



European Economic and Social Committee

SOC/371
Employee financial
participation in Europe

Brussels, 21 October 2010

OPINION

of the
European Economic and Social Committee
on
Employee financial participation in Europe
(Own-initiative opinion)

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On 17 February 2010 the European Economic and Social Committee, acting under Article 29(2) of its Rules of Procedure, decided to draw up an own-initiative opinion on:

Employee financial participation in Europe.

The Section for Employment, Social Affairs and Citizenship, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 2 September 2010.

In view of the renewal of the Committee's term of office, the plenary assembly decided to vote on this opinion at the October plenary session and to appoint **Alexander Graf von Schwerin** as rapporteur-general in accordance with Rule 20 of the Rules of Procedure.

At its 466th plenary session (meeting of 21 October 2010) the European Economic and Social Committee adopted the following opinion by 170 votes to nine with 22 abstentions:

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1. **Summary and recommendations**

1.1 Employee financial participation (EFP) offers an opportunity for businesses, employees and society as a whole to participate more, and more effectively, in the success of the increasing Europeanisation of economic activity. The European Economic and Social Committee therefore wishes, with this own-initiative opinion, to raise public awareness of this issue. **The aim is to encourage Europe to draw up a framework concept** which promotes Europe's economic and social cohesion by facilitating the application of EFP at various levels (e.g. profit-sharing, employee share ownership schemes, save-as-you-earn schemes).

1.2 As Europe has grown, businesses, particularly SMEs, have also expanded their area of activity across borders. **One of the flagships of the EU2020 Strategy** is to give a strong focus to the delivery of the Small Business Act, in particular with a view to improving the financial situations of SMEs. Here EFP can be one of the mechanisms implemented to support this goal and thus **enhance the competitiveness of European SMEs**. Independently of the size of the companies, the EFP models must respect company-based solutions and protect employee rights, accounting for the variations in companies and countries.

1.3 This own-initiative opinion therefore intends to:

- re-launch the debate on EFP at the European level and **give new impulses for an EU-wide discussion**;

- **raise awareness** and encourage social partners at European level and in the Member States to take up the issue in more depth;
- identify obstacles for cross-border EFP and **suggest possible solutions**;
- **urge the European institutions** to elaborate solutions where appropriate;
- **raise questions** that need to be further examined.

1.4 **The introduction of EFP must be voluntary.** It is **in addition to existing remuneration systems** and not a substitute while not impeding collective wage bargaining. It must be readily understandable for employees and to this extent complement other forms of employee participation. It must be independent of pension schemes but may be an individual complementary resource for employees once they are retired.

1.5 EFP may bring desirable benefits such as:

- **improvements in local purchasing power**, which in turn can boost a company's chances of success in a given region,
- a high-quality **component of good corporate management** which helps to improve incomes through participation in a company's success,
- as part of the process of **asset formation** it can have a **motivating effect** and thus contributes to a greater sense of identification with the company, reducing staff turnover.

1.6 Therefore **the EESC calls for a new Council recommendation** (like 92/443/EEC of 27.7.1992) concerning the promotion of EFP and proposals to deal with obstacles to cross-border plans.

1.6.1 The following measures should be adopted at an EU level as the next steps:

- (1) The application of EFP should be facilitated EU-wide **on the basis of common principles**.
- (2) The increased share and the diversity of forms of EFP should be analysed and made comprehensible in practical terms in order to **facilitate their application, particularly in SMEs**.
- (3) **Businesses operating across borders** should be offered help, particularly in overcoming tax obstacles in specific EU/EEA countries, in order to improve staff loyalty and their sense of identification with the company more effectively by means of EFP.
- (4) **Forms of EFP** should be developed, with a view to improving the **offer** by companies as well as the take-up by employees, individual incentives to asset formation, increasing employees' share in the results of the company, the cross-border transfer of entitlements.
- (5) The positive participation of employees based on ownership and the associated sense of responsibility could help to **strengthen corporate governance**.
- (6) **Examples of best practice** should continue to be publicised, thus contributing to the greater dissemination of EFP schemes. Related activities should be **supported by the EU budget through a dedicated budget heading**.

- (7) The implementation of **employee-buy-outs as a vehicle for business succession** should be encouraged since it can boost the continuity and thus the competitiveness of European enterprises while at the same time rooting them in the regions.
- (8) Wages and purchasing power of employees have remained behind productivity growth and revenues for shareholders¹. The backlash of the current crisis will also be tough for wage earners. EFP could, depending on its form, be a – **partial – compensation for losses of purchasing power and correct for recurring fluctuations** but it should not replace wage progression.
- (9) **Information sources on the implications of EFP** for businesses and employees as well as training and advisory services by impartial bodies, i.e. NGOs, **should be established**.
- (10) Where collective bargaining is practised, the conditions for EFP should also be the subject of collective agreements.

