3. Overview – Employee Financial Participation in the EU

Employee financial participation (EFP) either in the form of share ownership, individually or through trusteed plans such as ESOPs (Employee Stock Ownership Plans), or in the form of profit sharing has been practised in EU Member States for many years. Although, financial participation has been in the European Commission's focus of attention since the publication of the first "PEPPER Report" in 1991 it has only recently gained broader attention on the European level. As EFP can have a significant impact on a number of economic, social and employment issues in the EU, it is increasingly considered to be a relevant tool to contribute to the goals defined by the Europe 2020 strategy, most notably to establish “smart, sustainable and inclusive growth” within the European economy.

There are three main models of EFP from which a company may choose: profit sharing (cash-based, deferred or in shares), individual employee share ownership (employee shares or stock options) and employee stock ownership plans (ESOPs). Hence, EFP can be both share and cash based. Which EFP model a company chooses depends on a set of specific circumstances including the legal form of the company, the scope of intended involvement of employees and the result any EFP scheme is expected to produce. Depending on the respective model, EFP offers a range of positive effects on businesses, employment and the economy’s performance as a whole.

Benefits of EFP

EFP improves EU firms’ competitiveness by productivity gains arising from increasing employees' loyalty and identification with the company. But implementing EFP has many other positive effects for both sides, the employer company as well as the participating employees.

Improving workers’ performance and retaining key employees

- EFP schemes, both employee share-ownership and profit-sharing models, are known to significantly improve employees’ job satisfaction, increase their motivation and consequently boost workers’ performance and productivity which could eventually result in an increasing competitiveness of the company.
- Further, employee share ownership encourages workers to develop a sense of ownership and responsibility that increases their feeling of inclusion and the likelihood that their employers will engage with them and understand their concerns, perspectives and ideas. The mutual trust and appreciation could help employees to have a better understanding of the situation when their company faces challenges and can play a significant role in involving workers in information and consultation processes during restructuring.
- Implementing EFP schemes helps companies to retain skilled workers and highly qualified employees, and thus creates an incentive for employers to invest in the training of their workforce, given the greater likelihood of them retaining skilled workers in the long term. This is of special importance for SMEs, which face strong competition to attract and retain high skilled workers.

EFP and Corporate Governance

- Employee share-ownership may encourage a desired change from short to long-term incentives. Companies with a significant employee shareholder base gain a bloc of demanding but loyal shareholders made up of their own employees who understand the firm more intimately than outsiders ever could. In this way employees support management in resisting the prevailing short-term policies of the financial markets and may impose some constraint on opportunistic managerial behaviour and short term oriented management.
- Employee share ownership can in-crease employee participation and reward the assumption of new responsibilities at both the shop floor and shareholder levels including issues of transparency and exchange of information.
- EFP schemes could contribute to higher transparency of remuneration: employee shareholders having a “say on pay” contributes to making executive compensation transparent, a step toward more sustainable remuneration policies. As knowledgeable insiders they can exercise effective ‘oversight’.

EFP and Business Succession

- Employee Buy-Outs (for example through 'ESOP' Buy-Outs) constitute an alternative to selling a company to a competitor (strategic buyer) or to realizing a management-buy-out. Therefore, implementing an ESOP constitutes a valuable tool for business succession especially for owners of SMEs and micro enterprises which could otherwise struggle to find a suitable buyer and might be closed down when succession is not possible.
- Such employee buy-outs, which can also help workers take over companies in financial difficulty, may increase job security by safeguarding workers' own jobs and reducing uncertainty from possible buyouts by other companies.
- As the Commission has made the business transfer problem a priority of the Entrepreneurship 2020 Action Plan, promoting ESOPs as a relevant business succession tool is especially timely.

EFP on the EU policy agenda

EFP has been in the European Commission's focus of attention since the publication of the first "PEPPER Report" in 1991. With a view to a new Community instrument on the promotion of participation by employed persons in profits and enterprise results, the European Commission funded a research project with the specific aim of obtaining a good overview of the "state of the art" concerning financial participation by employees in the EU. Its conclusions are included in the PEPPER I report. A Council Recommendation followed this first report in 1992. This highlighted the importance the Community attached to the use of financial participation schemes and called for the direct involvement of Member States and the social partners. Following this, the Commission adopted the PEPPER II report in January 1997 designed to give a review of the effects of the previously mentioned recommendation 92/443/EEC in the Member States.

Based on the conclusions of these reports, in 2002 the European Commission launched a Communication on a framework for the promotion of EFP (COM (2002) 364 final). This communication established a working group of independent experts to analyse legal and legislative obstacles to the transnational diffusion of EFP, with concrete proposals for actions to tackle them. The European Commission published the report of this high-level expert group on 'cross-border obstacles to financial participation of employees for companies having a transnational dimension' in 2003.

The PEPPER III Report (2006) extended the previous two reports to cover the new Member States and Candidate Countries (Croatia, Bulgaria. Romania and Turkey) of the EU. In 2009 the PEPPER IV Report summarised and updated the previous reports. It presents conclusive evidence that the past decade had seen a significant expansion of employee financial participation in Europe but that, despite this positive trend, it seems that financial participation has been extended to a significant proportion of the working population in only a handful of countries.

The European Parliament has also repeatedly taken a positive stance towards promoting EFP. Notably, in its Resolution of 6 May 2009 on the Renewed Social Agenda (P6_TA (2009)0370), the European Parliament noted the importance of EFP schemes in providing an additional source of income for employees and suggested a European debate on possible solutions for a common EU framework regulation on EFP. A recent study on "Employee Financial Participation in Companies' Proceeds" (2012, ref. PE 475.098) commissioned by the European Parliament – which provides a comprehensive appraisal of the development of EFP in the EU – proposes an alternative approach to a common European framework on EFP, namely the introduction of a 29th regime that would implement an additional and optional second model of EFP alongside the national schemes. In its Own-Initiative Report on EFP (2013/2127(INI)), adopted on January 14th 2014, the Parliament suggests to further develop this concept and again highlights the paramount importance of EFP for the European economy.

The EU project "Implementation of the Pilot Project - Promotion of Employee Ownership and Participation"(MARKT/2013/019/F2/ST/OP) therefore assesses EFP across the EU-28 and aims at the formulation of possible regulatory and non-regulatory actions to promote EFP at EU level. The pilot project is part of the European Commission's 2012 Action Plan on European Company Law and Corporate Governance.[1]

[1] For additional information and more detailed analysis of EFP, see Lowitzsch, J., Hashi I. et al., 2012, European Parliament Study: Employee Financial Participation in Companies' Proceeds (PE 475.098),