Extended Country Report

Financial Participation of Employees in Poland

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1. Background

The most significant form of employee financial participation in Poland today is employee ownership, although, if we exclude one-person firms, generally employee ownership in Poland can be said to be marginal. It has been created primarily during the privatization process, especially in firms privatized by leasing and transformed into so-called 'employee-owned companies' (*spółki pracownicze*). Less significant forms of minority employee share ownership have emerged in privatization using methods other than leasing. Finally, workers' co-operatives, which existed under socialism, are still present in the Polish economy.

a) History

Workers' co-operatives have been part of the Polish industrial landscape since the late 19th century. Prior to the Second World War, they constituted a small part of a very broad and important co-operative movement which was strongly associated with the Polish Socialist Party and whose most important elements were housing, credit, and agricultural co-operatives.[1] In 1948, when the Stalinist era in the economic history of Poland was ushered in, national co-operative associations were established in order to integrate the co-operatives into the planning apparatus of the Communist state. These associations became the link in the planning chain between the central ministries and individual co-operatives, disaggregating planning directives and passing them on to co-operatives, whose members were thus deprived of the bulk of democratic decision-making rights that constitute the essence of co-operativism.[2] Because of this, the growth in the number of workers' co-operatives which occurred in the Communist era was no indication of the strength of genuine co-operativism in the Polish economy. An indication of the largely formal character of Polish workers' co-operatives under socialism is the fact that in the 2,049 co-operatives registered by the Central Association of Workers' Co-operatives as of December 1988, there were 501,400 employees but only 398,100 members.

During privatization Poland (alike Hungary) decided to tread a balanced path and - contrary to the other countries also undergoing the transition period choosing a

[1] The development of workers' co-operatives was a central element of the socialist vision of one of the party's founders, Edward Abramowski, whose ideas resembled to a large extent the syndicalism of the French anarchist Pierre-Joseph Proudhon. However, they only began to flourish (in a formal, numerical sense) under the Communist system of state planning which was almost diametrically opposed to Abramowski's conception of socialism.

[2] A further limit on the rights of members was inherited from the pre-war era: Since the passage of the 1920 law on co-operatives, Polish co-operatives had been characterized by group ownership; that is, the co-operative's basic capital fund, called the 'resource fund' (*fundusz zasobowy*) was indivisible, and individual members had no claim to any part of the collective property.

focused one-policy approach - chose a comprehensive concept.[3] The demand for 'social privatization' and the strong position of the state enterprises combined with the lack of private domestic capital gave rise to the government's 1990 decision to allow amongst other privatization techniques the introduction of a leveraged lease-buy-out (LLBO) model. The drive to make employee buyouts a major form of privatization came from the same movement which had supported employee self-management in state-owned enterprises during the 1980s. Advocates argued that in a market economy with a dominant private sector, the transition to employee ownership was the appropriate method for transforming employee control to conform to the institutional requirements of the new order.

Furthermore, besides preferential employee shares that existed from the very beginning, in 1995 Poland's version of voucher privatization, the National Investment Fund program was launched as a third type of privatization.[4] The Polish privatization law of 1990 represents a compromise between various visions of privatization, including those of the advocates of employee ownership, of commercial methods which would favour capital market development and foreign investment, and of voucher privatization which would enfranchise the population as a whole with no privileges for any particular social groups.

b) Social Partners

Due to the strong position of its state enterprises, Poland represents a special case. Evidence shows, that self-administration of the enterprises which was introduced in 1981 together with the resultant relative independence became a fundamental problem when transformation or liquidation was necessary. The central point of prime importance is that enterprises had to be integrated into the privatization process and the necessary initiative that this entailed as the enterprises often warded off and in some instances even blocked privatization. The organs of the enterprises had a strong position, relatively independent from the state. This together with the failure to establish direct state control, led to a position where the priority aims were not autonomy and introduction into the market economy but the attainment of control and conditional exertion of influence on the behaviour of the enterprises. Thus the paradoxical situation arose in which the State first needed to regain control over the 'state owned enterprises' before it could, as the owner, dispose with them within the framework of privatization. In so doing, the resistance of the workforce and partly also

[3] In East Germany Re-privatization or in other words the handing back of property to the expropriated former owners was of primary importance, in former Czechoslovakia the Voucher-Privatization is the main priority and in Romania and Russia the 'employee ownership' policy rules. Meanwhile Poland is heading for the middle road and so pursues all the above mentioned policies at the same time.

[4] Although voucher privatization does not correspond strictly to the definition of financial participation, under which only the workers of the company should be involved, it can lead in practice to substantial worker share-ownership.

the management, who would de facto disband themselves through the transformation, had to be counteracted.[5]

Although the position of ownership of the Treasury (state) was undisputed it could not freely dispose of its property, which is however essential if the privatization process was to proceed. This fact explains why Poland has distanced itself from a transformation decreed or, as in East Germany, even automatically enforced by law. Besides that there was a strong need for political control of decisions in this sensitive area. The parliamentary rules concerning transformation even the form of organizing body, 'the Ministry' are the visible products of the above situation; an independent state-holding, as exists in East Germany, would have tried to avoid just such political influence and the control of the Council of Ministries. This, however, was not wanted at all in Poland, if only because the numerous parties involved could not agree on a mutually acceptable concept.