2. Background

2.1 Council of the European Union and European Commission

As early as 1992 a Council (later Council of the European Union) recommendation concerning the promotion of participation by employed persons in profits and enterprise results² set out the **following principles, which the EESC supports**

- Regular application;
- Calculation in accordance with a predefined formula;
- Application complementary to the traditional remuneration system;
- Variable participation depending on company results;
- Benefits for all employees;
- Application to both private and public enterprises;
- Application to enterprises of all sizes;
- Simple models;
- Information and training for employees on models;
- Voluntary introduction and participation in models.

The 2002 European Commission Communication on a *Framework for the promotion of employee financial participation*³ confirmed these principles.

¹ See with further details D. Vaughan-Whitehead, *The Minimum Wage Revisited in the Enlarged EU*, 2010, Edward Elgar-ILO.

² 92/443/EEC.

³ COM(2002) 364 final.

2.2 The PEPPER reports drawn up at the instigation of the European Commission

2.2.1 Results. Positive dynamic of EFP

The PEPPER reports underline the continuing importance of this subject for European policy. The PEPPER-IV report⁴ notes the **significant rise in EFP in the EU 27 over the last decade**. In the period 1999-2005 the proportion of firms which offer employee share ownership schemes open to all employees grew by five percentage points from an average of 13% to 18%, in the case of profit-sharing schemes by six percentage points from an average of 29% to 35% (CRANET data, weighted average of all countries). In the same period the number of employees actually participating in these schemes also grew, although less rapidly (European Working Conditions Survey (EWCS) data).

2.2.2 Recommendations

The PEPPER IV Report calls for a **Council Recommendation on a European platform for EFP**. In accordance with the voluntary principle, the transnational “Building Block Approach” includes all forms of financial participation practised:

- 1) Profit-sharing (cash, deferred or in shares),
- 2) Individual share ownership (employee shares or stock options),
- 3) The ESOP concept (collective employee share ownership model financed from a profit share additional to remuneration).

This at the same time leaves scope for new forms of EFP. **All modules could be combined** for custom-made solutions.

2.2.3 Promoting optional tax incentives

While tax incentives are not a precondition for EFP, they have proved a positive and important leverage in those countries which offer them. Without prejudice to national Member States’ exclusive competence over taxation, **coordination, streamlining and mutual recognition** may help to stimulate EFP in cross-border operating companies. The **calculation of "effective tax rates"** for standardised scenarios would permit direct comparison between the EU 27 and thus ensure further harmonisation. As long as the European measures remain optional, conflicts with national law can be avoided.

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The PEPPER IV Report – Assessing and Benchmarking Financial Participation of Employees in the EU-27, Berlin, 2009; see <http://www.eurofound.europa.eu/areas/participationatwork/pepperreports.htm>; summaries in English, French and German downloadable at <http://www.intercentar.de/en/research/focus-financial-participation-of-employees/>.

2.2.4 Overview of the status quo

Social partners and political decision-makers need a clear, detailed overview of the range of national models currently used and their take-up. There are to date no specific, transnational data from surveys of EFP. This shortcoming should be remedied, for example by means of regular surveys.

2.3 Projects supported by the Commission: "Building Block Approach" for an EU model

2.3.1 In order to link the many and very varied EFP models which exist in the EU Member States, the European Commission has **promoted work on a "Building Block Approach"**.⁵ Here a distinction is drawn between the three basic forms of EFP in Europe (profit-sharing, individual share ownership and the ESOP concept; see also appendix).

2.3.2 The "Building Block Approach" **reflects the postulates of the European Commission** (being transparent, broad-based, etc.) and neither relies on nor excludes tax incentives. All of the different elements are voluntary for both enterprises and employees. They can be put together in any combination with the different building-blocks tailored to the specific needs of the given enterprise

2.3.3 The PEPPER IV report suggests that an EFP model that was used across borders and which benefited from uniform support in all EU Member States would improve the attractiveness of EFP for all concerned. Businesses operating in several countries would in particular benefit from the reduced administrative load of a uniform model, which at the same time facilitated portability from country to country. SMEs would benefit from the transparent uniformity and comparability of participation models.

2.3.4 Pending the establishment of an EU-wide model of this kind, efforts should in the meantime be channelled towards **mutual recognition** of the various national forms of financial participation, including their tax treatment.

