegno al sistema produttivo*', of July 13th 1993. In the new system for determining wages a number of centralised aspects were introduced, thanks to a concertative approach: the agreement imposes co-ordination in the sectoral negotiations and compatibility of wage increases, with macroeconomic objectives for the curbing of inflation.

nancial participation of employees is difficult due to a lack of official and regularly published data on its incidence in Italy.[163] Presently, the renewed interest for the diffusion of employee participation has stimulated new proposals and a reform including new rules to encourage flexible compensation systems and the increase of tax incentives. This initiative has been advanced by the government, with the agreement of unions and employers' representatives, and is under debate for the final approval. Both, employers associations and trade unions show mixed attitudes towards financial participation.

Trade Unions in principle agree on the positive effects of profit-sharing but are divided with respect to employee share ownership schemes. Of the major trade unions *Cisl* is in favour of share schemes and see them as a means to amplify participation in decision-making while the *Uil* believes it not to be the task of trade unions to promote share ownership. On the other hand, *CGIL* traditionally is opposed to share schemes, holding against it that the financial participation of employees may better be realised through special complementary funds (*'Fondi di previdenza complementare'*). Similarly employers associations are divided in their attitude. *Confindustria* wants to leave the topic entirely to individual enterprises without taking a stand. The organisations representing SMEs (*Confartigianato, Confcommercio*) are more open towards financial participation in the context of the creation of funds promoting regional development of SMEs.

In summary, the political situation in Italy is in evolution; all political parties agree on the introduction of fiscal incentives (namely, the reduction of taxation) that entice company level agreements that link the increase of remuneration to that of productivity. This postulate was also mentioned in the tripartite agreement of 23 July 2007 and although it has not been implemented yet, it can be expected to lead to a decrease of the fiscal burden on the part of remuneration that takes a form of profit-sharing. In spite that recently there has been more interest in the topic, the other forms of financial participation, e.g., employee shares, do not find the unanimous support of employers associations and trade unions.

2. Legal and Fiscal Framework

Special legislation, including tax incentives, exists for profit-sharing, employee share ownership and stock option plans.

[163] However, in 1997 the National Statistical Institute (ISTAT) has performed the first research to document the degree of flexibility in labour utilisation and in the pay setting system. It shows that around 9.9% of the companies with at least 10 employees have adopted firm level arrangements, while 38.8% of the total employment has been covered by the enterprise level agreements. Of the total amount of workers involved in company arrangements a vast majority of them, 73.4%, were employed in the industrial sector. Company-wide bargaining schemes are less present in small size enterprises: only 3.9% of the firms with 10-19 employees have signed company level contracts, while nearly half of the medium size companies with 200-499 and about two thirds of the large companies, with more than 500 employees, have adopted firm level bargaining. Similar differentials by size classes are present in the industrial and service sectors.

a) Share Ownership

Quoted companies that intend to provide share or stock-option plans to employees, members of the board of directors or consultants need the approval by the shareholder meeting and have to communicate information on the plan to both Consob (the Italian Securities and Exchange Commission) and to the public.[164] In 2006 legislation[165] introduced new prerequisites for benefiting from a flat capital gains tax rate of 12,5% instead of ordinary taxation for the value gained between the grant and exercise of the option or, in the case of share plans, the date the price is fixed and the date when the share is transferred to the employee: (1) the options are not exercised or the shares are not accrued before three years from when they were assigned; (2) at the moment when the employee exercises the option or the share is accrued, the company is listed in the market[166]; (3) - only for stock options - the employee shall maintain for the following 5 years from the date of exercise of the option an investment in securities for a value not less than the difference between the value of the shares at the moment of the assignation and the amount provided to the employee.

Share Plans - The Italian Civil Code regulates discounted Employee Shares in Joint Stock Companies. According to Art. 2441 V Civ.C. the pre-emptive right of shareholders can be suspended for up to 25% of newly issued shares by majority vote of the general assembly if these shares are to be transferred to employees; for more than 25% the vote requires the majority of capital held. In order to facilitate the acquisition of shares by employees, the legislator permits a company to advance funds, make loans, and provide security, with a view to acquisition by employees of the company, conditional that this 'financial assistance' is within the limits of distributable reserves (Art 2358 V Civ.C.). Furthermore, Art. 2349 and 2351 V Civ.C. permits the issuing of Special 'Employees shares' in capital increases with specific rules for form, tradability and rights. In particular Art. 2351 Cic.C. foresees that the statutes of the company may attribute to this type of shares the right to nominate an independent representative on the management or supervisory board; nevertheless Art. 2351, introduced with the 2003 reform of the Civil Code has not been used until today. Since 1999[167] tax exemptions have been introduced for shares held by employees granting a flat tax rate on the rise in value of 12,5% capital gain tax (instead of the progressive personal income tax rate) and an exemption from PIT on the benefit up to a threshold of originally 4 millions of Lire, which was successively fixed at 2066 EUR. The tax incentives are conditioned to the mandatory provision that shares have to be held at least for 3 consecutive years.[168]

Privatisation - Paragraph 381 of the financial law 2005[169] established that, in order to facilitate the privatisation process, the by-laws of companies in which the State has a relevant participa-

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164 Law No. 262 of December 28, 2005.

165 Pursuant to Law Decree No. 262 of October 3, 2006 (the so called 'Financial Law' – *La Finanziaria*) converted into Law No. 286/2006.

166 This condition substantially reduces the possibility of exemption from ordinary taxation for a large number of employees, considering that in Italy the number of companies listed on the market is rather low.

167 Decree Law 505 del 1999 Nr. Changing the Personal Income Law.

168 Art. 51 of the Law on Income Tax. Pursuant to the decision No. 97 of July 25, 2005 of the Tax Agency ('*Agenzia delle Entrate*') income from employee shares shall not be subject to income taxes if the shares assigned to the employees are sold within the blocking period if the sale does not depend on the will of the employee but results *ex lege*.

169 Law No. 266 of December 23, 2005

tion may indicate special financial instruments or categories of shares, which may be offered for free to all shareholders or *vis-à-vis* the payment of a compensation to specific shareholders.

Stock Option Plans - Specific rules regarding stock option plans were introduced 1997 with the ad hoc rules of Law Decree 314/97[170] aiming at implementing stock option plans. Furthermore, since 1999 the increase in value of shares offered to employees on the basis of stock options plans are exempted from the payment of the Progressive Income Tax and of the Social Security Contributions. Pursuant to amendments[171] the fiscal benefit of the rate of 12,5% (instead of the ordinary taxation rate) are now conditional on a five year blocking period and a maximum value of the assigned shares shall of the value of the annual gross retribution relating to the fiscal period preceding the one of the assignation. Stock options plans of 5 July 2006 onwards, that do not respect these conditions will also be subject to social security contributions.

b) Profit-Sharing

The National Company Law is not prohibitive to profit-sharing (quote di salario legate agli obiettivi di redditività/proddutivita) but setting the rules and principles is left to collective bargaining at company level. Tax incentives for profit-sharing were introduced with Decree Law No. 67 of March 1997 as a partial tax exemption for employer contributions up to a maximum of 1% of the total salary paid, which were subsequently amended.[172] Furthermore, under the 1997 Decree Law a 10% 'compulsory solidarity contribution', substituting the normal social security contributions, was introduced.

Presently, new rules that increase the tax exemption for employer contributions to a maximum of 5% were approved by Parliament[173] and the rules for application are being currently defined. Now, the employer benefits from a 25% reduction on social security contributions. The employee is exempted from social security contributions, which in turn are covered by the state in order to keep the initial level of contribution. Furthermore, the employee enjoys a tax deduction of 23% from PIT up to a maximum amount EUR 350.

c) Participation in Decision-Making

Although Art. 46 of the Italian Constitution recognises the right of workers to 'cooperate in the running of the companies in a manner and in the limits defined by the law', this regulation was never translated in to simple law. However, law no. 300/70 guarantees the freedom of trade unions and the right to be represented. The so called *'Intesa Quadro'* between the major trade unions Cgil, Cisl and Uil of 1 March 1991 introduces the unitari union representatives (RSU, rappresentanze sindacali unitarie) which may be founded in any company with more than 15 employees and that have the right to represent workers in general and in collective

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170 Art. 48, par. 2, lett. g) and g-bis) of the Italian Tax Code (ITC) as amended by Law decree 314/97 and 505/99. Law Decree 505/99 has amended the tax-favoured regime provided for share option plans.

171 Article 36, paragraph no.25, of Law-Decree 223 of 2006 provided expressly the abrogation of letter g-*bis* of the ITC. However, law 248 of 4 August 2006 (which converted Law-Decree 223 of 2006) re-introduced letter g- *bis* ITC adding new conditions.

172 In 1998 the share of the flexible wage exempted from payment of social security contributions was raised to 2% and in 1999 the tax relief was re-determined to a maximum of 3%.

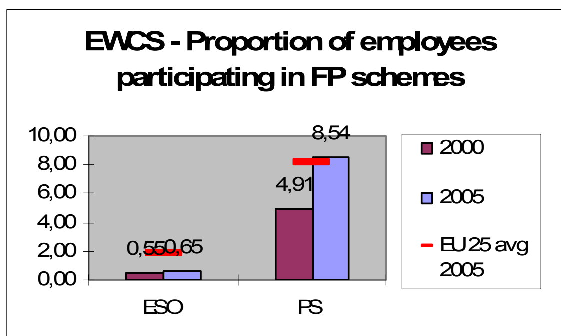
173 Law No. 247 of 24 December 2007.

bargaining. Information rights (e.g., about investment, planning, production, forecasts, technological changes) and consultation rights (e.g., on internal work rules and the working environment) are defined in collective bargaining contracts.[174] The recent transposition of the European Directives on Information and Consultation rights (D.Leg.vo 25/2007) into national law extends and strengthens the effectiveness of these rights in all companies employing more than 50 employees.

[174] OECD, Survey of Corporate Governance Development in OECD Countries, 2003, Paris.

XV. Latvia

The main trends in employees' financial participation in Latvia can be described as poorly developed and on the decline. During the transition period privatisation shaped the environment for employees' financial participation and influenced the current state of employee share ownership and profit-sharing. However, the transition process only led to a low level of employees' financial participation. By the end of 1998, shares with the nominal value of 27 million LVL had been sold for vouchers to 25,611 employees and former employees of the companies, amounting to 13.56% of the shares (LPA, 1998). According to another study based upon responses from 915 enterprises specifying their ownership structure for 1997, 1998 and 1999 (Jones and Mygind, 2005), in the period between 1997 and 1999, employee and former employee ownership decreased by 19.2% and 23.3%. Profit-sharing is reported only in 7% of 167 responding enterprises in a management survey from 1997, but 5 out of 28 of the enterprises with majority employee ownership.



1. General Attitude

The trade unions are quite weak: the current rate of unionisation in Latvia is 18%. The Free Trade Union Confederation of Latvia (FTUC**,** Latvijas Brīvo Arodbiedrību Savienība) is the biggest non-governmental organisation in Latvia; it protects the interests of employees who are trade union members at branch and inter-branch level, and represents 25 organisations.[175] Financial participation of employees is currently not on the trade unions agenda. The interests of employers are represented by the Latvian Employer's Confederation (LEC). With regard to the financial participation of employees, the Director General of the LEC, Ms. Elina Egle, declared in an interview that the Confederation's activities are in line with government legislation and that the financial participation of employees is outside the area of competence of the Confederation.

[175] Latvijas Republikas Likums par arodbiedrībām, Ziņotājs, No. 3/4, 31 January 1991 as amended.

The government is not concerned with the financial participation of employees, as the reduction of employment is considered to be the priority. The Ministry of Social Affairs concentrates its activities on solving problems related to the increase of minimum wages and allowances for the unemployed. Participation of employees has not been on the political agenda of Parliament. Most recently though, political parties and policy makers show a growing interest in the issue.

2. Legal and Fiscal Framework

Employee share ownership as well as profit-sharing are used in Latvian companies and are directly or indirectly regulated by legislation affecting the effectiveness of such forms of financial participation. Whereas no special legal regulation on profit-sharing exists, there are several pieces of legislation that touch upon employee share ownership and which should be interpreted in correlation with each other. Regulation of employee share ownership has not been developed systematically, so that the legislation partly creates incentives and partly inhibits the development of such schemes.

a) Share Ownership

Privatisation – Small privatisation started in November 1991 following the Law on the Privatisation of Objects of Trade, Catering and Services. The decision about privatisation method, initial price etc. was made by local Privatisation Commissions. Possible privatisation methods were: sale to employees, auctions to a selected group, open auctions and sale to a selected buyer. Purchasers had to be Latvian citizens or to have been living in Latvia for at least 16 years. Decrees of August 1992 and February 1993 contained a list, proposed by the sector Ministries, of 579 medium and large enterprises to be privatised. 400 of these enterprises were to be privatised by the public offering of shares, and in addition 147 were to be leased with the option to buy; later this list was expanded to 712 enterprises (Jemeljanovs, 1996, p. 205). However, except for the leasing option the privatisation proceeded very slowly and before the privatisation agency took over, only around 50 large and medium sized enterprises had been privatised. Large privatisation of state-owned property and land was and is being carried out by the Latvian Privatisation Agency (LPA) organised as a joint stock company under the Law on Privatisation of Property Units Owned by the State and Municipalities of 17 February 1994.[176]

Although the privatisation process is advanced, it is not yet complete, so that it is still possible for employees to acquire shares under special procedures as prescribed by law. Today, the

[176] The main privatisation method under this law is sale by tender to the highest bidder, supplemented by restitution and mass privatisation. Many of the largest enterprises have combined the sale of a dominating block of shares to a core investor and the sale of minority share holdings in public offerings.

Law on the Privatisation of Objects owned by the state or a municipality[177] (hereinafter referred to as PL) is the main regulatory act on the privatisation of enterprises.[178] It should be interpreted in line with the Law on the Reorganisation of State and Municipal Enterprises in Corporations of 8 July 1996[179], hereinafter referred to as RL. Shares of state owned corporations can be sold to employees in the course of privatisation even below the nominal value of such shares. However, the shares to be sold to the employees cannot amount to more than 20% of the share capital of the particular company (Art. 57 RL). If municipal objects are privatised by restructuring, the privatisation plan must contain a clause stating how many shares will be sold to employees as well as the discount, if such is applicable according to law (Art. 40.2.5 RL).

However, the 20% limit of employees share privatisation appears as a limitation of rights rather than an entitlement, due to the fact that there is no clear obligation in law to offer any shares at all to employees in a particular privatisation case.

State or municipal owned companies (2001) – According to the Law on State and Municipal Corporations[180], the government of Latvia or the respective municipal authority decides in which state or municipal company employees' shares can be issued (Art. 68 (1), (2)). Employee shares can only belong to employees and board members and cannot be alienated to other persons, even to other employees (Art. 68 (4), (5)). If the employment is terminated, or the member of the board leaves office, the employee's shares are transferred back to the company (Art. 68 (6)). This is one of the exceptions when a company is allowed to acquire its own stock (Art. 70). Where the company has acquired its employee stock, this must be transferred to employees within six months of that date. If the shares are not transferred within the aforementioned time period, the shares will be deleted and the share capital will be decreased respectively (Art. 71 (1), (2)).

Private Companies (2004) – There are three forms of corporations with important differences with regard to the regulation of share ownership of employees: the limited liability company, the private company, the shares of which are not publicly tradable objects, and the joint stock company, a company the stocks of which can be publicly tradable objects (Art. 134 (3), (4) Commercial Law[181], hereinafter referred to as CL). For limited liability company, there are no special legal regulations on employee share ownership so that general rules apply. By contrast, joint stock company can issue employee stock which can be acquired by employees in the broad sense, i.e. including managers (Art. 255 (1) CL). Employee stock shall be issued only on account of the net profit of the company and the total value of employee stock should not exceed 10% of the registered equity capital of the company (Art. 255 (4) CL). Another limitation concerning employee stock is the requirement that the Company's own capital should not become less than the registered capital (Art. 255 (5) CL). No voting right and right

177 The PL was adopted on 17 February 1994 (LV, 3 March 1994, No. 27) and, although amended, is still in force.

178 The PL provides for various methods of privatisation: sale, investment in share capital, increase of share capital by attracting private investors, or sale of shares to the management (Art. 2 PL).

179 LV, 19 July 1996, No. 122.

180 From 3 January 2001, LV, 19 Junly 1996, No. 122 as amended.

181 From 13 April 2000, LV, 4 May 2000, No. 158/160 as amended.

to liquidation quota are attached to employee stock issued according to Art. 255 CL.[182] Such stocks can be freely sold if the Articles of Association do not provide otherwise (Art. 255 (7) CL).

b) Profit-Sharing

There are no limitations in the law with regard to profit-sharing; however; there are also no exact regulations with regard to such profit-sharing. It is possible to declare that salaries are to be dependent upon the profit of the company and it is also possible to provide benefits in the form of premiums as well as other benefits directly connected with the profit of a particular company. However, all those benefits will be subject to personal income tax of 25%. In such a way the incentive to provide additional benefits is reduced since the benefits of profit-sharing are 25% less than they would be in the case of share ownership by paying out dividends to shareholders, because dividend payments are not subject to tax.

c) Participation in Decision-Making

There is no statutory employee representation at board level in Latvia.

The main form of workplace representation in Latvia is through the unions, but since the revised Labour Law (adopted by the Saeima on 20 June 2001, hereinafter referred to as LL, as amended) came into effect on 1 June 2002, it has also been possible to elect 'authorised employee representatives" (Art. 10 (1) LL). Both are involved in information and consultation and both can be involved in collective bargaining, although, non-union representatives can only negotiate if there is no union (see Art. 18 (1) LL). The employer shall consult with employee representatives on issues that may affect the interests of employees, in particular a decision which may substantially affect work remuneration, working conditions and employment in the undertaking (Art. 11 (1) 2) LL). The legislation implementing the Directive 2002/14/EC on information and consultation strengthened the legal position of employee representatives by setting out more clearly how information and consultation should be defined.

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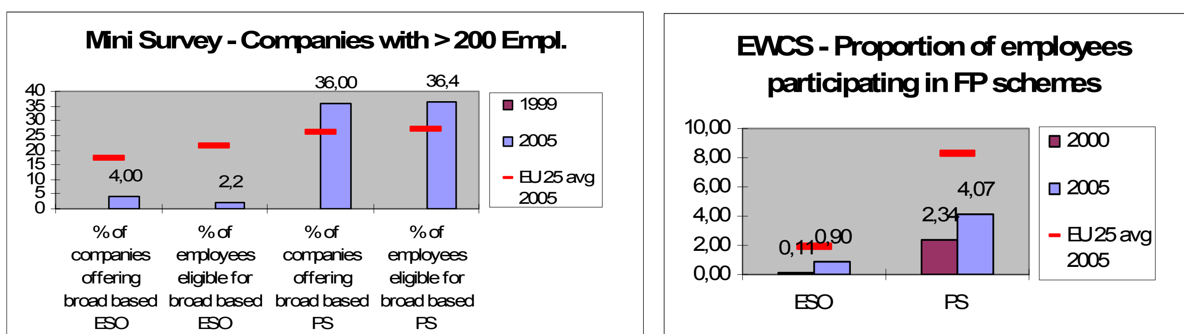
182 Employee stock issued by a private joint stock company according to Art. 255 CL should be differentiated from the stock acquired by employees in the course of privatisation. Limitations attached to employee stock according to Art. 255 CL, in particular lack of voting rights, do not apply to privatisation stock.

XVI. Lithuania

After Lithuania regained independence, employee ownership was used to facilitate privatisation. At the initial stage of privatisation 1991-1995, employee buyouts at a discount combined with the extensive use of vouchers by employees and leasing with the option to buy led to a high percentage of employee majority ownership. By 1994, fewer than 5% of the privatised firms in the programme implementing the Law on the Initial Privatisation of State-owned Property (LIPSP) had no employee ownership and the percentage of enterprises where the majority of privatised assets were taken over by employees increased from 3% in 1991-1992, to 65% in 1993, and to 92% in 1994-1995 (Privatisation Department at the Ministry of Economics). After most of the preferential rights of employees were abolished in 1995, employee ownership is on the decline changing partly to management and to outsider ownership. A manager-survey conducted in spring 2000 provides information on ownership at the time of privatisation or start as a new firm for 1993, 1996, 1999 and spring 2000 for 405 respondents (for details see PEPPER III, pp. 199, 205, Table 4). In 1993 around 50% of employees were owners in the whole sample of responding enterprises. However, the proportion of owners fell to around 1/3 in 1999. Not surprisingly, the proportion of employee owners was highest in employee-owned enterprises, but here also the proportion of owners fell from 76% in 1993 to 66% in 1999. No data is available on profit-sharing.

At present, in Lithuania, financial participation is rather viewed as an incentive for managerial employee motivation, initiated by managers and current owners of companies.



1. General Attitude

Trade unions are organised through the Lithuanian Trade Union Confederation (Lietuvos profesinių sąjungų konfederacija), the Lithuanian Trade Union 'Solidarumas' (*Lietuvos profesinė sąjunga 'Solidarumas'*) and the Lithuanian Labour Federation (*Lietuvos darbo federacija*). The Lithuanian Trade Union Confederation (headed by A. Sysas), is the largest and strongest union with over 120,000 members. In the early stage of transition unions promoted employee

ownership and actively contributed to place EO on the privatisation agenda in Lithuania. The General Secretary of the Lithuanian Trade Union Confederation, Ms Janina Matuiziene stated in an interview that trade unions have the general aim of higher wages for employees and are relating it to an increase in company profitability. No particular actions concerning the financial participation of employees are on the agenda of the Confederation, but this issue could be supported if any industrial trade union makes a proposition.

Employers are organised within the Lithuanian Confederation of Industrialists (Lietuvos pramonininkų asociacija), which is actively promoting the interests of Lithiuanian large businesses in the Lithuanian Parliament (Seimas), as well as in the Lithuanian Government, and Lithuanian Employers' Confederation (*Lietuvos darbdavių asociacija*). The question of the financial participation of employees was not discussed by the Lithuanian Confederation of Industrialists nor by the Lithuanian Employers' Confederation. M. Busila, currently acting as Director of the Department of Economics and Finance of the Lithuanian Confederation of Industrialists, declared in an interview[183] that the confederation had taken no official position on this issue, but supports initiatives of individual enterprises. He mentioned that different methods of motivation of employees related to participation are used in some of the enterprises, but usually these are applied to managers. In his opinion, such practices are distributed by the academic community and by branches of foreign firms. Recently, employers have been paying more attention to the motivation of employees, i.e. by financial incentives, because of the problem of increasing emigration of skilled workers.

The programmes of the coalition parties which came into power in 2004 including the Social Democrats (Lietuvos socialdemokratų partija LSDP), the New Union (Social Liberals) (Naujoji sajunga (Social liberalų partija)) and the newly established Labour party (Darbo partija DP) do not mention financial participation, they are aimed at increasing social guarantees, and reducing poverty and unemployment. Employee financial participation as well as participation in decision-making has not been on the political agenda of Parliament and the Government, so far there has been no discussion within the parties and in the Government.

2. Legal and Fiscal Framework

Financial participation of employees is barely regulated. Current legal regulations neither contain special provisions concerning PEPPER schemes nor provide companies with incentives to introduce them.

a) Share Ownership

Privatisation (1991, abolished 1995) – The first stage of privatisation started when the Law on the Initial Privatisation of State-owned Property (LIPSP) was passed in February 1991. The cornerstone of the fast privatisation in Lithuania was the voucher scheme.[184] Under

183 Interviews with Mr. M. Busila and Ms J. Matuiziene were conducted by Ms. Jone Sakalyte in March 2005.

184 Vouchers and cash quotas were only given to residents and had limited transferability (to relatives, later they could be used in exchange for outstanding housing loans).

LIPSP, employees had the opportunity to buy a certain percentage of shares in the first round of auctions at lower rates before most of the remaining shares were sold in public offerings in later rounds. The percentage of shares available for employees was increased from 10% in 1991 to 30% in 1992 and to 50% after the former Communist Party came into power in early 1993. The 20% extra shares reserved for employees after 1993 did not initially have voting rights, but later it was made possible for the general meeting to convert these shares into regular voting shares. The second stage of privatisation was based upon a new Law on Privatisation of State-owned and Municipal Property of 4 July 1995. Residual shares and some of the very large companies including public utilities and infrastructure enterprises were to be sold. The use of vouchers was abolished at this stage, and only cash privatisation was possible.

The third Law on Privatisation which is still effective was adopted on 11 April 1997. Currently, privatisation of the majority of enterprises in Lithuania is complete. However, privatisation is still possible and the respective legal regulations are still in force. The most important regulations are the Law on Privatisation of State Property and Property of Municipalities of 11 April 1997 as amended (hereinafter referred to as PL), the Law on Securities Market of 16 January 1996 as amended and the Law on the State Property Fund of 11 April 1997 as amended. The current PL does not contain any significant preferential rights for employees in the privatisation process.[185] However, if shares are privatised by public tender employees can be offered up to 5% of the shares owned by the state at par value. This provision is not applicable to enterprises under state control or to enterprises in which employees have already acquired shares of their enterprises under other laws (Art. 16 (3) PL). If shares are offered at a public tender or by direct negotiation, the final payment can be postponed for 5 years for employees (Art. 20 (3) PL).

Private Companies (1995, 2003) – In the course of capital increase, corporations (joint-stock companies as well as limited liability companies) can issue employee shares after all shares subscribed at the time of incorporation have been paid for (Art. 43 Law on Companies[186], hereinafter referred to as CL). The CL does not provide for a maximum percentage of the capital employee shares may constitute. Employee shares are to be distributed amongst employees wishing to purchase them, with the exception of the management (Art. 43 (2) CL). A restriction period of not longer than three years must be determined within which employee shares can be sold only to other employees (Art. 43 (3) CL). Within this period employee shares are not only shares of limited tradability, but also non-voting shares before the restriction period expires (Art. 43 (3.3) CL), although employee shares are ordinary shares (Art. 43 (1.1) CL). Art. 43 (5) CL stipulates that an employee must pay for subscribed employee shares before the expiry of the restriction period for the transfer of shares. The first payment should be made in cash within a short period; further instalments can be deducted from the employee's salary upon application of the employee. The corporation is not allowed to put pressure on employees to force them to purchase shares or to pay for shares by deductions from

[185] The PL allows for: public share subscription (for large and medium-sized enterprises), auctions (for small enterprises or spin-offs), tenders, direct negotiations and leasing with the option to buy.

[186] Law on Companies from 11 December 2003, No. IX-1889 (Valstybės žinios 2003, No. 123–5574) as amended; according to CL, shareholders have the pre-emptive right to acquire shares or convertible debentures issued by the company, unless the general meeting decides to withdraw the pre-emptive right for all shareholders. The decision to withdraw the pre-emption right in acquiring the company's newly issued shares or convertible debentures of a specific issue require a qualified majority vote of not less than 3/4 of all votes conferred by the shares of the shareholders present at the general meeting and entitled to decide on the issue (Art. 28 (2) CL).

salaries (Art. 43 (4) CL). After the expiry of the restriction period for the transfer of shares employee shares become ordinary shares and can be sold to third parties who are not employees of the company (Art. 43 (3) CL). Since most employees are minority shareholders, provisions on the protection of minority shareholders are relevant.

b) Profit-Sharing

There are no specific regulations concerning profit-sharing with employees. Since companies have to pay income tax on dividends, this is viewed as an expensive method of profit distribution; therefore priority is given to share buyback schemes. Employee monetary incentive schemes used in companies include payments of premiums and bonuses, in some cases related to company turnover and profits. Bonuses have tax advantages, since they are not double taxed as dividends are (firstly at corporate profit tax rate, secondly at income tax rate), but taxed only by income tax for individuals (33%).

c) Participation in Decision-Making

According to the Labour Code[187] (hereinafter referred to as LC), employees may be represented and protected by trade unions or by work councils (Art. 19 (1) LC).[188] The work council should be an institution made up of representatives of all employees. A trade union, however, can be established by a small number of all employees in an enterprise. Nevertheless, the power to negotiate with the employer has been vested in trade unions (see Art. 19 (1); 21 (2); 60 (4) LC). Trade unions are active in only a small number of private enterprises, but the special law on work councils (Art. 21 (1) LC) has not been adopted yet, so that no work councils can be established in practice. As a result, conditions favour the creation of trade unions and an expansion of their activities.

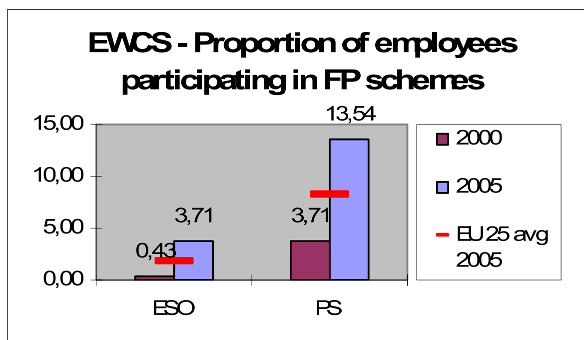
[187] Labour Code from 4 June 2002 in force since January 2003, No. IX-926 (Valstybės žinios 2002, No. 64-2569) as amended.

[188] Where an enterprise, agency or organisation has no functioning trade union and if the staff meeting has not transferred the function of employee representation and protection to the trade union of the appropriate sector of economic activity, the employees shall be represented by the work council elected by secret ballot at the general meeting of the staff (Art. 19 (1); 21 (2) LC).

XVII. Luxembourg

Only few cases of employee financial participation exist, prevailingly in multinational companies in the financial sector. It is assumed that the most common form is cash-based profit-sharing, but the data are unreliable, since the wide-spread bonus plans ('gratification') are generally not related to profits or other financial indicators and, therefore, are not genuine profit-sharing plans. Share ownership and stock option plans are few and very seldom broad-based.

According to a recent cross-country study, the percentage of enterprises operating different forms of financial participation plans in 2005 was as follows: employee share ownership plans 3.9%, profit-sharing plans 13.7% (EWCS). Approx. 25% of companies operated stock option plans in 2003 (EU Report on Stock Option Plans). Please note that these figures include executive plans.



1. General Attitude

The Government started to show interest in employee financial participation at the beginning of the 1990s. At the time policy makers were advocating especially voluntary profit-sharing, stressing though, that it should not become a part of collective agreements. Nevertheless, no concrete policy measures were taken and in recent years the issue has not been a topic. Employers' associations (organised in the Union des Entreprises Luxembourgeois, UEL) were generally opposed to financial participation schemes, preferring other flexible pay models; recently they have not taken a position though. The two major trade unions, the Onofhängege Gewerkschaftsbond Lëtzebuerg (OGBL) and the Lëtzebuerger Chrëschtleche Gewerkschaftsbond (LCGB) were sceptical towards employee financial participation, fearing to loose control over the collective bargaining process. Nevertheless, some collective agreements have incorporated elements of profit-sharing.