Among Polish managers traditionally[6] attitudes reflecting a conviction that decision-making powers should be concentrated in the hands of a small elite and that the role of the remainder of the work force consists solely of executing the decisions made by that elite have been prevalent.[7] However there is also evidence of a great deal of consultation with employee representatives on certain issues (generally connected with wages, benefits, and working conditions). It is worth noting that among workers the managerial option was fairly popular as well, indicated by 20.2% of the respondents from this group (Gladys-Jakóbik, 1995, p. 144). Research carried out in state enterprises in the early 1990s indicates that managers of these enterprises were successful in moving them closer to the Taylorist-managerial ideal over that period of time. Panków (1993, pp. 133-134) writes that during the early 1990s management of state and privatized enterprises shifted from a multicentric model (director, unions, employees' council) to a monocentric model (directorial) with some consultational

5 This problem was exacerbated in 1990 when the Ministries of Industry and the different Branches, which in the beginning were even supposed to be completely disbanded, were deprived of power. Until then, these institutions had a coordinating function and acted as a guarantee for a certain amount of state-direction of the otherwise rather autonomous state enterprises. When the implementation of the privatization was handed over to the Ministry for the Rearrangement of Property Relations - known as the Ministry of Privatization - access to the years of experience, the old Ministries had with the enterprises was simultaneously cut off. The new Ministry (for the foreseeable future) had to face the enterprises without the aid of this valuable experience.

6 On the roots of Polish Taylorism in the Communist era, see Federowicz (1992), pp. 39-41. The Communist elite's strong Taylorist orientation is illustrated in a characteristic statement from the 1950s: 'one-man control is the basic and inviolable method of industrial management. The full application of this principle in every socialist enterprise lies in the interest of its work force and that of the society' (cited in Kloc [1992], p. 71).

7 Thus, for example, the authors of a study analyzing the results of a survey of 465 Polish managers carried out in the 1990s characterize the attitudes of Polish managers as individualistic (i.e., relatively unwilling to engage in teamwork) and relatively uninterested in communication and negotiation with the firm's employees (Karpowicz et al., 1996; Chelminski and Czynczyk, 1991; Kloc, 1997, pp. 130-131).

elements; i.e., although the influence of organs representing employees on management diminishes, directors consult certain matters with trade unions (for example, matters of pay and benefits).

Survey research carried out in the 1990s repeatedly demonstrated that transition to employee ownership was the most preferred method of privatization for employees of state enterprises.[8] However, it appears that this preference for employee ownership reflected not so much the aspirations of state enterprise employees to some form of employee participation as the conviction that this type of privatization offers them the greatest possibilities for financial gain or is simply the least of possible evils.[9] Interestingly, the motives named most frequently by respondents for wanting to purchase shares did not include the desire to increase their influence on decision-making, but rather the hope that share ownership would provide employment security and material benefits in the form of dividends (Gardawski, 1995a, pp. 184, 186). Furthermore, research indicated that over time a desire to achieve benefits for employees became less important for managers as a motive for choosing employee buyouts as a privatization method (that is, one could say that they became less 'labourist' or 'participatory' and more 'managerial' or 'instrumental').[10]

These survey results provide us with indications that the development of employee ownership resulting from the privatization process in Poland was highly pragmatically motivated and not due to any commitment to employee involvement, and that this was

8 For example, when workers and managers were asked in a 1993 survey what form of ownership they would like to see in their enterprise (they could choose more than one type), 66% said they would like to see it remain state-owned and 63% said they would like it to become employee-owned; by way of comparison, foreign ownership was viewed favourably by 15% and private ownership by a Polish investor by 30% (Badora, 1994, p. 55).

9 Among the same respondents to the above-mentioned survey, for example, the desire to actually become an owner seems to be much rarer than the preference for employee ownership as a privatization method. When respondents were asked whether they would buy shares in the enterprise in which they worked if they had such an opportunity, 43% said they would, 38% said they would not, and 19% said they did not know; Kawalec (1994), p. 166. The low figures for 1993 may reflect the limited financial resources of the workers. A similar survey carried out a year later, after significant improvement in the Polish economy, indicates that the percentage of people willing to buy shares in the enterprises for which they work had grown impressively, as 60.9% of respondents expressed such willingness, 30.4% said they would not buy shares, and 8.7% said they did not know. Gardawski (1995a), pp. 184, 186.