3. Advantages of more widespread use of EFP

3.1 Advantages of financial participation for businesses

I With a view to the EU 2020 Strategy, the introduction of EFP can help businesses in Europe, especially **SMEs, to improve their competitiveness** by increasing employees' loyalty and identification with the company, in good times and bad. EFP thus contributes to securing the future in a sustainable way.

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For the results see J. Lowitzsch et al. *Financial participation for a new Social Europe*, Berlin/Paris/Brussels 2008; Rome 2009, Krakow 2010; downloadable in English, French and German at <http://www.intercentar.de/en/research/focus-financial-participation-of-employees/>.

- II A proportion of company profits are distributed to employees locally, which in turn helps to **increase regional purchasing power**.
- III EFP could help to **deal with the problem of demographic change**, by offering sought-after, highly skilled employees an attractive place to live and work. This **makes it easier to recruit specialist employees**.
- IV Improved motivation as a result of EFP helps to **increase company productivity** and to **improve the quality of corporate management**.
- V EFP could, depending on whether it is structured as equity or external capital, increase a company's return on equity or its ratio of equity capital to liabilities. This can **make it cheaper to obtain external capital, thus improving the company's credit rating**.
- VI A full or partial employee buy-out provides an appropriate **vehicle to facilitate transitions in ownership** and management of family enterprises and SMEs in order to secure their continuity.⁶

3.2 Advantages of financial participation for employees

- I Through EFP **employees can** voluntarily **benefit** from remuneration which is supplementary to the income from their labour and/or wage agreed by collective bargaining.
- II Employees are in this way given an opportunity to build up **long-term investment capital** simply, which can form additional resources for them once they are retired..
- III Employees who can participate financially in the company are likely to feel that their contribution to the company's success is taken more seriously. **Thus, they have greater self-esteem**.
- IV EFP offers them the opportunity to increase their autonomy in the workplace and to participate and **have their say in the company's strategy for the future**. In this way employees can help to secure their job in the long term.
- V As a complement alongside wages, EFP **improves the worker's financial situation** and provides a cushion in difficult times or when changing jobs.
- VI Given that the labour market is becoming increasingly European, however, it would be appropriate for **forms of EFP from one country** to be recognised in, and transferred to, another country when an employee goes to work abroad.
- VII In the event of **crisis or restructuring**, being tackled by management and workforce jointly, employees, who keep their jobs and their remuneration, can - temporarily - support their company in the interests of preserving their jobs.

3.3 Business succession and share ownership

- 3.3.1 The European Commission⁷ points out that as a result of an ageing European population "one third of EU entrepreneurs, mainly those running family enterprises, will withdraw within the

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This field of action has been highlighted in the Commission Recommendation on the transfer of small and medium-sized enterprises, 94/1069/EEC; reiterated in the Commission Communication on the transfer of small and medium-sized enterprises, OJ C 93, 28.3.1998, p. 2.

next ten years". This highlights the **enormous increase in transfers of company ownership**, which will affect up to 690 000 unquoted companies and 2.8 million jobs annually. As the largest sector of employers, SMEs and micro-enterprises are a major factor in labour market policy. A related question is whether companies affected by generational change and the jobs they provide can be maintained. Confronted with this increasing need for business transfers an **appropriately designed long-term EFP model which could perpetuate employees' jobs could facilitate the process**.

3.3.2 In respect to business succession above all **proven ESOP models can be useful** (see appendix). One of the main characteristics of the ESOP model is that it is especially tailored to the needs of unquoted companies. It encourages business owners to sell their enterprise to their employees and not to a third party and foresees the gradual acquisition of up to 100% employee ownership. This makes it possible to buy out one or more shareholders while not forcing other shareholders to give up their equity position. Employees do not have to invest their savings since the acquisition of the enterprise by its employees is financed by a profit share granted in addition to their salaries. For this reason **employees do not incur additional risk** under this concept. If the aim is the acquisition of a larger package of shares in a short time frame, financing by bank credit is employed; the loan is paid back from company profits usually over an average period of 7 years.

3.3.3 The proven model of **workers cooperatives** should certainly be borne in mind when drawing up a future European framework. There are a number of good practices (see appendix) when a worker buy-out of a company in the form of a cooperative may be an alternative to the closure of a company that does not have any successors. The EESC considers that the very specific question of the link between financial participation and business transfers should be dealt with in a separate text.

3.4 **Enterprise crisis and employee share ownership**

3.4.1 Businesses may experience financially difficult times. In this situation the **priority is securing the business's future**. Where a crisis or restructuring is tackled jointly by management and workforce, EFP ought to be possible in this emergency but potential pitfalls must be considered. A sustainable solution is therefore needed, which allows employees, who have kept their jobs and their remuneration (having regard to flexicurity and periods of unemployment/retraining), to participate in the long-term in the recovery of the company and the economy. Employees' justified self-interest in the company's profitability and thus its long-term success will have a positive impact.