2. Legal and Fiscal Framework

There are neither special legislation nor tax incentives for any form of employee financial participation.

a) Share Ownership

Broad-based share ownership and stock option plans, if any, exist in very few large multinational companies. There is no special legislation on these types of plans. Stock option plans can be divided in plans on potential options (not tradable at grant) and plans on tradable options (tradable at grant). Plans on tradable options for employees are very rare. In plans on potential options, the employee is liable to personal income tax at exercise, but not liable to social security contributions. The employing company can deduct the costs of the plan and is not liable to social security contributions.

b) Profit-Sharing

Cash-based profit-sharing is supposed to be most common. It is difficult to distinguish it from the commonly practiced bonus plan (gratification), which is not related to financial indicators though. Nevertheless, there is incidental evidence that sometimes collective agreements link this 'gratification' to company profits. Since collective agreements, except for those declared binding for branches, are not public, it is difficult to quantify the phenomenon. A positive exception is the collective agreement for the banking sector. Therefore, genuine cash-based profit-sharing plans, especially broad-based, will be very rare.

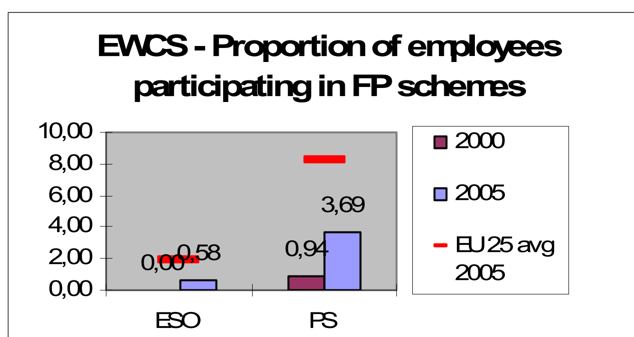
c) Participation in Decision-Making

There is no direct connection between participation in decision-making and financial participation of employees; in particular, financial participation plans cannot extend the existing rights in connection with participation in decision-making. In the companies with compulsory employee representation on the board (pursuant to Art. L. 426-1. of the Labour Code in state companies and companies with more than 1000 employees), employee representatives may influence the introduction and design of financial participation plans.

Except in the smallest workplaces, those with fewer than 15 employees, workers have a legal right to representation at work. The central element in representation at the workplace is the employee delegation, which is directly elected by all employees. In larger companies, those employing more than 150, there is another works council type body, the joint company committee. The employer is obliged to inform and consult the joint company committee about any financial or economic decision likely to have a significant effect on 'the structure of the business or the level of employment', including planned changes in the volume of production, investment policies, transfers and take-overs.

XVIII. Malta

In spite of the strong historical link to the United Kingdom which has been the source of much of Malta's law on Companies and Employment, in practice the financial participation of employees is not well developed, being neither well diffused nor enjoying much political support. The ramifications of the nationalisation programme in the 1970s and the privatisation drive of the 1990s – although diametrically opposed to each other – had the unintended consequences of introducing financial participation practices for employees in some larger enterprises. However, privatisation cannot be said to have been auspicious to workers' participation. The largest schemes in operation at two previous state owned enterprises are share ownership schemes, profit-sharing is rare. In most of the enterprises which have an operating financial participation scheme, the workers are unionised and the trade unions supported these schemes.



1. General Attitude

The government polices that have actually triggered the largest PEPPER schemes in practice in Malta were not focused upon the financial participation of employees but produced it rather as a side effect. Between 1971 and 1987 the newly elected government of the Malta Labour Party (MLP) embarked upon a programme of nationalisation as part of the de-colonialisation process, seven years after the attainment of political independence. The banking sector, at the time dominated by two major banks, was one of the targets of this nationalisation plan. The winding up of a 'widow and orphans' fund in operation in these banks prior to nationalisation resulted in the creation of a number of shares for the employees of one of these banks. The privatisation programme of 1990 adopted by the Nationalist Party (NP), in power since 1987, also had the unintended consequences of introducing financial participation schemes for employees in the banking sector. Reversing the process of nationalisation begun by the previous administration, the government divested itself of several entities in which it was a majority

shareholder.[189] A side effect of this privatisation process was the creation of a trust fund for the benefit of employees in one of the banks.

Inspite of this apparent lack of enthusiasm amongst the social partners, trade unions have supported all the schemes that were proposed and put into practice and have participated actively in their administration. The lack of collective bargaining at sectoral level makes it easier for the Maltese trade unions to be supportive of such schemes in practice. The trade union which has been most active in this respect is the Malta Union of Bank Employees. This is due to the fact that the two major banks, where the union is heavily represented, were the target of both the aforementioned nationalisation and privatisation programmes. The general trade unions, General Workers Union, the largest union in the island, and the Union of United Workers, were also involved in prolonged discussions with the Government about the introduction and implementation of a scheme in the public sector whereby employees were given the opportunity to set up cooperatives and submit tenders for contracts of work.

PEPPER schemes have never featured prominently on the agendas of the two major political parties. The present NP government is rather passive but not adverse to financial participation.

2. Legal and Fiscal Framework

Maltese law tends to refer to employee participation schemes indirectly; it tacitly recognises that Maltese firms may put such schemes in place (by means of private or collective agreements), rather than establishing a formal framework for their establishment or creating any noteworthy fiscal or other incentives. However, Maltese law does provide for the legal instrument for ESOPs, namely the trust vehicle. Tax incentives for financial participation schemes are few.

a) Share Ownership

Privatisation (1990) – The aforementioned privatisation drive which the Nationalist Party embarked upon in the early 1990s resulted in a share ownership scheme being put into place for the employees of two formerly para-statal entities[190] which were partially privatised.[191] However, these schemes did not have any statutory basis; they were set up and regulated by means of private agreements (both individual contracts and collective agreements) between the newly privatised companies and their employees. Interestingly, the statutes of two as yet un-privatised utility providers, the Enemalta Corporation[192] and the Water Services Corpora-

189 Restructuring became more urgent in view of the Maltese Government's formal application, sub-mitted in July 1990, to become a full Member of the European Union (Rizzo, 2003, p. 31).

190 By virtue of their nationalisation these two banks had become para-statal entities (independent statutory bodies within the realm of the public sector).

191 This was a trust fund, set up on behalf of employees, in the Bank of Valletta, a formerly state owned bank, and in Maltacom, a state owned telecommunication enterprise.

192 Enemalta Corporation Act, 1977 (Chapter 272 of the Laws of Malta).

tion,[193] explicitly permit the '*establishment, by the Corporation […] of schemes or incentives related to productivity or performance.*'

Private Companies (2004) – There is no statutory framework for share ownership or share option schemes. Maltese law does not regulate the exact conditions under which share option schemes may take place. It is up to individual companies to create their own schemes utilising general company and civil law principles as the legal basis. Provided that a company is empowered by its Memorandum and Articles of Association to implement employee financial participation schemes, employers wishing to adopt one of the two types of schemes can enter into private or collective agreements with their employees, setting out the scope, terms and conditions. Where the company establishing the scheme is itself the issuer of the shares to be offered to its employees, it is not considered to be providing an investment service in terms of the Investment Services Act 1994 (hereinafter referred to as the IS Act) and, consequently, will not require a licence under the IS Act.

The allotment of shares to employees must be made in accordance with the general rules on the offering and allotment of shares as contained in the Companies Act 1995 (hereinafter referred to as the CA). As a general rule, the CA prohibits companies from acquiring its own shares (Art. 105 para. 1 CA) or the shares of its parent company (Art. 110 para. 1 a) CA) or providing financial assistance for the purchase of its own shares or the shares of its parent company (Art. 110 para. 1 lit. b) CA). However, Art. 106 para. 4 CA and Art. 110 para. 2 CA derogate from the aforesaid general rule by providing that a company may both acquire its own shares or those of its parent and provide financial assistance where this is intended to facilitate the acquisition of shares by or for its employees or the employees of a group company.

It should also be noted that the CA generally allows companies to offer their shares at a discount or pay a commission to any person in consideration for his subscribing or agreeing to subscribe to any shares in the company. This may also apply where shares are to be offered to employees at a discounted rate as part of a corporate share ownership scheme. In this context the CA does not differentiate between discounted shares being offered to employees and where they are offered to third parties.[194] Tax law on the other hand does not offer any tax incentives of note for these schemes. With regard to stock options, Maltese tax law offers certain minor incentives. Under the Fringe Benefit Rules issued under the Income Tax Act,[195] share options are only taxable upon the exercise of the option.[196]

Employee Share Ownership Plans (ESOPs) – Maltese law does not contain any specific legislation concerning ESOPs. Recent Trust legislation,[197] inspired by Jersey legislation, successfully achieved a seamless integration of the UK common law concept of trusts into Maltese law. A Trust can take many forms, and although the concept originated in the UK, trusts are not exclusive to countries that follow the common law tradition. One of these civil law

193 Water Services Corporation, 1991 (Chapter 355 of the Laws of Malta).

194 Consequently, the following conditions apply across the board: (i) authority for the making of discounts must be given by the company's Memorandum and Articles of Association, (ii) the discount must not exceed 10% of the issue price or as prescribed by the Memorandum and Articles, whichever is less, (iii) the amount or rate of discount must be made public, and (iv) in no event may the value of the shares be reduced to below their nominal value as a result of such a discount.

195 Legal Notice 125 of 2001.

196 Rule 36 of the Fringe Benefit Rules (LN. 125 of 2001).

197 The Trusts and Trustees Act, 1988 (Chapter 331 of the Laws of Malta)

countries is Malta which, through the Trusts and Trustees Act 1988, as amended in 2004 (hereinafter referred to as the Trusts Act), allows Maltese individuals and companies to set up and be a beneficiary in trusts regulated by Maltese law. The Trusts Act does in fact contain an explicit reference to 'employee benefit or retirement schemes or arrangements' as forming the basis of a Trust.

Although traditionally used for hedge funds, the 'Collective Investment Scheme' (hereinafter referred to as CIS) may also be used as the basis for an ESOP.[198]

With regard to the taxation of ESOPs which fall within the definition of CISs, unfortunately the Income Tax Act 1948 does not distinguish between exempted and non-exempted CISs, so the income arising from CIS ESOPs will be taxable at the normal rate. For taxation purposes, a CIS is treated as a prescribed fund. Investment income, as defined in the Income Tax Act 1948, which is received by a prescribed fund, is subject to a withholding tax of 15% on bank interest and 10% on investment income other than bank interest. Other income and capital gains remain exempt in the hands of prescribed funds. When Maltese resident participants of the CIS (the employees) redeem, liquidate, or cancel their units in the CIS they will not be subject to a second withholding tax.

b) Profit-Sharing

Maltese employment law classifies profit-sharing arrangements between employers and employees as forming part of the wage of the employee. Maltese labour legislation also appears to envisage contracts of service that solely contemplate remuneration by way of commission or a share of the employer's profits,[199] although these are rarely used in practice. This treatment as a 'wage' implies that any share of the profits will be computed together with the employee's salary for the purposes of the imposition of income tax.

c) Participation in Decision-Making

There are no general statutory arrangements for board level representation in Malta. Employee representatives in companies at board level are only found in the state-owned and recently privatised sector and here they are becoming less common.

In Malta it is the union – provided it is recognised (that is the employer is willing to negotiate with it) – that normally represents the employee at workplace level (see 2002 Employment and Industrial Relations Act). But EU directives have led to new arrangements for non-unionised employees. But it does not seem that these have been taken up to any extent. 2002 legislation states that the employer has a duty to inform and consult the 'employees' representatives'. If the union is recognised, then it is informed and consulted. If there are union members but no

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198 'Collective Investment Scheme' defined in Art. 2 IS Act is any scheme which aims at 'collective investment of capital acquired by means of an offer of units for subscription, sale or exchange'. It must operate according to the principle of risk spreading and either (i) the contributions of the participants and the profits or income out of which payments are to be made to them are pooled; or (ii) at the request of the holders, units are or are to be re-purchased or redeemed out of the assets of the scheme or arrangement, continuously or in blocks at short intervals; or (iii) units are, or have been, or will be issued continuously or in blocks at short intervals.

199 Art. 22 (3) and Art. 36 (13) Employment and Industrial Relations Act, 2002.

recognition, then the union represents unionised employees. Non-union employees elect their representative in a secret ballot.

In the more general area of information and consultation, legislation introduced in 2006 has provided for additional structures. Unionised employees, where the union is recognised, are represented by their union in terms of their information and consultation rights. But if there are categories of workers who are not represented by the recognised union or unions, they elect their own representatives who, together with the union representatives, enjoy general information and consultation rights. The same rules apply if there are no unions in the company at all. The 2006 legislation, requiring the setting up of information and consultation structures, applied to companies with 150 or more employees from January 2006 and companies with 100 or more employees from March 2007. From March 2008 it will apply to companies with 50 or more employees.

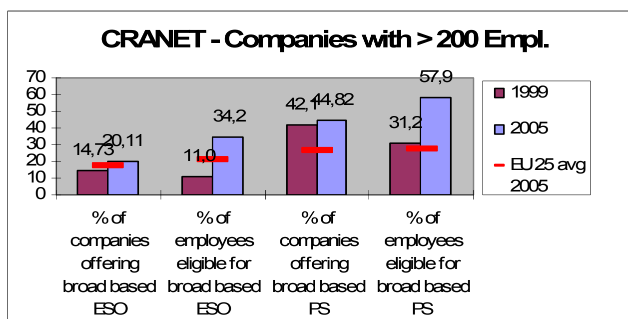
The key level for collective bargaining is the company level. There is also protection for those not covered by collective bargaining through a series of wage orders for specific industries that set minimum terms.

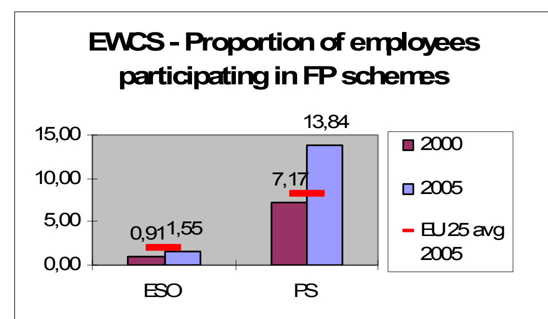
XIX. Netherlands

Employee financial participation schemes were introduced in the 1950s on behalf of expatriate executives from the United States. Many plans, especially share ownership and stock option plans, are still limited to top management. Savings plans, generally broad-based, have been implemented since the 1970s. In 1994, legislation on deferred profit-sharing, cash-based profit-sharing and stock options was enacted. Profit-sharing and share ownership plans combined with savings plans are the most common forms found in The Netherlands and thus may be considered typical.

A long-term study of the development of employee financial participation from 1996-2001 found that the number of enterprises with employee financial participation schemes more than doubled during that time period, from four percent to nine percent. Although these figures include executive plans, a trend could be observed: executive plans had decreased in number while broad-based plans had increased.[200] Profit-sharing plans showed only a five percent rise during the same period. The assumption was that this form of financial participation had peaked.

More recently, a study of employee financial participation in companies listed on the Amsterdam Stock Exchange showed that 62.5% of AEX companies offered such plans.[201] Stock option plans, offered by 41.7% of the AEX companies, were the most popular. These figures, however, also include executive plans. New nationwide statistics on various kinds of employee financial participation plans are currently being prepared by the Netherlands Participatie Institut, but as of March 2008 they had not been published.





200 Van den Tillaart, H./Poutsma, E. (1996); Sikkelbroeck, R. H. J. (2001).

201 Beursken, F. (2007), Werknemersparticipaties in Nederland: Theorie and Parktijk – Een Analyse van AEX ondernemingen, Master Thesis at the University of Rotterdam.

1. General Attitude

The government has given little support to employee financial participation of late, having concluded that such plans, especially those limited to executives only, the most prevalent, do not contribute to a more equitable distribution of wealth. Employers' associations traditionally backed only the management model; recently, however, they have begun also to favour broad-based plans for reasons pertaining to employee motivation.

Trade unions, which generally have been opposed to employee financial participation, recently have declared their support for broad-based plans on condition that no substitution for regular remuneration will be required. In 2001, the trade unions began a discussion on whether profit-sharing and broad-based stock option plans should be included in collective bargaining agreements. This proposal, however, has not been accepted.

2. Legal and Fiscal Framework

Savings plans, which may be combined with profit-sharing or employee share ownership plans, are the most typical forms of employee financial participation.

a) Share Ownership

Ordinarily there is no connection between share ownership and business form. An exception is the small family enterprise whose owners generally oppose employee share ownership because they fear loss of control.

Share Ownership Plans – Although public companies (Namloze Vennootschap) may transfer shares directly, limited companies (Besloten Venootschap) must utilize an intermediary because share transfer for them can be made only by means of a notarial deed. The intermediary chosen for this purpose is usually a foundation (Stichting Administratie Kantoor, SAK). It owns the employee shares, exercises voting rights and transfers depository receipts of shares to the employee shareholders. Other business forms can also be used as intermediaries. Tax incentives do not apply to share ownership not combined with a savings plan. The rules governing savings plans and corresponding tax incentives, discussed under profit-sharing above, also apply to share ownership plans. However, if savings are converted into shares or options, the annual maximum allowance is doubled (1,226 EUR in 2008).

Stock Option Plans – Stock option plans were originally limited to executives, but there has been an observable increase in the number of broad-based plans since the beginning of the 1990s. Options may be conditional (e.g., subject to a vesting period or a performance-related proviso) or they may be unconditional (i.e., tradable at grant). As of 2001, the employee could choose between two tax alternatives: unconditional options could be taxed at grant and conditional options at vesting, with no tax liability at the moment of exercise if held for more than three years, or tax could be imposed at exercise on the total capital gain. Tax incentives applied only if the stock option plan was combined with a savings plan under the same condi-

tions as for employee share ownership plans, however, these tax incentives were recently abolished so that taxes are now to be paid at exercise only.

b) Profit-Sharing

Profit-sharing is found in both cash-based and share-based forms. Since 2003, tax incentives for profit-sharing plans depend on their being combined with a savings plan. Under a savings plan, an employee may save from his pre-tax salary a legally specified maximum amount (613 EUR in 2008). Under plans which include at least 75% of employees, with employee shares being held in the savings plan for four years, a 15% flat tax is paid at exit in lieu of personal income tax and social security contribution. Under certain circumstances, the four year blocking period is waived (e.g., if the employee buys a principal residence, starts a new business, or takes a sabbatical or educational leave of absence).

c) Participation in Decision-Making

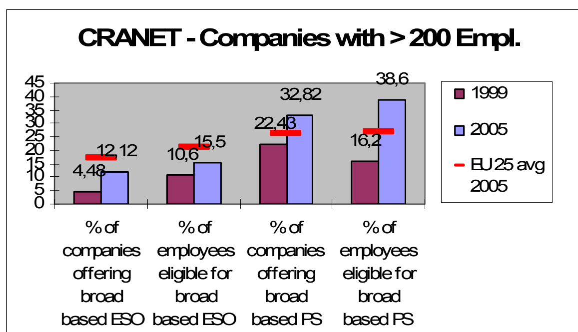
There is no direct connection between participation in decision-making and employee financial participation. The latter plans are specifically enjoined from extending those participation rights already in force. Moreover, employee financial participation is generally not a part of collective agreements. Companies with a workers' council must obtain council approval for any amendments made in 'the system of remuneration'. Broad-based employee financial participation plans are regarded as a part of this system. However, no approval of the workers' council is required in the case of 'discretionary plans', i.e., plans restricted to management only.

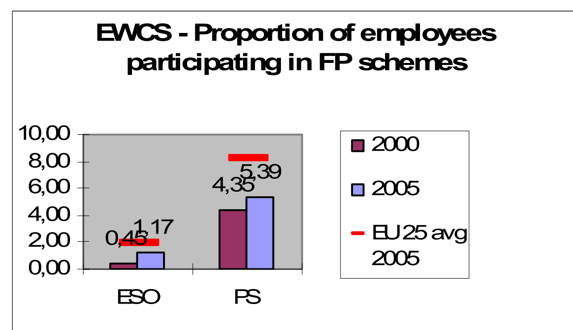
XX. Austria

The total number of financial participation plans, although still relatively small, has increased significantly since 2001 in response to the introduction of tax incentives. Only eight percent of plans currently active were established prior to 1990; 48% date between 1990 and 2000, and 45% after 2000.[202]

Recent measures promoting employee financial participation focus on share ownership. Currently eight percent of enterprises, mostly listed joint stock companies, have introduced employee share ownership plans; through these, 160,000 individuals, or six percent of the Austrian work force, own an average of five percent or less of shares in their employer firms.[203] Leveraged employee ownership plans (ESOPs), using the so-called employee participation foundation as a vehicle, were introduced in connection with privatization.

Stock option plans, generally not broad-based, have been implemented in one percent of enterprises. Profit-sharing plans are found in 25% of enterprises, mostly small and medium-sized trade companies.[204]





1. General Attitude

By the end of the 1990s, the government had become more supportive of employee financial participation. Behind this change in attitude were such factors as increasing competition with Eastern European economies, promotion of employee participation by the EU, and impending privatization of several large state-owned companies. Both the trade unions and employers' associations strongly support employee financial participation and cooperate with each other in this area.

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202 Vevera (2005); 54 et seq.

203 Kronberger/Leitsmuller/Rauner (2007): 11, 67.

204 Kronberger/Leitsmuller/Rauner (2007): 17.

After tax incentives were introduced in 2001, the Federal Workers' Chamber (BAK) and the Austrian Economic Chamber (WKO), in cooperation with the University for Applied Science Wiener Neustadt, conducted a study (2005) of the effects of financial participation on enterprise results and employee attitudes in individual companies. This study found that 80% of employer companies and workers' councils in firms which have employee financial participation plans are satisfied with the results, while 71% of enterprises without such plans would introduce them if the legal framework were improved.[205] In their proposals for reforming the legal framework, representatives of both employers and employees focus in part on the same issues: introduction of tax incentives for employee participants of profit-sharing schemes, higher tax incentives for participants in employee share ownership schemes, and more incentives to encourage small and middle-sized companies to introduce employee ownership schemes, especially leveraged ones like the ESOP.

The only controversial issue is whether employee financial participation should include a role in decision-making. Trade unions are critical of models which subject employees to risk, as with non-voting employee shares, without granting corresponding rights; they also object to schemes that benefit only management, e.g., stock options. Since labor law already requires employee participation in decision-making, this issue only affects small enterprises without workers' councils..

2. Legal and Fiscal Framework

The incidence of various models of employee financial participation depends on the business form. Share ownership plans are introduced in quoted joint-stock companies (AG) (45%), cooperatives (Genossenschaft), foundations (Stiftung), registered associations (eingetragener Verein) (50%), limited liability companies (GmbH) (6%). They do not exist in partnerships (OHG, KG, OEG, KEG, GbR).[206] An absolute obstacle to employee share ownership in partnerships is the institute of co-ownership under the Austrian company law; this institute is typical of Germanic legal systems.

Other obstacles to the spread of employee share ownership plans in limited liability companies include the strong position shareholders enjoy vis a vis management, the transfer of share ownership only by notarial deed, and the absolute prohibition against a company acquiring its own shares.

Employee share ownership is based on a direct participation model in 21% of enterprises.[207] Leveraged models are relatively rare due to high costs and complex administration; they are found in large publicly-quoted joint stock companies, especially those created by privatization.

The law on Capital Market Offensive of 5 January 2001 introduced tax incentives for employee share ownership schemes by amending the Income Tax Law (hereinafter referred to as

205 Krongerger/Leitsmuller/Rauner (2007): 10, 16.

206 Kronberger/Leitsmuller/Rauner (2007): 17.

207 Kronberger/Leitsmuller/Rauner (2007): 57.

'ITL') and the Capital Tax Law (hereinafter referred to as 'CTL'). Profit-sharing plans are found in every third limited liability company and every second private joint-stock company.[208]

a) Share Ownership

Employee share ownership plans are mainly based on direct share transfer. However, leveraged share ownership plans and stock option plans have become more widespread since 2001.

Direct Share Ownership Plans – A joint-stock company is generally prohibited from acquiring its own stock, but this does not apply to employee shares (§ 65, para. 1, no. 4, of the Law on Joint-Stock Companies, hereinafter 'JSCL'). A resolution of the general meeting is required to introduce employee shares which remains in effect for 18 months. Transfer of shares to employees in connection with a capital increase, excluding pre-emptive rights of existing shareholders, is possible if the resolution of the general meeting on the capital increase makes this exclusion (§§ 65, para. 2a, 153, para. 5, JSCL). No period for the transfer of shares to employees is specified in the JSCL, but this transfer must take place immediately after issue to comply with company law. Current and retired employees of the employer company and of affiliated companies may participate in an employee share ownership plan (§ 15 JSCL). The definition of affiliated companies was extended in 2005: companies affiliated within the economic sector under the company law and also companies which are members of an association in liability (according to § 30, para. 2a, of the Federal Law on Competition) are also deemed to be affiliated. A blocking period for the transfer of employee shares is not prescribed, but shares are usually held for at least five years for tax purposes. Pursuant to § 3, para. 1, no. 15(b) ITL, a tax allowance of up to 1,453.46 EUR applies to the benefit from the transfer of discounted shares if the shares are held for at least five years, the plan is broad based, and shares are held by the employees but deposited with a domestic credit institution or a fiduciary which administrates the shares and exercises voting rights according to the employee's instructions. This tax allowance applies only to current employees of a domestic or foreign employing company or an affiliated company. The employers' associations, trade unions and the legal literature all object that the tax allowance is too low and advocate an increase of up to 5,000 EUR. Taxation of dividends on employee shares depends on the economic ownership. If the employee has the economic ownership of shares, the capital yields tax or, upon application of the employee, half of the personal income tax, is imposed (dividends on shares of foreign companies are always taxed at half of the personal income tax) (§ 37, para. 4 ITL). If the employee is not the owner (e.g., if the employing company may buy the shares back at will or if the shares must be returned at termination of the employment contract), full personal income tax and social security contributions are imposed.

Leveraged Share Ownership Plans – By the Law on Capital Market Offensive of 5 January 2001, the ITL was amended also in relation to the taxation of private foundations. In view of prospective privatization of large state companies (e.g., Voestalpine AG, Vienna Airport AG, AMAG, Salinen AG), a model for 'strategic ownership' of employees had to be developed. An already existing business form, the private foundation, was chosen to serve as the vehicle of the leveraged employee share ownership plans. The new form 'employee participation foundation' (*Belegschaftsbeteiligungsstiftung*) (defined in § 4, para. 11, no. 1(c), ITL), is used as an intermediary company and enjoys tax allowances. It holds and purchases the shares, exercises vot-

208 Kronberger/Leitsmuller/Rauner (2007): 53.

ing rights, and transfers returns to the employees. In contrast to direct employee share ownership plans, the beneficiaries of leveraged plans enjoying tax concessions can also be retired employees and family members (spouses, children) of employees. A foundation can only be used for shares of domestic companies; the definition of affiliated companies in connection with the foundation was not extended in 2005. The value of its own shares or money for purchasing shares transferred to the foundation as well as the costs of establishing and operating the foundation can be deducted from the tax base of the corporate income tax by the employer company. The foundation distributes the amount of contribution by the employer company over nine financial years, and 1453.46 EUR per employee per annum is tax-free (§ 13, para. 1, last sentence, CTL). Dividends on shares held by the foundation are also tax exempt (§ 10, para. 1, CTL). However, the capital gains tax is imposed on contributions used for administration. The employee pays a capital gains tax on returns transferred by the foundation of up to 1453.46 EUR and full personal income tax, but no social security contributions on the amount in excess thereof. In literature it is objected that the economic activities of the foundation are restricted by law so that it cannot create reserves and make investments. In addition, this form cannot be utilised by small and middle-sized companies due to administrative complexity and high costs.

Stock Option Plans – Stock option plans are generally limited to management. Executive officers and members of the management bodies of joint-stock companies are allowed to acquire shares through stock options if the shares constitute not more than 20% of equity capital (§ 159, para. 5, Law on Joint-Stock Companies). However, a small number of broad-based stock option plans are also found. Taxation of stock options for employees depends on economic ownership. At the time economic ownership is transferred, the shares become taxable. The criteria for economic ownership are the relationship and tradability of options. According to § 3, para. 1, no. 15 (c) ITL, 10% in one year and 50% of the difference between the value of the underlying share at exercise of the option and the value of the underlying share at grant of the option are tax exempt if certain pre-conditions are met: the options must be non-tradable, the plan must be broad-based, and the value of the underlying shares at grant must not exceed 36,400 EUR. If options are deposited with a domestic credit institution or with a fiduciary, taxation of the remaining amount can be deferred until the acquired share is sold or the employment contract terminated, up to the 7th year following the option grant. The employer company can deduct the cost of shares.

b) Profit-Sharing

Although there are no tax incentives, profit-sharing schemes are relatively widespread, especially in small corporations. Most are cash-based and take into consideration such factors as turnover, EBIT, cash flow, etc., alone or in combination, and not necessarily balance sheet profit.[209] A profit-sharing plan may be introduced through a collective agreement, an in-house agreement, or an employment contract. However, an in-house agreement can regulate the preconditions, factors, calculation methods and form of payment (§ 97, para. 1, line 16, of the Law on Employment Contracts, hereinafter 'LEC') only if the factor to which the plan refers also considers the expenditure of the enterprise.[210] A plan not regulated by an in-house agreement is usually based on individual employment contracts whose content is not restricted in

209 KronberGer/Leitsmuller/Rauner (2007): 51.

210 This means that plans relating to turnover as a factor cannot be regulated by an in-house agreement.

this connection. A participating employee is entitled to examine the basis of his share calculation in the books (§ 14 of the Law on Employees). If the plan originates in a collective agreement, the workers' council is also entitled to examine the calculation basis, but not documents on individual wage payments (§ 89 of the LEC).

c) Participation in Decision-Making

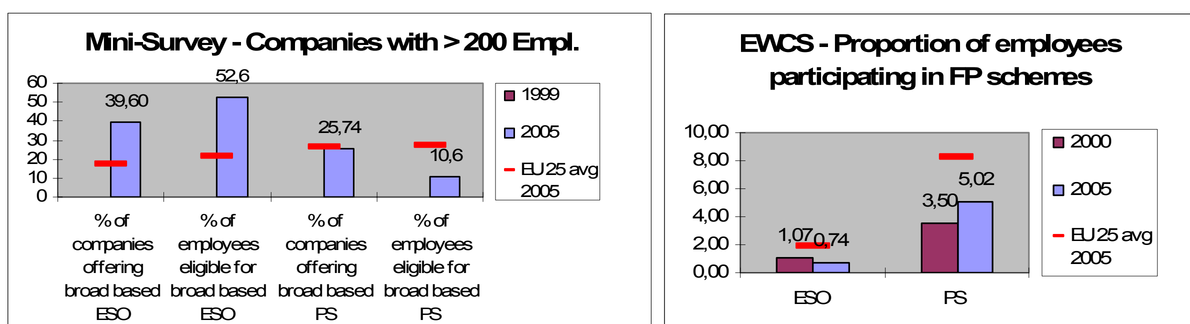
Under labour law, co-determination and participation rights of employees through their representatives are traditionally well developed. Employees send members to the supervisory board (§ 110, para. 1, 5, LEC) and are represented by the workers' council. There is no direct connection between participation in decision-making and financial participation of employees; in particular, financial participation plans cannot extend existing rights in connection with participation in decision-making. Certain aspects of financial participation plans can be regulated by a collective agreement and/or an in-house agreement; in this case, employees' representatives participate in negotiations and decisions. The following rights of the workers' council can be connected to financial participation: right to information (§§ 91, 92, LEC), right to consultation in the case of operational changes (§ 109, LEC), and right to demand elimination of employer's faults (§ 90, para. 1, LEC). Only 17% of enterprises operating financial participation plans indicated problems in connection with decision-making.[211] In general, problems arise only in small enterprises which do not have a workers' council.

