

Participative enterprises in Estonia

Dear Ladies and Gentlemen!

I have the great honour of being invited to this conference and to introduce to you in my report Estonia and the situation with participative enterprises in our country.

When we speak of employee participation in enterprise ownership in Estonia, it is difficult to find Estonian-language terms. Such notions as participative enterprise or employee ownership are relatively unknown in our country. Just like in other Eastern and Central European states, Estonia has just recently become liberated from the socialist sphere of influence and possesses features that are characteristic of a transition period and of a market economy.

Just as the pendulum of the clock measures time by swinging from left to right, the same happens in the history of countries of the world. Estonia, as well as other Eastern and Central European states, has been moving from left socialism and plan economy with great speed to the right, towards market economy and liberalism. This swing of the pendulum is clearly manifested also in the development of our enterprises.

In the beginning of the 1990-ies in Estonia started the period of state-wide privatisation. Buildings, real estate, enterprises that had previously been in state ownership, were now designated for privatisation. For this purpose were used individual privatisation vouchers, the value of which depended on the number of work years. 98 % of the whole apartment housing stock was privatised on the basis of these vouchers to the inhabitants of these flats. State enterprises were also designated for privatisation.

In Estonia there has been relatively little research done concerning participative enterprises and it is difficult to find information on this subject. To some extent this sphere has been researched by the Estonian Statistics Office and the Estonian Institute for Future Studies. In this report I will give a brief overview of the situation with participative enterprises in Estonia, their role in our society and future development perspectives.

In the end of the 1980-ies, along with the arrival of the “perestroika”, began formation of cooperatives in Estonia. At that time it was the first and only possible form of private enterprise. By the beginning of 1990 there were already 2000 such new cooperatives registered in Estonia. By August, 1993, this number reached 3000. In connection with legislative changes, in the following period the majority of these cooperatives were re-registered as other juridical forms of enterprises.

The process of enterprise privatisation was swift in Estonia. If in 1991 more than 90 % of enterprises in the service and trade sectors belonged to the state or the local authorities, then in 1994 the percentage of privately owned enterprises in the service sector reached 83 % and in the trade sector – 90 %.

In 1995 there were 16 % of enterprises that were employee-owned and 10 % of enterprises were management-owned.

The employee ownership type of enterprises was most widespread in the agricultural sector, almost 40 % in January, 1995. Management ownership was more extensive in fishing, mining and wood processing industries – 27 %. In 1997 the total number of management-owned enterprises reached 26 %.

Our society developed in the direction of decreasing of the number of large employee-owned enterprises and simultaneous growth of firms with external participation and management-owned firms.

The process of privatisation and founding of new enterprises was just the beginning of the development of new structures of ownership.

As we can see from the information above, the number of employee ownership or participative enterprises, initiated in the beginning of the 1990-ies, has been on the decrease during the last decade, these enterprises now taking other shapes. The main reason for this change of shape is the inadequate understanding of the participants about the rules of a free market economy. The employees that became part-owners of their enterprises in the beginning of the 1990-ies preferred to exchange their shares for money. At the time of the introduction of the Estonian Kroon, from 1992 onwards, the majority of our population preferred to be in possession of some cash and lacked clear understanding of the implications of having a share in owning a business. So, quite often the shares were bought out by the management or by foreign investors. On the one hand, this decreased the level of employee participation in enterprise ownership, yet at the same time enabling more a flexible and professional running of a business, which in its turn helped such a business to cope in this new economic environment. It has a straight connection to the quick development of Estonian economy when compared to some other Eastern or Central European countries.

On the basis of the data from the Estonian Statistics Office, we can see that employee participation in enterprise ownership in 1990 made up 13 % of all the enterprises, in 1995 – 11 % and in 1997 8 %. From the year 1997 this percentage has remained more or less at the same level. The enterprise environment has become homogeneous and employee participative ownership of enterprises does not play an important role in the Estonian economy.

Estonian Business Register has data about the amount of companies in Estonia but there is not information available about employee participation in these companies.. Taking into account the different enterprise forms we can say that the number of employee owned or participative enterprises in Estonia is around 5000. It is almost 7 % of all the enterprises. 931 of these are worker cooperatives. The majority of the participative enterprises are in retail sales sector (30 %) and in agricultural sector (18 %), but also in industrial sector (9 %).