10 In a 1993 survey conducted in a sample of employee-owned companies privatized through the end of 1991, managers were asked what their motivation was for choosing privatization by employee leasing. The two most frequently-named motivations were the conviction that this method would ensure that management and decisions would be in the hands of employees (mentioned by 32% of the respondents), and the hope for material benefits for the employees (mentioned by 46%). When managers from a sample of employee-owned companies privatized in 1992 and 1993 were asked the same question in 1995, none of them gave the two above-mentioned answers; instead, the two most popular answers were the perception that this was the cheapest method to buy the enterprise (27%) and the perception that this was 'the best privatization method' (36%) (Szostkiewicz, 1996, p. 76).

the case not only for managers but also for employees themselves. This interpretation is borne out, furthermore, by research concerning the evolution of management styles and ownership structures in employee-owned firms following privatization, as will be discussed below. Strong evidence in support of this thesis can also be found in cases in which employees rapidly and at great profit sold the shares they had acquired at preferential prices or for free in so-called 'capital privatization.'[11]

Institutions created to support employee-owned firms in Poland include the Union for Employee Ownership (*Unia Wlasnosci Pracowniczej*), the All-Poland Chamber of Employee-Owned Companies (*Ogólnopolska Izba Gospodarcza Spólek Pracowniczych*) in Poznan, and the Gdansk Employee Ownership Bank (*Bank Wlasnosci Pracowniczej SA w Gdansku*); however, their significance for the process of employee-led privatization in Poland was very limited. Thus, as of early 1996, the Union for Employee Ownership, founded in the autumn of 1990, had only 76 member firms, some of which were still state-owned. In addition to lobbying activities and the organization of annual conferences on the subject of employee ownership in Poland, the Union's activities included the provision of assistance to enterprises in the process of employee leasing privatization and of legal aid and various types of training programs to member firms. As of early 1996, the All-Poland Chamber of Employee-Owned Companies had 105 member firms (all of them privatized) and was also primarily focused on lobbying activity. The Employee Ownership Bank, in operation since September 1990, had, by late 1995, aided in 30 employee leasing privatizations (concentrated mostly in southern Poland) by means of so-called 'privatization bonds' (these bonds were sold to the state enterprise being liquidated; the money was then lent by the bank at preferential rates to the employees for the purpose of financing share purchases).[12]

c) Codetermination and Privatization

Codetermination on the strategic, entrepreneurial level exists in form of an obligatory one third representation of employees in the supervisory boards of privatized companies. The possibility to abandon this representation from the moment the state ceases to hold more than 50% of the shares foreseen by the old privatization law[13] (PrivL'90) was eliminated in the new privatization law[14] (PrivL) coming into force in

[11] For observations concerning the large scale of sell-out of employee shares acquired in capital privatization, see Szomburg et al. (1994), p. 30 and Landowska (1995).

[12] On the Employee Ownership Bank, see Dryll (1995), pp. 42-43.

[13] Law on Privatization of State Owned Enterprises of 13th June 1990, Dz. U. 1990, No. 51, Pos. 298; 1991, No. 60, Pos. 253; No. 111, Pos. 480; 1994, No. 121, Pos. 591; No. 133, Pos. 685; 1996, No. 90, Pos. 405; No. 106, Pos. 496.

[14] Law on the Commercialization and Privatization of state Owned Enterprises of 30th August 1996, Dz. U. 1996, No. 118, Pos. 561; No. 156, Pos. 775; 1997, No. 32, Pos. 184; No. 98, Pos. 603; No. 106, Pos. 673; No. 121, Pos. 770; No. 137, Pos. 926; No. 141, Pos. 945; No. 98, Pos. 60; 1998, No. 106, Pos. 668; 1999, No. 40, Pos. 400; No. 101, Pos. 1178; 2000, No. 15, Pos. 180; No. 26, Pos.

early 1997. Furthermore the new regulations (Art. 11, 12, 60 PrivL) provide a detailed procedure of the election and qualification of the representatives, extending the representation to initially two fifths of the members and from the moment the state ceases to hold more than 50% of the shares one third (Art. 14 PrivL) and granting them protection of their labour contract for the time of their term and the following year (Art. 15 PrivL) (see Boc et al., 1997, pp. 1 ff.).

The rise of codetermination is again to be seen in the context of the loss of power of the organs of self-administration of the state enterprises undergoing privatization. The PrivL'90 for case of transformation into commercial companies reserved the necessary initiative exclusively to the enterprises organs alone or together with the funding organ. A transformation decreed was the exception, possible only after application of the Minister of Privatization and by decision of the Council of Ministers. In respect to the privatization initiative the new PrivL grants the same powers to the Minister of Privatization as to enterprises organs and funding organs. Likewise in the case of 'liquidation privatization' a shift in the right to initiate proceedings was to be observed. Although Art. 41 para. 1 PrivG only names the joint initiative of Director and Workers Council, it is not enumerative (see Kozlowska-Chyla, 1997, pp. 1 ff.). More important though is the rule of paragraph 2 which explicitly abolishes the Directors and Workers Councils veto against the privatization decision resulting from Art. 63 of the Law on State Enterprises (SoEL)[15]. Furthermore participation rights of the Workers General Assembly, e.g., the necessity of requesting their opinion prior to transformation, were deleted. As compensation incumbent members of the Workers Council were granted a specific protection against lay-offs for the time of their term and the following year in Art. 45, 61 PrivL.