211 Kronberger/Leitsmüller/Rauner (2007): 67.

XXI. Poland

The most significant form of employee financial participation in Poland today is employee ownership. Poland's privatisation programme was characterised by significant incentives for employee participation, especially in firms privatised by leasing and transformed into so-called employee companies (*spółki pracownicze*). Ownership structures in these companies have, on the whole, been relatively stable, with non-managerial employees retaining, on average, a significant portion of enterprise shares. Research conducted in the late 1990s on a sample of 110 employee-leased companies privatised between 1990 and 1996 showed that on average, the share of non-managerial employees in ownership decreased from 58.7% immediately after privatisation to 31.5% in 1999. Approximately 32% of leasing-privatised firms were still majority-owned by non-managerial employees by mid-1999. Over time, more and more shares were also found in the hands of outsiders (probably due largely to retention of shares by people whose employment relationship with the firm ceased for whatever reason), and the presence of strategic outside investors (including foreign investors) had begun to be felt in a minority of firms by the end of the last decade (see PEPPER III, p. 237: Table 3). Less significant forms of minority employee share ownership emerged during privatisation using methods other than leasing. Insiders possessed only 12.7% of shares at the beginning of 1998, and this fell to 11.4% two years later.

Although, presently all forms of financial participation are also available for use in employee compensation schemes outside of privatisation, there are no tax incentives to do so, and no interest in the development of such schemes can be observed either in political or trade union circles.



1. General Attitude

No interest in the further development of PEPPER schemes can be observed either in political or trade union circles. The positions of trade unions like Solidarność with regard to PEPPER schemes and other forms of workers' participation were – and still are – not consis-

tent and often ambiguous. On the one hand they were profiting when the loss of power of the organs of self-administration of the state enterprises undergoing privatisation was compensated. On the other hand there was political pressure from the trade unions to avoid bankruptcy and liquidation of the companies and, consequently, often also resistance against radical restructuring. Institutions created to support employee-owned firms in Poland include the Union for Employee Ownership (*Unia Własności Pracowniczej*), the All-Poland Chamber of Employee-Owned Companies (*Ogólnopolska Izba Gospodarcza Spółek Pracowniczych*) in Poznań, and the Gdańsk Employee Ownership Bank (*Bank Własności Pracowniczej SA w Gdańsku*); however, their significance to the process of employee-led privatisation in Poland was very limited. Thus, as of early 1996, the Union for Employee Ownership, founded in the autumn of 1990, had only 76 member firms, some of which were still state-owned.

It is clear that since the mid-1990s the principal openly declared aim of the privatisation policy was the maximisation of budget revenues, and that therefore all but the smallest state enterprises were to be privatised by commercial methods (in spite of the fact that it was actually the larger employee-owned companies which tended to attain the best financial results). In addition, privatisation policy makers have sought to encourage enterprises using this method of privatisation to find outside investors, and for this purpose, a clause was included in the 1996 Privatisation Law which would make pure management-employee buyouts difficult or even impossible by requiring at least 20% of the shares of a leasing firm to be purchased by persons not employed in the firm. No incentives have been provided by policy makers for the extension of employee financial participation other than privatisation schemes.

2. Legal and Fiscal Framework

In Poland the legal framework, in principle, provides various forms of PEPPER schemes, embracing on the one hand share ownership and profit-sharing and on the other cooperatives and the private sector as well as enterprises undergoing privatisation. However, no incentives have been provided by policy makers for the extension of PEPPER schemes. All forms of participation are available for use in employee compensation schemes, although there are no tax incentives to do so.

a) Share Ownership

'Employee Companies' (1990, 1996) – The so called employee companies emerged though Leverage-Lease-Buy-Out (LLBO) privatisation (Woodward, 1998), which is one form of so-called liquidation privatisation, thus it is applied not to incorporated companies, but to state enterprises. A newly established private company concludes an agreement with the State Treasury to lease the assets of the state enterprise for a maximum period of 15 years.[212] According to Art. 39 PrivL, since the beginning of 1997 liquidation privatisation (leasing, fast-

[212] Until 2002 Art. 52 para. 1 PrivL foresaw a maximum of 10 years; the legal regulations for LLBOs are to be found in Art. 39 para. 1 No. 3 and 50 to 54 PrivL; it is reserved exclusively for Polish nationals and as an exception also legal persons (Art. 51, para. 1 No. 2 PrivL).

track-sale and contribution-in-kind) requires:[213] relatively good financial and market conditions; no requirement for substantial investment to modernise, replace, develop equipment etc; a yearly turnover of max. 6 millionEUR; not more than 2 million EUR equity consisting of two enterprise funds; having management and employees willing to undertake the financial risk involved in embarking upon a common investment (including third parties). The interest payment (referred to in Polish regulations as the 'additional payment' [*oplata dodatkowa*]) was set at 30% (75% of 40%) if the central bank refinance rate were to exceed 40%[214] and later in 1993 this was lowered to 50% of the refinance rate.[215] Moreover, a leased company can apply to its founding organ for a reduction in the interest payments owed by the company as a result of postponements during the first two years of the leasing period if its investment expenditures out of profits amount to at least 50% of its net profit. Finally, the corporate income tax law allowed the firms to include the interest portion of the lease payments as costs in their accounts, thus reducing their tax liability.[216] The new privatisation law in 1996 additionally leveraged the financial lease contracts in order to enhance the creditworthiness of employee-leased firms when applying for bank loans. Art. 52 PrivL gives the possibility that full ownership may be acquired before the end of the contract if one third of the total amount of the leasing rates have been paid, provided approval of the balance sheet for the second business year of the company. A payment of more than half of the total leasing rates cuts down the blocking period by half. Because of the difficult conditions on the Polish credit-market, this regulation has in practice become very important.[217]

Employee shares in Capital Privatisation (1990, 1997) – The new PrivL came into force in early 1997; according to Art. 36 employees can acquire 15% of shares for free, with the restriction that these shares are exempt from free trade[218] for two years, and for three years in the case of employees elected to the management board (Art. 38 para. 3 PrivL). They are required to state their claim within 6 months before the registration of the company, otherwise the right expires, and can execute it for 6 months after the sale of the first share. Shares are allocated in groups made up according to the time spent in the enterprise. The total value of allocated shares according to these claims may not exceed the sum of the average salary in the public sector in 18 months multiplied by the number of employees acquiring shares. This rule applies not only to commercialised companies undergoing capital privatisation and those included in the Mass Privatisation Programme but was extended to 15% employee participation in a 'direct privatisation' transaction embracing sales of an enterprise as a going concern as well as in kind contributions of an enterprise (Art. 48 para. 3, Art. 49 para. 4 PrivL). The only remaining exception is commercialisation via debt-to-equity-swaps.

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213 These criteria were altered with the new Privatisation Law in 1996 which set up additional financial hurdles, giving room to the suspicion that the government intended to reduce liquidation privatisation.

214 Ordinance of the Minister of Finance of May 7 1991, Monitor Polski 1991 No. 18, Pos. 123.

215 Ordinance of the Minister of Finance of May 13 1993, Monitor Polski 1993 No. 26, Pos. 274.

216 Law on Corporate Income Tax of February 15 1992, Art. 15.

217 Furthermore Art. 54 PrivL foresees the possibility to regulate the specific conditions of such leverage by Ordinance of the Council of Ministers including the possibility to reduce the threshold of paying 20% of the net value of the object of the lease stated in Art. 51 para. 1 No. 3 PrivL to 15%. In this context Art. 64 PrivL granted existing Employees Companies the right to renegotiate their contracts within 3 months of the Ordinance coming into power.

218 This does not apply to shares allocated in an Employees Pension Fund set up under the Law on Employees Pension Programmes of 20 April 2004, Dz. U. No. 116, Pos. 1207.

Private Companies (2003) – In deviation from the general prohibition to acquire own stock, Art. 362 para. 1 of the Commercial Companies Code (CCC) permits a company to acquire its own shares in order to offer them to current employees or retired employees of the company or employees of an affiliated company provided there is a minimum of three years of that business relationship.[219] In this case Art. 393 No 6 CCC requires a decision by the general shareholders assembly and Art. 363 para. 3 CCC states that the shares shall be transferred to the employees within twelve months of acquisition. According to Art. 362 para. 2 CCC the possibility of the acquisition of the company's own shares in this case is limited to the extent that the total nominal value of the shares may not exceed the value of 10% of the enterprises' equity capital and that the purchase price together with the transaction cost may not be higher than the reserve made from the company's own profits (Art. 348 para. 1 CCC).[220] Additionally under the current legislation joint stock companies may issue new shares to be transferred to employees in the context of so-called conditional capital increases, with Art. 448 para. 2 No. 2 CCC expressedly referring to the possibility of transferring shares to employees in the case where they have previously acquired claims from profit-sharing. According to Art. 448 para. 1 CCC a prerequisite to this form of capital increase is that the relevant employees are identified in the decision of the general shareholders assembly about the capital increase.[221] The matching regulation is Art. 442 para. 1 CCC which stipulates the possibility of capital increases financed by the company's own capital, again referring to Art. 348 para. 1 CCC concerning reserves made from the company's own profits.

In order to facilitate the acquisition of shares by employees, by Art. 345 para. 2 the CCC the legislator has deviated from the general prohibition to leverage the acquisition of its own stock. Conditional upon the creation of a reserve (Art. 348 para. 1 CCC), the company may advance funds, make loans, and provide security, with a view to acquisition by employees of the company or employees of an affiliated company. Furthermore, in principle, employees may received stock options, including options to acquire shares on a privileged basis (at below-par prices or even free of charge) although no specific regulations exist (Ciupa, 2001, p. 203).

Pre-emptive Right of Purchase of an Enterprise under Insolvency Law (2003) – With the Insolvency and Reorganisation Law (IRL) a completely new version of Polish insolvency law[222] became effective on 1 October 2003. Embracing regulations on both bankruptcy and arrangement proceedings, interestingly, the IRL contains a hidden leverage for setting up employee companies in the context of liquidation procedures. If the sale of the debtor's business as one or several functioning units is not possible, then each asset should be publicly auctioned by the administrator under supervision of the judge-commissioner. If assets are not sold at a public auction or the judge-commissioner does not accept the offer, the judge-commissioner can order a second auction or determine the minimum price and conditions of sale and allow the administrator to find a purchaser or allow the administrator to sell assets free of procedural restrictions. The sale of real estate and ships free of procedural restrictions

[219] This regulation had its origin in the harmonisation with the *acquis communautaire*, i.e. the implementation of the second Council Directive of 1976 (77/91/EEC; OJ L 26, 31.1.1977, p. 1).

[220] Art. 347 para. 3 and 348 para. 1 CCC provide the possibility to allocate enterprise profits to special funds while not paying them out as dividends to shareholders, thus allow share based profit-sharing.

[221] The issuing of shares to be acquired by employees in this case shall not be considered as a public offering but as a 'private subscription' (Art. 431 para. 2 No. 1 CCC).

[222] Dz. U. 2003 No. 60, Pos. 535. For a detailed analysis of the new law see Zedler (2003).

must be approved by the creditors' committee. In this case a company consisting of at least half of the debtor's enterprise's employees and being a commercial company with the participation of the Treasury has a pre-emptive right of purchase of the enterprise or functioning enterprise units (Art. 324 IRL). The sale of movable property free of procedural restrictions must be approved by the judge-commissioner (Art. 326 et seq. IRL).[223]

b) Profit-Sharing

The possibility of implementing profit-sharing, i.e. a form of remuneration, in addition to pay systems, directly linked to enterprise profits is stipulated in Art. 347 para. 3 and 348 para. 1 CCC for joint stock companies (*tantiema)*.[224] Furthermore, as already mentioned, share-based profit-sharing is regulated in the context of conditional capital increases according to Art. 448 CCC, stressing the possibility of transferring shares to employees especially for the situation where they have previously acquired claims from profit-sharing. The general type of scheme linked to enterprise results is referred to in Polish as a '*bonus*' but has no legal foundations. Other practices presently sanctioned by law are compensation forms linked to an employee's individual results (gain-sharing) which are not usually linked to enterprise results and thus do not constitute PEPPER schemes.[225]

c) Participation in Decision-Making

Codetermination on the strategic level exists in the form of an obligatory representation of employees on the supervisory boards of commercialised companies of, initially, two fifths of the members and - from the moment the state ceases to hold 100% of the shares - one third (Art. 14 Law on Commercialisation and Privatisation, hereinafter referred to as PrivL[226]). Furthermore Art. 11, 12, 60 PrivL provides a detailed procedure for the election and qualification of representatives while Art. 15 PrivL grants protection of their labour contract for the time of their term and the following year (Boc, Guziński and Kocowski, 1997). New in the context of 'social compensation' is the participation of an employee representative on the executive boards of privatised enterprises employing more than 500 employees (Art. 16 PrivL). Outside privatisation the development of participation in decision-making has been very limited, even in companies where employees hold significant share packages. Poland remains dominated by an elitist and managerialist corporate culture which minimises the opportunities for participation. Almost all progress which has been made in the area of decision-making participation in Poland can, however, be ascribed to the European Union.

Although it seems that the development of both direct and indirect (representational) employee participation in decision-making processes in employee-owned companies is rather

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223 Ordinance of the Ministry of Justice of 16 April 1998, Dz. U. No. 55, Pos. 360, entered into force on 14 May 1998.

224 See decision of the Supreme Court of 5 May 1992, I PZP 23/92, Bibl. Prac. No- 25, p. 96.

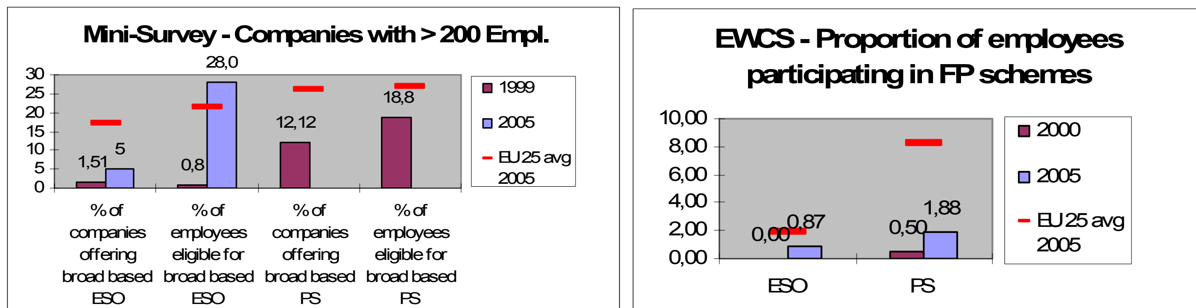
225 Such as other forms of remuneration, e.g., gratifications (gratyfikacja, nagrody, nagrody jubileuszowy), thirteenth salary, commissions (prowizja; used frequently, if not universally, in the case of sales force employees) and various types of bonus schemes. For details see Ciupa (2001); 'Premie I nagrody dla pracowników', Rzeczpospolita of 3 Oct. 2005.

226 Of 30 August 1996, Dz. U. No. 118, Pos. 561, republished in Dz. U. 2002 No. 171, Pos. 1397, No. 240, Pos. 2055, with subsequent amendments.

low, there are signs that some potential for the development of genuine employee involvement could be resting latent in these firms. In many Polish employee-owned companies, for example, no dividends have been paid out - even after two to three years of functioning as a private firm - due to decisions to plough back profits in the form of investment or not to pay dividends until the lease is paid off. The fact that employee shareholders can be convinced to vote in favour of such 'austerity' plans provides some evidence that the entrepreneurial attitudes characteristic of genuine ownership and participation may be present amongst the work forces of certain employee-owned companies.

XXII. Portugal

No tradition of employee financial participation has emerged in Portugal for reasons both historical and economic. The Portuguese economy is still based on small companies under continuous family ownership; these owners oppose granting participation rights to employees. Moreover, flexibility in employment and labour costs, as well as relatively low unemployment, have been achieved without financial participation. Employee share ownership and stock option plans were promoted in connection with privatization in the 1990s after the French example. However, this did not lead to any substantial increase in employee share ownership because a significant number of employees, prior to the share transfer, had signed contracts waiving their rights and agreeing to sell their shares immediately after the end of the blocking period. Currently, only a few plans are operated by large multinational companies primarily in the financial and insurance sector; the majority of these are cash-based profit-sharing plans; however, single cases of employee share ownership and stock option plans do occur (e.g., Siemens, EDP, Portugal Telecom, Cimpor).



1. General Attitude

The government is indifferent to employee financial participation. Nor are employer associations interested since wage flexibility has been achieved by other means. Initially, the trade unions were suspicious of financial participation, but they have changed their attitude since 1988 and now try to promote it. However, this is true only of independent trade unions, e.g., SIMA (Sindicato das Indústrias Metalúrgicas e Afins), which has proposed to include financial participation in collective agreements. The largest trade unions, UGT (Uniao Geral de Trabalhadores) and CGTP (Confederacão Geral de Trabalhadores), generally do not support such initiatives.

2. Legal and Fiscal Framework

A small number of financial participation plans are operated primarily by large companies in the financial and insurance sector; many of these plans are limited to executives. Cash-based profit-sharing schemes predominate.

a) Share Ownership

The number of share ownership and stock option plans is very small, executive plans included. The existing plans are purported to be modeled on similar plans in the U.K. and Ireland.

Share Ownership Plans – Share Ownership Plans were used on a larger scale in the privatization process between 1989 and 1998. According to Art. 10 and 12 of the Framework Privatisation Law of 1990, a certain percentage of the capital reserved for acquisition or subscription had to be reserved for current employees and, if employed by the company for more than three years and not dismissed as a result of a disciplinary proceeding, for former employees as well; the blocking period was for two years. As to privatization of individual companies, special law containing specific conditions (e.g., the relation of pre-emption rights of employees to pre-emption rights of other individuals), in compliance with the Framework Privatisation Law, were enacted. The employees had to pay a certain price determined by the Minister of Finance. On shares held for at least two years, gains in share value were not taxed. In addition, the employees enjoyed tax incentives if they purchased shares offered for public sale by the state; they could deduct up to 30% of total taxable income, up to a fixed amount.

Stock Option Plans – Stock Option Plans are often limited to executives. Since the total number of stock option plans, including executive plans, is very small, the number of broad based stock option plans will probably be fewer than ten. There are no special rules on taxation of stock options in financial participation plans for employees; employee stock options, like other types of stock options, are subject to the personal income tax at exercise, and no social security contributions need be paid.

b) Profit-Sharing

Both cash-based and share-based profit-sharing schemes exist, with the percentage of cash-based profit-sharing schemes being much higher. Profits allocated to employees are usually transferred immediately, but under certain conditions can be blocked for one to two years. Conditions are determined at the company level. Since 1969, the profit share of the employee has not been treated as remuneration, exempting employees from personal income taxes and social security contributions on this amount (Art. 261 of the Labour Code). However, the profit share must be based on an individual agreement covering a specific period, otherwise it will be fully taxable. The employer company can deduct distributed profit transferred to the employees.

c) Participation in Decision-Making

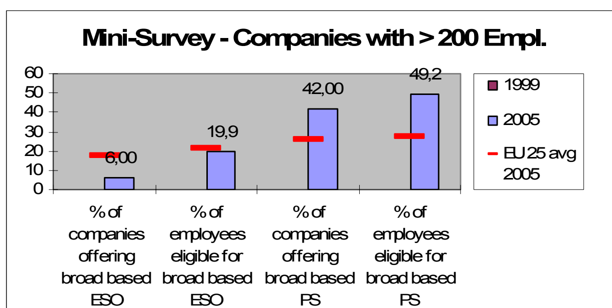
No direct connection exists between participation in decision-making and employee financial participation; in particular, financial participation plans may not extend the existing rights in connection with participation in decision-making. Negotiations at industry level, between employers associations and the unions are the most important element in Portugal's collective bargaining arrangements. Company level agreements cover much fewer employers. Portugal has traditionally had a high level of collective bargaining coverage – partially through the extension of agreements by the government. However, this high level is under threat as legal changes now make it easier for agreements to lapse. Financial participation is not a part of collective agreements, although the trade unions have proposed including such schemes on several occasions.

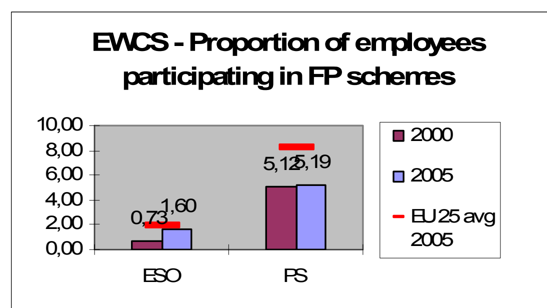
The Portuguese constitution refers to the rights of employees to elect representatives on the governing bodies of state-owned companies and other public bodies – rights that were never implemented. In addition, in 1999, legislation removed the right of employees to elect a member of the management board. There is no employee board level representation in private companies. Although in theory there are two channels of workplace representation of employees in Portugal, through the workplace union representatives and through an elected works council, in practice works councils are rare. They only exist in large companies where unions are strong. The rights of both are limited to information and consultation, with no opportunity to block management decisions. Although consultations on financial participation plans are not compulsory, they sometimes take place, especially in the case of profit-sharing plans, to improve the design.

XXIII. Romania

The idea of employee financial participation in Romania is relatively new, apart from some pseudo schemes attempted under the communist regime. PEPPER schemes emerged during the early privatisation process when mass privatisation and insider privatisation via an ESOP-like scheme were the major privatisation methods. The prevailing form is employee share ownership, mainly by the ESOP method. It is estimated that, by the end of 1998, over a third of all industrial firms in the State Ownership Fund had undergone ESOP privatisation (with average employee ownership of 65% and a median of 71% (Earle and Telegdy, 2002; World Bank, 2004). In addition, ESOP participants were the largest owner group in one-fourth of Romanian privatised firms, which makes this method the most important tool of state ownership divestiture in the country (see Earle and Telegdy, 2002; also PEPPER III, pp. 251 f.: Tables 1-3). Nevertheless, after more than ten years of transition, only 40% of the total number of large enterprises and around two-thirds of its medium-size enterprises are privatised. The number of state-owned or state-controlled firms in Romania is larger than the total number in the remainder of Central and Eastern European countries combined.[227]

Since 2001 cash-based profit-sharing, referred to as 'The Fund of Employee Profit Participation', are compulsory in companies and in autonomous bodies with the state as single or majority owner. As an average proportion of labour costs, at a national level, net profit directly paid to employees in 2003 was about 2.2%, while 70.3% was distributed from salary funds, including premiums and benefits.[228] Although presently, the number of cases of profit-sharing is still limited, their number is increasing gradually.





[227] According to the most recent available data (World Bank, 2004), at the end of 2003 there were about 1,300 state-owned enterprises and another 600 enterprises de facto under state control.

[228] Although compulsory, interview evidence reported, that in practice it is seldom applied and, if applied, concerns a rather small number of employees.

1. General Attitude

Employees are represented by a number of large trade union confederations, such as 'The Confederation of the Democratic Trade Unions from Romania', The National Trade Union Confederation 'Meridian', The National Trade Union Confederation 'Cartel ALFA', The National Trade Union Block, and The National Confederation of the Free Trade Unions from Romania 'Fratia'. The employers' associations are even more dispersed than the trade union movement, with eleven employers' associations registered. In many cases of privatisation of utilities and the oil and gas industry, employees have purchased shares through trade unions, since the unions are very strong and have substantial influence in these sectors and they have the right to appoint at least one member to the board of administration in these industries. In some cases (e.g. the sale of 8% of the social capital of the PETROM Company, representing a total value of about 200 million EUR) the trade unions tried to achieve an amendment of the relevant law, so that employees' associations controlled by the trade unions rather than individual employees become the purchasers of the offered shares. Such cases illustrate that the interests of trade unions and of their legal representatives are not necessarily in line with the interests of individual employees and that sometimes trade unions also tend to achieve their goals at the expense of employees' rights. Furthermore, the consultations and negotiations with trade unions are important for employers because they still hold a very strong position within the tripartite council (National Social and Economic Council), which also includes the government and the employers' associations. Employers' associations have not yet addressed the issue of financial participation of employees.

At present, the problem of the financial participation of employees is not given priority by the government or political parties. The last significant commitment by policy makers was in 2001 the introduction of the mentioned compulsory cash-based profit-sharing scheme, 'The Fund of Employee Profit Participation'. The only aspect of financial participation of employees currently addressed by the government is the sale of minority shares to employees in public enterprises where privatisation is underway in such sectors as the utilities (or the so-called *Régies autonomes*), oil and gas and banking, but also such state companies as the National Lottery and the National Printing House. Due to the recent change of orientation in economic privatisation policy towards sale to strategic outside investors, including foreign investors, government support is expected to be rather declining. Since, in some of these privatisation cases, trade unionists and representatives of political parties are suspected of insider deals and corruptive practices at the expense of employees, the credibility of governmental support for the financial participation of employees is considered by the general public to be relatively low.

2. Legal and Fiscal Framework

Currently, Romanian law does not contain a systematic legal framework regulating employee financial participation. However, several laws linked with the privatisation process were passed which had an impact upon the extent to which the concept of employee financial participation has been spread, with mass privatisation and an ESOP scheme being the major methods. The only legal regulations on profit-sharing are concerning a compulsory scheme in

(majority) state owned companies to which National Labour Collective Agreements are applicable.

a) Share Ownership

Privatisation (1991, 1995, 1999) – The Romanian Privatisation Law 58/1991 set up a number of 30% of shares to be transferred for free applying different privatisation methods, with voucher privatisation being the main focus. Although Law 58/1991 did not provide incentives for insider privatisation in voucher privatisation, it contained regulations on preferential treatment for employees and management with regard to the sale of shares through the national Privatisation Agency (*Fondul Proprietătii de Stat*). According to Art. 48 of Law 58/1991 on Privatisation, employees (including the management) of the respective enterprise had a pre-emptive right to purchase the offered shares on advantageous conditions. In the case of a fixed price sale the 'insider share price' had to be 10% lower than the public price; in the case of a sale by means of competitive bidding the insider offer had to be accepted by the Privatisation Agency as long as the offered price is not lower than 90% of the highest public bid. This preferential treatment was also extended to the direct sale procedure where the insider offer had to be accepted by the Privatisation Agency in the case of an equal negotiation result with other interested parties.

By means of Law 55/1995 on the Acceleration of the Privatisation Process, the aim of the 30%-quota was re-emphasised, the privatisation agency established a list of suitable enterprises and issued the so called 'nominal value vouchers for privatisation' (*cupoane nominative de privatisare*) to be spread amongst the resident population.[229] For the first time, this new law contained a real incentive for employee financial participation in voucher privatisation. While the general public owning the aforementioned nominal value vouchers for privatisation could trade their vouchers only for shares of companies to be chosen from a list of suitable enterprises issued by the privatisation agency, Art. 5 of Law 55/1995 on the Acceleration of the Privatisation Process offered the opportunity for certain persons to acquire shares of non-listed companies in exchange for their vouchers. This was possible for employees and the management of state companies who were interested in exchanging their vouchers for shares of the company they were employed by.[230] The same privilege was granted to former employees (pensioners or the unemployed) who had their last employment contract with the respective firm.

Employee Stock Ownership Plans (1992, 1994, 1997) – ESOP associations root in Rule 1/1992 on the Standard Procedure for the Privatisation of Small Enterprises by the Sale of Shares which came into force in January 1993. Although focused on the privatisation of so-called 'small enterprises'[231], this regulation defines insider privatisation via an ESOP-like scheme as the standard privatisation procedure. This ESOP-like privatisation had to be im-

[229] Only persons who had not made full use of their property vouchers received according to Law 58/1991 were granted the new vouchers for privatisation. The main difference to the old system was that the new vouchers were not tradable. Furthermore, the new vouchers could only be exchanged for the shares of just one company while the old property vouchers could still be used for the purchase of shares of one or more different companies.

[230] Art. 5 lit. a) and b) of Law 55/1995 on the Acceleration of the Privatisation Process.

[231] The maximum size of these enterprises is determined by the number of persons employed on average within the reporting year which is set at 50 employees; see annex 2 of Government Decision 10/1992 on the Approbation of the Statute of the Privatisation Agency, published in M. Of. 208/1992.

plemented by means of direct negotiations with interested employees and management staff, having priority over the second method which is defined as a more or less public tender procedure. The procedure is aimed at selling either all or at least a majority part of the shares to employees. However, the shares were not acquired directly by participating employees but by an incorporated association of share owners.[232] Law 77/1994 on Associations of Employees and Members of the Management in Companies in the Privatisation Process provided the specific regulations required for widespread use of this ESOP privatisation model. It allowed employees and the management of partly or fully state owned enterprises which were to be (fully or partially) privatised to establish ESOP associations.[233] The number of ESOP associations was limited to one for each enterprise to be privatised, so any competition between associations over the purchase of one specific enterprise was excluded by law. Membership of the ESOP association was voluntary, but it was also a precondition for making use of the advantages and exclusive rights with the result that every employee seriously considering the purchase of shares had to become a member of the respective association. While the voucher privatisation came to an end (no more new vouchers being issued while the tradability of the old vouchers was restricted by several legal deadlines), the legislation on ESOP associations remained in force for the most part. In this context, Emergency Ordinance 88/1997 only defines a rough legal framework for the employee shareholder associations and refers for the details to the general legal provisions governing associations and foundations.

The law states that a minimum of 30% of the total number of employees and management staff have to participate in establishing the ESOP association. ESOP associations can only perform activities listed by law 77/1994; as already mentioned above, the associations were granted specific rights in the privatisation process which offer advantages to insiders. The enterprise has to disclose all relevant commercial and financial information to the founding committee of the association; also the costs for a feasibility study in the preliminary stages of the buy-out have to be borne by the enterprise. The ESOP association buys and administers the shares for its members. The membership is open to employees with unlimited labour contracts with at least half-time employment and to members of the management of the respective enterprise. Furthermore, former employees, both unemployed and pensioners, belong to this privileged group. The main decision-making body of the association is the general meeting in which each member of has one vote. The general meeting decides upon the ESOP associations Articles of Association which must contain strict rules with regard to the distribution of shares purchased by the association. This privatisation procedure, initially for small enterprises, was aimed at selling all or at least a majority part of the shares by means of the ESOP method, thus the result of a successful privatisation under this regulation was also the acquisition of the majority voting rights for the benefit of the participating employees. However, as the shares obtained via instalment options are not acquired directly by employees and management staff but by the interposition of an association with an autonomous legal personality, the voting rights are also exercised by the ESOP association. The extent of participation in decision-making therefore depends upon the decision-making procedure inside the association and the way the members' decisions are transferred to the shareholders' meeting.

