

**TAKING ACTION:
PROMOTION OF EMPLOYEE SHARE OWNERSHIP
IN THE EUROPEAN UNION**

- ESO AND LONG-TERM INVESTMENT**
- THE CALL ON THE EIB TO FINANCE ESOPs**
- ESO & THE COMMISSION PROPOSAL ON AN ELTIF REGULATION**

Centre Albert Borschette (CCAB)

30 January 2014 in Brussels

Dr Jens Lowitzsch, Professor of Comparative Law, East European Economic Law and European Legal Policy;
European-University Viadrina Frankfurt/Oder; contact: lowitzsch@europa-uni.de

For more information <http://www.intercentar.de/en/research/focus-financial-participation-of-employees/>

Overview of the issues

- **Background: EC Action Plan on Corporate Governance**
 - ESO = long-term investment -> stabilising effect on cap.markets
 - Transparency / Sustainability / Responsibility
 - Topic has arrived at the core of economic policy
- **Broader Policy Approach**
 - Green Paper on long-term financing in Europe
 - EP Own Initiative report on long-term financing
- **Financing Business Succession in SMEs -> Call on the EIB**
 - Modernising the EIB products & Boosting SME lending
 - Mezzanine financing in ESOP transactions
- **Linking ESO and the EU's Long Term Investment strategy**
 - Regulation on European Long-term Investment Funds (ELTIF)
 - Increasing attractiveness of ELTIFs for retail investors

Action Plan to modernise Corporate Governance

-> The role of Employee Share Ownership (ESO)

ESO = **long-term investment** -> stabilising effect on capital markets

-> is seen as counter weight to speculative short-term investment

Three interlinked issues relate ESO to corporate governance:

- information sharing (-> **Transparency**)
- long-term shareholding (-> **Sustainability**)
- participation in decision-making (-> **Responsibility**)

Firms with ESO gain a bloc of demanding but loyal shareholders,

-> their employees, who **know the firm better than outsiders**

(Employee) shareholders having a “say on pay” contributes to

-> making **executive compensation more transparent**

ESO increases participation & rewards assumption of responsibility

-> at the **shop floor level and the shareholder level**

Long-term financing in the EU: 2013 Green Paper & ECON Own-Initiative Report

Private households are found to be the main source of funds for financing investment,

-> although they generally prefer liquidity and easy redemption.

Employees holding stock in their employer company have a different perspective;

-> they tend to have a commitment to long-term investment.

Promoting ESO:

-> contributes to Green Paper objectives

-> Increasing attractiveness of LTI for retail investors

Proposition to the European Investment Bank to modernise SME lending

Promoting Employee Stock Ownership Plans (ESOPs) as a vehicle for business successions in SMEs

- Commission has made business transfers one priority of the Entrepreneurship 2020 Action Plan
- The Small Business Act (SBA) and the 2011 Review of the SBA for Europe have specifically addressed the area of business transfers

Among intangible investments eligible for financing:

-> Costs incurred in enterprise transfer enabling continuation of economic activity (financing < EUR 1m).

Context: COSME and HORIZON

Both the COSME and the HORIZON program expressly support SMEs

-> promoting employee buyouts should be included as an option to finance business successions.

Both offer equity and debt instruments building on the same platforms:

- COSME to all SMEs
- Horizon 2020 to innovative SMEs and mid-caps

Integrating employee share ownership into the EU's Long Term Investment strategy

Context: Commission proposal for a Regulation on European Long-term Investment Funds (ELTIF)

-> Employee share ownership schemes are eligible assets for the anticipated ELTIFs

Introducing specific sub-classes of ELTIFs into the Regulation (Whereas...") with the aim of

- Financing business succession of SMEs through ELTIFs
- Financing growth of SMEs through ELTIFs

-> Increasing attractiveness of ELTIFs for retail investors (EP own-initiative report)

Overview

Composition of the of the ELTIF vehicle

(Limitations for certain types of assets / issuers in % of total value of the ELTIF)

<p><i>min. 70%</i> of its capital invested in eligible investment assets and invest no more than:</p> <ul style="list-style-type: none"> (a) 10% of its capital in assets issued by any single qualifying portfolio undertaking*; (b) 10% of its capital in an individual real asset*; (c) 10% of its capital in units or shares of any single ELTIF, EuVECA or EuSEF; (d) 5% of its capital in assets referred to in Article 8(1)(b) where those assets have been issued by any single body. 	<p><i>max. 30%</i> of its capital in liquid securities (liquidity buffer) allows:</p> <ul style="list-style-type: none"> (1) to manage the cash flow that arises while the long-term portfolio is being constituted and (2) to place surplus cash that is achieved 'between investments' – that is when a long-term asset is sold in order to be replaced by another.
<p><i>max. 20%</i> aggregate value of units or shares of ELTIFs, EuvECAs and EuSEFs in an ELTIF portfolio shall not exceed;</p> <p><i>max. 5%</i> aggregate risk exposure to a counterparty of the ELTIF stemming from over the counter (OTC) derivative transactions or reverse repurchase agreements</p>	<p><i>max. 30%</i> borrowing of cash provided:</p> <ul style="list-style-type: none"> - it serves the purpose of acquiring a participation in eligible investment assets; - it is <i>contracted</i> in the same currency as the assets to be acquired with the borrowed cash; - it does not hinder the realisation of any asset held in the portfolio of the ELTIF; - it does not encumber the assets held in the portfolio of the ELTIF.