Totally new in the context of 'social compensation' is the participation of an employee representative in the executive boards of privatized enterprises employing more than 500 employees foreseen by Art. 16 PrivL. This novelty exceeded the content of the 'Agreement on the Enterprises' of 1993[16] which foresaw such codetermination in companies with more than 2,500 employees.

d) Current National Policy

It is clear that since the mid-1990s the principal openly declared aim of privatization policy has been maximization of budget revenues, and that therefore all but the smallest state enterprises to be privatized by commercial methods (in spite of the fact

306; No. 31, Pos. 383, republished in Dz.U. 2002, No. 171, Pos. 1397; No. 240, Pos. 2055 (altering the title by abolishing the 'of State-Owned Enterprises'; 2003, No. 60, Pos. 535; No. 90, Pos. 844.

15 Law of July 19, 1991, Dz. U. 1997, No. 75, Pos. 329.

16 'Pakt o Przedsiebiorstwo', also named 'Kuron –Pakt' after the Minister for Labour and Social Affairs *Jacek Kuron* .

that it is precisely the larger employee-owned companies which have tended to attain the best financial results). In addition, privatization policy-makers have sought to encourage enterprises using this method of privatization to find outside investors, and for this purpose, a clause was included in the 1996 privatization law which would make pure management-employee buyouts difficult or even impossible by requiring at least 20% of the shares of a leasing firm to be purchased by persons not employed in the firm (although it also states that the Minister of Ownership Transformation – now the Minister of the State Treasury – may allow for exceptions).

No incentives have been provided by policy makers for the extension of employee financial participation other than privatization schemes. No interest in development of such schemes can be observed either in political or trade union circles. Moreover, the present development of non-financial participation (i.e., participation in decision-making) has been very limited, even in those companies where employees hold significant share packages with the little progress which has been made in this area to be ascribed to the European Union by obliging policy makers to implementing the *acquis communautaire.*

2. Types of Schemes and their Legal Foundations

In Poland the legal framework, in principle, provides various forms of PEPPER schemes, embracing on the one hand share ownership as well as profit-sharing and on the other the co-operative and the private sector as well enterprises undergoing privatization. No incentives have been provided by policy makers for the extension of PEPPER schemes, though. All forms of participation are available for use in employee compensation schemes; however, there are no tax incentives to do so.

a) Co-operatives[17]

The transformation of the Polish economy which began in 1989 brought a number of essential changes to the co-operative sector. In January 1990 the central co-operative associations were liquidated and the formation of associations of co-operatives was banned. In August 1991 the Parliament passed a law allowing for the conversion of the 'resource funds' into share funds in all types of co-operatives (except housing co-operatives), which resulted in the creation of genuine individual shares for members. This law also lifted the ban on the formation of associations of co-operatives, thus eliminating an essential barrier to co-operative development which, in 1990-1991, appears to have played an important role in the decline of the co-operative sector.

[17] Information on Polish workers' co-operatives in this section is drawn from Chyra-Rolicz (1995) and Jones (1993).

Co-operatives are legally defined in the Law on Co-operatives from September 1982 (in the following LoC).[18] A co-operative is a voluntary association of natural (minimum 10 founders) and/or legal (minimum 3 founders) persons created with the purpose to provide an economic activity or to safeguard the economic, social or other need of its members. According to Art. 36 para. 3 LoC it is a legal person and every member of a co-operative may participate in the management, each member having one vote in decisions; in co-operatives having exclusively legal persons as members the statutes may stipulate something. The co-operative is liable for its obligations with all her assets, its members are not liable (Art. 68 LoC). In principle each member is entitled to a share of the profit of the co-operative according to the contribution of the respective member; the volume of distributed profit is set by the general meeting, the rules of the distribution of the profit between the members stipulate the statutes (Art. 75 ff. LoC). Furthermore, in the case of the liquidation of the co-operative Art. 135 para. 3 LoC stipulates that each member receives a liquidation quota according to his share. The profit shares of co-operatives are taxed like any capital gain (i.e., on shares).

b) Leveraged Lease-Buy-Outs[19]

Of the many privatization methods used in Poland, LLBO privatization has been the most popular, especially at the beginning of the process (1992-1993). LLBO privatization is one form of the so called liquidation privatization, thus it is applied not to incorporated companies, but to state enterprises. In the balance sheet, these do not have capital, but funds, and as a result, assets, not shares, are the object of the leveraged transaction. A newly established private company concludes an agreement with the State Treasury to lease the assets of the state enterprise for a period of no longer than 15 years.[20] The contract is made directly between the company and the enterprise's founding body without the participation or intermediary of a financial institution such as a bank. Once the contract has been signed, the state enterprise is struck from the register of state enterprises (or 'liquidated' to use the expression popular in Poland) and from a legal viewpoint ceases to exist as a state enterprise. It would be more correct to say that the enterprise has been wound up.