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232 This association is called 'Programul acţiunlor salariaţilor' [Employee's Share Programme]. When the law came into force there was no special legislation governing this specific kind of association, therefore the old Law 21/1924 on Legal Entities was applied special regulations came into force.

233 So-called management and employee associations; the Romanian term is 'asociaţiă salariatilor şi membrilor conducerii'.

The ESOP association may purchase the shares as a representative of individual members. In this case the shares are distributed directly to members and administered by the members themselves once they fully pay up for the shares with cash or offer privatisation vouchers in exchange for them. Yet the main advantage of the ESOP association scheme in comparison to the individual purchase of shares is the use of the credit facilities offered either by the Privatisation Agency itself or by external banks. In this case the shares are not bought in representation of individual members but in the name of the entire association; the shares are not vested directly to individual members, but kept by the association until they are not entirely paid for, serving as credit securities during this period. The ESOP associations' members have pre-emptive rights concerning the unvested shares taking in consideration criteria like employment duration, position in the firm and salary. In case the right of pre-emption is not exercised by members, the respective shares may be distributed to new employees of the enterprise. As soon as all shares are distributed to the members, the association has to be dissolved. Law 77/1994 additionally offers preferential instalment options[234] for shares purchased by ESOP associations. This starts with a low advance payment and is complemented by a minimum repayment period of five years and a maximum interest rate of 10% per year. Against the background of a high inflation rate during the 1990s, the interest rate limit especially turned out to be remarkably advantageous.

Private Companies – The legal framework with regard to Romanian company law is defined by law 31/1990[235] on companies, republished in November 2004 and recently modified (October 2005).[236] Romania has only partially made use of the tools/exceptions offered by the Second Council Directive 77/91/EEC of 13 December 1976 to promote employee financial participation by means of corporate legislation. Regarding the permission to acquire the companies' own shares for its employees (Art. 19 III Council Directive 77/91/EEC) Art. 104 lit. b) the Law on Companies offers an exception with respect to the acquisition of shares for the workforce of the company; this regulation is in contrast to the restrictive general regulation for this kind of transfer in Art. 103 Law on Companies, which requires an extraordinary shareholder's meeting in the case where the company intends to acquire its own shares. The second exception the Romanian legislator made use of is Art. 105 III Law on Companies based on Art. 23 Council Directive 77/91/EEC (the encouragement of share acquisitions by employees by permission to advance funds, make loans or provide security, with a view to acquisitions). While Art. 105 Law on Companies specifically prohibits any advancement of funds, the issuing of loan schemes or the providing of securities with the purpose of encouraging the acquisition of shares by any third party, para. III of this article provides an exception to this rule when the shares are purchased by employees of the company. Additionally, there are some provisions protecting the rights of minority shareholders.[237]

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[234] Regarding Art. 52 of Law 77/1994 the Privatisation Agency is bound by these conditions. Furthermore, the Agency has to accept a certain amount of privatisation vouchers (property vouchers) in exchange for the shares to be transferred.

[235] M. Of. No. 33/1990.

[236] The most recent amendment/modification incorporated here was by Law 302/2005, published in M. Of. No. 953/2005.

[237] I.e., preference shares without voting rights are limited to 25% of the total share capital; the number of votes attached to one share may be limited only for the holders of more than one share; a shareholders' meeting has to be called on the request of shareholders representing a minimum of 10% of the total share capital; various information rights with regard to accounting issues; and the right to apply to court for a detailed fi-

b) Profit-Sharing

In 2001 the government passed Ordinance 64/2001 on the Repartition of Profits Obtained by State and Municipal Companies with the State as Single or Majority Owner.[238] The regulations cover state or municipal enterprises which are either constituted in the legal forms provided for by Law 31/1990 on Trading Companies, with the state as single or majority owner, or in a specific legal structure which is still widely in use in relation to public utilities.[239] The ordinance regulates the details of profit distribution, such as reserve funds, payouts to owners and the coverage of losses from previous years. In Art. 1 lit. e), the ordinance also contains a provision which sets the maximum payout rate for employee profit-sharing at 10% of the overall profit of the enterprise (10% in the case of companies, or 5% in the case of autonomous bodies, depending upon employees' performance and contribution to the financial results).[240] There is currently no provision regarding a minimum rate and it should also be noted that the number of state firms actually making a profit is still low. Nevertheless, Ordinance 64/2001 is one of the few laws expressly dealing with the issue of employee profit-sharing. Against the background of the pronounced encouragement of ESOP privatisation schemes, profit-sharing in companies privatised this way should be widespread as a side effect of share ownership. As the ESOP privatisation policy particularly favoured the sale of smaller enterprises to employees and management, profit-sharing schemes should be over-represented in the sector of small and medium sized firms.

c) Participation in Decision-Making

While the old legislation before 1990 emphasised employee participation in decision-making in an almost redundant way[241], the privatisation laws passed since 1990 contain no special regulations concerning this issue. Also the notion of employees' co-determination, i.e. like in German law, was not introduced. The Company Law does not provide any legal means for the privileged participation of employees in decision-making. However, it contains various provisions protecting the interests of minority shareholders. The new Labour Code of 2003[242] as well as the nation-wide collective agreement with trade unions of 2005 contain regulations for some compulsory consultation procedures to be carried out if changes to labour conditions are planned by the management.

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nancial audit by shareholders representing a minimum of 10% of the total share capital. Currently, there is no squeeze-out or sell-out regulation in Romanian company law.

238 Ordinance 64/2001 on the Repartition of Profits Obtained by State and Municipal Companies with the State as Single or Majority Owner, published in M. Of. No. 536/2001; the regulation abrogated earlier regulations, e.g., Ordinance 23/1996 on the same issue.

239 This form is called 'regiă autonoma' and is governed by specific regulations.

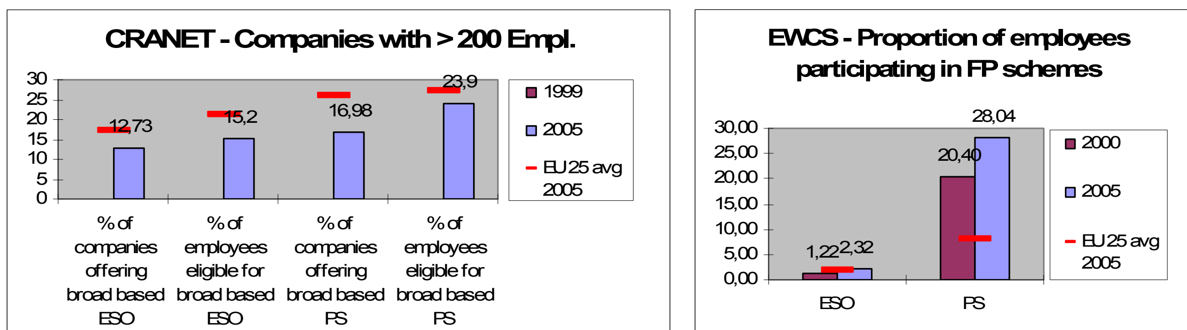
240 Supplemented by Governmental Disposition No. 298/25 February 2002 for the approval of the explanatory note regarding the establishing of the amounts making the object of the profit repartition conforming to the Governmental Ordinance No. 64/2001 and their reflection in bookkeeping – published in the M. Of. No. 157/2002.

241 The old Labour Code from 1972 alone mentions this concept in more than 20 articles, admittedly with virtually no implications in practice.

242 Law 541/2003 on the Labour Code, M. Of. No. 913/2003.

XXIV. Slovakia

In spite of political declarations during the mid 1990s, in reality, PEPPER schemes have not played any notable role and financial participation has remained marginal. In general, the environment for employee participation was more favourable than in the Czech Republic as the major difference driving this claim occurred in the privatisation design in Slovakia that was revised after the split of Czechoslovakia in December 1992. Starting with a focused policy favouring the voucher scheme, the new government changed to traditional privatisation methods - in particular trade sales but also insider privatisation - in its second privatisation wave. The populist government in the mid-1990s used employee shares as an appendix together with managerial types of privatisation to assure the smooth property transfer to closely-related parties. However, the subsequent reformist government abolished this system and from 1998 the *Dzurinda* government focused on the revenue oriented privatisation of the remaining state enterprises which included telecommunications, gas utilities and large banks. The private ownership structure which emerged is totally dominated by external types of ownership or managerial ownership.



1. General Attitude

Current and past general attitudes towards employee participation can be characterised as 'unsuitable for Slovak economics'. External ownership is the most preferable form of ownership and no incentives to encourage different types of ownership or employee participation are provided. A possible explanation might be a pervasive notion of the positive effects of (mainly foreign) external owners on the performance and profitability of firms. Surveying past and recent literature on enterprise sector development and corporate governance in Slovakia reveals that there is no professional or public interest in employee participation. Moreover, insider shares were not even mentioned; at best managerial ownership and buy-outs are dealt with. In general, attitudes toward employee participation are similar to the situation in the Czech Republic. The trade unions as a whole also seem uninterested: the only document on

the website of the Confederation of Trade Unions of the Slovak Republic that mentions employee shares is about social dialogue, not about shares as a form of corporate governance; the occurrence is only casual, and does not seem to bear any weight at all.

Today, political parties seem to ignore this issue with the exception of the Communist party which explicitly mentions employee shares; however the programme is from 1994 and has not been modified since then. Based upon these, partly anecdotal, pieces of evidence we claim that the probability that employee shares will become a focal issue of government economic policy in the near future is low, as it is of interest only to the far left of the political spectrum and not of interest to the trade unions, government or general public. A possible reason is high unemployment.

2. Legal and Fiscal Framework

At present under Slovak law - similar to the Czech Republic - specific employee financial participation programmes or a particular law or regulation created to regulate specific issues concerning PEPPER schemes do not exist. The only form of employee participation in the ownership structures of corporations covered by general laws have been – to a limited extent – regulations on the acquisition of shares by employees and profit-sharing in joint-stock companies.

a) Share Ownership

Privatisation (1995, abolished 1996) – The Slovak Republic National Council Act No. 192/1995 was the basic legal act, accelerating primarily direct sales, simultaneously subsidising domestic entrepreneurs, and enabling them to participate in the privatisation process under favourable economic conditions. Direct sales were to be used for enforcing employee ownership, obliging the transferee either to issue employee shares that accounted for 10% of the companies' equity capital or to enable employees to acquire at least a one third[243] stake in the transferees' equity (SNAZIR, 1997, p. 10). Instalment payments scheduled for 5-10 years with the first instalment at about 20% of the purchase price were foreseen in order to off-set the domestic financial capital shortage.

Private Companies (1989, 2001, 2004) – In 2001[244] the concept of genuine 'employee shares' as a special type of share was abolished in favour of the possibility for joint-stock companies to include rules in their statutes under which their employees may buy company shares at a discount. According to § 768c para. 17 Commercial Code[245] (hereinafter CC) previously issued 'employee shares' had to be converted into regular shares by a decision of the general shareholders assembly by January 2004 (Moravčík et al., 2004, § 768c para. 17 CC, p. 1287 ff.).

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243 A twist appeared in this year, when all the privatised firms were required to issue 34% of their share capital in employee shares: This requirement was abolished within half a year and the privatisation law then only mentioned an option to issue employee shares, not a requirement to do so.

244 Law 500/2001 Z.z., effective as of 1 January 2002.

245 Of November 5, 1991, Sb. 1991 No. 513; last amended by the Law of April 3, 2005, Sb. 2005, No. 315.

In the case where the conversion requirement was not met, § 768c para. 14 CC stipulates the possibility of the liquidation of the company by court decision. § 204 para. 4 CC introduced the possibility of the acquisition of shares on preferential conditions to replace 'employee shares'. The general prohibition for a company to acquire its own stock which is regulated in §§ 161a and 161 f CC is in principle an obstacle to the introduction of employee shares (Moravčík et al., 2004, § 209a CC, p. 694). However, the corporation charter can allow that, pursuant to the rules laid down in § 161 a para. 2 lit. a) CC, introduced in 2004, a company can acquire its own stock with the aim of transferring them to its employees; those shares have to be transferred within 12 months of acquisition by the company. Furthermore, under the current legislation joint stock companies may issue new shares granting employees favourable conditions in the context of so-called mixed capital increases according to § 209a para. 1 CC, i.e. the capital increase of a company issuing new stock financed by the companies' own capital. According to § 204 para. 4, the general shareholders assembly can decide that a certain number of those shares can be offered to employees at a lower price than the emission price; the difference shall be paid from the own resources of the company.

In order to facilitate the acquisition of shares by employees the legislator has provided the possibility that a company may fully pay for the stock which is acquired by the employees of the company. § 204 para. 4 CC states that a prerequisite to the preferential conditions for the purchase of shares by employees is that the volume of the overall value of the granted discount for the issued shares has to be covered by the company's own resources (Moravčík et al., 2004, § 204 CC, p. 674). The terms will be decided by the general shareholders meeting. In the case of the aforementioned mixed capital increase, applying § 204 para. 2 CC and in analogy to § 209a para. 3 and 5 CC, the total discount may amount to 70% of the share price provided that the remaining 30% is paid by the employees at the moment of the transaction, unless the down payment for the acquisition is financed otherwise (Moravčík et al., 2004, § 204 CC, p. 674 f.). In fact § 161e para 2 CC, introduced in 2004, contains an additional regulation permitting the company, in deviation from the general prohibition to leverage the acquisition of own stock, to do so in order to facilitate the acquisition of shares by employees of the company (Moravčík et al., 2004, § 161e CC, p. 574). The company may give loans to their employees in order to acquire newly issued shares or to buy them from third persons as well as guarantee such loans from third persons provided for that this does not endanger the company's own funds. Thus the acquisition of shares by the employees of a particular company may be accomplished by the company by discounting the purchase price, by providing credit and financing, by acting as guarantor or by a combination of all three preferential conditions.

b) Profit-Sharing

There is no prohibition in the Slovak legal system with regard to profit-sharing by companies with their employees. However, the only explicit regulation is provided for by § 178 para. 4 CC which states that – in accordance with the corporation charter – employees may be entitled to a share in the company's profits (Cash-based profit- sharing). The corporation charter or the general shareholders meeting may also stipulate that the part of profits that is allocated to the employees is used exclusively to purchase shares on preferential conditions or to make up the discount granted to employees in such a purchase (Share-based profit-sharing) (Moravčík et al., 2004, § 178 CC, p. 609 ff.). Furthermore, share-based profit-sharing is mentioned in the context of capital increases. As a rule a capital increase requires the decision of the general shareholders assembly, but § 210 CC – in accordance with the corporation charter – fore-

sees delegation to the management board. § 210 para. 4 CC regulates a capital increase by the issuing of shares to be transferred on preferential conditions to employees. It stresses this possibility especially in the case where the general shareholders assembly has previously decided that the part of the profits that it allocates to employees is used exclusively to purchase these shares. All those benefits will be subject to personal income tax of 19%.

c) Participation in Decision-Making

According to § 200 of the Slovak CC, joint-stock companies (similar remnant as in the Czech case due to common initial conditions) with more than 50 employees must have 1/3 representation of employee-delegated members on the supervisory board. There are no special rules for participation of employees in decision-making with regard to PEPPER schemes or privatisation matters. With regard to employee shareholding the general rules of the Commercial Code concerning shareholders rights apply.[246]

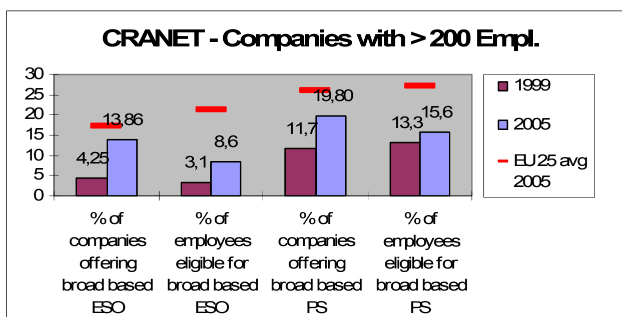
[246] For limited liability companies see §§ 114, 122, 123, 125 ff., for joint stock companies see §§ 178, 179, 180 ff. CC.

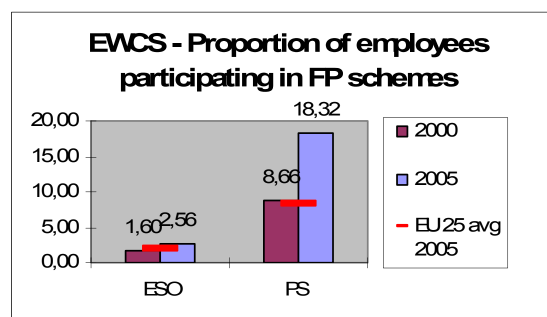
XXV. Slovenia

Slovenia has a long tradition of employee participation, starting with employee self-management since the 1950s. The strong tradition of employee involvement in corporate affairs is in fact reflected in both the Slovenian model of privatisation and in the development of Slovenian company law. Furthermore, in contrast to other Eastern European countries, Slovenia has retained relatively strong political support for the financial participation of employees to the present time, with respective draft laws being presented in 1997, 2002 and 2005. Although Parliament did not pass either of the draft laws, associations established by supporters of financial participation promote a legal framework. Their efforts finally led to a success: on 29 February 2008 the Law on Employee Share Ownership and Financial Participation was adopted by the Parliament.

Damijan et al. (2004) observe that insider ownership decreased by more than 10% in the period 1998-2002 (from 38.52% to 26.17%). The number of firms in the dominant ownership of employees (managers excluded) declined from 74 to 26. Amongst these firms, 10% of firms had no employee owners, in 25% of firms the employees held less than 5% of shares, while in half of the firms in the sample, the aggregate level of employee ownership did not exceed 18.4%. There were only 25% of firms in the sample with employee ownership exceeding 40% of firm capital.

By contrast, profit-sharing schemes are seldom used. Kanjuo-Mrčela (2002) finds that only about 7% of the 41 large Slovenian firms have actually constituted a 'fund of own shares' in order to remunerate their employees. About 32% of the firms introduced the possibility of employee profit-sharing in their Articles of Association. This possibility however often remains unexploited (in 22% of firms in the sample).





1. General Attitude

Debates concerning the establishment and preservation of employee ownership and other forms of financial participation started in the early 1990s. In 1995 a group of enterprise representatives, union representatives, journalists and academics established the DEZAP (Employee Ownership Association). DEZAP's main task is to stimulate the existence, enlargement and effective use of employee ownership in Slovenia. To achieve this objective, the Association promotes the adoption of suitable legislation on employee ownership, provides professional assistance to, and training and education of, employee owners, develops networks of employee-owned firms and promotes cooperation with other firms and international organisations. Similarly, all forms of employee participation are supported by the Association of Works Councils (Studio Participatis, currently consisting of 100 members).[247] Nevertheless, Trade unions have a differentiated standpoint and, e.g., opposed the 1997 profit-sharing law because it was proposing the introduction of profit-sharing along real wage concessions, something which also explained the final rejection of the law. Finally, the promotion of employee financial participation, e.g. by tax allowances, is stated as one of the objectives of the Slovenian Association of Managers for 2005 (Združenje Manager).[248]

The Slovenian Economic Ministry established an expert group in October 2002 to prepare the regulations on employee share ownership and other forms of financial participation. A similar and more detailed proposal was provided by Simoneti, Bohm, Gregoric, Cankar and Borec (2002). Both propositions are aimed at a more efficient organisation of current employee ownership in Slovenian firms and provide grounds for further employee participation in profit and, most importantly, corporate ownership. The two expert groups agree that the implementation of the profit-sharing and share ownership schemes should be voluntary. However, the adoption and success of such schemes is conditional upon the introduction of corresponding changes in the tax system, which would provide some tax allowances for both employers and employees participating in such schemes. The introduction of tax relief has in fact been the main obstacle to the adoption of the Law on Employee Financial Participation in 1997. A new draft Law on Employee Financial Participation was submitted to Parliament by the Social Democrats in 2005, but rejected. All draft laws, with the exception of the 2006 draft law, were based on the proposition that employee financial participation plans should be compulsory. For that reason, the employers were strongly opposed to the adoption of such laws proposed by centre-left governments. The 2006 draft law was prepared by the first centre-right government in co-operation with the social partners and agreed upon in the Economic Social Council in December 2007. This draft law was adopted by the Parliament on 29 February 2008.

2. Legal and Fiscal Framework

The new Law of 29 February 2008, which entered into force in April 2008, regulates share ownership and share-based profit-sharing plans (without stock option plans) and contains

247 <http://www.delavska-participacija.com>.

248 <http://www.zdruzenje-manager.si>.

strong tax incentives for the eligible schemes. However, the Ministry of Finance has not yet issued the Order, on the basis of which tax incentives could be applied. When the Order is issued, the interested companies will be obliged to register with the Ministry to become eligible for tax incentives. However, privatisation law, on the basis of which employee ownership first emerged in Slovenia, and general company law should be addressed as well.

a) Share Ownership

Privatisation (1993, 1997) – The possibility to privatise companies was introduced by the Law on Ownership Transformation of 1992[249] (hereinafter referred to as LOT), determining that companies and the social capital could be sold to workers or third parties, defining a special form of workers' participation in social capital. Companies in social ownership were transformed[250] into corporations and issued shares in the amount of the value of the social capital. The shares could be distributed by internal distribution of shares, internal sale of shares, sale of shares to outsiders, and sale of assets to outsiders. The LOT provided for the mandatory distribution of 40% of the social capital to different funds (10% to the Pension Fund, 10% to the Restitution fund[251] and 20% to the Development Fund for further sale to Privatisation Investment Funds). The firms were then entitled to distribute (in exchange for employee vouchers) up to 20% of ordinary shares amongst its current and former employees, including retired employees. Registered shares, obtained by workers, were not transferable for a period of 2 years after the issue date, except when transferred as an inheritance. In practice, however, employees found ways to sell the shares before the expiry of the restriction period and many of them sold them immediately.

Furthermore, companies had discretion over the allocation of the remaining 40% of their capital (after the distribution of 40% to different funds and 20% to inside owners); they could either sell them to insiders (internal buy-outs) or outsiders (outside privatisation). Within the internal buy-out, workers could buy shares with the profit of the companies belonging to the participants of the internal sale programme as well as with their salaries and other funds. The workers could also obtain a part of the shares against overdue salary claims or other due claims against the company. Furthermore, the option of the so-called 1/5 company model was introduced in order to support employee participation in ownership. For privatisation purposes, Slovenian citizens were granted vouchers; the value of vouchers granted to each individual depended upon the duration of employment (Art. 31 LOT). Vouchers could be used to obtain shares in the company of employment within the scope of the internal distribution of shares (the initial 20%), to obtain shares of Privatisation Investment Funds, to purchase shares of other companies privatised by the public sale of shares, and to purchase shares or other property of the Republic of Slovenia and state-owned companies offered to the public against vouchers (in the latter case, vouchers could not be freely traded).

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[249] Of 5 December 1992, OG RS 55/1992, as amended

[250] The LOT emphasised ownership transformation rather than privatisation, which, nevertheless, was the final goal of the law. Transformation was the interim stage, allowing for the acquisition of ownership by workers and other Slovenian citizens of existing social capital (public funds).

[251] The Slovenian Restitution or Compensation Fund has to issue debenture bonds to re-privatisation claimants who did not get their nationalised property returned in kind. The Slovenian Compensation Fund obtained funds from the non-distributed public funds.

Certain measures were taken in order to preserve employee ownership after privatisation, starting with the 2-year (4-year) restrictions on trading with shares gained from internal distribution (internal buy-out). To prevent the decline in employee ownership, some firms decided to limit trading by internal acts, namely through 'shareholder agreements'; which prohibited the sale of employee shares to outsiders and provided for the representation of employees in the firm's decision-making process. However, shareholder agreements were easy to abandon and difficult to administer (Mrčela, 2002). Upon the proposition of DEZAP, the Slovenian Chamber of Commerce and the Association of Free Trade Unions, an amendment was introduced to the Takeover Law of 1997, which provided for the possibility of an institutional organisation of inside owners in the firms Workers Associations (mentioned earlier as WAs) and which exempted them from public bids (Art. 81). By the amendment to the Take-Over Law, Worker Associations became professional proxy organisations and as such had to act according to the Takeover Law (Art. 298) and the provisions of the Company Law.[252] The aforementioned laws regulating transformation and privatisation have not been abolished, but they are not applied in practice, since privatisation is generally complete.

Private Companies (2004, 2008) – With the transposition of the Second Council Directive 77/91/EEC of 13 December 1976 into Slovenian CL 2004, companies can buy own shares up to 10% of the subscribed capital for distribution amongst their own employees and employees of associated companies within a one-year period (Art. 240 CL). This can be done both by joint stock company and by limited liability company; there is no restricted tradability for shares acquired in this manner. Furthermore Art. 241 CA allows companies to advance funds, make loans, and provide security, with a view to acquisition of the company's shares by employees of the company or employees of an associate companies. Pursuant to Art. 318 CL, part of the profit can be distributed to employees in the form of new shares if the general meeting makes such a decision.

Under the new Law of 29 February 2008, employees obtain a 70% tax relief from distributed shares, if the shares are held one year, and a 100% tax relief, if the shares are held three years, up to the annual amount of 5,000 EUR. In addition, no social security contributions are imposed on the benefit. In the original draft law, only employees covered by collective agreements, i.e. with the exception of management and other key personnel with individual contracts, were eligible for tax incentives. However, in the finally adopted version of the Law all personnel categories are included, but the amount is limited. The maximum annual amount for financial participation should not exceed 20% of the company profit or 10% of the total gross salary. The employing company is entitled to deduct the value of distributed shares from the tax base of corporate income tax.

b) Profit-Sharing (1993, 1993)

The new Law of 29 February 2008 applies also to share-based profit-sharing, but not to cash-based profit-sharing. The rules of the Law explained in the section on share ownership are relevant also for share-based profit-sharing.

252 A draft framework Law on Employee Financial Participation was submitted to Parliament in October 1997 but was never discussed. As stated above, a new proposition of the Law on Employee Profit-Sharing was sent to Parliament in April 2005 but was again refused following Parliamentary discussions.

Further, general provisions of company law may become relevant. In Art. 228, the new CL of 1993 regulates the use of net profit. Primarily, the profit must be used for covering losses and creating legal and statutory reserves. The rest of the profit, but not more than 50% of the net profit, may be used for other reserves and, if the Articles of Association provide for it, for paying a part to employees and members of the management and supervisory boards.[253] This is to be decided upon by the general meeting as part of the decision on profit distribution. The CL thus makes profit-sharing possible provided that there is enough profit to cover losses, legal and statutory reserves, that the possibility to use part of the profit for employees is contained within the Articles of Association of the company, and that the general meeting makes such a decision.[254] The participation amount is usually determined as a percentage of the annual profit of the company.

c) Participation in Decision-Making

Art. 75 of the Constitution provides that workers participate in the management of economic units and institutions in the manner and under the conditions as determined by the law. This constitutional provision was implemented by the special Law on Workers' Participation in Management of 1993[255], regulating the manner and the conditions for workers' participation in the management of economic units regardless of the ownership form, including cooperatives.[256] According to this law, workers participate in management by submitting initiatives, by demanding information, by consultations with their employer, and by participation in decision-making, including the right to reject employers' decisions. In particular, workers are entitled to nominate from 1/3 to ½ of supervisory board members and, in firms with more than 500 employees, one member of the management board. Since employees who obtained shares in the course of privatisation, as a rule, are minority shareholders, special provisions of the CL on the protection of minority shareholders apply. These special rights relate to the general meeting, the right to information, the right to examine the books, and the right to lodge a complaint against the decisions of the general meeting. On the other hand, these rights do not include the right to replace the management.

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253 Only the Articles of Association can regulate that members of the management board are granted the right to participate in profit-sharing for their work (Art. 252 (1) CL).

254 It is also possible that participation in profits is defined by the meeting of shareholders (Art. 276 CL), but, by systematic interpretation of special provisions in conjunction with general provisions, it can also be concluded that in this case the general meeting has to amend the Articles of Association.

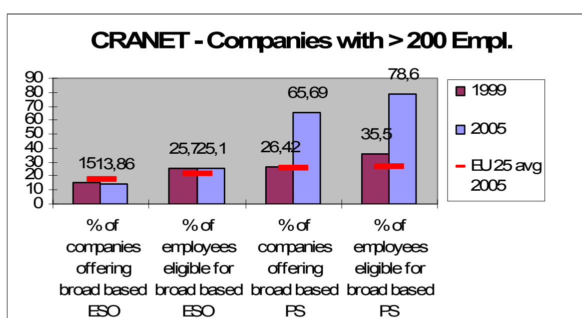
255 Of 6 August 1993, OG RS 42/1993, as amended.

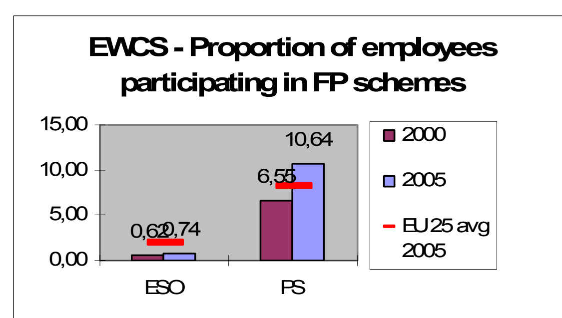
256 Individual specific provisions on employees' co-management are integrated into the special laws for different economic sectors, e.g., the Energy Law, Banks and Savings Banks Law, Insurance Company Law.

XXVI. Finland

Personnel funds are the only form of financial participation enjoying fiscal incentives and promoted by the social partners. In 1989, the Council of State appointed a committee to determine new forms of co-operation to enhance economic democracy, competitiveness and productivity. The committee formulated a draft law in 1987.[257] The draft law addressed voluntary personnel funds as a key element. The target of the funds was to enhance efficiency in the companies, 'innovations' at all levels and a balanced division of decision-making and responsibilities. The law was enacted in 1989 (814/1989). Immediately after the law was adopted, it attracted great attention, thus the majority of the funds working today were established then. The interest in personnel funds has recently grown. Altogether 82 funds have been established between 1990 and April 2007, of which 28 have been closed down. There are 54 operating personnel funds with about 126,000 members covering over 5 % of the whole workforce. It has been not clarified why the number of funds is not higher. One reason is obviously the recession period in Finland at the beginning of the 1990s. Another reason could be that other pay systems which are closer to the operational processes became more common. The Ministry of Labour made a study (1999) about the funds which had closed down. In ten companies out of 13 the reason to close the fund was company arrangements such as mergers and acquisitions. Another reason was a shift towards performance-related pay (two cases in the forest industry).

