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 desirablebenefits 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 shareholders[1]. 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 results[2] 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.

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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 report[4] 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.

4 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.

5 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.

6 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.

3.3 Business succession and share ownership

3.3.1 The European Commission[7] 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 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.

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

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 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 governance[8] 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.

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 trusteed 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 employees[9]. 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: AUCHAN[10] (France); HOMAG AG[11] (Germany); Pfalz Flugzeugwerke (PFW Aerospace AG)[12] (Germany); Voestalpine AG[13]

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

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/mitarbges.pdf, p. 32 et seq.

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

(Austria); Oktogonen Foundation[14] (Sweden); Herend-ESOP[15] (Hungary); Tullis Russell-ESOP[16] (UK); Eircom-ESOP[17] and Aerlingus-ESOP[18] (Ireland).

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 demonstrated[19] 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 companies[20].

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.

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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, 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/.

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.

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-making[21]. When workers own, control and manage their enterprises, experience shows that these guaranteed rights lead to better economic results and a higher capacity to 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/.

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

APPENDIX
to the
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Appendix I

The Building Block Approach to an EU model

The publication entitled "Financial participation for a new Social Europe" (available in EN, DE, FR, IT and PL at http://www.intercentar.de/en/research/focus-financial-participation-of-employees/) sets out the path to a European solution and could serve as background material for the EESC opinion. It is a response to the European Parliament's report on capital formation and the Commission communication referred to at the beginning of this opinion. The proposal that it puts forward for a Council Recommendation on a European platform for financial participation utilising the Building Block Approach could then be voluntarily implemented on the basis of reciprocal recognition. An example of this is the December 2009 recognition of the French FCPE model and its tax deferment by the German tax authorities (a decision was also taken on equal treatment of similar German models).

Definition of the three basic elements of EFP

Referring to the catalogue of minimum requirements (e.g., being transparent, broad-based, etc.) the Building Block Approach reflects the existing postulates of the European Commission and neither relies on nor excludes tax incentives. All 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. The building blocks should consist of the three basic EFP elements:

1. **Cash-based and deferred profit-sharing**

In cash-based profit sharing and deferred profit-sharing schemes, part of an employee's remuneration is directly linked to the profits of the enterprise. In contrast to individual incentives, this concept involves a collective scheme which generally applies to all employees. The formula may include profits, productivity and return on investment. Bonuses are normally paid in addition to a basic fixed wage and provide a variable source of income. They may be paid out in cash or on a deferred basis into a company saving scheme, and can be invested in the capital markets or the company's shares.

2. **Employee share-holding (stock options and employee shares)**

In share ownership plans, shares may be distributed for free or may be sold at the market price or under preferential conditions. The latter may include sale at a discount rate (Discounted Stock Purchase Plan), sale at a lower price through forms of delayed payment (usually within a capital increase), or by giving priority in public offerings to all or a group of employees. To defer the valuation problem in unlisted SMEs, capital participation may initially take the form of an employee loan to the company, creating corporate debt (external capital) subsequently converted into company shares. Valuation of the shares designated for acquisition through the loan can be postponed until the moment of the actual conversion into shares (debt-to-equity) without impeding the implementation of the scheme.

Employee stock options, unlike executive stock options granted to reward individual performance, are broad-based. The company grants employees options which entitle them to acquire shares in the company at a later date, but at a per share price fixed at the time the option is granted. Potential gain from rising stock values is the primary reward conferred by options.

3. Employee Stock Ownership Plans as collective schemes

Employee Stock Ownership Plans (ESOPs) are funded by the company either contributing shares to the plan, contributing cash that the plan uses to buy shares, or by having the plan borrow money to buy new or existing shares. The schemes may be combined, resulting in the following essential structure:

(i) The company establishes an employee share ownership fund in favour of its employees (in continental Europe in the form of a limited company, foundation or association; in the UK and North America usually a trust-ESOT).

(ii) The fund is usually financed by a combination of company contributions and borrowings. Company contributions often are part of a profit-sharing agreement with the employees. The trust may borrow money directly from a bank or from the company, which in turn may take a loan from a bank or other lender. Shares are either acquired directly from the existing shareholders or by means of a new share issue.

(iii) The shares are held collectively in the trust, and are only allocated to individual employees accounts, or distributed, after a particular holding period.