In addition to the above provided statistical data I should also mention the fact that the public at large lacks understanding on the subject of participative enterprises – they are not perceived as standing separately and possessing certain unique strengths. In

our young democracy there has not been enough information provided about various flexible forms of enterprises.

The activities of enterprises in Estonia are coordinated by Commercial Code. The activities of profit making cooperatives are coordinated by Commercial Associations Act. There is also special legal act - Non-Profit Associations Act - coordinating the activities of non-profit organisations and associations. According to the existing legislation employee owned enterprises can belong to any legal type of entrepreneurship.

The minimum capital for starting a new enterprise according to both Commercial Code and Commercial Associations Act is ca 2600 EUR.

Today the legislation does not have any advantages for participative enterprises. It is clear that there will not be any supportive amendments also in near future as long as the understanding about this enterprise sector is so little known. Therefore the very first priority for Estonian participative enterprises sector should be rising of public awareness, education and training

Participative enterprises have an important role in the state social policy and social economy. Together with cooperative sector, participative enterprises are important cornerstones of the social economy. For example, 30 % of Estonia's retail trade market is occupied by the shops of the Central Union of Estonian Consumer Associations'. In agriculture, 30 % of milk is produced in dairy co-operatives. Both employee participation in enterprise ownership and worker co-operatives, these two different forms of employee involvement in the management of a business are closely interconnected and play a joint important role in the social economy sector.

The well-known professor Francis Fukuyama stresses the importance of social capital in the society. According to Fukuyama's definition, social capital is one of the three types of capital, next to physical and human capital. Social capital is the ability, based on value orientations and unofficial norms of behaviour shared by people, to work together in the name of common goals and to have mutual trust. This is accompanied by several virtues, such as honesty and duty.

Fukuyama states that it is easier to create social capital inside an organisation with certain borders than in the society as a whole. Social capital means shared norms and values, which can be considered also characteristic of organisational culture. When studying effectively managed business organisations, we can notice that their management relies not on formal bureaucracy but on commonly shared value orientations both among the management and the employees as a whole, allowing them to have effective communications. The majority of problems with organisational efficiency is caused by the hierarchical system of management, where information moves from top to bottom and vice versa very slowly, and this is accompanied by lack of flexibility, distortions of the process of decision-making and other faults.

When people trust one another and act as a team, the results of their work are better.

Social capital plays a vital role both in politics and in economy. Every economic system is based to a large extent on co-operation. While one acknowledges strong individualism of enterprises, it should still be noted that every business is formed

through creation of a group of people who begin to cooperate. Social capital that is based on common values enables one to avoid paying the transaction costs, to decrease bureaucracy and money spent on lawyers, etc.

An enterprise where employees are connected by a joint interest in moving the enterprise forward, developing it, is the best carrier of social capital. Participative enterprises deserve special mention here. As we can see, post-socialist states are in this respect no different from countries of Western Europe. Estonia and other Eastern and Central European states may be different with respect to our recent history, but at the same time we all face the same challenges – urbanisation, globalisation, swift dwindling of energy resources. The spreading of the ideas of social economy in the whole of Europe plays its important role in strengthening enterprises, especially their social side, in every country. Estonia today lacks a co-operation network and coordinated activities of participative enterprises, and here we can draw on the experiences of Western states without repeating their mistakes.

In Estonia the attitude towards participative enterprises has so far been as towards an inevitability of the period of transition. There does not exist the understanding of possibilities of employee enterprises for creating new workplaces and of their role as the foundation of social economy – both on the public and state level.

The Estonian Union of Cooperative Housing Associations has during the last 2 years been involved in development of such a form of enterprise in Estonia within the framework of EU's SCOPE project. In the year 2001 first steps were taken towards uniting Estonian participative enterprises and worker cooperatives. A handbook of the corresponding content has been published. Also, in December of 2001 the first conference on social economy took place in Estonia, attended by representatives of all EU candidate states and various member states. For the first time in Estonia the issues of social economy and employee participation were raised for the general public and state officials, representatives of local authorities and of the third sector were invited to discuss these issues.