In Finland there is an increasing interest towards financial participation. Social partners want to improve organisational and pay flexibility. Personnel funds are seen as a good instrument by current government and social partners to achieve flexibility. At the time being these parties are discussing methods of how facilitate and promote the use of personnel funds. Current existing incentives for both employees and employers do not seem to enhance the use of personnel funds as much as intended.





257 First official discussions about employee wage earner funds (as they were called at the time) took place in 1981 at a general meeting of the Central Organisation of Finnish Trade Unions (SAK) and a meeting of the Central Organisation of Clerical Employees and Public Servants (TVK). In both meetings, suggestions about developing employee wage earner funds were made. These suggestions were based on political discussions at the end of the 1970s on financial democracy and employee participation. The idea of wage earner funds in Finland was attributable to the model of collective wage earner funds developed in Sweden by Rudolf Meidner. The US ESOP was also a source of inspiration.

1. General Attitude

The majority of the Finnish employees are members of the unions. The unionisation rate is around 70-80%, and about 90% of all wage and salary earners are in the sphere of the collective bargaining agreements. There are several employers' and employee organisations. The largest employers' associations are Confederation of Finnish Industries (EK) in the private sector; the Commission for Local Authority Employers (KT) and the State Employer's Office are the main associations in the public sector. The largest employee associations are The Central Organisation of Finnish Trade Unions (SAK), The Finnish Confederation of Salaried Employees STTK, and the Confederation of Unions for Professional and Managerial Staff (AKAVA). At the moment the Centre party has the majority of the seats in parliament and they have the ruling majority with the Coalition party when the Social Democratic party is in opposition.

Wage increases are agreed collectively, while companies may adopt profit-sharing and other performance-based payments independently without any negotiations. A few collective agreements have though, included negotiation about performance based pay. Personnel funds are the only subject that is discussed by the social partners. Employee and employers' associations promote personnel funds and the government alike. Options and share ownership are not viewed to be proper subject for collective bargaining. Some of the employee associations would like that profit-sharing or performance based pay would be subject to the collective wage bargaining negotiations. The employers associations think that the companies should have the flexibility to decide unilaterally whether such pay forms are used.

2. Legal and Fiscal Framework

a) Employee ownership

Employee Shares - Companies may issue shares to employees at a favourable price. The advantage is tax-free if the discount is 10% below the current price and the majority of employees have access to the advantage (Income Tax Law § 66.1). The dividends from publicly traded companies is tax-free for 30 % and is taxed as capital income for 70%. The company is taking 19% in tax before the payment to the employee. This tax is deductible from the employee taxation. Those companies that are not publicly traded may pay dividends tax-free if the earning per share is less than 9%. Maximum earning per employee is 90 000. If this is exceeded 30% is tax-free and 70% is taxed as capital income.

Personnel funds are in some cases employee ownership, when the personnel fund is investing the assets into the company. They are though here defined as profit-sharing.

Stock Options[258] - The first stock option plans in Finland in publicly traded companies were launched in 1987. A large increase in the use of options in Finland took place in 1998-2000, when the stock market was at record highs. The majority of the option schemes are used in publicly traded companies (or in companies that are preparing for initial public offering). The schemes used are either broad based or selective. The broad based schemes are for all employees or at least to the majority while the selected schemes are mostly managerial schemes. Broad based schemes became popular in 1998-2000, but their popularity has waned. The Finnish Law on Joint-Stock Companies (624/2006) requires that the companies should report all relevant conditions and changes in the stock option schemes to the shareholders. The Finnish stock options are either given for free or in exchange of a loan to the company which is paid back usually in 1-3 years. Options can typically be first exercised 2-4 years after they have been granted. The exercise period may extend from few months to few years. The price is usually set so that it corresponds to the price of the share at the time the option was granted. Stock options are taxed as earned income. The employer pays social security contributions on options.

b) Profit-sharing

Personnel Funds - In Finland personnel funds have been the most frequent form of employee financial participation since 1990. The Act on Personnel Funds (814/1989) was issued the 15th September 1989 (amended several times thereafter).

The personnel funds are deferred profit-sharing plans, allowing investment into the equity of the company and thus involve an element of employee share ownership.[259] They are company level agreements even though there is a law giving the frames for the action i.e. they are regulated by the 1989 Personnel Funds Act. The payments to the fund should be (at least to 50 %) accumulated from company profitability indicators. The employer retains the right to choose the criteria of profit-related payments, but it must be fixed typically a year in advance. There is a possibility to use also other measures of efficiency, for instance quality or physical productivity. At the time being companies do not, however, use this possibility to a large extent. Payments are made once a year.

Personnel funds are established by a collective decision of the employees. It is required that 2/3 of all personnel groups support the establishment of the fund. The law on personnel funds requires that all employees are included in the plan; only senior management may be excluded. A company must have at least 30 employees in order to set up a personnel fund of this kind, while in the case of corporate groups there can also be joint funds for all the member companies. A personnel fund is registered with the Ministry of Labour and it possesses legal personality in its own right. However, it may engage only in the activities referred to in the Personnel Funds Act (814/1989). The funds are investing the capital either in shares of the own company or other companies, in investment funds, bonds or in bank accounts. Through these investments, the financial gains of the employees extend beyond a mere share in company profits.

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258 Based on data from the doctoral thesis of Mikko Mäkinen (2007), Essays on Stock Option Schemes and CEO Compensation. Acta Universitatis Oeconomicae Helsingiensis, A-291, Helsinki School of economics. Panu Kalmi (2005) Inventory study for the project 'Changes in the patterns of employee financial participation in Europe".

259 The discussion draws from Vartiainen and Sweins (2002) and Sweins (2004).

The capital in the personnel fund is divided into individual accounts and sometimes a collective part, which is used either for administrative costs or other costs of the fund. The shares are distributed to employees typically either in relation to base pay or in relation to hours worked. Equal shares are also used to some extent. The individual shares of the members are locked in for the first five years of membership. After that, a member can withdraw up to 15 % of the value of her accumulated fund share. When the employee is retiring from work, he or she is entitled to withdraw the value of the fund share either immediately or in parts within four years. According to the law minimum information that the fund has to give each employee about his or her share is at least once a year by a letter. From the employees' standpoint the fund is a deferred-payment scheme, which should foster their commitment to the company from which profit-related payments originate.

Personnel funds enjoy several tax advantages. For employees, 20 % of the pay-outs from the fund are tax-free (§65 Income Tax Law 227/96). The fund does not pay any taxes on its earnings (§20 Income Tax Law). Employers do not have to pay pension- nor social security contributions and no taxes for the profit paid to the fund. The profit paid to the fund is tax deductible for the company as professional expenses (§8 Business Tax Act). There have been some amendments in the legislation during the time. In 1996 there was a change of the vesting period from 10 years to 5 years, and the amount of annual withdrawals was extended from 10 % to 15 % (Personnel funds Act 1660/95). In 1999 (344/99) there was an amendment which allowed the funds to be established also in civil service departments and in state owned companies. Instead of profit the governmental offices are using measures of performance. In 2000 (1145/99) there was a change in the law that gives the employees a possibility to draw out their share as cash if that is also made possible by the personnel fund regulations. The internationalisation and globalisation lead to a change that also international Finnish companies may take in use profit-sharing together with a personnel fund to cover also the foreign subsidiaries and their employees (499/2002). For foreign employees employed by a Finnish company it was possible yet earlier to belong to a personnel fund. Some other minor amendments have also been done during the existence of personnel funds.

Altogether 82 funds have been established between 1990 – April 2007, of which 28 have been closed down mainly due to mergers and divestments. The majority of the funds have been established in the beginning of the 1990´s. After the recession in the middle of the 1990´s there have been only few funds established each year. In more recent years the popularity of the funds has increased. In 2005 there were 8 new funds registered, which is more than in any other year after 1991. In April 2007 there are 54 operating personnel funds with about 126.000 members, which cover over 5 % of the whole workforce.

Even though Finnish personnel funds were inspired by Swedish wage-earner funds and US employee stock ownership plans, important differences exist between these schemes. Neither Employee Share Ownership Plans (ESOPs) nor wage-earner funds (WEFs) are profit-sharing schemes; in the former, the trust acquires the shares by borrowed capital, whereas the latter were sponsored by the Swedish government by the taxation of profits.[260] Whereas personnel funds typically distribute their shareholdings quite widely and invest also on other securities, employee share ownership plans invest only on their own firm. The main difference between personnel funds and wage-earner funds is that the former are completely voluntary and operate at the level of the firm, whereas the latter operated at the national level for the benefit of

[260] See Blasi and Kruse (1991) for a description on ESOPs and Whyman (2004) for a recent account on WEFs.

the entire workforce. In the design of Finnish personnel funds, the employers explicitly wanted to avoid the Swedish obligatory model.

Performance related pay - There is no legislation and there are no incentives for performance related pay. The performance related pay may be paid to the employees from company profit or from budgeted money or it may be a mixture of both. The plans may also be related both to individual performance as well as collective performance. That means that part of the performance related pay plans used in Finland may be defined as profit-sharing and part are not. It is however, not possible to distinguish the 'pure' profit-sharing plans from plans more like gain-sharing. To understand how widespread performance related pay is some statistics are presented.

Of those employees belonging through the employer to the Confederation of Finnish Industries (EK) 52% are participating in some performance related pay scheme[261]. This concerns about 500 000 employees. Performance related pay i.e. other than personnel fund is used in 1/3 of the companies. EK estimate that in the whole private sector (also not members) there were 46% of the employees joining the performance related pay schemes. There are differences between sectors and personnel groups. The pay schemes are usually covering the whole workforce, but they may cover only a part of the workforce. PRP was more common in the industry sector (69%) than in the service sector (44%) or building sector (40%).

c) Participation in Decision-Making

On 1 July 2007, a new Law on Cooperation (334/2007) was enacted. The aim of the Law is to develop co-operation and working conditions by giving the employees more knowledge about the phase of the enterprise and the future plans to develop the operations in the enterprise in co-operation and to enable employees to participate in the decisions on work, working environment, and the employees' position in the enterprise.

The Finnish Personnel Funds are connected to decision-making procedures and the Act of co-operation (19 § 334/2007) states that, there should be negotiations before establishment of a fund. Two-thirds of the employees should be voting for the funds before it is possible to establish a fund, and there should be negotiations in case of renunciation and dissolution of the fund.

Co-determination, employees' representation on the supervisory board is prescribed in the law 725/1990 (Finnish companies) and in 758/2004 (Societas Europaea and European co-operatives). In companies with over 150 employees, the employees have a right (if they wish) to elect representatives in the company management. The level of representation is supervisory board (if it exists), or board of directors, or management groups in different units of the company. Employees have the right to elect one-fourth of the members at the relevant layer. The representatives have the same rights, duties and responsibilities as the other members elected by the company. However, they do not have the right to take part in handling of matters that involve elections or dismissals of company management, terms of managerial contracts, and terms of personnel employment relationships or measures in case of industrial actions. There is no data available for how many companies have employees in the supervisory board.

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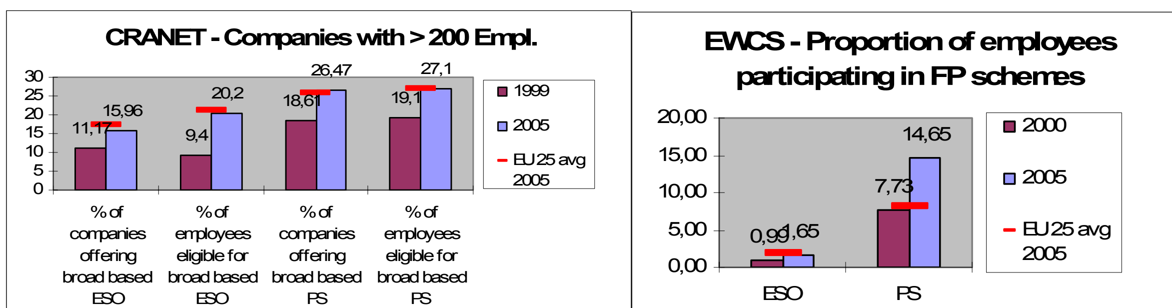
261 Based on data from The Confederation of Finnish Industries (EK) which is the leading business organisation in Finland. EK represents the entire private sector and companies of all sizes.

XXVII. Sweden

There is no specific system for direct promotion of employees' financial participation in profits or shares in Sweden, despite the fact that discussions about financial participation i.e. wage earner funds started in Sweden already at the beginning of the 1960s. The Law on wage earner funds was enacted in 1983[262], whereby the majority of the assets were placed in shares of large companies. The obligation to make contributions to the funds was abolished in 1990.[263] There are no common definitions of different pay systems in Sweden, which makes comparisons difficult. There are no statistics on how many companies use financial participation. In Sweden there is no particular national promotion for financial participation. One of the main thoughts behind the taxation reform in the late 1990s was that all different sources of work income should be handled in the same way, and therefore there are no income tax reliefs for the employees.



Profit-sharing foundations are used, but the extent is unknown because they are not registered with any authority. Performance-based pay is used in several companies and the collective agreements leave place for them. Performance based pay is based both on collective and individual results. It is not possible to distinguish, how many of these plans actually are profit-sharing plans. One study shows that 19 % of the employees were involved in broad-based profit-sharing plans and 12% in broad-based share ownership plans in 1998 and the number seems to have increased since.[264] The Swedish Trade Union Confederation's studies show large differences between different groups. In 1998, profit-sharing was most common among

262 The funds got their assets from 20 % tax on the company real profit and from an increase in pension contribution. The public sector also participated in the funds.

263 In 1991 the political right wing won the elections and started to close down wage earner funds. The draft law brought into the Parliament stipulated that the existing funds should be closed down and no new funds should be established. The accumulated capital of 22 billion SEK in shares was intended to be used to enhance private ownership and savings, but this proposition was rejected, since it would lead to volatility of financial markets. The government decided that 10 billion would be invested in research promotion and the remaining amount in subsidies for pension schemes.

264 Wurz S. (ed.) 2003. European stock-taking on models of employee financial participation - Results on ten European case studies: General value and background of employee financial participation-Sweden, p 116-128.

younger employees in the private sector with a full-time job and highly paid men working in the industry sector.

1. General Attitude

The employer associations view financial participation as a good method of obtaining increased flexibility of labour costs depending on the success of the business. The trade unions are afraid that financial participation will be mixed with general pay, and thus they are neutral and sometimes negative towards financial participation because they fear that it would have an effect on the regular pay increases. The issue of financial participation is on the local level and the central associations more often debate the employer end employee tax situation concerning financial participation programmes. The attention from the government is fairly low and therefore there is not direct promotion of financial participation. The general view from the state is that taxation should be same despite the income. In some cases there are exempt from social security contributions and a lower pay roll tax is paid instead and sometimes the employees' taxation is postponed. The history of wage earner funds may still affect the debate on financial participation.

The unionisation rate of workers during the first quarter of the year 2005 was 79.2 %. The main employee associations are LO, The Swedish Confederation of Professional Associations (SACO) and TCO. The Confederation of Swedish Enterprises is the main employer association.

2. Legal and Fiscal Framework

a) Share Ownership

The employer may offer stock purchase programmes to the employees to a discount price, but there are no incentives available. The employees are paying tax as from income on the difference between the discount and the market price, and the employer pays social security contributions at the time of grant if the price is below the market price. Future gains are taxed as income of capital.

Stock option programmes became more common in Sweden during the 90's. One of the reasons was the tax situation, where tax is paid on income of capital which is lower than income of service. The leverage of gain was also expected to be high considering the development on the stock market. The employer has no contributions at time of grant. Social security contributions are paid at time of exercise. Employees do not pay tax at time of grant. Options are taxed as income of service at the time of exercise and future gains are taxed as income capital (Income Tax Law 1999/1299 44§12). Employee stock options normally have following characteristics; only available to employees within a company or group, it gives a right to acquire shares at a certain time for a certain price, normally the employees gets them for free, and the option's exercise period id normally 5-10 years long, the option is not normally valid if

the employee leaves the company. Employee stock options are not considered as financial instruments and thus, tax situation is not as favourable as for other options. At the time of exercise the difference between the market price and the exercise price of the shares is taxed as income of service and social security contributions also are paid. This may lower the interest in employee stock options, because this may involve high risks for the employer since it may lead to large social security contributions in the future.

b) Profit-Sharing

Profit-sharing foundations are defined already in a law in 1962/381. The first profit-sharing foundations were established in early 1970's. A profit-sharing foundation where companies share part of their profit with their employees by allocating part of the profit to a foundation according to certain established legal rules and principles. When the company decides to pay part of the profit to a profit-sharing foundation, the employees i.e. often the union representatives can create a foundation and the charter of foundation which describes the regulations of the foundation for example how to invest the assets. If it is a listed company, the assets are often partially invested in company shares.

There are some requirements that should be fulfilled in order to have a profit-sharing foundation (1990/659). The employer contribution should be based on rewarding the employees for their efforts. At least one-third of the employees have to participate. The profit-sharing contribution has to be vested for at least three years after contribution. The assets should be secured for future payments to the employees. The terms and conditions should be equal for all participants. When a foundation is dissolved the assets are being paid to the employees not to the company. The profit-sharing foundation has the purpose, to administer the allocated profit assets according to specific directions to which it is bound. Contributions to the foundations were exempt from any social security contributions or pay roll tax during 1992-1997 this probably affected the number of new funds. The employer pay today a payroll tax 24,26 % at time of grant (1996/97:21 s.25) instead of a social security contribution 32,28% which is paid on wages. The employees' do not have any tax incentives; they pay tax as income of service at time of future payments from the foundation. The foundation is paying capital tax 1,5 ‰ of the capital (Law on Governmental Capital Tax (§20 1997:323).

The aim of the profit-sharing foundations is to motivate, engage and make the employees conscious about the result. There is no systematic registration of the profit-sharing foundations and therefore it is not possible know the extent of how many profit-sharing foundations exist. The most famous profit-sharing foundation is the foundation of Handelsbanken called Oktogonen, which was enacted in 1973. From that year Handelsbanken has paid part of the profit to the foundation (1992 is the only exception). Every employee gets the same share of the profit and the share is paid to the employee when he or she turns 60. The foundation was the biggest shareholder in 2004. It owned 10,1 % of the voting shares and 9,6 % of the capital. One third of the capital in the foundation was held in Handelsbanken shares and the rest was invested in publicly traded shares.

Cash-based profit-sharing exists but it is not regulated by law. No incentives exist for cash-bonuses. There are no statistics available on profit-sharing.

c) Participation in Decision-Making

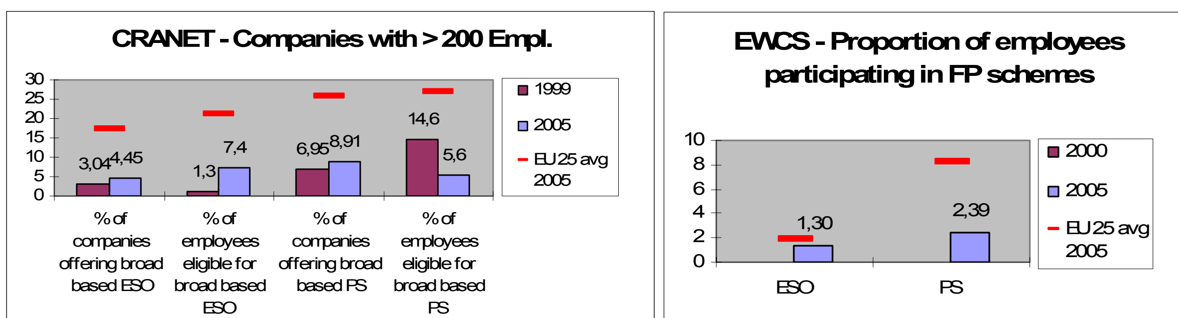
The Law on Board Representation (1987/1245) for employees of joint stock companies and co-operative enterprises/ organisations is also linked with the Law on Co-determination at Work (1976/580). The Law on Board Representation entitles local trade unions to appoint two representatives to the board of directors if the company has at least 25 employees. If the company has at least 1,000 employees and operates in several industries or business sectors, the trade union has the right to appoint three board representatives. Under the Law on Co-determination at Work all important matters concerning the relation between employer and employees' organisations shall be determined by negotiation. The employee is always represented by the trade union organisation that has the right to negotiate. In the case of the employer, the right of negotiation may be exercised either by an employers' organisation or by the individual employer.

The Law on Co-determination at Work (MBL 1976/580) is central to labour law. It covers all issues on the relation between employer and employees' organisations in the entire labour market. Both the employer and employee concepts are to be given a wide interpretation. However, financial participation is not addressed in this Law.

XXVIII. Turkey

On the whole, financial participation of employees has not played any notable role and has remained limited in Turkey. Share ownership schemes have been implemented mostly in the context of privatisation and in multinational companies while profit-sharing is found amongst private companies. Compared to Eastern European Countries, privatisation was not the all-determining economic issue in Turkey, and only acomparatively small number of enterprises were privatised. However, participation of employees in privatisation on preferential conditions was considered to have positive effects by the majority of policy makers as well as social partnersand most political forces, so that the employees of many privatised enterprises have become share owners and incentives such as discounts, payment by instalments and loans werde used. Anecdotal evidence has been found for ESOP-like schemes based upon associations and foundations which collectively hold the shares of the employer firm (e.g. Adana Kağıt Torba Sanayii T.A.Ş. and Teletaş Telekominikasyon Endüstri Ticaret A.Ş.) for employees, who benefit from contributions of company profit in the acquisition of these shares. The legal framework contains no special regulations concerning PEPPER schemes and in some aspects even inhibits their further development, although reforms of the Commercial Code are underway. Except for the tax deductibility of employers' contributions and specific tax exempt associations and foundations, there are no direct incentives to set up PEPPER schemes.

According to a study of corporate governance in Turkish publicly traded companies, dated 2007, 3-4% of publicly traded companies have employee share ownership programs, and 15% have employee pension funds and other funds or foundations for retirement or unemployment insurance. Over 20% of the companies have profit-sharing, though no distinction is made between broad-based schemes and ones targeted only at management (board members) (Küçükçolak and Özer, 2007, p. 5, p. 12: Table 7).[265]



265 Data results from a questionnaire based on the practices of corporate governance principles by the respondents, namely the Istanbul Stock Exchange (ISE) member firms and companies listed on the ISE, and a statistical evaluation of the findings. 115 members firms out of 205 and 243 ISE companies out of 308 were included.

1. General Attitude

Today, employee financial participation is not a current issue for trade unions, their position is inconsistent probably due to lack of knowledge about possible schemes. Their attitude can be described as generally positive, considering that, with a consistent legal framework established by the government, employee ownership can be beneficial not only for employees, but also for the economy. On a national level employees are represented by the Confederation of Rights of Turkish Workers' Trade Unions (Hak İş), the Confederation of Turkish Workers' Trade Unions (Türk İş) as well as the Confederation of Revolutionary Workers' Trade Unions (DISK). During the discussion of the Tax Reform of 1968, the attitude of the Conservative Hak-İş towards employee participation was more positive and clear than the attitude of the Türk-İş. Employers, generally, present themselves as opposed to employee participation, in particular to participation in decision-making and employee ownership, and most collective agreements are influenced by this attitude.[266] Employers are, primarily, represented by the Turkish Industrialists' and Businessmen' Association (TÜSİAD) as well as the Turkish Confederation of Employers' Associations (TİSK). However, according to a report of the TÜSİAD participation of employees in privatisation is considered as positive by broadening income distribution and avoiding labour disputes (TÜSİAD, 2002; Gürol, 1994, p. 95). Nevertheless, according to a survey conducted by the Capital Markets Board of Turkey (CMB) in 2004[267] amongst the companies listed at the Istanbul Stock Exchange (ISE), 56% of the responding companies were in favour of employee participation in the management of the company. Employee participation has been discussed by academics, politicians and trade unions since the tax reform of 1968.

The 58th Government (Justice and Development Party) published its instant action plan in 2002[268] which encourages Turkish citizens working abroad to invest their savings in the privatisation of Turkish enterprises. According to the party programme, it is intended that companies subject to privatisation will be primarily offered to employees, along with other selected target groups. Accordingly, the Privatisation Law was amended in 2003[269] to stipulate that employees can participate in privatisation conducted by public offer.

2. Legal and Fiscal Framework

Under Turkish law there is no specific employee share ownership programme or any particular law or regulation governing specific issues of employee share ownership, as in other countries. The forms of employee financial participation covered by different laws are profit-sharing,

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266 Such was the basic line in an interview with Bülent Pirler, General Secretary of TİSK, and Enis Bağdadioğlu, Deputy Manager of their Research Department.

267 Survey on the Implementation of Corporate Governance Principles conducted by CMB of Turkey in 2004; 249 companies out of 303 responded to the survey.

268 The plan published in 2002 after the Justice and Development Party came into power classifies the activities to be undertaken into 205 groups and phases them into periods of 3 months, 6 months, one year, continuous, long term etc. taking into consideration the scheduled deadlines.

269 Law No. 4971 of 15 August 2003.

stock options and – to a limited extent – regulations on the acquisition of shares by employees. Legislation permits employee share ownership, on the one hand in joint-stock companies during privatisation and on the other in private companies by setting up welfare funds and mutual assistance funds for the benefit of their employees. Apart from tax deductibility for employers' contributions to specially tax exempt associations and foundations, there are no direct incentives to set up PEPPER schemes.

a) Share Ownership

Privatisation (1984, 1994, 2003) – The privatisation programme in Turkey was initiated in 1983. Privileges for employees in connection with privatisation were introduced by Decree no. 18514 of the Public Participation Fund of 13 September 1984, regulating the administration, usage and other issues of the fund. Pursuant to the regulation, specific provisions benefiting employees as well as the local population could be introduced in the case of share sales. In 1984 the first related Law No. 2983 was enacted, followed by Law No. 3291 in 1986.[270] According to Decision no. 54 of the Housing Development and Public Participation Board[271] of 30 April 1987, shares of enterprises to be privatised should primarily be offered to employees, local residents, and Turkish citizens working abroad. Pursuant to Art. 18 of Law No. 4046 on the Implementation of Privatisation of 27 November 1994[272] (hereinafter referred to as PrivL), privatisation could be conducted by sale, lease, the granting of operational rights, the establishment of property rights other than ownership, profit-sharing and other legal dispositions depending upon the nature of the business. In the context of a share deal, the sale of shares to employees is expressly regulated and - depending upon the privatisation decision in each individual case - employees may be entitled to purchase shares at a discount and/or to pay by instalment. Furthermore, Law no. 4971 of 15 August 2003 amended some laws and the decree law on the establishment and duties of the General Directorate of National Lottery Administration, amending Art. 7 PrivL, stipulates that employees can participate in privatisation conducted by public offer. In this context the possibility to grant credit to employees from funds of foundations set up by the employer company (see below d) ESOPs) according to Art. 468 and 469 of the Turkish Commercial Code[273] (hereinafter referred to as CC) is important. Thus, acquisition on preferential terms, such as deferred payment by instalments, credit from established foundations and discounted prices, is amongst the possible incentives stipulated by privatisation legislation to leverage employee ownership in privatisation.

Private Companies (2003) – Turkish commercial law does not contain special rules on employee share ownership with regard to their acquisition, the limitation of the number of shares or the issue of employee stock, for any business form so that general rules apply. Nevertheless, the Corporate Governance Principles of June 2003 which are recommended by the Capital Market Board for adoption by individual listed companies promote PEPPER schemes.[274]

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270 See <http://www.oib.gov.tr/baskanlik/yasal_cerceve_eng.htm>.

271 A policy making body at Ministerial level under the Prime Ministry to carry out the policy.

272 As published in the Official Gazette No. 22124 on 27 November 1994 and most recently amended by Law No. 5398 of 3 July 2005 published in the Official Gazette No. 25882 on 21 July 2005.

273 Law No. 6762 dated 29 June, 1956, enacted on 2 July, 1956, published in the Official Gazette No. 9353 on 9 July, 1956.

274 Employee financial participation is mentioned in connection with shareholders' rights (Principle 6.2), transparency of financial information (Principle 3.1), and participation of shareholders in management (Principle 3.2).

Generally, corporations are not allowed to acquire their own stock (Art. 329 CC) and unlike regulations in other countries, exceptions from this general rule do not include special rules on employees' shares.[275] Thus, even if freely disposable equity of the amount necessary for this purpose is available, Art. 329 CC is an obstacle to all schemes that enable employees to acquire shares, if part of the price or the whole price of the stocks is paid for by the company (e.g. acquisition below market price, free shares, premium, bonus, etc.). However, there is no restriction to offering shares to employees on favourable conditions in the course of a capital increase provided that the price is not lower than the nominal value (Art. 286 CC). Furthermore, according to Art. 14/A of Capital Market Law (CML), if permitted by the company's Articles of Association, publicly held joint stock corporations may issue and offer to the public non-voting shares that are preferred with respect to dividends.

If a foreign multinational company wishes to implement financial participation plans for employees working in its subsidiary or group companies in Turkey in accordance with the rules of the home country, it has to register the plan with the CMB which evaluates the application and approves or rejects it. It should conduct the sale through an intermediary institution such as a bank, special finance institution or a brokerage house.

Employee Stock Ownership Plans (ESOP) – Although there is no implementation of genuine ESOPs in Turkey we observed ESOP-like schemes based upon associations or foundations which collectively hold the shares of the employer firm for employees with the employer company contributing from company profits to facilitate the acquisition of shares by employees. In fact, according to Art. 468 (1) CC, funds allocated for assistance to employees shall be set aside from the property of the company and a foundation can be set up in accordance with the provisions of the civil law with the funds being the estate of the foundation.[276] As such, welfare funds or mutual assistance funds created for the benefit of employees are allocated to the foundation (or association) which in turn can invest in the stocks or other securities of the founding company. Thus, by using the provisions of Art. 468 (1) and 469 (3) CC it is possible to overcome the constraints of Art. 329 CC prohibiting a company to acquire its own shares. Furthermore, the foundation deed may provide that the property of the foundation shall consist of a debt to the company resulting in the possibility to credit finance the acquisition of shares by employees. According to Art. 469 (3) CC - even if the Articles of Association contain no provision - the General Assembly can decide that funds are to be set aside for creating and maintaining assistance funds for employees. After setting up a foundation or other organisation for the benefit of employees, the founder company can provide the resources either by payments from profits on the basis of a General Assembly resolution or from the optional reserves for social purposes. As a rule the allocations shall be regulated by the provisions regarding assistance funds determined by the Articles of Association. Employers' contributions to foundations (associations etc.) up to a maximum of 5% of the current year's profit that have been granted tax exemption by the Council of Ministers are tax deductible. Of course, employees can also contribute to the assets.