The legal regulations for LLBOs are to be found in Art. 37 para. 1 No. 3, Art. 38 and 39 PrivL'90 and Art. 39 para. 1 No. 3, Art. 50 to 54 PrivL. It is reserved exclusively for polish natural and as an exception also legal persons (Art. 38 para. 1 No. 4 PrivL'90; Art. 51 para. 1 No. 2 PrivL). The so called employees company concludes a contract with the Treasury, which is represented by the founding body of the enterprise. In general it is leasing contracts that are involved. They concern operative leasing, that is

[18] Dz. U. 1982, No. 30, Pos. 210, newly published on May 10th, 1995, Dz. U. 1995, No. 54, Pos. 288.

[19] See *R. Woodward,* 'Employee participation in Polish employee-owned companies: A statistical analysis', in: Bartlett and Uvalic, eds. (1998).

[20] Until 2002 Art. 52 para. 1 PrivL foresaw a maximum of 10 years.

limited to a particular period of time, as well as financial leasing, whose aim is the acquisition of full ownership.

The trend of LLBO privatizations sinking over time is due to a decrease in the number of state enterprises that meet the financial criteria required for liquiation privatization and such also for an LLBO transaction:

- relatively good financial and market condition;
- not requiring substantial investment to modernise, replace or develop equipment etc.;
- relatively low net value (up to USD 10 million);
- having management and employees determined to undertake the financial risk involved in embarking on a common investment (including third parties) in a given enterprise.

These criteria were altered with the new Privatization Act of 30 August 1996 setting up additional financial hurdles since the beginning of 1997, giving room to the suspicion that the government intended to reduce liquidation privatization. Thus for liquidation privatization (leasing, fast-track-sale and contribution-in-kind) Art. 39 PrivL requires[21]

- a yearly turnover of max. 6 million € and
- not more than 2 million € equity comprising the two enterprise funds.

LLBO companies are sometimes referred to as ‘employee companies’, in other words EBOs. Even though this is a fairly popular description in Poland, it is misleading: First of all, employee participation in companies is not limited to privatization where the enterprise is leased. Cases where all or the majority of the stock or shares have been acquired by ‘insiders’ have occurred in the case of a trade sale or an asset sale, where the buyers of the shares or the business are companies wholly or substantially made up of the enterprise’s employees. Secondly, even when all the shares in an LLBO privatization are taken over by ‘insiders’, the subsequent sale of shares to third parties, or the natural or enforced reduction in the number of original employees bring about a situation where the companies’ ownership structure begins to resemble those privatized with the participation of ‘outsiders’.

Prerequisite for concluding the leasing contract are that the contract must be concluded in favour of the company and over half of the companies´ employees are from the liquidated enterprise.[22] Due to this last condition pure management companies (MBO) never occur as Employee Companies. It is the Management-Led Employee-Buy-Out, that is a buy out of both groups under the direction of the

[21] The initial draft, which passed parliament on June 30th, 1995 but was not signed by President Walesa foresaw a cap of 12 million € yearly turnover and 6 million € equity; the introduced requirement of a small or medium sized enterprises with less than 500 employees was dropped though in 2002.

[22] The PrivL90 required additional, that after the votes of the employees’ assembly have been collected the employees’ council must also give their consent (Art. 38 para. 1 No. 1).

management, which is the rule.[23] Furthermore Art. 51 para. 1 No. 4 PrivL from the end of 1996 on requires 20% of outsiders to be involved in a LLBO transaction. It is common though for persons not employed in the enterprise to take part in an LLBO privatization, already to the end of 1994, more than 20% of the companies set up for this purpose have involved a strategic investor. As an additional organisational and financial hurdle Art. 51 para. 1 No. 3 PrivL requires that the members of an Employees Company pay 20% of the net value of the object of the lease before the company can start doing business.

In the case that the enterprise is not leased but constitutes a contribution-in-kind Art. 50 para. 1 PrivL requires that the shareholders, the treasury excluded, pay 25% of the net value of the equity before the company can start doing business.