(iv) The loan may be repaid by direct cash contributions from the company to the fund, monies received from sale of shares to the share-based profit-sharing scheme, or dividends on the shares held in the fund.

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Appendix II

Overview of national EFP models as of 2008, PEPPERIV report at:

http://www.eurofound.europa.eu/areas/participationatwork/pepperreports.htm

Summaries in EN/DE/FR/IT/PL at:

http://www.intercentar.de/en/research/focus-financial-participation-of-employees/the-pepper-iv-report/

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Appendix III

Examples of best practice

1. The French Auchan model for increasing employee loyalty and motivation

In 1961, Gérard MULLIEZ opens the first store AUCHAN in the « Hauts Champs » area of Roubaix (Nord). Other openings follow, firstly in France, then in Spain, in Italy, in Luxemburg, in Portugal, in Hungary, in Poland, en Romania and also in China, in Taiwan, in Russia, in Ukraine and Dubai, i.e. 13 pays. 4 core businesses: hypermarkets, supermarkets, shopping centres, banking.

AUCHAN is the world's 11th largest food retailer and n° 7 in Europe. € 39,7 billion in revenue before tax 2009; € 2,348 billion in EBITDA; € 661 million in profit for the year attributable to owners of the parent; 243 000 employees (average full-time equivalent).

A corporate vision: To improve purchasing power and quality of life of the greatest number of customers, with responsible, professional, committed and respected employees. **A single ambition:** To be a leading, innovative, multi-channel retailing group. **Unshakeable values:** Trust, sharing and progress.

An entrepreneurial project based on participative management:

- Share knowledge**:** training, information
- Share decisions**:** trust, enabling initiatives
- Share profit and stock: profit sharing and employee share ownership.

Financial participation, which complements individual earnings, is carried out by a compulsory profit sharing scheme ("participation" introduced in 1968) and a voluntary profit sharing scheme ("intéressement" introduced in 1972). In the framework of a savings plan these two schemes give employees the opportunity to acquire shares of the company.

Today AUCHAN GROUP stock is owned up to 87% by MULLIEZ Family and up to 13% by 110 000 employee shareholders in France, Spain, Portugal, Italy, Luxemburg, Poland and Hungary). The share value is fixed, yearly, by a college of 3 independent experts.

2. Employee Stock Ownership Plans (ESOPs) as a UK business succession tool

Employee share schemes are increasingly used in the UK as a business succession tool, though not nearly so often as in the USA. The main body of this report highlights the tragic situation all over Europe every year when privately owned businesses fold because their owners are no longer able to stay involved, but don't have anyone close to handover their business to, or who sell to asset strippers who close production centres and sack employees just to improve the operating margins of what survives. Owners who use ESOPs do not have to surrender control – they can sell ten, 20 or

30 percent of the equity to their employees if they choose. Some even decide to sell 100 percent of the business to their employees via one type of ESOP or another.

2.1 How is it done?

Set up an employee benefit trust. Basically, the company provides funds to the trustees, perhaps in the form of a loan. Alternatively, if the company is not privately held it can underwrite borrowing by the trust from a bank or other third party. The trustees use these funds to acquire shares from the retiring shareholder on impartial terms. The shares are used to set up an employee share scheme. This allows the owners to offer the chance of participation to all the full-time employees, under the same terms, though employees are not obliged to become shareholders. However, if a company's future is threatened - without radical re-organisation being imposed- then almost all the employees tend to participate. If established under a government tax-sponsored regime such as SAYE-Sharesave, Enterprise Management Incentive or the Share Incentive Plan (SIP), the employee share plan incentives will be taxed at low rates (or even escape tax altogether). A tax-efficient result is available for the selling shareholder, for the company and for its employees. These transactions can be attractive to proprietors who seek continuity in the business whilst receiving value for their shares.