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[275] 329 CC widening the exceptions is under consideration; this, in consequence, might open the way for companies to acquire their shares for their employees, although, employee financial participation is not mentioned in the draft. In parallel the Capital Markets Law is subject to an amendment and in this case acquisition of own shares with the object to give them to their employees including by publicly held joint stock companies is apparently under consideration.

[276] In accordance with Art. 468 I and 469 III other than the aforementioned vehicle of a foundation also an association, a cooperative, a corporation or any other organisation for the benefit of employees may be used.

b) Profit-Sharing

Art. 323 of the Code of Obligations stipulates that any agreement can be set up by which a share in the profit is granted to employees in addition to their basic fixed wage. In publicly held joint stock companies this may only be the case where it is regulated by the Articles of Association (Art. 7 of a Communiqué of the CMB[277] hereinafter referred to as DivComm). In joint stock companies 10% of the net profit each year must be retained as a reserve until it equals 20% of the capital ('first allocation' Art. 466 (1) CC). If dividends to shareholders exceed 5% of the annual profit or if profit is distributed not as an entitlement from holding shares, e.g., to employees, foundations, management of the company, then an addition 10% of the amount of profit to be distributed must be retained as a 'second allocation'. Joint stock corporations with shares not traded on the stock exchange are required to distribute the first dividend principally in cash. However, companies that are not exempt from independent auditing[278] can distribute the first dividend in cash and/or in the form of bonus shares (share-based profit-sharing). Corporations which partly or wholly prefer share-based profit-sharing of the first dividend are required to obtain approval from their shareholders. Dividends of shareholders who did not exercise their right or had no opportunity to do so are paid out in cash. In cases of making donations or distributing profit shares to foundations (see the foundations discussed above in the ESOP section) another Communiqué of the CMB[279] further requires that these payments should not result in 'inconsistent' transactions[280], that information regarding the donations needs to be given to shareholders at the General Assembly and that the necessary information needs to be disclosed and published in the ISE Daily Bulletin.[281]

c) Participation in Decision-Making

Turkish companies are not required to include stakeholders in the corporate governance process, and there is no obligatory regulation about the participation of employees in the management of the company. However, roughly one third of traded companies do have a program for the participation of employees in the management (Küçükçolak and Özer, 2007, p. 9: Table 3, p. 12: Table 7).[282]

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277 On Principles Regarding Distribution of Dividends and Interim Dividends to be Followed by Publicly Held Joint Stock Corporations Subject to Capital Market Law; Serial: IV, No. 27 published in the Official Gazette No. 24582 dated 13 November 2001, see Art. 8.

278 In accordance with Art. 3 (a) DivComm of the Communiqué on Principles Regarding Exemption Requirements for Issuers and Removal from the Board's Register Serial: IV, No. 9 published in the Official Gazette No. 22154 on 27 December 1994.

279 Communiqué on Principles and Rules on Financial Statements and Reports in Capital Markets Serial: XI, No. 1 published in the Official Gazette No. 20064 on 29 January 1989.

280 Defined by Art. 15 (6) Capital Market Law: in the case of transactions with another enterprise or individual with whom there is a direct or indirect management, administrative, supervisory, or ownership relationship, publicly held joint stock corporations shall not impair their profits and/or assets by engaging in deceitful transactions such as by applying a price, fee or value clearly inconsistent with similar transactions with unrelated third parties.

281 According to Communiqué on Public Disclosure of Material Events Serial: VIII, No. 20 published in the Official Gazette No. 21629 on 06 July 1993, amended with Serial: VIII, No. 39 published in the Official Gazette No. 25174 on 20 July 2003.

282 Data results from a questionnaire based on the practices of corporate governance principles by the respondents, namely the Istanbul Stock Exchange (ISE) member firms and companies listed on the ISE, and a sta-

The Capital Markets Board of Turkey (CMB) Principles recommend that companies establish mechanisms and models to encourage stakeholders' participation in management, while giving priority to employees and without hindering the company's operations. The CMB Survey conducted in 2005, however, did not include any information on the proportion of listed companies that have adopted mechanisms providing for stakeholders to participate in management (e.g. through representation on the board or through an advisory council to the board) (OECD, Corporate Governance in Turkey: A Pilot Study, 2006, pp. 65 f.). Stakeholders who serve on the board would, under the law, have the same access and rights to obtain information as other board members.

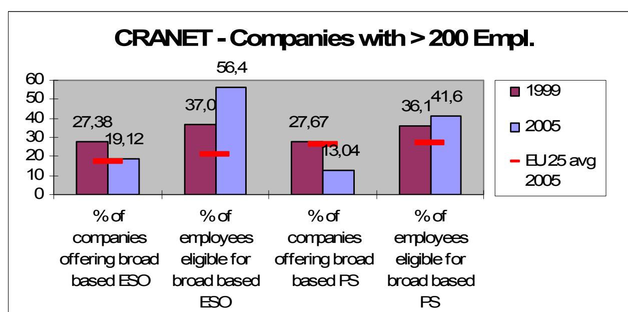
tistical evaluation of the findings. 115 members firms out of 205 and 243 ISE companies out of 308 were included.

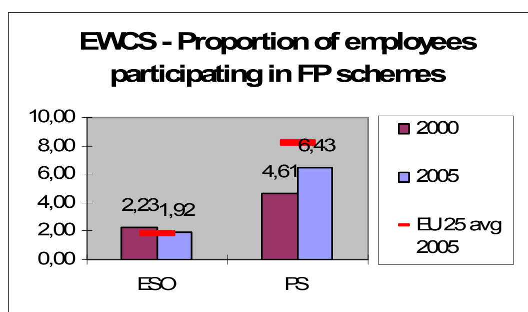
XXIX. United Kingdom

Profit-sharing plans first appeared in the UK at the end of the 19th century, while employee share ownership plans were introduced in the 1950s. These plans, however, remained small in number until the introduction of tax incentives in 1978. Approximately 5,000 companies currently maintain Inland Revenue-approved employee financial participation schemes.[283] With the abolishment of the last approved profit-sharing plan (Profit-Related Pay (PRP) or Approved Profit-Sharing Scheme (APS)) in 2002, the remaining approved plans, as well as numerous unapproved plans, are all share-based.

Approved plans operated in a 2006 breakdown as follows: Share Incentive Plans (SIP) - 830 (costs of the plan for the Revenue GBP 320 million); Savings-Related Share Option Schemes (SRSO) or Sharesave or SAYE Schemes - 960 with approx. 2 million employees (costs of the plan for the Revenue GBP 420 million); Company Share Option Plans (CSOP) - 3030, but with much less employees than SRSO (costs of the plan for the Revenue GBP 205 million); Enterprise Management Incentives (EMI) - 2570 with 27,000 employees (costs of the plan for the Revenue GBP 170 million).[284]

Many companies combine several approved plans and also operate unapproved plans, for which no statistics are available. Since approved plans are based on long-term holding and withdrawals which are not reported to HM Revenue and Customs, it is impossible to determine the exact number of employees participating in plans at a given moment.





283 www.ifsproshare.org, Log-in 10/19/2007.

284 www.hmrc.gov.uk/stats/emp_share_schemes/menu.htm, Log-in 10/9/2007. The difference between the data in the comparative tables and in the country profile is attributable to the last update of statistics by the HM Revenue and Customs. The costs of the plan are comprised of tax losses and National Insurance Contribution (NIC) losses.

1. General Attitude

Successive governments have committed themselves to supporting employee financial participation plans and promoting widespread share ownership for reasons both ideological and pragmatic. These include making enterprise more democratic, developing financial markets and fostering social welfare. The government, together with the London Stock Exchange and a consortium of major companies were the original founders of ifsProShare. This is an independent organization which promotes wider share ownership and financial education. It still plays an important role in promoting the interests of companies having financial participation plans, disseminating information on best practices and consulting with companies interested in setting up such plans.

The Confederacy of British Industry (CBI) and other employers' organizations generally support the employee participation plans proposed by the government, especially employee share ownership plans, but they have also criticized some approved plans for lack of flexibility. The government responded to this criticism by introducing the more flexible Share Incentive Plan. The CBI also set up a special task force to discover why employee shareholding has been declining since the 1990s. The government used these research findings to design new employee financial plans to reverse this decline.

Trade unions over the years have taken a dim view of employee financial participation on the grounds that it would undermine the traditional collective bargaining process. This was their reason for strong past opposition to Profit-Related Pay Schemes. Recently, however, they have changed their attitude. The Trades Union Congress (TUC) has declared itself in support of employee financial participation schemes that are broad-based, and if both employees and employee representatives are consulted before introduction. Recently some trade unions have themselves proposed new schemes of financial participation.

2. Legal and Fiscal Framework

All employee financial participation plans are divided in Inland Revenue approved and unapproved plans.. Plans introduced under the annual Finance Acts must be approved by and registered with Inland Revenue; they enjoy substantial tax and NIC exemptions, especially for employees, enumerated in the Income and Corporation Taxes Acts.

Unapproved plans may be introduced at the employer's discretion, but receive no special tax incentives. Approved plans must conform to law; unapproved plans are more flexible. Under current legislation, all approved plans (and typical unapproved ones as well) are employee share ownership plans. Unapproved plans are used for granting shares, options or cash equivalents that exceed legal maximums to individual employees or to employees not UK tax subjects. Unapproved plans are usually combined with approved plans. A plan with an approved and unapproved part is also possible.

a) Share Ownership

Share ownership plans can be approved and unapproved. There are four approved share ownership plans under the current legislation: one direct share ownership plan with several modifications (SIP) and three stock option plans (SRSO, CSOP and EMI). Whereas SIP and SRSO are broad-based, CSOP and EMI can be selective. Although unapproved plans are not regulated, there are certain types of plans which are most wide-spread: Long-Term Incentive Plans (LTIP), Restricted Share Plans and Unapproved Option Plans. Whereas LTIP and Restricted Share Plans are prevailingly used for executives, Unapproved Option Plans are often broad-based complementing an approved plan. In the following, only approved plans will be addressed.

Inland Revenue Approved Share Ownership Plan – *Share Incentive Plan (SIP)* was introduced by the Finance Act 2000 and replaced the PRP on which it is partly based. It is more flexible than previous plans due to several possible modifications and has longer holding periods to prevent tax evasion. The employing company has to set up a trust which attributes shares to the employees. The shares can be attributed for free ('free shares'), at a discount or at the full price ('partnership shares') and as a match by the employing company to the partnership shares ('matching shares'). Dividends on all types of shares can be reinvested in additional shares ('dividend shares'). Each modification is linked to specific requirements; if the requirements are met, substantial tax incentives both for employees and the employing company apply (generally, exemption from personal income tax and national insurance contributions). The plan must be applicable to all employees, with a possible exemption of employees who were employed by the company less than 18 months, and generally on the same conditions. The tax exemption applies to all modifications after a holding period of 5 years or if the employment ceases on an earlier date due to injury, disability, death, retirement, redundancy, transfer under the Transfer of Untertaking (Protection of Employment) Regulations 1981 or on the employing company ceasing to be an associated company. If the shares acquired under the plan are sold immediately after withdrawal, no capital gains tax must be paid. In the following, specific requirements are presented.

Free shares cannot be withdrawn from the trust during the holding period which can last from 3 to 5 years. However, if the employee withdraws the shares or the employment ceases for other than above reasons between the third and the fifth year, personal income tax and national security contributions are payable on the lesser of market value on the award date and the market value on the withdrawal/cessation date. If the employment ceases for other than above reasons before the end of the holding period of 3 years, full personal income tax and national security contributions are payable. The share of an employee in the plan is limited to GBP 3,000 per annum. Partnership shares are purchased using a part of the pre-tax remuneration of the employee according to the agreement between the employee and the employing company. The shares are purchased by the trust either within 30 days of pay deduction or of the end of a specified accumulation period of up to 12 months. If an accumulation period is agreed upon, the price of the shares is the lower of the market price at the beginning and at the end of the period. The share of an employee in the plan is limited to GBP 1,500 per annum. After the 5-year holding period or in the case of cessation of employment for the above reasons, the employee is exempted from paying the personal income tax, and the employer is exempted from paying the national security contributions. However, the employee is only exempted from paying the national security contributions if the total earnings are below the ceiling of national security contributions. If the employee withdraws the shares or the em-

ployment ceases for other than above reasons between the third and the fifth year, personal income tax and national security contributions are payable on the lesser of the amount of the employee contributions for purchase and market value of shares on the date of withdrawal/cessation. Matching shares can be offered by the employing company in the proportion up to 2 matching shares for each partnership share. They are allocated to the employee on the same day as partnership shares are acquired. As far as the holding period is concerned, the same rules apply to matching shares as to free shares. Up to GBP 1,500 of dividends per annum can be used to purchase dividend shares. The general holding period for dividend shares is three years. If the shares are withdrawn or the employment ceases for other than above reasons within 5 years of the acquisition of the shares in respect of which the dividend was paid, the employee is liable to personal income tax on the dividend payment used to purchase the shares. However, there is no liability to national insurance contributions.

Inland Revenue Approved Stock Option Plans – *Savings-Related Share Option Scheme (SRSO) or Sharesave or SAYE Scheme* was introduced by the Finance Act 1980 and is currently the most popular plan as far as the number of participants is concerned. It must be applicable to all employees, with a possible exception of the employees with a relatively short time of service. The basic structure of the plan is as follows: the employee enters into a Save-as-you-earn (SAYE) contract with a nominated bank or building society about saving a specified monthly amount (GBP 5-250) by deduction from after-tax remuneration for 3, 5 or 7 years and the employing company grants him share options over the maximum number of shares he will be able to purchase at the exercise price with his SAYE savings. The SAYE contract always includes a tax-free bonus added to the savings on completion, whose amount depends on the duration of the contract and whose rates are determined by the Treasury. The exercise price of shares can be up to 20% under the market value of the underlying shares at grant of the option. At maturity of the SAYE contract, the employee is entitled to choose whether he exercises the option and retains or sells the shares or takes the savings and bonus in cash. If these requirements are fulfilled, the employee is not liable to personal income tax at grant or exercise. However, he is liable to capital gains tax at the sale of shares.

Company Share Ownership Plan (CSOP) was introduced in 1984 as Discretionary Share Option Scheme (DSOP) and relaunched in 1996 under the current name with amended requirements. It is a discretionary plan which is often limited to the executives, but can also be broad-based. It is often connected to performance indicators, i.e. a performance condition must be met before the option can be exercised. The following requirements must be satisfied for approval: the value[285] of outstanding options per employee must not exceed GBP 30,000 at grant; the exercise price is not less than the market value at grant; the exercise period is not shorter than 3 and not longer than 10 years after grant.[286] If the requirements are fulfilled, the employee is not liable to personal income tax at grant or exercise.

Enterprise Management Incentives (EMI) was introduced by the Finance Act 2000 in order to help small higher risk companies to recruit and retain highly qualified employees. It is applicable to companies with gross assets less than GBP 30 million.[287] The plan can be selective; it was even restricted to 15 employees until 2002, but this restriction was abolished. No approval of the

285 The value is equal to the number of shares multiplied by the exercise price.

286 Before 2003, an additional requirement had to be fulfilled: the exercise period had to be not less than 3 years after any previous tax-free exercise. This requirement was abolished.

287 Originally, the volume of assets was GBP 15 million (until 2003), but it was considered necessary to substantially increase it.

Inland Revenue is required, but it must be notified of each award of stock options under EMI within 92 days. The total market value of options granted must not exceed GBP 100,000 per employee and GBP 3 million for the company. If the requirements are fulfilled, neither employees nor the employing company are liable to personal income tax and national insurance contributions at grant or exercise. However, they are liable to capital gains tax at the sale of shares.

b) Profit-Sharing

At present there are no approved or conventional unapproved financial participation plans in the form of profit-sharing plans. However, a few unapproved bonus schemes might be both broad-based and profit-connected; if so, they could be considered as cash-based profit-sharing plans.

There used to be an approved profit-sharing plan — Profit-Related Pay (PRP) or Approved Profit-Sharing (APS) — which was exceedingly popular until terminated in 2003. There were 14,275 of these plans in 1998, covering 4.6 million employees. The plan, however, was mainly used as a means of avoiding taxation. Since it did not lead to a wider employee shareholder base, while causing heavy tax loss, the government phased it out in 1999, and completely abolished it in 2002. It was replaced with the SIP in 2000. Some employees, however, may have yet to withdraw their shares from the earlier plan.

c) Participation in Decision-Making

There is no direct connection between participation in decision-making and financial participation of employees; in particular, financial participation plans cannot extend the existing rights in connection with participation in decision-making. General provisions of labour law, e.g. concerning equal pay and prohibition of discrimination, also apply to financial participation plans.

UK employees have no statutory right to representation at board level and, with very few exceptions, this is also the case in practice.

There is no common structure for employee representation in the UK and in many workplaces it does not exist. Unions are the most common way that employees are represented and they can now legally compel the employer to deal with them, but only if they have sufficient support. Most non-union workplaces have no employee representation, and the regulations implementing the EU directive on information and consultation are unlikely to change this.

Only a third (33.5%) of employees in the UK are covered by collective bargaining. In the private sector coverage is lower, at around a fifth. The key bargaining level is the company or the workplace. In the public sector, where two-thirds of employees are covered, industry level bargaining is more important.

Part 3 – Comments on the Benchmarking Results

I. Lessons from PEPPER I to PEPPER IV

Milica Uvalić

1. Introduction

'Financial participation' refers to various forms of participation of employees in enterprise results. It includes two main types of schemes: (1) profit-sharing, namely the sharing of profits by the providers of both capital and labour by giving employees, in addition to a fixed wage, a variable part of income directly linked to profits or some other meassure of enterprise results, which is paid either in cash or in enterprise shares; and (2) employee share ownership, including Employee Stock Ownership Plans (ESOPs), which assures employees an additional source of income related to enterprises results, either through dividends and/or the appreciation of employee-owned capital (Uvalić, 2001, p. 10). Over the last twenty years, the term has been used to distinguish these forms of employee participation from the more traditional forms which enable the participation of employees in decision-making, either through workers councils or co-determination on company boards (such as the most well-known system of Mitbestimmung in Germany). In 1990, a new abbreviation was also born to cover the various forms of financial participation, namely PEPPER – Participation of Employees in Profits and Enterprise Results.[288]

It is worth recalling that employee financial participation has been on the agenda of the European Union (EU) for almost two decades. In 1989, the Commission of the European Communities (CEC) decided to include employee financial participation among the priority objectives of its Action Programme for the implementation of the Community Charter of Basic

[288] The acronym PEPPER was proposed by Mario Nuti at the Workshop on Employee Financial Participation held in 1990 at the European University Institute in Florence.

Social Rights of Workers (Commission, 1989). This initiative led to the preparation of the first PEPPER Report (Uvalić, 1991), reviewing the experience with employee financial participation in the then twelve EU Member States. On the basis of the PEPPER Report, the EU Commission prepared a Recommendation on PEPPER which was adopted by the European Council in July 1992, inviting Member States to facilitate the spreading of PEPPER schemes in practice (Council of the EC, 1992). The information on individual EU countries experiences' was updated in the Commission's PEPPER II Report (see Commission, 1997). These first two PEPPER Reports described the variety of employee financial participation schemes that have developed in the EU Member States (the EU-12 and EU-15 respectively). More recently, the PEPPER III Report (Lowitzsch et al. 2006) extended the previous two reports to describe the experience with the application of financial participation schemes in fourteen countries - the twelve new EU Member States that entered the EU in 2004 and 2006, and the two Candidate Countries.[289] Finally, this report gives the most recent assessment of financial participation in the whole EU, reporting for the first time comparable empirical data for all the EU-27 Member States and two Candidate Countries (Croatia and Turkey).

From a historical perspective, it should be stressed that the general environment for the development of financial participation has been very different in the older with respect to the younger EU Member States. This is why it seems important to share the rich experience gained with PEPPER schemes in the EU-15 with the new and incoming EU Member States. Due to the specific pre-1989 socialist legacy, PEPPER schemes of the type known in the developed market economies have had no tradition in Central and Eastern Europe. As illustrated in the PEPPER III Report, employee share-ownership has been the prevalent type of scheme implemented during the 1990s, and this for very different reasons than those which have motivated the introduction of schemes in some of the older EU Member States. This renders the task of diffusing information on employee financial participation from the older towards the new EU Member States even more important.

This chapter aims to discuss some of the main lessons to be drawn from the experience with employee financial participation accumulated in the European Union over the last several decades. In what follows, the principle reasons why employee financial participation has been promoted are briefly recalled (section 2). Next, the main characteristics of PEPPER schemes, as reported in the PEPPER I through PEPPER IV Reports, therefore the experience of both the old and the new EU Member States and Candidate Countries, are examined (section 3). The paper ends with a few concluding remarks regarding the general framework of PEPPER schemes in the EU (section 4).

2. Why Promote PEPPER?

Government policies promoting PEPPER schemes have usually been motivated by the desire to introduce greater flexibility in payments systems and by commitments to a property-owning democracy and peoples' capitalism, as was the case in the UK in the 1980s. The deeper mo-

[289] Cyprus, Czech Republic, Estonia, Hungary, Lithuania, Latvia, Malta, Poland, Slovakia and Slovenia as countries that joined the European Union on May 1st 2004, Bulgaria and Romania, which became EU Member States in January 2007, and Croatia and Turkey as Candidate Countries.

tives for promoting PEPPER schemes, however, are found in the rich theoretical literature on the potential benefits of employee participation in enterprise results.[290] The theoretical arguments in favour of employee financial participation are based on two main groups of positive effects which are expected from such schemes.

First, employee financial participation is likely to improve workers' incentives. The change from a rigid system of guaranteed wages in which rewards are independent of effort, to a system which provides employees with a part of income directly linked to enterprise performance, will increase individual motivation and commitment, and will provide for greater identification of employees with the interests of their firm, thus resulting in higher labour productivity and improved overall enterprise efficiency. In the case of employee ownership schemes, employees will be more interested in enterprise performance if they receive dividends or can gain from the appraisal of the value of their shares (Uvalić, 1991).

Second, financial participation schemes provide more flexible systems of remuneration, since a part of employee earnings is variable and depends directly on enterprise performance. More flexible remuneration is expected to enable more flexible employment policies, and as such could contribute to lower unemployment. In the case of employee share-ownership, enterprises may also be able to offer lower wages, since workers will be receiving a part of their income as shareholders; the wage that management must offer workers to persuade them to accept it will be lower if employees are likely to lose capital gains and dividends by rejecting the wage offer. Wage moderation may in turn lead to less variable employment policies, which can lower the risk of unemployment.

There is also a more practical reason for promoting employee financial participation in the EU. Since PEPPER schemes were more diffused, in the 1980s and the 1990s, in the two countries which are the EU's main competitors - the United States and Japan - their wider use in the EU Member States is considered a potential source of increasing EU competitiveness. Although more recent estimates suggest that there may be more schemes in the EU than elsewhere (see Pérotin and Robinson, 2003), this argument has not lost its relevance. In view of the EU objectives laid down at the Lisbon (2000) and Barcelona (2002) European Councils, of making the EU the most competitive and dynamic knowledge-based economy in the world, any scheme that has the potential of contributing to increasing enterprise competitiveness in the EU Member States is clearly of paramount importance.

3. Lessons from PEPPER I to PEPPER IV

We will point to some main lessons to be drawn from the long experience with employee financial participation in the EU. As in the PEPPER reports, we will focus on four main issues: (1) the general attitude of the government and social partners towards PEPPER schemes; (2) the existing legislative framework; (3) diffusion of PEPPER schemes; and (4) evidence on their effects. The very different political, economic and historical context before 1989 in Western and Eastern Europe has fundamentally influenced all relevant issues regarding PEPPER

[290] There is an enormous literature on these arguments. For a survey, see Bartlett and Uvalić (1986), Bonin and Putterman (1987), or Uvalić (1991).

ever since. This is why these issues will be discussed separately for the old and the new EU Member States.

a) General Attitudes

In the older EU Member States, we find a variety of positions of governments, trade unions, and employers associations on PEPPER. Whereas in countries such as France and the UK, PEPPER schemes have had a very long tradition and have been supported by specific legislation as well as fiscal incentives, this has not been the case in many other EU countries. One of the most intriguing questions, therefore, is why in many EU countries has there been lack of support of PEPPER schemes by governments and/or social partners.

There are essentially two groups of reasons why financial participation has not been actively promoted in individual EU countries. The first reason is simple, as it derives from the lack of interest, and the consequent absence of any position (in favour or against) employee financial participation. The second reason is more complex and derives from the very different understandings of the potential benefits and risks of financial participation schemes, as will be briefly illustrated below.

There is an enormous heterogeneity of views of governments, trade unions, and employers associations, some fiercely against and others in favour of financial participation. Traditionally, the strongest critisizers of PEPPER schemes in several west European countries have been the trade unions, though for different reasons in the various national contexts. Trade unions have opposed financial participation because they feared that it would provoke more inequality in workers earnings, or because of the dual risk involved of workers losing both their jobs and savings in case of enterprise closures. In countries like France or Germany, some trade unions have been strongly opposed to primarily employee capital ownership, regarding radical changes in the economic system the only way to secure a more equal distribution of wealth. In France and in the UK, not only trade unions but also parties to the left have strongly opposed financial participation because it was the conservative governments in both countries that have promoted PEPPER schemes and have pushed for the adoption of specific legislation. In many other EU countries trade unions have accepted PEPPER, but have argued that schemes must remain outside the framework of collective bargaining and must represent an addition, and not a substitute, to wages.

The rethorics has increasingly changed in recent years. Contrary to the situation in the late 1980s, today many trade unions recognize that capital and labour may pursue similar interests. It has become acknowledged that employee financial participation can strenghten workers incentives, improve intra-firm human relations, and increase wage flexibility. In France in recent years, the political forces to the left have, for the first time, legitimised PEPPER schemes, recognising they can provide a better division of value-added in the interest of the labour force without loss of competitiveness of the enterprise, thanks to the variable nature of profit-related bonuses and their excemption from social security contributions. Financial participation is sometimes also regarded as an important instrument for enriching the social contract and social dialogue. PEPPER schemes are viewed as a means to increase employee remuneration and redistribute power in their favour.

Regarding the position of employers associations in the older EU Member States, they have usually supported voluntary PEPPER schemes and opposed any binding arrangements. Some employers associations have also argued for the introduction of tax incentives, considering

PEPPER schemes an important instrument for improving employee motivation and commitment. Employers confederations most frequently accept financial participation, regarding it a means for obtaining a closer identification of employees with their enterprise, offering workers a personal stake in their company, and increasing intra-enterprise cooperation. There are, however, employers associations which do not actually have a concrete standpoint on PEPPER, primarily in those EU countries where financial participation has not been very widespread.

In many old EU Member States, PEPPER schemes have become part of a new culture of industrial relations based on innovative managerial strategies and more flexible remuneration policies. There has been an unusual convergence of economic thought from opposite ends of the political spectrum. On the left, with the collapse of state socialism as an economic ideal, workplace democracy has emerged as the principal institutional reform that commands widespread support among critics of capitalism; employee control of enterprises, it is hoped, will succeed where state control has failed in equalizing power and wealth and in decreasing worker alienation and exploitation. On the right, in turn, there has been an increased discouragement with the efficiency of traditional forms of labour-management relations, and in search of an alternative, many have turned to employee ownership (Hansmann, 1990, p. 1751). Minority employee ownership within traditional firms has thus been accepted by both left and right-wing political parties, including many trade unions which have traditionally opposed it. Its advantages are particularly stressed within the context of property owning democracy, which ought to ensure more widespread ownership than traditional capitalism.

Passing to the new EU Member States, the general attitudes towards PEPPER schemes of governments and the social partners are remarkably different than in the older EU countries, particularly in the countries from Central and Southeast Europe (CSEE). The general attitudes towards PEPPER schemes have been strongly influenced by the legacies inherited from the communist times and the priorities imposed by the post-1989 transition to multiparty democracy and market economy. The specific political and economic system that existed before 1989 in the CSEE countries has also crucially shaped a number of important institutions, including trade unions and employers associations. Thus during communism, the political influence, bargaining power and role of trade unions and employers associations were marginal; although there was practically a 100% rate of workers unionisation in most CSEE countries, this had little meaning since trade unions did not have any power to influence wage levels or other issues regarding working conditions.

As part of the historical turn in 1989, a radical trasformation of institutions such as trade unions and employers associations has also taken place throughout CSEE. However, these changes have most frequently led to the adoption of a hyper-liberal economic and social model, with particularly flexible labour markets, weak trade unions and scarse diffusion of collective bargaining (see Nuti, 2007). Thus the model of industrial relations adopted in CSEE resembles primarily the UK model; in practically all CSEE countries except Slovenia, less than 50% of workers are covered by collective bargaining and only a small percentage of the workforce is unionised.

This background in part explains the lack of interest for employee financial participation in the new EU Member States from CSEE. The various forms of employee participation, whether in decision-making or in financial results, are frequently viewed as not fitting into the new model of liberal social and industrial relations. Employee financial participation is erroneously regarded as a leftist idea and related to the concept of self-management and workers manage-

ment rights that existed in pre-1989 Yugoslavia, Poland and Hungary. The word 'participation' is most frequently misinterpreted and its promotion confused with the desire to re-introduce outdated concepts and practices which have long been abandoned. Consequently, employee financial participation has hardly ever appeared on trade union's policy agenda, only in a few CSEE countries have trade unions actually promoted employee ownership within the privatisation process, and they have not developed institutions to protect employee shareholders. Trade unions have been particularly critical about profit-sharing, since the deep economic crisis which accompanied the transition has clearly not favoured the introduction of profit-sharing. The fall in living standards has led workers to primarily claim higher basic wage increases, rather than flexible profit-sharing bonuses.

As to employers associations in the CSEE countries, their position on PEPPER has been passive and in most countries has not yet developed into a clear official standpoint. Though this seems to be the prevalent case, there are exceptions, such as the employers association in Slovenia which recently has been trying to obtain tax concessions from the government for enterprises implementing financial participation.

The main conclusion that can be drawn from the ongoing analysis is that in both Western and Eastern Europe arguments advanced against employee financial participation have been prevalently political in nature. However, the reasons for rejecting financial participation in the former communist countries are entirely different than those encountered in the older EU Member States. In the CSEE countries, the rejection derives primarily from a basic misunderstanding regarding the nature of PEPPER schemes.

b) Legislation

The experience with profit-sharing and employee share-ownership in the older EU Member States clearly confirms that schemes have been most diffused in those countries where concrete legislative measures have been introduced to support them (e.g. in France, the UK or Ireland). The lack of specific legal provisions on employee financial participation, which would provide a different fiscal treatment or other type of incentive, seems to have been a major obstacle for its introduction.

