



# ***The Promotion of Employee Ownership and Participation***

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*Executive summary*



Inter-University Centre

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## **Abstract**

This Study provides an overview of the development of employee financial participation, in particular employee share ownership, across the EU-28. Against the background of the policy development of the past 30 years, it highlights the growth of financial participation of employees over last decade using the most recent 2013 European Company Survey data which also show employee financial participation's potential positive impact on employment and productivity. The study analyses a range of policy options in depth and makes recommendations to the Commission in the form of a five-point plan. Most importantly, it proposes the establishment of a Virtual Centre for employee financial participation including an effective tax rate calculator in the short term, the development of a code of conduct in the mid-term, and an optional "Common European Regime on Employee Financial Participation" in the long term. Overcoming the barriers especially to cross-border plans, is particularly important in view of the potential described in this study for EU companies to implement such schemes and benefit from their impact.

## Executive summary

### Background and aim of this Study

The European Commission's interest in employee financial participation (EFP) has grown substantially since publication of the first PEPPER Report in 1991 and the Council Recommendation on EFP of 27 July 1992. Opinions drafted by the European Economic and Social Committee, most recently in 2010, as well as Reports and Studies by the European Parliament and a **2014 Resolution on EFP** emphasised the growing importance of EFP, particularly with respect to small and medium-sized enterprises (SMEs).

Against this background, the Commission included the promotion of employee share ownership (ESO) in its **Action Plan to reform European company law and corporate governance** and embarked on **the 2013/14 Pilot Project**. Based on the most recent data on the scope and impact of various EFP schemes in EU companies and the legal and regulatory changes in individual Member States, the aim of this Study is to identify the main obstacles to cross-border EFP schemes and to **develop detailed policy recommendations** for the promotion and encouragement of employee ownership at EU level.

### Types of EFP plans, their benefits and increasing incidence

Financial participation of employees can take a variety of forms:

- **individual employee share ownership** (employee shares or stock options);
- **Employee Stock Ownership Plans** (ESOPs, i.e., collective employee share ownership, with shares acquired through an intermediary entity, financed by a share of profits allocated to employees in addition to their remuneration);
- **profit sharing** (PS, i.e., in cash or shares, paid immediately or deferred).

Thirty years of research have confirmed that companies partly or entirely owned by their employees are more profitable, create more jobs and pay more taxes than their competitors without employee ownership. At the **macroeconomic level**, EFP leads to higher productivity and, therefore, higher competitiveness and growth as well as strategic stabilisation of ownership. At the **company level**, it can contribute to solving problems such as absenteeism, labour turnover and the retention of key employees, as well as business succession and funding, especially in SMEs and micro-enterprises. At the **regional level**, EFP encourages enterprises to stay rooted in their home communities, enhancing the purchasing power of employee households while discouraging outsourcing and hostile takeovers. Of course, it is also important to take into account the potential negative aspects associated with ESO, such as the risk borne by employees.

The most recent rounds of different **large scale cross-country surveys** (2010 European Working Conditions Survey, 2010 CRANET, 2013 European Company Survey (ECS)) show that in the last 15 years—despite the period of economic and financial crisis companies increased their offer while employees continue to expand their participation in ESO plans in Europe. According to the ECS data, between 2009 and 2013 the proportion of firms offering **ESO schemes rose from 4.7 per cent to 5.2 per cent** (an increase of 10 per cent) and that offering **PS schemes from 14.3 per cent to 30.2 per cent** (the incidence more than doubled).

## Challenges for the promotion of ESO

The ECS data suggests that firms with ESO or PS schemes are more likely to experience significant increase in both productivity and employment. However, despite the acknowledged positive effects and the widespread use of EFP schemes throughout the EU, they have been extended to a significant proportion of the working population in only a handful of Member States. Today, about **68 per cent of firms in the EU do not provide any form of financial participation to their employees**. At the same time, the latest analysis of the ECS data estimates that at least **300,000 small firms across the entire EU-28 could be potential candidates for the introduction of EFP**. If these prospective firms actually decided to offer an ESO or PS scheme, there would be a significant improvement in both productivity and employment—and thereby competitiveness—of these firms.

ESO is much less frequently used in Europe than, e.g., in the U.S. If this **still largely unexploited potential** is to be harnessed, the further development of financial participation, ESO in particular, should be part of an overall strategy for stimulating sustainable and inclusive growth of the EU economy. However, **barriers especially for cross-border EFP plans arise** from: a) differences in regulatory density, application and legislative requirements of national legal frameworks or b) differences in the fiscal treatment of existing schemes. Although the scope and types of these obstacles are diverse, the actual effect on the spread of cross-border EFP schemes is the same; firms will need to collect a large quantity of information, which will involve high costs and considerable expert knowledge—two obstacles that many companies, especially SMEs, may not be able to overcome.