2.2 An employee benefit trust is established

- The trust mechanism is financed by bank loans to purchase the company shares and to receive company profits to pay off the bank loans.
- The trust dispenses the shares to the employees through bona fide employee share schemes but also buys back the shares from the employees for subsequent recycling when they sell. Existing shareholders sell piecemeal to the employee share trust as a capital gains tax transaction to make shares available for employee share schemes and as a cash extraction mechanism. The shares are recycled through the trust for successive generations of employees who sell their shares on retirement.
- First, the company shares must be independently **valued** – not so easy if it's privately held. Obtaining value: the sale should take place on impartial terms, which will be subject to official scrutiny. HM Revenue & Customs generally attaches much lower values to private company shares than to quoted shares on the grounds that private company shares cannot be traded. If the sale has taken place at a price higher than HMRC consider fair they may seek to assess the difference to income tax. However if an employee trust has been established this can be used to create an ***internal market*** in the shares, which permits share sales by employees within the company. The existence of an internal market removes part of the justification for discounting the value of private company shares and can therefore result in a higher value.

2.3 Case history: Child Base

Based in Newport Pagnell, Buckinghamshire, Childbase, which is 50% privately-owned and 50% employee-owned, recorded pre-tax profits of £2.7m on a turnover of £27.7m last year. It is currently 31st among the Sunday Times list of 'Best 100 companies to work for in Britain'

What began as one nursery for 20 children in an English village is today a major business. As Child Base's chief executive officer Mike Thompson explains, his company operates 38 nurseries for children across south-east England, employing 1,100 staff. There has been a radical change in the long-term direction of the organisation, to carry Child Base forward as an employee-owned business. Child Base was a family business – Mike Thompson was in day-today charge and his father was the chairman. The Thompsons were the major shareholders, although the company also had a number of external investors. But over the past ten years this has changed. Staff at each of the nurseries have been encouraged to acquire shares in the venture, initially on a "buy one, get one free" basis, but most recently on a three-for-one basis. The remaining private shareholders are committed to transferring their shares to the Employee Benefit Trust, so that employees can either hold their own shares or own them collectively within the EBT. Meanwhile, the Thompson family holding is down to around 28 percent. The target for the next decade is to see the employee share holding increase to 100 percent.

Mike Thompson points out that shares have increased in value significantly over the past six years, with dividends increasing from 6p to 12.5p. Child Base organises share dealing days twice a year, in May and November, when shares can be bought or sold at the value set by the company's accountants. Child Base includes elected representatives on the Employee Benefit Trust, and Mr Thompson has to justify his position as chief executive by ability and not simply by the size of his share stake. Child Base's profits have provided a mechanism for the company (via the Employee Benefit Trust) to buy out some of the existing shareholders, including part of the Thompson family's own holding, an arrangement which Mike says offers investors a fair and equitable exit route.

2.4 **Case history: Parfetts**

Parfetts is a cash and carry business with operations at six locations across England.

Alan Parfett started the company with his wife and eldest son Steve in 1980. Alan retired in 1989 and Steve Parfett took on the role of Managing Director. As Steve's own retirement approached, the issue of business succession was considered. With no immediate prospect of the business being handed over to a third generation, the Parfett family took the decision in 2008 to transfer into employee ownership.

'We looked at all options, including a management buy-out, selling to overseas investors or selling to the competition,' says Steve Parfett. *'However, we did not want to see the company broken up and renamed. Having worked with John Lewis in my younger days, I spoke to them and began to appreciate there was a vibrant employee ownership sector, which sounded the ideal route to take.'* Steve says that the family felt it was more important to sustain the successful organisation built up over 28 years rather than to get 'top dollar' for the business: *'We're happy to do this to see the name of the business going forward and retaining independence.'* Parfetts two-stage process includes a phased handover to ensure continuity. The family has sold a majority shareholding to the employees,

demonstrating its commitment to employee ownership. The target is that Parfetts will be completely employee-owned within seven to ten years. (source: John Lewis Partnership).

3. The Voestalpine employee foundation as an example of strategic participation

Voestalpine AG has had an employee share ownership scheme since November 2000. It was developed within the group and, with its focus on the "strategic ownership" of employees of their own company, it constitutes a special case in the discussion of employee share ownership. The long-term block vote of the participating employees makes the workforce, with more than 10% of the shares, a major shareholder in the group.

3.1 The Voestalpine Group

Voestalpine AG is an international group specialising in steel manufacture and processing. The group consists of five divisions and approximately 300 companies operating in around 60 countries. Group headquarters is in Linz, Austria. Total turnover of around EUR 8.55 bn and EBIT of EUR 352 m for the financial year ending March 2010, achieved despite the extremely difficult conditions of the worldwide economic crisis, make Voestalpine currently one of the most profitable European steel producers. Worldwide the group employs a workforce of 39 800, about half of them in Austria.