3.4.2 Financial participation in the company for which you work is often seen as posing a **twofold risk**. Critics of EFP often argue that, in the event of the company's insolvency, the employee would risk losing both his job and his invested capital. A clear distinction needs to be made

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Communication entitled Implementing the Lisbon Community Programme for Growth and Jobs COM(2006) 117 final.

between share ownership which is on top of the employee's salary and the kind where employee's savings are invested in the employer company. In the latter case the claims of employees should have priority, i.e. rank higher than those of other creditors in the event of failure and/or liquidation.. Furthermore, **pooling of risks and re-insurance solutions** should be stimulated also for cross-border situations.

3.5 **Corporate governance and employee share ownership**

- 3.5.1 Without prejudice to other forms of co-determination and employee influence on corporate decisions, employee share ownership may, depending on the way it is structured, lead to **participation in decision-making processes, via shareholder voting rights**, executed individually or collectively, i.e., via an intermediary entity.
- 3.5.2 Companies which issue large numbers of **employee shares** have a group of demanding but **patient and loyal shareholders**, their own employees, supporting them in resisting the prevailing short-termism of the financial markets. **Sustainable corporate decisions** and acceptance of **long-term corporate social responsibility (CSR)** by managers rather than excessive risk-taking are the desirable side-effects of this kind of EFP.
- 3.5.3 Capital participation of employees as shareholders ensures that the long-term interests of the company tend to dominate. **Good corporate governance**, which helps to ensure the long-term continuation of the company, is most likely the consequence.
- 3.5.4 Anyone whose stake in a company is his own job naturally wants full transparency on company accounts and participation in company decisions. In this way participation based on share ownership complements participation based on information, consultation and participation rights.

3.6 **Share ownership and participation in decision-making**

- 3.6.1 Contrary to widespread concerns – especially in companies without previous experience in this field - **EFP does not restrict the employer's autonomy**, but rather supports him in his decision-making processes.
- 3.6.2 For other shareholders in the company it is an advantage to know that they have the company's employees on board as shareholders, who are pursuing the same objectives. Positive **participation by employees based on ownership rights** and the resulting sense of responsibility can contribute to better corporate governance⁸ and offers the opportunity to exchange suggestions concerning enterprise strategy, thus enriching the choice of company decisions, within the limits described above. Employee shareholders must have the same rights as other shareholders.

⁸ In Austria, for example, there is the option of structuring EFP in the form of an intermediary entity.

3.6.3 Finally, it should be made clear that ownership rights acquired through EFP cannot and should not change either acquired co-determination rights in the Member States concerned or the contractual employer-employee relationship. These remain unaffected by EFP.

4. **A European approach: building blocks for practical problems and solutions**

The development and promotion of easily understandable and practicable models for European EFP would be of great political significance for the shaping of the European economic and social area. In principle participation in such models should remain voluntary for employers and employees. Their financing is supplementary to remuneration of labour and/or wages agreed by collective bargaining or profit-sharing.

4.1 **Combination of employee share ownership and profit-sharing as future trend in EFP**

4.1.1 With respect to deferred share-based profit-sharing – especially concerning the possible deferred taxation of employee’s benefits – three steps should be distinguished:

- The initial phase of sharing company profits with the employees.
- An intermediate phase when accumulated monies are invested in company stock.
- The final phase when the acquired shares are released to the employees.

4.1.2 Forms of share ownership, where the **acquisition of shares via a trusted fund** is financed by a profit share paid in addition to wages, already exist. This is normally done via a separate intermediary entity, which manages the shareholding held in trust for employees⁹. The governance of these trusts should be direct expression of all employee shareholders, with no influence from the management, in a democratic elective way. **Best practice examples of intermediary entities holding employee shares** are: AUCHAN¹⁰ (France); HOMAG AG¹¹ (Germany); Pfalz Flugzeugwerke (PFW Aerospace AG)¹² (Germany); Voestalpine AG¹³ (Austria); Oktogonen Foundation¹⁴ (Sweden); Herend-ESOP¹⁵ (Hungary); Tullis Russell-ESOP¹⁶ (UK); Eircom-ESOP¹⁷ and Aerlingus-ESOP¹⁸ (Ireland).

⁹ In continental Europe usually a limited company, foundation or association, in the UK and North America a trust.

¹⁰ Purpose: enhancing loyalty and employee motivation; <http://www.groupe-auchan.com/emploi.html>.