Preferential interest rates are applied for the lease payments. The interest payment (referred to in Polish regulations as the 'additional payment' [*oplata dodatkowa*]) was originally set by the Finance Ministry at 75% of the rate of refinancing which applies to the commercial banks at the Polish National Bank. Moreover, a leased company can apply to its founding organ for a reduction of the interest payments owed by the company as a result of postponements during the first two years of the leasing period if its investment expenditures out of profits amount to at least 50% of its net profit. Later, it was determined that if the central bank refinance rate were to exceed 40%, the interest rate would be set at 30% (75% of 40%).[24] Finally, the corporate income tax law allowed the firms to include the interest portion of the lease payments as costs in their accounts, thus reducing their tax liability.[25] In 1993, the interest rate was lowered again, to 50% of the refinance rate.[26]

The new privatization act of 30 August 1996 additionally leveraged the financial lease contracts in order to enhance the creditworthiness of employee-leased firms when applying for bank loans. Stating in Art. 52 PrivL the possibility that full ownership may be acquired already before the end of the contract if one third of the total amount of the leasing rates has been paid, provided the approval of the balance sheet of the second business year of the company. A payment of more than half of the total leasing rates cuts down the blocking period in half. Because of the difficult conditions on the Polish credit-market, this regulation has in practice become very important. Furthermore Art. 54 PrivL foresees the possibility to regulate the specific conditions of such leverage by Ordinance of the Council of Ministers including the possibility to

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23 Here one can see that this form of participation should act as a safety valve in regard to the political expectations within 'Social Privatization'. Although in practice MBO occurs much more frequently and although experience has shown this to be more successful, a specific mention of it in the Privatization Law was rejected. Instead the much less frequent EBO was emphasized which shows again that it is not economical but political considerations that dominate the development of the concept.

24 Ordinance of the Minister of Finance from May 7 1991, Monitor Polski 1991 No. 18, Pos. 123.

25 Law on Corporate Income Tax from February 15th, 1992, Art. 15.

26 Ordinance of the Minister of Finance from May 13th, 1993, Monitor Polski 1993 No. 26, Pos. 274.

reduce the threshold of paying 20% of the net value of the object of the lease stated in Art. 51 para. 1 No. 3 PrivL to 15%. In this context Art. 64 PrivL granted existing Employees Companies the right to renegotiate their contracts within 3 month after the Ordinance came into power.

In the above mentioned case of an in-kind-contribution of the enterprise members of an Employees Company constituted exclusively of employees of the enterprise and the treasury have to pay only 10%[27] of the net value of the equity before the company can start doing business, while at the same time Art. 49 PrivL requires 25% for non-employee or mixed companies.

Nevertheless, the Evaluation of the object of the lease, that together with the aforementioned rate of interest, provides the basis for the calculation of the leasing rates is problematic. This evaluation is carried out by certified public accountants, who are commissioned by the Ministry of Privatization, and is usually set too high. Negotiations which would take account of the low financial capabilities of the Employee Companies often did not take place because the Ministry wanted to safeguard itself from accusations of 'flogging the family silver' at too low a price through low evaluations. As a result the starting position of these companies was often poor, especially as credit is expensive and difficult to get.

It is worth stating that Poland does not have group ownership similar to the workers' collectives in Russia and the trusts associated with ESOPs in the United States. In Polish LLBO companies shares are owned individually and may be sold and inherited. The moment an employee leaves the company he does not automatically have to sell his shares to another employee or transfer them to a collective or trust. Thus the general rules of the Commercial Code concerning voting rights of shares and participation in decision making apply (see above I. 3.).

c) Employee Shares in Capital Privatization

Provisions concerning preferential employee-shares, giving workers the right to acquire 20% of the shares of a privatized enterprise at half of their nominal value, were adopted already in the PrivL'90. With the new PrivL coming into force in early 1997 these regulations were modified: From now on according to Art. 36 PrivL employees can acquire 15% of the shares for free with the restriction of these shares being exempted from free trade[28] for two years, and for three years in the case of employees elected to the management board (Art. 38 para. 3 PrivL). They are required to state their claim within 6 months before the registration of the company, otherwise the right expires and can execute it after the sale of the first share for 6 months. Shares are

[27] Till the end of 1996 privatization rules required 20%.

[28] This does not apply to shares allocated in a Employees Pension Fund set up under the Law on Employees Pension Programmes from April 20, 2004, Dz. U. 2004, No. 116, Pos. 1207.

allocated in groups made up according to the time spent in the enterprise.[29] The total value of allocated shares according to these claims may not exceed the sum of the average salary on the public sector in 18 months multiplied with the number of employees acquiring shares.[30] This rule applies not only to commercialized companies undergoing capital privatization but was extended to a 15% employee participation in 'direct privatization' transaction embracing sales of an enterprise as a going concern as well as in kind contributions of an enterprise (Art. 48 para. 3, Art. 49 para. 4 PrivL). The only remaining exception is commercialisation via debt-to-equity-swaps.

d) The Mass-Privatization Programme (MPP)

After being delayed for at least four years for political reasons the mass privatization program resting on the Law on National Investment Funds and their Privatization[31] was finally implemented in 1995. The law provided for the establishment of 15 National Investment Funds (NIF) by the state to be managed by special consortia of Western and Polish partners (commercial banks, investment banks, consulting firms) selected through an international tender offer while management and supervisory boards should maintain a polish majority and their shareholders should be exclusively polish citizens.[32] The fund managers were to be remunerated through a combination of fixed annual fee, a performance fee of 1% per year based on the value of their assets and a loyalty fee of 5% of their assets at the end of the 10-year contractual period. This was expected to encourage fund manages to embark on value maximising strategies which aligned their interests with those of the ultimate owners of enterprises in their portfolios.[33] The NIFs were registered in the end of March 1995, management contracts for 14 funds were concluded until mid July 1995[34], the first 413 enterprises were allocated shortly afterwards, another 99 followed December of that year.