There has also been established Estcoop, the Estonian Associations Worker Cooperatives, Participative Enterprises and Social Economy Organisations, the first and foremost aim of which is to coordinate activities in this sphere in Estonia and inform our society of the existence of such structures. Estcoop perceives its near-time goal to be explanation to the public and to the state that social enterprises, where attention is paid to the employees, have their unique strengths in business competition and they also carry an additional value – that of increasing of the feeling of social security in the country. As an example, we can look at our Northern neighbour, Finland, where with the assistance of state-created development agencies many new worker cooperatives were established in the second half of the 1990-ies, and through this simple action large numbers of new workplaces were also created, especially in rural districts. Here we can learn from the strengths of our neighbour and implement such state support in our own country. It is clear that without strong public support there will be no progress in the development of participative enterprises in Estonia. That is why the recently established Estcoop aims first of all towards doing explanatory work on the state and local authority levels.

Hereby we have to stress the important work of CECOP, the European Federation of Workers' Cooperatives, Social Cooperatives and Participative Enterprises in developing the cross-European cooperation between social economy organisations and participative enterprises. CECOP has done an enormous work in raising the awareness about this sector in European Union level.

And to finish, I would like to stress that participative enterprises along with worker co-operatives and other forms of social economy enterprise are still underdeveloped in Estonia. Yet we cannot doubt the necessity of such enterprises now that Estonia is about to join the European Union. It is clear that as there is a lack of in-depth research into activities and efficiency of different enterprises, these issues has not been considered to be a priority on the state level. The Estonian Association of Worker Co-operatives, Participative Enterprises and Social Economy Organisations sees its role first of all in uniting such enterprises. It is clear that a form of enterprise management that takes into account interests of the employees needs additional research and coordination so that in the future in Estonia would also develop a strong layer of participative enterprises.

Thank you for your attention!

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Development of Central and Eastern European Network for promoting Employee Ownership and Participation

On behalf of the Institute of National Development and Cooperation in Estonia and myself, I would like to say thank you to the Exec.Dir. Marc Mathieu of the European Federation of Employee Share Ownership in Brussels and to Janos Lukacs and Katalin Monigl-Toth in the Budapest EFES office for inviting me to this conference, a conference that in my estimation could be a historical milestone in the development of employee ownership and participation, not only in Eastern and Central European nations, but also in the world-wide movement of employee ownership development as a viable alternative to the traditional free market system. I know that in Estonia we are taking on this challenge and I hope that many of you will join us. Lets make that important step together.

A few words about the guidelines that were sent to the participants. The guidelines contain four requests. I must apologize for not being able to provide you with any meaningful data or commentary about the first three. In my opinion employee ownership and workers participation in Estonia is limited to very few enterprises.. There are apparently some firms who have instituted various forms of worker participation programs in their business organizations, but I think that the cases are rare and insignificant in terms of an overall national ownership culture. Instead, my focus will be on the vision of employee ownership and participation in Estonia.

I will explore the Estonian vision of employee ownership by covering the following topics.
I will

- a) list three events that in my opinion have played an instrumental roll in making employee ownership a viable alternative to the traditional capitalist free market system in Estonia;
- b) attempt to explain why the concept of employee ownership was not feasible in Estonia right after the declaration of independence in 1991;
- c) argue why the privatization program in Estonia has failed;
- d) propose an action plan for the development;
- e) emphasize three topics/subject matters that need to be addressed;;
- f) finish the discussion by offering some words of caution as we are trying move forward.

The events that in my opinion have lead us to believe that employee ownership is now a viable concept are summarized below.

The first event was in March, 1991 when I personally had an opportunity to introduce the employee ownership idea to the Head of the State of Estonia, Arnold Ruutel in Washington, D.C. when he was visiting the White House and met with President George Bush. The submission was very concise, only two pages long plus a short preamble that in essence summarized our socio-economic problem. The preamble of my submission read:

The Plan is founded upon the following assumptions:

- 1. That the root cause of wars and conflicts between nations and peoples are hunger, homelessness, and s e v e r e inequalities of income distribution;*
- 2. That the traditional free market system is incapable of responding to the above injustices, since a significant degree of income inequality is functionally essential to its conventional mode of behavior*
- 3. that there are new economic systems conceivable, of which the proposed plan is one, that can make the free-market system work better, both economically and politically.*

I am arguing that one attractive alternative is to promote employee ownership as a means to make productive capital ownership possible for the economically impoverished sector of society. This would help to make the market system work much more productively. It would provide solutions to the problems of economic efficiency, distribution and justice which are left unsolved by conventional economic theories and practices.