¹¹ Purpose: financing of growth; <http://www.homag.com/de-de/career/Seiten/mitarbeiterkapitalbeteiligung.aspx>.

¹² Purpose: EADS spin-off; <http://www.netz-bund.de/pages/mitarbg.es.pdf>, p. 32 et seq.

¹³ Purpose: privatisation and strategic shareholding; http://www.voestalpine.com/annualreport0809/en/management_report/employees.html.

¹⁴ Purpose: enhancing loyalty and employee motivation; see Handelsbanken, Annual Report 2009, [http://www.handelsbanken.se/shb/inet/icentsv.nsf/vlookuppics/investor_relations_en_hb_09_eng_ar_rev/\\$file/hb09eng_medfoto.pdf](http://www.handelsbanken.se/shb/inet/icentsv.nsf/vlookuppics/investor_relations_en_hb_09_eng_ar_rev/$file/hb09eng_medfoto.pdf), pp. 53, 56.

¹⁵ Purpose: privatisation as well as enhancing loyalty and employee motivation; <http://www.herend.com/en/manufactory/story/>, lacking details on ESOP, see year 1992.

¹⁶ Purpose: business succession; <http://www.tullis-russell.co.uk/group/about/>.

4.1.3 In order to permit the wider dissemination of intermediary entities facilitating employee share ownership, work should be done on the best practice examples (see also appendix).

4.2 Tax incentives and mutual recognition of EFP schemes

4.2.1 It has been demonstrated¹⁹ that tax incentives are not a precondition for EFP, but surely an **effective instrument for promoting their dissemination** in countries that offer them. Although they are the most widely used promotion instrument, a European regulation of tax incentives would go beyond European Union competences and conflict with national legislative powers. But as in reality transnational activities and career profiles are increasingly common, the fact that forms of EFP continue to be purely national in scope means that it cannot be expanded in Europe to the extent desired. Often the only way of introducing EFP in foreign branches is therefore to buy in expensive local expertise, which makes introduction so expensive that the idea is generally dropped. An **optional simple, uniform incentive model, with the same tax arrangements and incentives throughout the EU**, could considerably boost the number of cases where there is a willingness to introduce EFP, as this would make it easy to structure schemes available throughout a group of companies²⁰.

4.2.2 **Deferred taxation** could be taken as a lowest common denominator basis principle for a proposed model.

4.2.3 Before a European model with uniform tax incentives is established, **mutual recognition of the schemes** of the individual EU Member States should be the aim. This would improve the attractiveness and practicability of EFP even without a uniform European solution.

4.2.4 Besides tax incentives, companies can also grant effective incentives such as the discounting of shares issued to employees.

4.3 EFP in cooperatives

4.3.1 **Workers' cooperatives are a good example** for EFP, particularly when a majority of employees are both owners and workers. In compliance with the cooperative values and principles recognised world-wide, all worker-members have full participation rights in decision-making²¹. When workers own, control and manage their enterprises, experience shows that these guaranteed rights lead to better economic results and a higher capacity to

17 Purpose: privatisation and strategic shareholding; <http://www.esop.eircom.ie/>.

18 Purpose: privatisation and strategic shareholding; <http://www.aerlingus.com/aboutus/investorrelations/shareregister/>.

19 The PEPPER IV Report, Part. I, Chapter IV, pages 56-58.

20 See Thyssen Krupp: <http://www.thyssenkrupp.com/de/investor/belegschaftsaktie.html>.

21 See for instance ILO recommendation 193 on the Promotion of Cooperatives.

survive the crisis and therefore the long-term maintenance of their jobs in their regional living environment. Legally constituted representation will stimulate a framework for increased financial participation.

4.4 **EFP in the public sector**

- 4.4.1 The vast majority of EFP schemes apply to limited or public limited companies, where implementation is relatively simple. Certain types of enterprise, particularly in the non-profit sector - and thus their employees - are either excluded from this possibility by definition (public sector, non-profit organisations) or have very limited access to this arrangement (associations, foundations etc). There are, however, large numbers of people working in these areas, who should also have access to EFP.
- 4.4.2 Notwithstanding the principle of subsidiarity, the aim should therefore be to develop a model which offers the opportunity of financial participation to **all vocational groups and forms of enterprise**, taking into account the specific situation of the public sector.

Brussels, 21 October 2010.

The president
of the
European Economic and Social Committee

Staffan Nilsson

N.B: See appendix: the appendices can be consulted in English, French and German at <http://www.intercentar.de/en/research/focus-financial-participation-of-employees/eesc-own-initiative-opinion-soc-371/>.