## Policy options and recommended measures to promote EFP

If the policy objectives of promoting EFP at the EU level are to be successful, measures beyond the assessment of the current situation and the identification of best practice are necessary. Considering the current interest in EFP, triggered by the 2014 EP Resolution as well as the Pilot Project, immediate action is advisable in order to maintain momentum. **Information sharing and awareness raising measures** are crucial in the short to medium term; creating a level playing field for EFP through **a European legal framework** is important in the long term.

A package of different short, medium and long-term initiatives, combined in a **Five-Point Action Plan to promote EFP** coordinated and promoted by the Commission, is suggested. As a first step the launch of a “**Virtual Centre for EFP**”, presented in this Study, could be an effective means of making the necessary and relevant information provided by this Study available to those needing such information (especially SMEs). The promotion of best practice examples for EFP could be best accomplished by means of a voluntary **Code of Conduct for EFP**, to be regularly amended by, e.g., a **Commission Expert Group**. Parallel measures to raise awareness, e.g., a **European EFP Day**, could accompany and frame the above measures.

With regard to the much needed **transparency on taxation and social security contributions** for the various national EFP schemes, the **online effective tax rate calculator**, presented in this Study, would make it possible to quantify the effective tax burden for EFP schemes across the EU-28 and thus provide a representative comparison of the effect of tax systems as well as of specific tax incentives. However, this tool would need to be tested with stakeholders and practitioners to collect feedback.

The establishment of a binding legal framework on EFP through hard law instruments, e.g., by means of a **Framework Directive on EFP**, would lead to the harmonisation of national legislation. This would clearly have the largest impact on removing obstacles to EFP, particularly to cross-border schemes. However, to avoid conflict with existing national EFP models, a more pragmatic policy option would be to develop and implement an optional **Common European Regime for EFP** either through a Regulation or a Directive. Either variant would present the most ambitious policy option in the long term.

As part of the Pilot Project, the **conference "Taking Action: Promotion of Employee Share Ownership"** was organised on 30 January 2014 in Brussels. The Conference was followed by an online survey of participants. The positive feedback from the Survey indicates the commitment of the stakeholders to take actions to promote EFP in the future.

### **Focus: EFP information centres**

An important element of an information and awareness raising campaign, an integral part of the Pilot Project, is the **establishment of an information platform for EFP**. Here, European firms could find both general information on national legal frameworks and information on fiscal treatment of different EFP schemes in the EU-28 to assist in deciding whether or not to introduce a cross-border plan. The costs, impact and administration of such an information platform would differ according to its form, e.g., whether they would be physical or virtual.

**A virtual information centre** would deliver best results vis-à-vis the given criteria. The main advantage of the *Virtual Centre for EFP*, proposed in this Study, in comparison with physical centres, would be to **provide quality information at low cost** (EUR 780,000 compared with EUR 3.6m per year for one physical centre and EUR 6.2m for 28 centres). The virtual centre is more cost effective since it requires only one central administrator. This facilitates **quick response to local market changes** via push updates to the web application and shorter communication lines in general. However, the larger and more personal scope of the physical centres could justify their higher costs. Their establishment, however, could be made conditional on self-sustainable financing.

**Programmed as a web-based plug-in**, the prototype of the *"Virtual Centre for EFP"* could be easily integrated into an unlimited number of existing websites. Since well-established information channels used by the target groups would have a multiplier-effect, the coverage is potentially wide and the cost low. **Regular updates of the information would be managed centrally** through the back end. The cost of launching the Virtual Centre and the CETREPS Calculator for a pilot period of 18 months is estimated at EUR 75,000. Once tested, the operating cost for the Calculator (EUR 100,000 per year) and the annual operating cost of the Virtual Centre (EUR 250,000 per year) are estimated to be roughly EUR 1m for a pilot phase of three years.

### **Legislative proposal for a Common European Regime on EFP**

An optional Common European Regime on EFP would introduce a **"market approach" to harmonisation**, triggering competition between the existing national rules and the newly introduced second EU-wide regime, similar to the approach in the proposal for a Common European Sales Law. Employers and employees in all EU Member States could **choose to operate EFP plans under one single European regulatory**

**framework.** At the same time it would do without the conventional EU harmonisation procedure. Excluding taxation issues, this proposal would be the least invasive legislative measure and thus could be expected to achieve the necessary consensus within the **ordinary legislative procedure according to Art. 114 TFEU.**

Since national best practice influencing the common European regime would be expected to prevail in this market-based approach, over time this development could eventually lead to **mutual approximation of national regulation.** Furthermore, in many countries rules on EFP are only rudimentary. The common European Regime would be above all an optional solution to **complement national law where rules do not or not sufficiently exist.** While in some Member States the common European regime would introduce coherent rules for the first time, in the majority of countries, it would overlap only with the area of existing national regulation dealing with a specific EFP scheme. Only in a minority of Member States would it actually duplicate national law.

Firms could also utilise the Common European Regime on EFP in domestic settings. This advantage is of primary importance for **SMEs, which could easily extend a plan based on the optional common European regime across borders, as they grow and expand.**

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