The second event, that has improved the over-all climate for the development of employee ownership, happened about ten month ago, at a time when 26 prominent Estonian social scientists of the Estonian Academy of Science signed an open letter, stating that *"Estonian society has reached a political, social and ethical crisis. The powerful have removed themselves from the citizenry in such a degree that already one has to talk about two different factions of Estonia."* Another words, Estonian society has been divided into "the have and have nots". The "have" are the rich and the " have nots" are the powerless middle and the lower poverty stricken class. The gap between the two Estonias is continuing to grow. The open letter created a political debate and crisis in the Estonian political arena that eventually, in fall 2001, returned to the presidency the popular and pragmatic, previous Head of State of Estonia, Arnold Ruutel, who was defeated five years ago by President Lennart Meri, an intellectual and charismatic politician whose political orientation was very supportive of the traditional free market system. This event was followed by the crisis in government in February this year, bringing down the right wing oriented government, lead by Prime Minister Mart Laar, whose economic policy was emphatically supportive of privatization at any cost.

As a result of privatization, Estonia became the darling of Wall Street ideology. The whole story is best described by John Nellis, who writes in January 1996 on FDP Home Page how Estonia's public and private assets have been sold to foreign investors. Under the headline "Finding Real Owners - Lesson from Estonia's Privatization Program " he writes:

"The Estonian government has privatized more than 90% of its industrial and manufacturing enterprises. ...unlike most countries in Eastern Europe and the former Soviet Union, Estonia has avoided selling its state-owned enterprises into the control of insiders - workers and managers in the firm or financial institutions tied to the state. Instead, the Estonians have used a modified version of the German Treuhandanstalt's group tender method, which help to ensure that privatized firms have real owners serious about creating a productive enduring business and willing to pay a meaningful price."

The mastermind of the Treuhandanstalt's privatization program was the Estonian born German businessman, Andres Bergmann, who, while leading the sale of Estonian resources at wholesale prices to whoever was able to pay the highest price, Mafia included, formed new banks and financial institutions for himself in Estonia. As a result of such mismanagement his enterprises are now bankrupt, including his bank. He has been charged with fraud and is waiting for court hearings in an Estonian jail.

The above is important, because it explains partly at least, why we didn't succeed in promoting employee ownership in Estonia during the 1990s. During that period most people didn't dare to speak about it in public. Communism was defeated and the capitalist mode of the free market economy was the only good idea to be imitated. The few who made some overtures to question the ethics and flaws of the capitalist free market movement were quickly labeled as the proponents of "Bolshevik economics" - and that was enough to end the debate, if there was any.

And, finally the third event that has created a favorable climate for employee ownership building happened during the presidential election campaign forums when candidates outlined their political platforms. It was then when the newly elected president Arnold Ruutel had the political courage to tell the people of the "Two Estonias" that has split the nation into two distinctive socio-economic factions. In order for Estonia to survive as a small nation in the turmoil of the globalized world order, he called on the people of Estonia to start striving together towards democracy and a just society as " One Estonia".

Thus, the introduction of the employee ownership idea to Pres. Ruutel in 1991, the publication of the open letter by the social scientists of the Two Estonias, and the consensus seeking by Pres. Ruutel during the presidential election time have ushered in a new era in Estonia that could allow the politics of employee ownership to become a real alternative economic policy for Estonia. It can be implemented immediately. It would be financially feasible and it could be implemented without any delay. We would like to call it: *"Action Estonia - a new initiative in Europe"*.

The objective of the program is to draw attention to a new alternative for economic development that would reduce economic disparities between people and nations at a time when human intellectual and productive capabilities are such that economic security and prosperity could be provided for all. The intent of the plan is to demonstrate how it is possible to develop full participatory democracy and economic security, not in the far distant future, but now.