The majority of shares of each company (60%) was given to the 15 National Investment Funds, with the remaining 40% going to employees (15%)[35] and the Treasury (25%). For each company, one of the 15 NIFs received 33% of shares and thus became the 'lead fund' for that company. The remaining 27% were divided

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29 The principles of the forming of these groups are set in detail in an Ordinance of the Minister of Privatization of April 3rd, 1997, Dz. U. 1997, No. 33, Pos. 200.

30 For state enterprises, that on the day of being struck from the register of state owned enterprises have balanced their financial duties with both, the treasury as well as the social security fund the yearly average salary is taken as criteria.

31 Being passed on April 30th, 1993; Dz. U. 1993, No. 44, Pos. 202; 1994, No. 84, Pos. 385; 1997, No. 30, Pos. 164, No. 47, Pos. 298 (with subsequent amendments).

32 For the legal framework see: 'Dokumentacja prawna programu powszechnej prywatyzacji', Warszawa 1992.

33 For details of the Polish mass privatization, see Hashi (2000).

34 Polish banks were represented in 9 consortia; majority control of the consortia was reported in three cases of polish and in 6 cases of foreign institutions.

35 Employee preferential shares according to Art. 36 to 38 PrivL; see above c).

between the remaining 14 funds (each holding just under 2% of shares). Thus in 512 enterprises the 15 NIFs held each 33 to 35 'control shares' and an average of 477 shares ranging between 1 and 2%. The 25% shares held by the treasury were intended to be used e.g. to buffer devaluation of pensions and satisfy re-privatization claims.[36]

The Polish MPP was based on the principle that National Investment Funds (NIFs) will act as 'active owners', take control of their lead companies of which they hold a 33% share, embark on policies that will enhance their efficiency as well as their value and turn them into profit making, market responsive firms. Over the ten-year period of their agreement they step by step would transform them into genuine 'private' institutions, listed on the stock exchange or sold to strategic investors. By the end of this process, NIFs themselves will be turned from *'venture capital'* type funds, heavily involved in the operations of their companies, to typical investment or mutual funds, which are not directly involved in the affairs of their companies.[37]

e) Pre-emptive Right of Purchase of an Enterprise under Insolvency Law

With the Insolvency and Reorganisation Law (IRL) a completely new version of the polish insolvency law[38] became effective on 1 October 2003.[39] Embracing regulations on both bankruptcy and arrangement proceedings, interestingly, the IRL contains a hidden leverage for setting up companies consisting of at least half of the debtor's enterprise's employees in the context of the liquidation procedures.

According to Art. 306 ff. IRL Liquidation of debtor's assets is carried out generally by selling the movable and immovable assets, by collecting or selling claims of the debtor and by realizing other rights related to the debtor's assets. The administrator is obliged to try to sell the debtor's business as one unit or as several functioning business units. The administration of assets is extended to the continuation of the debtor's business or its lease, if it is possible to conclude an arrangement or to sell the business at a later time at a higher price. The scheme often used in practice of temporary leasing of the business with an option of purchase is now regulated by law in Art. 316 IRL, which gives room for a lease-buy-out similar to the one of the LLBO described above. Upon the sale of the business as one unit, the purchaser does not assume the liabilities of the debtor according to Art. 317 IRL as opposed to Art. 526 of the Civil Code; he purchases the business free of encumbrances.[40]

If the sale of the debtor's business as one or several functioning units is not possible, then each asset should be publicly auctioned by the administrator under supervision of

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[36] See Rzeczpospolita from August 26th, 1992: 'Fabryki zamiast emerytury' (Industrial plants instead of pensions); according to a resolution of the Polish Sejm from Mai 9th, 1992.

[37] For a good summary of the results compare Hashi (1999), p. 14.

[38] Dz. U. 2003 , No. 60, Pos. 535.

[39] For a detailed analysis of the new law see Zedler (2003).