This has also been the case in the CSEE countries, as illustared in the PEPPER III Report (see Lowitzsch et al., 2006). Given the lack of more general support for financial participation in the CSEE countries, if we exclude privatization laws which have favoured he acquisition of shares by employed workers, there have been limited cases of legislation promoting PEPPER schemes. Those countries with privatisation laws envisaging the sale of shares at privileged terms to insiders have also been the countries that ended up having a substantial number of firms owned by employed workers and managers (e.g. Poland or Slovenia). The existence of privatisation laws favouring acquisitions by employees at privileged conditions has been fundamental for the diffusion of employee share-ownership throughout CSEE.

The findings of all the PEPPER Reports have suggested that there are not many legal obstacles for the introduction of financial participation schemes in the EU. However, the adoption of a framework law promoting PEPPER has always proved useful, as it has offered the general legal framework to guide enterprises in their adoption of financial participation. One of the main lessons of the PEPPER Reports is that specific legislation on PEPPER is important. Although there have been cases where financial participation schemes have been applied by enterprises even without legislation on PEPPER (as for example in Italy), the experience ac-

cumulated so far in the majority of EU countries suggests that the adoption of schemes has been greatly facilitated if there were concrete laws to promote them. Employee ownership and profit-sharing have spread particularly in those countries where there were laws to promote and support them – as in France and the United Kingdom, or in Poland and Slovenia.

c) Diffusion

In the older EU Member States, a favourable general attitude within a given national framework has usually led to some supportive legislation on PEPPER, and this has clearly facilitated the spreading of schemes in practice. This has been the case in all EU countries where PEPPER schemes have been rather diffused, such as in France and the UK, suggesting a clear link between general attitudes, favourable legislation, and diffusion of schemes in practice. In the four largest EU countries, around 19% of private sector employees are covered by some form of financial participation (Pérotin and Robinson, 2003). It is interesting to note that in France, the country where PEPPER schemes have had the longest tradition, in recent years the share of variable pay has increased,[291] confirming a tendency to pay increases in workers income increasingly through variable remuneration.

In the CSEE countries the situation is quite different. As illustrated in the PEPPER III Report (Lowitzsch et al. 2006), it is primarily thanks to the privatization of many state-owned firms in the 1990s that we have seen widespread employee share ownership in most CSEE countries (all except the Czech and Slovak Republics). The fact that employees were frequently offered privileged conditions for buying shares of the enterprise of employment was not determined by convinctions of employee ownership being an instrument to strengthen incentives, but because this method of privatisation was chosen by default. In the absence of other potential buyers, sales of enterprise shares to insiders was a frequently used method in many countries, leading to a number of employees becoming shareholders of their firm. Moreover, in most CSEE countries, the importance of employee shareholding has substantially declined over time, as workers chose to sell their shares to external owners upon expiry of the imposed time limits. Since the mid-1990s, the general trend has been a decline in both the share of employee ownership within firms, and in the number of employee-owned firms. Dominant employee ownership has survived in a relatively small number of firms, although most CSEE countries still have a number of firms with some proportion of employee-owned shares.

The PEPPER III Report has also shown that there has been little profit-sharing in the new EU Member States. Although company laws in most CSEE countries do envisage the possibility for firms to introduce some form of profit-sharing, in practice it seems that this possibility has been used only in some countries. Where implemented in CSEE, profit-sharing has been introduced on a purely ad hoc basis, rather than in a systematic way assuring regularity in its application (as e.g. in France).

Some of these trends are confirmed by the most recent data provided in this report. The report has tried to fill some of the gaps which derive from unsatisfactory general statistics on the application of PEPPER schemes in the EU Member States. Given that national statistics on the diffusion of PEPPER in individual countries are generally poor (with the exception of a few countries like the UK and France), whereas sources such as CRANET or the European

[291] Profit-sharing bonuses have increased from 3.1% in 1996 to 4.5% in 2003 of total pay, while 'participation' schemes from 3.8% to 4.6%.

Working Conditions Survey (EWCS) are very broad international surveys, which include only some questions focusing specifically on financial participation and do not cover all EU countries, this report has tried to compare all available data on financial participation and to collect comparable indicators for those EU Member States for which data were not provided elsewhere.

The results reported in this report confirm some of the findings of the previous PEPPER Reports. Among the many findings is that in 2005, broad-based employee share ownership was very frequently present in large firms in countries such as Poland, Bulgaria, Denmark, Croatia and France, whereas profit-sharing was diffused primarily in France, Finland and Germany. Interestingly, some of the desirable characteristics of profit-sharing – that it is paid on a regular basis and according to a predefined formula – were found to be frequently absent in many enterprises introducing profit-sharing. This report also gives comparable indicators regarding employee coverage by various types of financial participation schemes, diffusion of employee share-ownership and profit-sharing by enterprise size and sector, and changes in some of these indicators that have taken place from 1999 to 2005.

d) Empirical Evidence

The main conclusion that can be drawn from existing empirical evidence from both the old and the new EU Member States is that no straightforward generalisations are possible regarding the effects of PEPPER. There is ample evidence from western market economies that employee share-ownership and profit-sharing have had positive effects on workers incentives and productivity (see, e.g., Blinder (ed.), 1990). The evidence from CSEE countries is of more recent origin, it is much more limited, and it is almost exclusively based on the experience with employee share ownership. There have been studies on some CSEE countries – including the Baltic countries, Poland, Hungary and Slovenia - indicating that the post-privatization performance of employee-owned firms has been similar to that of other types of firms (see Uvalić and Vaughan-Whitehead, 1997), though there have also been other studies reporting less optimistic results (for a broad survey, see Djankov and Murrell, 2002). New empirical evidence is clearly needed from both the old and the new EU Member States before further conclusions can be drawn.

4. Concluding Remarks

The ongoing analysis allows us to point to the main differences between the experience with employee financial participation in the older EU Member States from Western Europe, and the younger EU Member States from Central and Southeast Europe. These key differences are summarised in Table 6.

Table 6. Main differences in PEPPER across the European Union

Old EU Member States (West)	New EU Member States (East)
Long tradition (since the 1950s).	A recent phenomenon (1990s).
Variety of different forms (PS, ESO, ESOPs).	Almost exclusively ESO, through privatization.
Actively promoted in a number of countries, also on a continuous basis (regularity).	Only ESO promoted, but as a one-off measure (through privatization). Profit-sharing either not considered, viewed with suspision, or introduced on an ad hoc basis (no regularity).
Advantages seem to have outweighted the disadvantages.	Empirical evidence inconclusive, still very limited and prevalently on ESO.

Returning to the question posed initially - how to explain the lack of general support for PEPPER by governments, trade unions and employers associations, and the corresponding absence of supportive legislation which also explains the limited diffusion of PEPPER schemes in many EU countries - three groups of factors seem important:

(1) Lack of information: in many EU countries, little is known about the positive experiences gained with PEPPER in France, the UK, or elsewhere;

(2) Rejection of PEPPER on ideological grounds: PEPPER is confused with leftist ideas such as self-management, and is not considered or acknowledged as part of modern managerial practices;

(3) Economic conditions in the new EU Member States have not facilitated the introduction of PEPPER schemes, thus favouring the standard wage employment contract.

It is important to remove the ideological barriers to the diffusion of PEPPER schemes, also by facilitating the spread of general information about successful examples of implementation of financial participation. The EU could play an important role in this regard, by continuing to promote employee financial participation in the now enlarged EU, as a follow-up of its earlier initiatives in this area. By informing governments and policy makers in the new Member States and Candidate Countries of its various PEPPER initiatives, by reporting on the rich experience gained in many EU countries reported in the PEPPER I to PEPPER IV Reports, and by indicating the positive effects such schemes have had in a variety of national settings, such action could contribute to a more widespread diffusion of employee financial participation in the enlarged EU.

In chosing the most appropriate PEPPER schemes, enterprises throughout the EU have numerous options available – from profit-sharing schemes in cash or in shares, to various forms of employee ownership, including Employee Stock Ownership Plans. These various types of PEPPER schemes could interact and be implemented simultaneously, depending on the specific needs and context.

However, since the success of PEPPER schemes can depend on certain key features, the experience accumulated in the older EU Member States should probably be taken into account. In the first PEPPER Report it was recommended to adopt schemes of a certain type, with some key characteristics (Uvalić, 1991, pp. 194-6). The ten general characteristics of financial participation that were recommended in the PEPPER I Report, which were subsequently also

adopted in the European Council 1992 Recommendation on PEPPER, are therefore worth recalling again:

(1) Regularity in application: PEPPER schemes ought to be applied by enterprises on a regular basis;

(2) Pre-determined formula: Employee benefits from PEPPER ought to be calculated according to a predetermined formula;

(3) Supplement to wages: Employee benefits from PEPPER must represent an addition and not a substitute to wages;

(4) Calculation of employee benefits: The amount which employees receive on the basis of PEPPER should not be fixed in advance but ought to be variable, linked to some measure of enterprise performance;

(5) Beneficiaries: PEPPER should benefit primarily employees, and ought to be made available to all or the larger part of employees;

(6) Enterprise type: PEPPER should be applied in all types of enterprises, both private and public;

(7) Enterprise size: PEPPER should be applied in all enterprises irrespective of size; sufficient opportunities ought to be created for bringing schemes within the reach of small and medium-sized firms;

(8) Simplicity: It is advisable to avoid PEPPER schemes of a very complex nature;

(9) Employee information and education: For the success of any type of PEPPER scheme, it is important to supply adequate information to all employees concerned;

(10) Voluntary nature of PEPPER schemes: Participation in PEPPER schemes should not be imposed either on companies nor on employees.

These are some of the main elements to be taken into account when applying employee financial participation schemes in the future, in line with the European Council's Recommendations on PEPPER adopted in 1992.

II. Financial Participation and the Work Challenges of the 21st Century

Daniel Vaughan-Whitehead

1. Introduction

No doubt the literature on workers' financial participation is rich and has helped to better identify the scope but also the incidence of the different forms of workers' participation in enterprises' profits and results. These studies have helped the policy makers to better identify the potential benefits and eventual risks related to the use of these schemes. This led in particular to the action decided by European institutions –notably the European Commission and the European parliament– in favour of financial participation and consequently motivated more governments in the EU to introduce such motivational schemes.

Nevertheless the use of workers' financial participation seems to have reached an important cross road. First as it was recently reviewed (PEPPER III) the latest EU enlargement waves have shown how poorly developed financial participation schemes are in the 12 new EU Member States. But beyond this, financial participation has to be reconciled with a new international environment and a new world of work that is changing radically not only in the new EU Member States but in Europe as a whole. While many studies on financial participation have focused on the economic impact of these schemes, what we propose here is of a different nature. It is important to better define the new context in which financial participation has now to evolve. This will allow us to identify on the one hand what new obstacles may limit the recourse to financial participation schemes and on the other hand what new challenges may encourage them in the future. The analysis includes the two main forms of financial participation, profit-sharing schemes and employee-ownership schemes along two main questions: Will profit-sharing remain an important payment mechanism and what elements in the new world of work in Europe could eventually modify its scope and incidence? Will employee-ownership schemes continue to attract both employers and employees in a constantly changing labour market?

The following sections present some of the main trends – in terms of policy issues, globalisation or changing work patterns – that we believe may influence in one way or another the development of financial participation schemes (see summary in Table 7). This will allow us to discuss some of the challenges that must be faced for further developing financial participation schemes.

Table 7. The new world of work and the new obstacles and opportunities for Financial Participation (FP), Profit-Sharing (PS) and Employee Ownership (EO) Schemes

The 10 new work challenges	Obstacles to PS and EO development	Opportunities for PS and EO development
Feature 1. - Deregulation of the labour market - Tax incentives mainly related to job creation	Less (legal and tax) incentives for promoting PS or/and EO	Governments and employers could be more keen in providing incentives if the advantages of PS and/or EO were better highlighted
Feature 2. - External flexibility prevailing	- Wage flexibility less attractive than employment flexibility - High employees' turnover act as disincentives to PS and EO in the company	- Negative effects of external flexibility may highlight the benefits of internal flexibility (with PS and EO representing key policy tools) - FP to be integrated in flexicurity agenda
Feature 3. - Increased recourse to atypical work contracts	Fragmented labour force not favourable to PS and EO schemes Higher fraction of the labour force not covered by FP	PS or/and EO for all may offer an opportunity to overcome dual labour force
Feature 4. - Along globalisation unequal distribution of growth - Wage moderation - Wages often a residual payment along the supply chain	- Squeezed wages do not leave much space for PS; - EO more risky investment because of profits more volatile and less dependent on workers' efforts	- PS could offer a means to better redistribute part of the profits to the workers - EO could motivate workers in global operations if complementary and not a substitute to basic wage. - Both schemes would help workers to better benefiting from global growth
Feature 5. - Increased number of low wage earners and of working poor - Increased wage disparity	- Workers look for basic wage increases rather than FP - Look for immediate return and not from long term EO - Lack of trust in these schemes because of declining living standards and purchasing power	- In a context of low pay, PS could provide a useful tool for automatically increasing wages when and where profits increase - EO could act as useful complementary pay if investment into EO not coming from basic wage (but from PS for instance or savings plans)
Feature 6. - Outsourcing and recourse to migrants to reduce labour costs - Greater volatility of profits	- Main aim is to reduce costs and employers generally not keen in implementing PS - Workers should be aware of EO risks and decide accordingly - Higher labour force turnover not favourable to FP	- PS and EO could prove to better motivate the labour force (skilled and unskilled) - PS and EO would help ensuring a climate of trust and dialogue (one of the flexicurity common principles) - These schemes should be applied to all.
Feature 7. Longer working hours as source of workers' additional income	-PS neglected by the workers (and the employer) for improving workers' income - EO not leading to immediate cash income	- PS could be related to hours worked - FP could improve work intensity without de-motivating workers - Longer working hours is rather an element of internal flexibility (so could be combined with profit-sharing)
Feature 8. Changes in work organization with increased shift work and unsocial hours	Create differences between the employees (between those working unsocial hours and those who do not) and is thus not optimal for FP development	- FP schemes could take into account such organizational changes - FP could help motivating workers toward new work organization - Workers could better accept unsocial hours because sharing companies' profits and capital

Feature 9. - New types of jobs in services (homework for elderly people, telework, self-employment etc.)	- New relationship 'worker-client' (replacing the 'worker-employer' one) for which PS and EO cannot be much applied - An increasing % of labour force will be excluded from PS/EO (self-employed etc.)	- The challenge is to identify ways to introduce FP in these new types of services - FP continues to be promoted in large firms - FP could also become an important tool in SMEs to motivate the labour force
- New types of workers	- Migrant workers, interim agency workers who are generally under different work and employment conditions	- PS and EO could be applied to all these workers if employer's willingness - Would reduce labour force fragmentation
Feature 10. Weakening social dialogue	- More difficult to distinguish PS and wage bargaining - Employers' temptation to use it as a substitute for basic wage increases - Trade unions more reluctant to implement PS	- PS may play an important role in wage bargaining provided that risk of income loss for the workers is avoided or limited - EO should be kept separate from wage bargaining to provide additional source of income

Source: table compiled by the author.

2. Policy Issues: The Challenges for Financial Participation

a) Toward a Shrinking Number of Incentives Provided by Public Authorities?

As emphasized in several EC reports, the provision by the authorities of initiatives for promoting financial participation schemes is essential to the growth of these schemes. It is quite significant that these schemes have developed the most in France and the UK where there has been specific legislation by the government to encourage this type of schemes.

It is on this ground that the European Commission advised the governments (see EC, 2002) to develop all different means at their disposal for encouraging enterprises to develop such schemes. Three main means at disposal of the state can be distinguished:

1) The elaboration of a law that provides a frame for enterprises to implement[292] and promote such schemes;

2) The provision of tax incentives generally both for employers and the workers is a policy tool that has also proved to be performing with regard to the development of financial participation;

3) The setting-up of a general public campaign in favour of the development of these schemes has generally accompanied the above two means to ensure their success and widespread implementation.

However, the context in the EU over the past decade did not seem to be very favourable to such three types of initiatives from the governments. The existence of high unemployment rates in the 90s has led most governments to place their fight against unemployment at the

[292] In France for example the deferred profit-sharing law does also provide a concrete formula to be followed by all enterprises with more than 50 employees.

core of their governmental action, an approach that the prospects of a world financial crisis may further strengthen. Tax incentives were mainly provided to enterprises, generally SMEs, that could create new jobs. Limited economic growth – or even recession in a few of them– also imposed governments some more restriction in the use of tax incentives. The legislative route seems to be difficult, first at the EU level since the European Commission has declared that no new legislation especially in the social field should be adopted at the EU level (Verheugen, 2005). Similarly national Member States may be reluctant to adopt new legislation – although the experience is rather mixed so far (see Part 1, Chapter I, Table 2) – but rather aim at reducing regulations on the labour market with the hope that more freedom given to enterprises to hire and fire will induce them to create more jobs and generate a more fluent labour market. In fact where new labour legislation is put in place it is generally to modify the hiring and firing conditions or to encourage new forms of atypical employment. New labour law is thus aimed more at deregulation than at 'protecting' workers.

At the same time however a too extreme shift toward external flexibility has led to new legislation aimed at 're-protecting' the workers as was the case recently in the UK where new legislation was introduced to better regulate the use of interim agency operations with migrant workers or to better limit the abuses of the 'gang-master' phenomenon. Similarly in the last few years several national governments have introduced (UK, Ireland, Cyprus) or are discussing the possible introduction of (Germany) a national statutory minimum wage to avoid social dumping brought by migrant workers in terms of lower pay and lower working conditions. In the same vein financial participation could be further encouraged by national governments either by labour law or through tax and company laws aimed at compensating some adverse effects on workers' de-motivation brought by higher work intensity, unsocial hours, atypical forms of contract. Financial participation – by covering all employees – could also represent the cement to avoid a dual labour force between permanent and temporary workers. All would be concerned by the good financial health of the company they are working for, even on a short-basis. The new context could thus be favourable to public authorities' initiatives to develop financial participation schemes.

b) Internal vs. External Flexibility or Toward a More Complex Framework?

The public authorities' willingness to curb unemployment figures has led them to favour the process of entry and exit from the labour market and the promotion of an 'external flexibility' model. Since profit-sharing schemes do mainly represent an element of 'internal flexibility' that allows wages to go down in a period of economic downturn and help the employer to keep his margins – by automatically decreasing its labour costs – without having to reduce the labour force, several studies have shown that profit-sharing could bring wage flexibility and employment stability, a process that can lead to better human capital and higher workers' motivation. If employers however were encouraged by public incentives to rather opt for using employment rather than wages as the flexibility route this may lead to a higher turnover in exit and entry on the labour market but undoubtedly lead to greater employment instability. This high rotation of the labour force is contrary to the original aims of profit-sharing of creating loyalty and motivation among employees by ensuring them employment stability in exchange of wage flexibility. The current context of employment policy may thus be interpreted as not favourable to profit-sharing but also employee-ownership schemes – as a tool to create a long-term partnership between labour and capital. At the same time policy makers have also in-

creased their recourse to longer working hours which clearly represent an element of internal and not external flexibility, so that the policy framework is more complex than expected.

In such a context financial participation may clearly have an important role to play, first to compensate some of the negative effects of external flexibility on workers' motivation, and second to accompany in a smother way some of the work organization changes such as longer working hours, unsocial hours, and shift work. Financial participation could for instance be integrated in the flexicurity debates which are precisely aimed at helping the employers to move toward a better employment and investment environment while also helping the workers to preserve their basic interests and concerns. In fact financial participation schemes could precisely help to put into implementation many of the common principles of flexicurity retained by the heads of states and governments of EU Member States, such as 'a better balance between external and internal flexibility', 'a climate of trust and dialogue', 'a better workers' adaptability capacity' (EC, 2007).

c) Increased Recourse to Atypical Work Contracts

Many governments in the EU in their attempts to 'deregulate' their labour markets promoted different forms of atypical employment: fixed-term contracts, part-time work, employment through interim agencies and – a category which deserves particularly careful analysis – self-employment. Most employers' federations had been pleading for years for such more flexible labour contracts.

While open-ended contracts remain most common, the rise of fixed-term contracts affects the majority of EU countries. First, **fixed-term employment** increased from 12.1% of total employment in 1998 to 14.2% in 2005 in the EU-25.[293] Another form of temporary work particularly worth taking into consideration is **agency work**.[294] Temporary agency work is still a new form of employment in most eastern European Member States. It is often considered that this is due to the use of other forms of irregular contract and particularly 'self-employment' (employment on the basis of civil contracts rather than employment contracts). However, agency work is on the rise. **Part-time contracts** may also provide another source of flexibility. In some countries it has been developed as a flexible arrangement to improve the labour market situation. Part-time work has increased in most EU countries, rising from 15.8% of total employment in 1998 (EU-25 average) to 18.4% in 2005 in the EU-25.[295] Finally, **self-employment** is a very heterogeneous category.[296] Globally, it has increased slightly but steadily over the last decade, representing 10.3% of total employment in 2005 in the EU-25. Case studies show that this type of self-employed are often regular employees who have been asked by their employer – mainly to avoid social contributions and taxes – to shift from a regular employment contract to a self-employment contract. This is also the case in construc-

[293] It became even more widespread in the 12 new Member States, with a percentage of 15.6 compared to 14.0% in the EU-15.

[294] Agency work is most prevalent in the UK, then in Luxembourg, the Netherlands and France, followed by Belgium, Denmark and Finland.

[295] Part-time work may be a positive choice, mainly for the purpose of finding a better balance between work and family. In some cases however it is imposed. We can observe an increase in the percentage of 'involuntary' part-time workers (Eyraud and Vaughan-Whitehead, 2007).

[296] The self employed can be employers (self-employed with employees) or individual workers under a self-employment contract (self-employed without employees).

tion, which in many countries represents the second largest proportion of self-employed without employees after agriculture. The concerns of the European Commission regarding this problem were expressed in a recent report on free movement of workers across the enlarged EU: 'The problem of persons posing falsely as self-employed workers to circumvent the law should be dealt with by Member States' (EC, 2006b).

This review has shown the increase in all dimensions of non-standard contracts. While it continues to concern a minority of workers, quantitatively as well as structurally, it has become a major feature of the labour market. This clearly is influencing the development of financial participation which is more adapted to a core and not peripheral labour force. One of the basic principles of profit-sharing and employee-ownership is in fact to cover all workers and not only the core labour force. A greater fragmentation of the labour force is thus rendering more difficult the implementation of such basic principle. It may be difficult – and may be inefficient – to try covering self-employed or even workers on stand-by projects who clearly feel less concerned – because of their disadvantaged employment status – by the profitability of the company.

On the other hand profit-sharing and employee-ownership for all employees may offer an opportunity to overcome the tensions within this dual labour force. Despite their different employment status and different wage treatment all workers employed by the company could feel committed to the enterprise through some sort of financial participation schemes and other participatory practices (for instance in decision-making). Extending financial participation to atypical forms of contract may thus represent one future challenge with many potential positive effects on the social climate, workers' motivation and productivity.

3. Impact of Globalisation

a) Unfavourable Distribution of Economic Growth

Another factor that may influence the growth of financial participation schemes is related to wage developments and more generally to the redistribution of growth. First the redistribution of economic growth reveals to be increasingly unequal along the development of globalisation. Higher economic growth experienced in several countries does not seem to be automatically translated into a higher share of wages in GDP.[297] On the contrary, this **wage share has declined** rapidly for instance in fast-growing countries, as for instance in Brazil, Republic of Korea, South Africa but also China. It has also declined significantly in the United States, Canada and Japan. According to OECD (2006: p. 186): 'nominal wage growth (in Member States) has fallen well short of increases in productivity for several years, driving the share of national income to a low level. This unusual moderation of wages appears to be an international phenomenon.' The wage share has also fallen in Europe, as shown in a recent comparative study carried out by the European Commission (EC-2007). After having increased in the EU during the 1960s and the first half of the 1970s with a peak of 69.9 per cent of GDP in

[297] The wage share is an indicator of the distribution of income between capital and labour. It represents the ratio between the total compensation of employees (according to the system of national accounts) and gross domestic product (either at market prices or factor cost).

1975, the wage share began a gradual decline and reached a low level of 57.8 per cent of GDP in 2006. A downward trend is also observed in the 12 new EU Member States so that their recent membership is not expected to alter the overall trend in a significant way.

Economists take the view that such evolution of the wage share depends on **two main factors**: first the evolution in the ratio of capital to labour, mainly due to technological and sectoral changes — for instance, with new technologies replacing middle-income workers or the growth of banks and financial companies. The increasing **capital-labour ratio** would also be due to a general fall in the number of employees due to restructuring. The second goes beyond the capital-labour ratio and emphasizes the fact that the rate of return to capital could grow more than the rate of return to labour. And indeed in some countries a declining **ratio of wages to profits** has been observed, for instance, in China but also in industrialized countries like Austria, Canada, Australia,[298] and several Central and Eastern European countries, which have also experienced some wage moderation. More generally we also witness a disconnection between the evolution of wages and productivity developments that should normally go hand in hand. No doubt financial participation may help to rebuild such an essential relationship not only for social peace but also for economic growth.

In EU countries in particular **wage moderation** represents an important trend of the new world of work. In Spain, for instance, wage moderation, backed by the two major Spanish trade union federations, is seen by many analysts as one of the key elements behind the huge employment growth experienced in the country. The same logic explains concessionary bargaining. As for flexible working time, whether at the central level as in Ireland or in the process of the decentralisation of collective bargaining, there are many examples of concessionary bargaining moderating, freezing or even decreasing wages.[299]

Against this background, both profit-sharing and employee-ownership may help to better distribute the fruits of economic growth. It is precisely the rising return on capital that makes co-ownership more attractive and as such may provide for alternative ways to generate a better distribution of companies' profits and growth. Promoting workers' participation in enterprise's profits and capital may be part – by allowing workers to become owners or to share profits – of a re-distributional policy agenda. Of course the way these schemes are implemented will have differentiated effects on inequalities, between for instance a financial participation scheme which is equally offered to all employees, whatever their position and background, and one that would offer more opportunities and more benefits to managerial employees.

b) The Incidence of Low Pay and Working Poor

In a context of wage moderation the increased proportion of workers at low pay (defined as wages under 60% of the median wage) and the phenomenon of working poor have attracted the attention of the media and policy makers. This is another factor that does influence the space left for financial participation schemes to develop. According to the European Commission there are more than 8 million such working poor in former EU-15. This number would

[298] Authors' own calculations.

[299] Even in Denmark, where concessionary bargaining is limited, there are examples of major wage concessions as, for example, for SAS Ground Service in February 2005 or in one of the Tulip Slaughter Houses in Ringster in December 2004, where 300 workers had to accept wages 15% below the industry level to keep their jobs.

probably double (no calculation seems to have been made yet on EU-27) if the 12 new EU Member States were taken into account. The majority of low-wage economies (above 30% of employees paid a wage under 60% of the median wage) are in the 12 new EU Member States, with the exceptions of Portugal and the UK (32.2%), whereas the highest wage economies (under 15%) are from the former EU-15: Denmark, Italy, Belgium, Finland and Sweden.

The phenomenon of low pay and working poor obviously influences the development of financial participation. The experiences of Central and Eastern European countries provide a good illustration since the prevalence of very low pay in their first years of transition obviously motivated the workers to look for immediate increases in wages rather than for a share in hypothetical profits. This low purchasing power has also explained the progressive dilution – workers selling their shares for cash – of employee ownership over the transition in spite of the fact that this type of property form had become – by default – one of the most important privatization forms (Uvalic and Vaughan-Whitehead, 1997). This is also one of the main reasons that explain the poor development of profit-sharing in these countries (PEPPER III, EC 2006b).

However while this situation may change over time along the catching-up process in wages and living standards that is expected in these countries, wage moderation may continue to be on the policy agenda in former EU-15 countries, with effects on the number of low pay workers. The challenge here for financial participation consists in contributing to reduce the number of low pay workers by allowing wage increases and dividends whenever possible.

In this regard it is encouraging to observe that financial participation schemes after their growth in the 1990s did not lose much ground. This is the case of profit-sharing schemes that not only maintained an important position in countries like France and the UK where they had developed the most, but they also slowly expanded in other EU countries like Greece, Spain and others (see data on financial participation developments in this volume). Recently Slovenia has also introduced new legislation encouraging the development of profit-sharing schemes. But this is the case for employee-ownership too, with a greater number of large enterprises having recourse to employee ownership over time (European Federation of Employee Share Ownership, 2008). Employee ownership definitely represents a precious tool in terms of income and asset formation with two challenges though. First there is a need to extend these schemes beyond managers and high-level employees, to cover all employees; and second, to encourage the use of employee ownership among small and medium enterprises.

c) A Race to the Bottom through Outsourcing and Migrant Workers

Globalisation creates a constant pressure on enterprises to minimize their wage costs. This has motivated many of them to have recourse to outsourcing on the one hand, and to migrant workers paid at lower wages on the other hand. This outsourcing policy is clearly another extreme way of implementing external flexibility and is thus reinforcing the other trends already described. Since the main aim is to reduce costs employers may generally not be keen in implementing profit-sharing whose basic aim is not to reduce costs but is of a radically different nature. As already seen above the use of profit-sharing among sub-contractors is often difficult because of the small margin left to them by the buyers, a process in which wages are treated more as a residual payment rather than a priority – and well planned – payment. This would not impede employers to have recourse to profit-sharing or employee-ownership

schemes for instance to motivate their remaining workforce – generally higher skilled – in their home-country.

On the other hand profit-sharing may not play against the employer search for greater competitiveness since it can also help to better motivate both unskilled and skilled employees. It further represents one way to keep wage costs flexible enough and could thus provide some eventual alternative to outsourcing. The problem is that this takes place within a race to the bottom in terms of labour costs – led by low labour costs of China – that the home-country workers are pretty sure to lose in the end because of being unable to compete and to continuously lower their wage claims. The co-existence of migrant workers with local workers in a company that could apply financial participation for both groups of workers could represent an interesting alternative in terms of competitiveness. The British economy by welcoming migrant workers from new EU Member States has shown that this could lead to a dynamic economy that remains competitive in terms of labour costs while progressively upgrading its technological and quality contents.

At the same time the increased volatility and internationalisation of profits are playing against the transparency of profit-sharing and employee-ownership schemes advocated in the literature. Profits seem to have become dependent on a much larger spectrum of policies: capital investment, marketing, diversification of products and activities, as well as outsourcing that the workers cannot influence much. In such a context, however, using financial participation and in particular employee-ownership may represent a way to motivate workers within their company's global operations. They equally help to make employees share more of the fruits of global economic growth.

4. Structural Changes in the World of Work

a) Changing Patterns of Work: New Types of Jobs and Workers

The changes that took place in terms of activities may also influence the scope of financial participation. Most European countries have experienced a declining share of manufacturing activities and an increased share of services over the last decade. There is notably a current growth in new types of services such as home care services for old people or for children, as well as more tele-working. Home services in particular are expected to continue expanding as the work force ages and life expectancy increases; they introduced, however, a radically different relationship between the employee or a group of employees and the employer, since the employer may now be the individual client. This type of relationship clearly makes it difficult to measure individual and collective performance and renders financial participation more difficult to apply. The growth of very small enterprises further introduces a new context for the implementation of workers' financial participation schemes.