The model is built on a synthesis of three important economic principles / theories. The key idea is employee ownership, supported with land and monetary reform.

The outcome of the new economic model is a more productive economy. The program provides an opportunity to reduce homelessness and hunger in the world, and if properly supported with appropriate land and monetary policies would eradicate homelessness and provide an opportunity for every family household in Estonia to own their own private home. This would be record achievement never attempted yet.

The program could be described as cooperative, consensus seeking, self-organizing, and family and community oriented. It is supportive of small and medium size businesses.

Finally, I would like to underline three important topics/subject matters in order to succeed:

1. The need to place more emphasize on community and national development

The objective of the program is to develop a socio-economic system where basic human needs such as shelter, food, health-care, education and leisure would be fulfilled. Research and sound reasoning tell us that a focus on the economics of community and national development, if properly complemented with new ideas such as employee ownership, land and monetary reform will lead us to a better and more just economic system. It could preserve the nation's cultural and economic identity at a time when foreign dominance often undermines a nation's sovereignty and economic independence. The move doesn't mean that the exchange of goods and services between nations should be curtailed. International trade is not a new idea, but globalization is. The whole issue is best articulated by Professor Herman E. Daly, who in his Farewell Lecture to the World Bank in January 1994 advised the World Bank to *"move away from the ideology of global economic integration by free trade, free capital mobility, and export-lead- growth- and toward a more nationalist orientation that seeks to develop production for internal markets as the first option, having recourse to international trade only when clearly much more efficient. At the present time global interdependence is celebrated as a self-evident good. The royal road to development, peace, and harmony is thought to be the unrelenting conquest of each nation's market by all other nations. The word "globalist" has politically correct connotations, while the word "nationalist" has become to be pejorative.*

2. The need to know the difference between democracy and capitalism

The historical experience in combating economic poverty, both past and present, has quite clearly demonstrated that this cannot be accomplished within the parameters of the existing capitalist system. The fact is that the present free market system is impotent to fight poverty effectively, because in the present context of the free market system we have perverted the meaning of capitalism versus democracy. Almost invariably the two ideas are understood as if they are compatible and even, mean the same thing. The truth is that *"democracy and capitalism have very different beliefs about the proper distribution of power. One believes in a completely equal distribution of political power, "one man, one vote", while the other believes that it is the*

duty of economically fit to drive the unfit out of business and into economic extinction. Survival of the fittest and inequalities in purchasing power are what capitalistic efficiency is all about"

The quote is from the 1992 book by Prof. Lester Thurow, *The Future of Capitalism*. He is a respected American economist from the Massachusetts Institute of Technology.

3. The development of self-reliance and new wealth in Estonia by the citizenry themselves

The real importance of employee ownership program is that it will offer poor households as well as poverty stricken communities to find economic security and prosperity through building capital ownership into their household and community inventory - becoming new owners of productive capital that will provide them with a second income in addition to their labor wages.

The community development organizations should avoid outside investment and use it only as a last resort. Foreign equity investment can be a costly business, because while it is true that it can provide new employment opportunities to build and purchase new capital assets in the community, including high technology, it doesn't mean that the community will necessarily benefit from the investment in the long run.

Before welcoming new investors to a community, it is wise to first carefully investigate alternative development plans that are based on community self-reliance and sustainability, employing its own labor and capital resources. The employee and community capital ownership alternative should definitely be considered as a good alternative.

In Summary - a word of caution:

I am confident that the employee ownership idea is feasible and it will work in reality, *but only*, if certain steps are first accomplished with a substantial support from the citizenry and community leadership. It should:

- * harness the political will of elected members in the national assemblies to pay attention to the proposal, and subsequently, to support legislative action that will allow the program to work in reality;

- * develop an effective awareness and educational program that should be presented to the general public and to political and business leaders. The program should be produced as a public service via television, radio, newspaper, internet and community educational facilities. It should be taught already at high schools.

- * find resources, both human and financial, that are necessary for building the national and community infrastructures which are necessary for a sustainable economic development of the community, and that priority is given to the basic human needs to be fulfilled for every family household, i.e. building homes, producing food and providing appropriate health-care and education for all.

O l a f K l a s e n

Budapest, 1st of March, 2002