3.2 Strategic basis and development of the model

In the course of the discussions between group management and the works council on the full privatisation of the group in spring 2000 (at that time the government held a 38% stake - now the group is fully privatised), the idea was mooted - which was unprecedented in Austria at that time - of a massive workforce stake in an economically successful company. The workforce as a major shareholder would stabilise the ownership structure and support the long-term development of the group. In addition to this basic objective, workers were also to be offered the opportunity of participating in the company's success. A private foundation was jointly set up to manage the workforce's equity stake.

3.3 The Austrian model

The Austrian system of collective agreements provides for "opening clauses", under which parts of overall wage increases may be used for a specific purpose. This instrument was used on a number of occasions in Austria to finance share allocations in accordance with company agreements. Shares were also issued to workers regularly in connection with annual bonuses (profit-sharing). The tax relief available in Austria on share issues of this kind increases their value. All employees in Austria are included in the model on this basis. As the beneficial owners of shares, employees are entitled to dividends and they combine their voting rights throughout their period of employment at the group through the Voestalpine private foundation for employee participation. This joint management of shares by trustees makes it possible for the workforce to act collectively as a major shareholder at group general meetings.

3.4 The international model

Because of different legal bases, it has not been possible to "export" the Austrian model in its existing form. A compact model had to be developed which, despite major differences in tax law and also labour law in Europe, could be used in the most diverse countries. Beginning in the Netherlands (from 2004) and later in the United Kingdom and Germany (from 2009), a model of this kind was implemented following extensive development work. Employees were offered the opportunity of acquiring shares in their own company at discounted prices. The shares entitle their owners to dividends and cannot be sold for a period of five years. Voting rights are combined on an international basis through the Voestalpine private foundation for employee participation. The joint policy line to be taken in discussions at the AGM is hammered out through the group's European works council. The average participation rate for these three countries is around 15%. International employee participation is being steadily developed, with the planned successive integration of other countries.

3.5 Experience at the group

At present around 21 400 employees in 49 Austrian companies and 32 companies in the Netherlands, the United Kingdom and Germany own shares in their own company through the two variants of the model. In total employees currently hold 13.3% of voting rights in Voestalpine AG (more than 22 million shares) and thus at present constitute one of the group's three largest shareholders.

After ten years of experience of employee participation, the stakeholders in the model, management and the works council, but also the workforce as a whole, can conclude that the experiment has been successful overall. Share ownership has undoubtedly fostered greater identification with the company and encouraged employees to take a greater interest in the group's economic progress. The participation model makes it possible to participate personally in the company's success through dividend payments and possible increases in the value of shares by the time they are sold. In particular employee participation in the form of strategic ownership extends the workforce's opportunities for contributing to the group's long-term development, which can be seen as a useful complement to the participation rights of employee representatives laid down in labour law. The workforce's massive participation in Voestalpine AG's share capital also constitutes a "poison pill" to guard against hostile takeover bids, it brings stability to the ownership structure and offers partnership in major corporate decisions through group general meetings, in the interests of all employees.

With the development of this employee participation model, the in-house partners in Voestalpine AG have reacted creatively to new challenges. The model's success to date and its high level of acceptance by the workforce form the basis for ongoing development and the rolling out of employee share ownership to employees throughout the group.

4. Cooperatives – Transferring ownership of an enterprise to its employees as a workers' cooperative

Many companies disappear and will continue to disappear in France for want of anyone to take them over. One possible solution to this problem is insufficiently well known: the transfer of ownership of the company to its employees in the form of a workers' cooperative (French: SCOP). This means transferring to the workforce the means of production which they themselves have helped to prosper. It also involves the owner in a managed handover of control to company employees. The transfer is progressive as shareholders withdraw. In this way the industrial capital is preserved, along with the company's relationship with its customers, suppliers and partners. Sellers and buyers receive support throughout the process from the Scop Entreprises network.