At the same time firms in more traditional activities become 'entrepreneurs' and less and less 'employers'. They try for instance to restrict their core workforce and to develop subcontracting, and new forms of commercial relations (with individuals, other firms or organisations) in order to share the risk of the employment relationship to the employees and/or to other firms and organisations. With this notion of employer – who is normally the entity implementing

and monitoring a financial participation scheme – being more difficult to define, financial participation schemes may become less relevant as a management or human resources tool.

The challenge here would be to study the potential development and effects of financial participation schemes in this new type of services. At the same time financial participation schemes should find its role in the development of new services small and medium enterprises. Finally, both profit-sharing and employee-ownership could be efficiently applied to new categories of workers such as migrant workers and interim-agency workers, precisely to ensure their efficient integration and motivation in their work environment. This would help reducing the gap currently appearing between this expanding part of the labour force and more permanent employees, and thus limiting the potential conflicts and productivity loss that this could generate on the labour market.

b) The Structural Weakening of Social Dialogue

Financial participation prospects should also be seen within the current social dialogue context notably characterized by the continuous decline in trade union membership, a decentralization of wage bargaining, wage moderation through flexibility – or 'flexicurity'– tradeoffs at company level, and stronger bargaining power of employers along outsourcing and the recourse to migrant labour. This trend is even more striking in new EU Member States, with a continuous decrease in the trade union membership and in the coverage – already very low – of collective bargaining at both branch and enterprise level.

When and where they are involved in decentralized bargaining, trade unions are generally pushed by the employers to negotiate new types of trade-offs, such as wage increases against longer working time, or wage cuts for maintaining employment etc. In a context of wage moderation and wage concessions at enterprise level, trade unions may thus fear that financial participation schemes will act as a substitute rather than a complement to normal wage increases normally negotiated through collective bargaining rounds. The distinction between financial participation – and in particular profit-sharing – and wage bargaining is thus essential to gain trade union support of financial participation schemes. Here the national experiences are very diverse. In some countries like France profit-sharing comes on the top of the wage increase bargained at firm level and thus acts as a complement to social dialogue on wages. In other countries on the contrary profit-sharing has acted rather as a substitute for wage increases as in the UK, something that clearly explains the trade unions' opposition to this type of schemes. The experience of a country outside the EU, Brazil, is particularly interesting since the possibility for social partners to negotiate profit-sharing schemes at enterprise level has led to a un-precedent development of collective bargaining and collective agreements.

This new world of work is clearly leading the trade unions to new priorities. In particular to face the continuous fall in membership the trade unions have engaged into efforts to promote mainly national level (or possibly sectoral) negotiations, for instance on wage increases. All systems implemented at enterprise level are seen with increased suspicion by the trade unions and do not meet their consent. Trade unions in the recent past have thus pushed for the minimum wage settlement, for wage negotiations on average wage or hourly wage increases at national level, as well as for the generalization of the extension clause, which allows a collective agreement for instance at sectoral level to be generalized to all companies and workers of that sector even for those companies that have not signed the collective agreement. Paradoxi-

cally, this move may lead to further decrease collective bargaining and trade unions bargaining strength at local level.

While the difficulties in organizing labour should be understood, trade unions may also understand the benefits they could get from strengthening their action at local level. In this regard financial participation schemes may also give them the opportunity to obtain increased total worker remuneration packages in the current period of wage moderation. It could help them to find new tradeoffs in the flexicurity arena and to progressively come out of the wage moderation era.

5. Concluding Remarks

Workers' financial participation has remained for years on the EC policy agenda (see PEPPER I, II and III Reports). Several studies have multiplied to put the emphasis on the positive effects that this type of schemes may have both on the economic and social sides. As highlighted by the EC, 'Financial participation is one important element that may contribute to EU countries' competitiveness while preserving its social cohesion.' (EC, 2002). The European Commission reports also described as 'disappointing the low use of these schemes considering their importance for productivity, wage flexibility, employment and employees' involvement'; before insisting that 'the development of financial participation schemes is strongly influenced by government action, in particular by the availability of tax incentives' (EC, 1997, PEPPER II Report).

On the one hand, many governments in the EU have continued to develop financial participation schemes (see Part 2, Country Profiles in this volume). On the other hand, however, the world of work has been changing fast and may limit the recourse to financial participation. There is thus an urgent need to reconsider financial participation within this new environment, especially since the most recent developments on the labour market – as shown here – do not seem to be always favourable to extending financial participation to a large portion of the work force.

In particular the priority given by most European governments to less regulation especially through removing all barriers to hiring and firing has obviously put more emphasis on external flexibility – that is, employment adaptability. As a result, internal flexibility (based instead on employment stability to maintain the labour force motivation and skills and achieved notably either through greater pay flexibility – which can be brought by profit-sharing schemes – or through workers' motivation – brought by employee-ownership) is less perceived as a priority policy option.

At the same time however the world of work is complex and is continuously evolving. Not only new forms of work organization are emerging – such as the growth of atypical forms of work or the recourse to shift work and unsocial hours – but the number of working hours does also have a tendency to increase, an element that may be more associated to internal rather than external flexibility. No doubt financial participation needs to adapt to this complex and changing world of work, first to accompany some of the changes that are taking place in work organization, but also to motivate the labour force in a context which seems to be do-

minated by sometimes extreme wage moderation and casualisation of the employment relationship.

Globalisation and its effects are also challenging the current nature of financial participation. Employers have increased external flexibility even further through a more systematic recourse to outsourcing or the employment of migrant workers. Wage developments described in this paper confirm the employers' success in minimizing wage costs, with an unequal distribution of growth between wages and profits, and a general move toward wage moderation in almost all European countries that has contributed to generate an increased proportion of low pay and working poor. This is a movement against which trade unions seem to be rather powerless in a context of continuous decline in membership and the shrinking coverage of social dialogue.

Moreover the increased recourse to atypical forms of contracts such as fixed term contracts, self-employment, and interim agency work thus leading to a fragmentation of the labour force further strengthened by the development of atypical working time arrangements such as shift-work or week-end work. The development of financial participation is made difficult by such labour force fragmentation and the recent growth of new types of services – such as home care for the elderly etc. – that modify the traditional employer-employee relationship.

At the same time financial participation may provide some policy answers to some of the effects of globalisation, such as the continuous decline of the wage share in economic growth. Profit-sharing and employee-ownership could represent the way to better share economic growth. Profit-sharing and employee share ownership schemes may help to provide solutions to the current unequal distribution of growth and wage moderation process. Distributing part of companies' profits or dividends to the workers may help to ensure a more fair distribution of growth and guarantee that employees' income would increase whenever and wherever possible according to individual enterprise performance. By linking wages to the companies' profits or capital, it may also represent a way to reconcile the employees with the global operations of their companies.

The advantages of profit-sharing and employee-ownership schemes in terms of workers' motivation, investment in human capital, and enhanced productivity could also be brought back to the attention of employers and public authorities to counter some of the negative effects expected – and already observed in many places – with regard in particular to the vulnerability of workers, overall quality of jobs and long-term growth from the extreme use of external flexibility and outsourcing (Eyraud and Vaughan-Whitehead, 2007).

Financial participation, if it were extended to all types of employees, could also contribute to limit the devastating effects of the emergence of a dual labour force, and provide a way to reduce the gap between permanent workers and more insecure workers (such as migrant and interim-agency workers).

Moreover if the traditional routes for promoting financial participation schemes such as legislation or tax policy are more difficult than before, other routes must be investigated. Financial participation schemes should first be more systematically placed within the corporate social responsibility agenda. Financial participation might furthermore be promoted through a coordinated approach of EU actors, e.g., through the open method of coordination (that is, a better exchange of practices and benchmarking).

At the same time should we not rethink the role of social dialogue and collective bargaining at decentralised level with regard to financial participation schemes? No doubt financial partici-

pation could start being discussed within the current flexicurity negotiations at company level. In addition to this, at a moment in which many economic and social issues, including wage policy, are negotiated in many countries in tripartite discussions at the national level – often leading to tripartite or economic and social pacts – it is time to put the promotion of financial participation also on the tripartite agenda as a policy tool and to discuss how its different forms may contribute to pursue general economic and social goals.

Obviously some of the obstacles to financial participation identified in this article –such as organisational changes, recourse to additional working hours or atypical work contracts – are not totally new. What is new, however, is the whole international context of globalisation and internationalisation in which financial participation has to operate and which has brought new systematic types of business models such as outsourcing, minimization of wage costs, dominance of external flexibility through labour deregulation and more freedom to hire and fire workers. Both the new employers' vulnerability to international competition and the new strategies of the trade unions – for instance to go back to centralised wage-fixing to avoid risky tradeoffs at company level – have to be taken into account as well.

Financial participation must be reconsidered in this new world of work environment, if it is to develop further. Otherwise it will not be able to serve as a policy tool to address some of the major issues brought by globalisation, in terms for instance of wage disparity, poverty, and uneven distribution of the fruits of economic growth.

III. Suggestions for Initiatives

Jens Lowitzsch

The analysis of the legislative framework in the 27 EU Members States and the two Candidate Countries has shown, that regardless of data source, the past decade has seen a significant expansion of employee financial participation in Europe. This is true of both profit-sharing and employee share ownership, although profit-sharing is more widespread. Throughout the European Union, the percentage of enterprises offering various PEPPER schemes is on the rise. Between 1999 and 2005, broad-based share ownership schemes increased from an average of 19% to 26% (unweighted country averages). On the other hand, – despite of this positive trend – it seems that financial participation has been extended to a significant proportion of the working population in only a handful of countries.

The comparative analysis of the general attitude of governments and social partners still shows a lack of concrete policy measures supporting PEPPER schemes, and limited interest both by trade unions and employers organisations. Instead of being actively promoted as in some old EU Member States, employee financial participation has (with some exceptions) most frequently not been considered, or has been viewed with suspicion.

On the basis of these principal findings of the PEPPER IV Report suggestions for future initiatives which could contribute to a more widespread diffusion of employee financial participation in the enlarged EU are being made to the EU Member States as well as to the Commission.

1. Promoting PEPPER Schemes at the National Level

The potential beneficial effects of employee financial participation should not be neglected. A growing body of empirical evidence appears to back up these claims.[300] To summarise, existing evidence suggests that financial participation can deliver real benefits for employees, enterprises and national economies. However, despite this potential, it remains under-utilised in most Member States, and is unevenly distributed within the EU.

➢ **The challenge: Legislating PEPPER Schemes**

In conformity with much of the Western experience, the lack of specific legal provisions on employee financial participation in the new Member States, which would provide a different

300 Financial participation has been statistically linked with greater productivity and with higher profits (profit-sharing: Festing et al., 1999; share ownership: Blasi et al., 2004). Furthermore, these effects appear to be strengthened by the presence of other kinds of employee involvement (Kim, 1998).

fiscal treatment or other type of incentive, seems to have been a major obstacle to its introduction as well as a cause for decreasing incidence. Probably some policy action in this domain would be essential in the new Member States and candidates. The Western experience with profit-sharing and employee ownership clearly confirms that schemes have been most diffused in those countries where concrete measures have been introduced to support them.

- **Share Ownership Schemes: Developing a long-term perspective**

Given the prevailing economic conditions in most of the new Member States from Central and South Eastern Europe, the beneficial effects could be even more important than in the EU-15 economies. Nevertheless, share ownership has been introduced rather as a one-off incentive to employees within the privatisation process. Policies actively promoting not only the introduction of such schemes but also their continuous support have been almost non-existent. On the other hand employee financial participation has been actively promoted by a number of western governments, as well as by the EU, precisely because it is expected to lead to a number of positive effects in the long run.

- **Profit-sharing: Strengthen incentives and increase productivity**

Profit-sharing, in particular, despite its limited diffusion in the newcomers from Central and Eastern Europe[301], is likely to become far more relevant in these countries, stimulated by the rich experience with these schemes in the EU-15. The need to strengthen incentives and increase workers productivity in the future should generate more favourable attitudes towards flexible remuneration schemes such as profit-sharing. Furthermore, profit-sharing enhances loyalty and motivation among employees by ensuring them employment security in exchange for wage flexibility. Both effects may help to encourage employers to utilize wages rather than employment as the instrument of flexibility. This, in turn, would discourage higher turnover in the labour markets, and contribute to greater employment stability.

- **Internal versus external flexibility: Profit-sharing and flexicurity**

The public authorities' desire to reduce unemployment figures has led them to favour the process of entry and exit from the labour market and the promotion of an 'external flexibility' model. Profit-sharing schemes are an element of 'internal flexibility' that allows wages to go down in a period of economic downturn and help the employing company to keep its margins – by automatically decreasing its labour costs – without having to reduce its labour force. Several studies have shown that profit-sharing could bring wage flexibility and employment stability. This is in line with the common principles of 'flexicurity' retained by European Commission and Council, such as 'a better balance between external and internal flexibility', 'a climate of trust and dialogue' and 'a better workers' adaptability capacity'. Thus, especially against the background of the changes of the world of work and as a means of achieving internal flexibility (as opposed to external flexibility) profit-sharing can play an important role in the flexicurity-approach.

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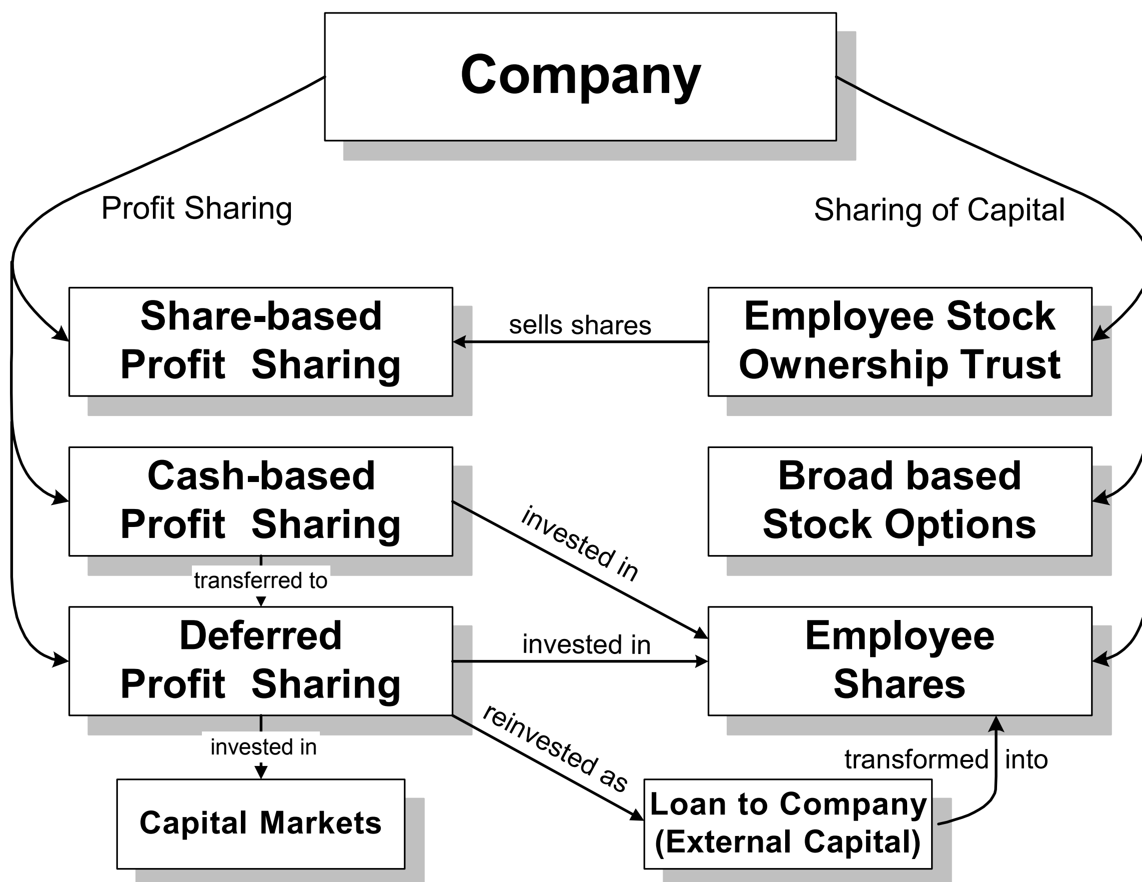
301 In the early 1990s, the general economic conditions – recessionary trends, falling wages, low or negative profits – have not favoured the adoption of profit-related remuneration schemes. Changes in the area of labour relations have usually provided laws based on the standard wage employment contract, which together with rigid tax provisions, do not allow much flexibility in payments systems.

2. The Building Block Approach: Developing a common model for financial participation across the EU

The 'Building Block Approach' as an open platform model ideally responds to the need for developing schemes at the European level in order to support financial participation more actively and to overcome national differences in taxation policy. At the same time, such a framework, while providing a broader incentive system, delineates what companies may do without inviting sanctions from regulatory, legal and taxation authorities.



➢ **Providing a broad incentive system with flexible solutions**

A model must be compatible with those already established in the Member States: Relatively widespread in the EU-15 are profit-sharing schemes, stock options and employee shares. In countries with an Anglo-American tradition, e.g., the United Kingdom and Ireland, but also in some transition countries, such as Hungary, Croatia and Romania, ESOP-models are to be found. The Building Block Approach reflects this diversity, while opening national practise to new forms of financial participation. The building blocks consist of the three basic PEPPER

elements:[302] (1) Profit Sharing (Cash-Based, Deferred and Share-Based); (2) Employee Shareholding (Stock Options and Employee Shares); (3) Employee Stock Ownership Plans as Collective Schemes.

- **A future EU recommendation: Implementing the legal foundations of a European Model**

The European Platform consisting of the proposed Building Blocks could be framed as a Recommendation addressing the problem of national implementation by a recognition procedure by Member States. As a result of this procedure, each Member State would recognise individual elements from the European Platform drawn up in the Recommendation as equivalent to a plan drawn up under its own laws and provide equivalent benefits. This sets up a distinct legal entity for the chosen Building Block for companies to refer to throughout those countries that decide on recognition.

- **Building on existing national legislation originating in the acquis**

Given the above described difficulties in arriving at a supranational compromise, in order to reach a regulation at the supranational level, the simplest solution is to build on existing national legislation originating in the Acquis Communautaire. A rare example of such legal 'common ground' are some of the national rules on listed and unlisted joint stock companies originating in the implementation of European Law i.e., the second Council Directive on Company Law 77/91/EEC. Further investigation of other common existing regulations in this field is needed.

3. PEPPER Schemes for SMEs: Employee Stock Ownership Plans (E-SOPs)

In addition to well known forms of financial participation (e.g., employee shares and profit-sharing), the Building Block Approach introduces a lesser known but flexible form of collective share ownership: the ESOP. While, for example, share-based profit-sharing schemes have only one source of funds (i.e., direct contributions from the employer company), the ESOP can obtain financing from such different sources as: (I) a loan from the employer company, a selling shareholder or a financial institution such as a bank; (II) dividend earnings; (III) sale of shares to its related share-based profit-sharing scheme; and (IV) contributions from the employer company.

While share ownership generally involves additional risk for employees, the ESOP avoids this consequence. Although employees, as in other share ownership schemes, are encouraged to allot part of their wealth into the shares of their own companies rather than those of other companies, resulting in concentrated rather than diversified risk, there is this fundamental difference: ESOP debt is funded by appropriately timed contributions from the company to a employee trust (ESOT). Thus the scheme provides an additional benefit to basic wages. The employee's salary remains unaffected. Furthermore, ESOPs make employees more motivated

[302] For a detailed technical description of the different mechanisms and schemes see 'Financial Participation for a New Social Europe' by *J. Lowitzsch et al.*, Berlin/Paris/Brussels 2008.

and productive while at the same time making enterprises more competitive.[303] Finally, there is an additional advantage to the company: shares are not sold to outsiders; thus there is no risk of loss of control and the company remains local. As such ESOPs could be an important tool for solving the problems of business succession in family-owned enterprises, strengthening bonds between enterprise and community, while keeping jobs local and more wage income spent at home.

- **Heads of family enterprises will be retiring en masse in the next ten years**

A recent Commission Communication from 2006[304] stated that with the aging of Europe's population, 'one third of EU entrepreneurs, mainly those running family enterprises, will withdraw within the next ten years'. This portends an enormous increase in business transfer activity which could affect up to 690,000 small and medium-sized enterprises and 2.8 million jobs *every year*. It is anticipated that as a consequence of the new forms of business finance now coming into use, transfers within the family will decrease, while sales to outside buyers will rise. The entrance of international investors into what used to be primarily domestic markets will broaden the range of potential buyers for European small and medium-sized enterprises. This process is likely to threaten the successful regional structure of European (family-owned) businesses and will profoundly affect the European Community itself. This field of action has been highlighted as one of the main objectives of the Council Recommendation of 7 December 1994[305] and recently by the European Commission, explicitly stressing the importance of ownership transfers to employees as a specific measure for facilitating business succession in SMEs.

- **ESOP as a vehicle for business succession**

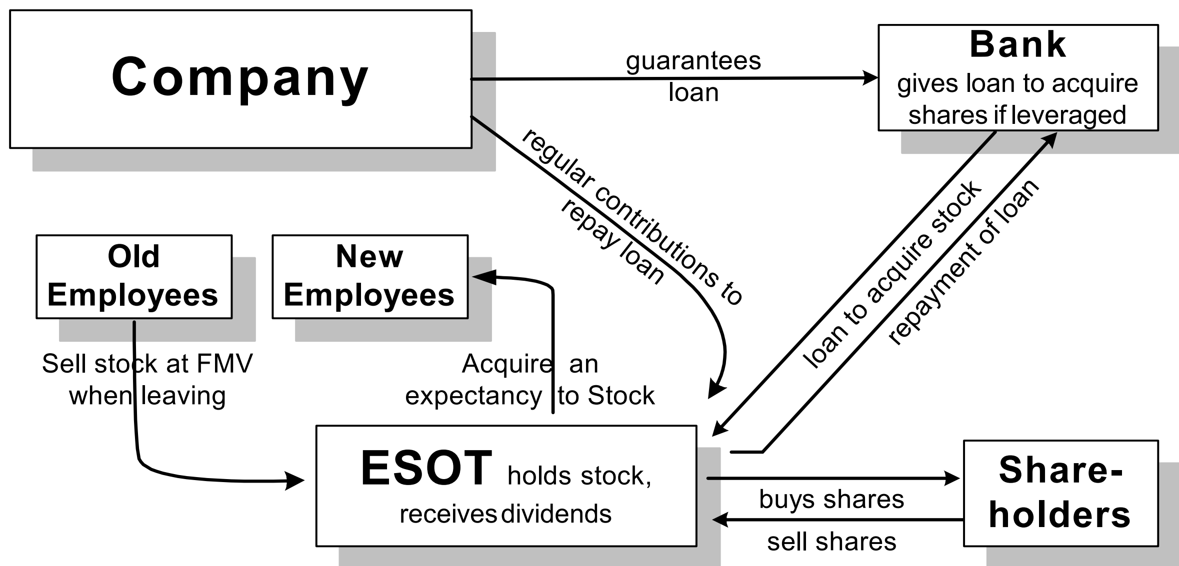
A full or partial ESOP buy-out provides an ideal vehicle to facilitate transitions in ownership and management of closely-held companies. The ESOP creates a market for retiring shareholders' shares, which is of major importance to unlisted SMEs having no other ready source of liquidity. ESOPs may easily buy-out one or more shareholders while permitting other shareholders to retain their equity position. This is one of its major advantages from the shareholders' perspective. At the same time, ESOPs give business owners the opportunity to diversify their investment portfolios without the costly process of going public. Furthermore, there is no dilution in equity per share of current stockholders since no new shares are issued and all shares are bought at fair market value. If the ESOT borrows money to buy shares, the company repays the loan by combining any dividend income of the trust with its own tax-deductible contributions to the plan. As the loan is repaid, a number of shares equal to the percentage of the loan repaid that year is allocated to employee accounts, usually on the basis of relative compensation. In this way the ESOP creates a market for retiring shareholders' shares at a price acceptable to the owner - a market which otherwise might not exist. At the

303 For a recent, comprehensive overview of the positive economic evidence (esp. for ESOPs) see *J. R. Blasi, D. Kruse, A.* Bernstein, 'In the Company of Owners', Basic Books, New York 2003; they find an average increase of productivity level by about 4%, of total shareholder returns by about 2% and of profit levels by about 14% compared to firms without PEPPER schemes.

304 Implementing the Lisbon Community Programme for Growth and Jobs, on the Transfer of Businesses – Continuity through a new beginning, from 14.03.2006 COM (2006) 117 final.

305 On the transfer of small and medium-sized enterprises, 94/1069/EEC, with explanatory note, Official Journal No C 400, 31. 12. 1994, p. 1; reiterated in the Communication from the Commission on the transfer of small and medium-sized enterprises, OJ C 93, 28.3.1998.

same time, when a change of control is appropriate, ownership is transferred to motivated employees who have a vital interest in the company's long-term success.



Thus the ESOP may be an attractive alternative to selling the business to outsiders, especially when there is a desire to keep control of the business within a family or a key-employee group.[306] As a trusteed plan, the ESOP is designed to separate control over the shares in the trust from the 'beneficial owners'. The trustee exercises the voting rights while the employees are the financial beneficiaries of the trust. The trustee may, in fact, be the very person who has just sold some or all of his shares to the trust. For smaller firms especially, it is much easier to contemplate a gradual transfer of ownership by creating a market for the shares of those who wish to sell at the present moment, while enabling those who wish to hold their shares to retain their equity interest permanently or at least until some later date. The result is the opportunity of gradually cashing out without giving up immediate control.[307]

4. Promoting PEPPER Schemes through Tax Incentives

In spite of the difficulty of their implementation at the European level (because of the exclusive jurisdiction of national legislation over tax law), tax incentives remain powerful tools for enhancing and broadening financial participation. This is especially true when they remain optional for the Member States and not subject to a unanimous vote of approval. Countries

306 The ESOP may also be used to buy out dissident shareholders.

307 Once the loan is paid off, of course, most companies make some arrangement for the presence of employee representatives on the plan committee.

could voluntarily offer tax incentives singly or in groups. Such a step would create an increasingly favourable environment in which countries having an advanced tradition, such as France or the United Kingdom, would encourage emulation. Optional preferential treatment as part of the Building Block Approach requires distinguishing between profit-sharing schemes, share ownership schemes and employee stock ownership plans.

- **Tax incentives are not a prerequisite to PEPPER schemes but they effectively promote financial participation where they exist**

On the one hand financial participation schemes without tax incentives sometimes may have a higher incidence than those with tax incentives. Therefore tax incentives are not to be considered a prerequisite to the development of financial participation. On the other hand countries with a long tradition of employee financial participation as well as countries where tax incentives are quite recent, universally confirm the positive impact of tax incentives.

- **Tax incentives should (and in most countries do) target those taxes which constitute the heaviest burden in the national taxation system.**

Usually these are the progressive personal income tax and social security. Many countries therefore provide: (1) exemptions from social security contributions for certain plans (e.g., France, Belgium, UK, Ireland, Finland); (2) levying a capital gains tax (e.g., UK, for dividends Belgium); (3) levying a special low tax (e.g., France) in lieu of personal income tax, and (4) tax allowances for personal income tax (e.g., Austria, Finland, Ireland).

- **Some forms of tax incentives are more favourable for certain types of plans and also lead to higher efficiency:**

For share ownership and stock options as far as benefit taxation is concerned: generous valuation rules combined with a favourable taxation moment (often linked to holding period), and, if possible, exemption from SSC for both the employer company and the employee.

For dividends and sale of shares: a special tax rate or capital gains tax in lieu of personal income tax and, if necessary, exemption from SSC.

For ESOPs and Intermediary Entities: exemptions from income tax on share acquisition[308] or on share sale if the profit is realised after a holding period or within a retirement program; the company may qualify for tax relief on both interest and principal payments on the loan; sale of stock to an ESOP on a tax-deferred basis if the proceeds of the sale are reinvested in securities of other domestic corporations (tax-free rollover).

For profit-sharing: a special tax rate in lieu of the progressive personal income tax as well as exemption from SSC for both the employer company and the employee.

[308] In Ireland this is the case only where the ESOP comprises an ESOT working in tandem with an Approved Profit Sharing Scheme.

5. Informing Governments and Policy-Makers about the PEPPER Initiatives

The development of financial participation schemes across the EU is strongly influenced by national policies, in particular by the availability of an appropriate legal framework, tax incentives and other financial advantages. As a result, different laws and sometimes mandatory rules in different countries often require specific forms of financial participation, forcing companies to tailor the design of an international plan accordingly. Here the EU has an important role to play in promoting employee financial participation throughout the newly-enlarged EU. It could disseminate information and proposals on this subject as a continuation of earlier initiatives in this area.

6. The Need for Consistent and Reliable Data

In line with prior Commission activities a Community initiative should launch at an EU wide, comparative, focused survey of financial participation. Since no cross country data focussed on financial participation is available at present, the PEPPER IV benchmarking is a compromise intended to cope with the existing data deficit without undertaking a new survey. There were inconsistencies between different data sources which showed different scales of financial participation, for example, a much larger offer (CRANET) than the actual take-up rate by employees (EWCS). This discrepancy in the cross country data can probably be attributed to diverse definitions and methodologies employed as well as a diverse emphasis of the surveys. To facilitate a discussion of individual country scores on different indicators vis à vis comparable scores of other EU Member States, and to obtain a reliable overall picture, a more comprehensive and consistent data base is indispensable. The Commission should support additional research specifically designed to fill this gap.

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This Report summarises and updates the previous PEPPER reports. It is the result of the Commission funded project "Assessing and Benchmarking FP in the EU 27".

Complying with the concept of the PEPPER reports and building on them it provides a solid basis for leveraging the development of Financial Participation in the European Union in the context of the current reform process triggered by the European Commission and Parliament.

The Project closes the gap between PEPPER I/II (1991, EU-12 / 1997, EU-15) and PEPPER III (2006, 10 new Member States / 4 Candidate Countries). Furthermore it implements benchmarking indicators developed by the European Foundation for the Improvement of Working and Living Conditions in all 27 EU Member States and Candidate Countries.

The Report is divided into three parts. The first part consists of an overview chapter which provides a summary of the benchmarking project and the current situation of employee financial participation in countries under consideration, as well as chapters presenting and discussing the benchmarking results as well as a chapter on the fiscal framework and tax incentives in the EU-27. The second part consists of country profiles, each covering four main issues: (1) a short introductory summary; (2) the general environment for employee financial participation, highlighting the background, the attitudes of social partners as well as government policies; (3) the legal foundations for different forms of participation, including the incentives for application of schemes; and (4) a brief synopsis of participation in decision making. The third part of the Report summarises the experience of employee financial participation in Western and Eastern Europe, its role in the changing world of work in the 21st century and its relevance in the context of the European integration process. Finally recommendations and suggestions for further initiatives are made.