The first step is to work with the seller and his entourage: accountant, lawyer, investment adviser and even the family. A complete case-by-case analysis is conducted of the appropriateness of a transfer of ownership to the employees. All obstacles are identified, both objective and real ones, and subjective ones - arising mainly from a change of perspective, in order to ensure that the employees will be able to keep the company on course. Management potential in particular is examined. More often than one might think there will be one or more individuals among the employees capable of becoming managers. And if not, external recruitment can be envisaged. Apart from the human aspect, there is also the financial one: Will the employees be able to finance the buyout?

Scop Entreprises explains in detail the advantages of a cooperative approach: indivisible reserves constituting a collective asset which ensures the company's financial soundness, fair participation in major decisions on the basis of the one person, one vote principle, close connection with the local area, motivation and dynamism harnessed to the project. Not only the seller but also the employees have to be convinced of their ability to take over their own company, with or without the assistance of one or more external buyers.

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4.1 Preserving the structure in competition with the major distribution groups

Récapé Scop SA, meat retailer, Haute-Garonne, 120 employees. Buyout from retiring owners in 2004.
The history of Récapé goes back to1974, with its establishment as a limited company by Max Récapé. In 1998, eight years after the company went public, the founder retired and chose to sell out to company employees. In 2004 the shareholders' agreement expired and several of the managers retired. In order to prevent the generational transfer problem recurring, the youngest associates decided to convert the company into a workers' co-operatives.

"We became a cooperative in November 2004", recalls Michel Rayssac, CEO of the cooperative. "But according to the experts who advised us we had already been behaving like a cooperative for years!" Philippe Benzoni, accountant with the firm Sygnature, adds: "The Récapé shareholder pact described the operation of a cooperative without realising it! Rather than looking for an external investor, the associates decided to become a cooperative, a course of action which responded to the company's needs: to ensure stability, involve workers democratically and attract finance while reducing previously very heavy business taxes."

Opening up the company's capital to employees also boosted the company's equity. Since late 2005 all employees have been able to take a capital stake in the cooperative, following an information campaign by managers. "The objective of becoming a cooperative was twofold: to maintain the company's structure in competition with the major distribution groups and to bring about a transfer of ownership which treated everyone fairly", Michel Rayssac recalls. With just over 100 employees and 12 branches in the Haut-Garonne department, the Récapé cooperative is a major local actor in the meat trade (shops, processing of meat products, distribution). Its turnover for the last financial year was EUR 14 million.

Pierre Liret. *Site : www.recape.fr*

4.2 **Ceralep, a world leader in its sector**

Ceralep, electrical insulators, Drôme, 50 employees. Employee buyout following the company's liquidation by a pension fund in 2003.

The Ceralep factory, at Saint-Vallier in the Drôme region, a manufacturer of electrical insulators for pylons and electrical cables, which seemed set to close in early 2004, was saved by its workforce who set up a cooperative. When the commercial court at Romans decided to liquidate Ceralep on 28 January 2004, only a few employees and trade union activists believed that the company still had a future. Among them were Bruno Piazza and his deputy, Robert Nicaise. The company was productive and the workforce skilled, but PPCI, the US pension fund which put the company into liquidation, had run down the company's business in order to poach its customers. The representatives of the CGT trade union on the works council lost no time and obtained promises of firm orders. They also had the idea of setting up a workers' cooperative. However, the savings of the employees interested in the scheme were not sufficient to raise the EUR 100 000 needed as a financial guarantee for the cooperative. The works council then made a public appeal in the markets of the region and distributed leaflets. The Drôme General Council and a number of municipalities contributed, and in less than four weeks contributions from employees and some 800 individuals made it possible to make an application to the Romans commercial court, which on 15 April 2004 ratified the establishment of the cooperative, which was able to keep on 53 employees out of an original total of 92. Robert Nicaise took on the management of the cooperative. Since the buyout, Ceralep has exceeded its targets each year (annual production 1 200 tonnes) and has moved back into profit. Today it is a world leader in the manufacture of very large, one-piece insulators, and the European leader in high and very high voltage insulators. The company has held onto its customers (Areva, Nexans, ABB, Siemens etc.) for its traditional insulators and it is working on new projects with the French atomic energy agency (CEA) for the storage of nuclear waste. Investment is the cooperative's priority: "The workforce knows that, if we are to meet orders, we need good production facilities, and that if we want wage increases, we have to make profits", Ceralep's CEO commented.

Website: **www.ceralep.com**

Extract from an article by Gérard Méjean which appeared in Le Monde on 13 February 2007