[40] The exemption from liability is applicable also to mortgage, pledge, registered pledge and registration in the ship register which was already stated in the 1997 amendment to the Bankruptcy Act.

the judge-commissioner. If assets are not sold at a public auction or the judge-commissioner does not accept the offer, the judge-commissioner can order a second auction or determine the minimum price and conditions of sale and allow the administrator to find a purchaser or allow the administrator to sell assets free of procedural restrictions. The sale of real estate and ships free of procedural restrictions must be approved by the creditors' committee. In this case a company consisting of at least half of the debtor's enterprise's employees and being a commercial company with participation of the Treasury has a pre-emptive right of purchase of the enterprise or functioning enterprise units (Art. 324 IRL). The sale of movable property free of procedural restrictions must be approved by the judge-commissioner according to Art. 326 ff. IRL.[41]

f) Company Law

In deviation from the general prohibition to acquire own stock, Art. 362 para. 1 of the Commercial Companies Code (CCC) permits that a company acquires its own shares in order to offer them to current employees or retired employees of the company or employees of an affiliated company given a minimum of three years of that business relation.[42] In this case Art. 393 No. 6 CCC requires a decision by general shareholders assembly's and Art. 363 para. 3 CCC that the shares shall be transferred to the employees within a twelve-months time period from the moment of acquiring them. If the transfer is not carried out within the mentioned time period, Art. 363 para. 5 CCC stipulates that the shares have to be sold or the share capital will be decreased respectively. According to Art. 362 para. 2 CCC the possibility of acquisition of own shares in this case is limited to the extend that the total nominal value of the shares may not exceed the value of 10% of the enterprises equity capital and that the purchase price together with the transaction cost may not be higher than the reserve made from the company's own profits according to Art. 348 para. 1 CCC.[43]

Additionally under the current legislation joint-stock companies may issue new shares to be transferred to employees in the context of so called conditional capital increases, with Art. 448 para. 2 No. 2 CCC expressively referring to this possibility of transferring shares to employees for the case that they have previously acquired claims from profit-sharing. Prerequisite to this form of capital increase is according to Art. 448 para. 1 CCC that the concerned employees are identified in the decision of the general shareholders assembly's decision about the capital increase. The issuing of shares to be acquired by employees in this case shall not be considered as public offering but

[41] Ordinance of the Ministry of Justice from 16 April 1998, Dz. U. 1998, No. 55, Pos. 360, entered into force on 14 May 1998.

[42] This regulation had its origin in the harmonisation of the Polish legal system with the *acquis communautaire,* i.e. the second Council Directive from 1976 on Company Law.

[43] Art. 347 para. 3 and 348 para. 1 CCC provide the possibility to allocate enterprise profits to special funds while not paying them out as dividends and thus allow share based profit-sharing.

according to Art. 431 para. 2 No. 1 CCC a 'private subscription'. The matching regulation is Art. 442 para. 1 CCC stipulating the possibility of capital increases financed by the companies own capital again referring to Art. 348 para. 1 CCC concerning reserves made from the company's own profits (see above).

In order to facilitate the acquisition of shares by employees with Art. 345 para. 2 the CCC the legislator has deviated from the general prohibition to leverage the acquisition of own stock. [44] Conditional on the creation of a reserve according to Art. 348 para. 1 CCC the company may advance funds, make loans, provide security, with a view to acquisition by employees of the company or employees of an affiliated company.

An issue to be mentioned in the context of employee share ownership is a new regulation introduced at the end of 2003[45] which in the case of joint-stock companies, where the major share owners (not more than five owning together at least 95% of all shares and each single one not less than 5%), permits them to make a final share buyout offer to the remaining minority shareholders (squeeze out). In such a case the minority share holders, which on some occasions may be employees of the company would have an obligation to sell the shares to the major shareholder.

Furthermore, in principle, employees may received stock options, including options to acquire shares on a privileged basis (at below-par prices or even free of charge) although there exist no specific regulations.[46] In practice in such cases, the amount of share capital affected is usually a limited and specified amount and is often subject to restrictions concerning subsequent resale.

g) Profit-Sharing

Profit sharing started to operate in the 50ies encouraging the creation of employee funds from company profits in state owned enterprises. These funds began to represent an substantial part of employees remuneration in 1990, when employees were given the possibility to invest these 'rewards' in state treasury bonds under substantially preferential conditions (Vaughan-Whitehead et al., 1995, Introduction, p. 8). In case of profit related bonuses in SOEs there has been a trend during the period of transition 1990-1994 to relate them more concretely to profit levels (Chilosi et al., Country Chapter Poland in Vaughan-Whitehead et al., 1995, p. 55). Some provisions on profit related rewards in SOEs were agreed upon in the 'Pact on Enterprises'.

Among the practices sanctioned by law presently are compensation forms linked to an employee's individual results (gain-sharing). Here a distinction should be made between commissions (*prowizja*; used frequently, if not universally, in the case of sales

[44] For details see Lewandowski (2004), p. 594.

[45] Art. 418 CCC modified with the last amendment from Dec. 12th, 2003, Dz. U. 2003, No. 229, Pos. 2276.

[46] See Ciupa (2001), p. 203.

force employees) and various types of bonus schemes.[47] Of the latter the most frequently used is referred to in Polish as the *premia*[48] constituting a predetermined proportion of pay conditional on fulfilling certain criteria stipulated usually in an regulation on enterprise level. However, all these schemes are usually not linked to enterprise results.[49]

The possibility of implementing profit-sharing, i.e. a form of remuneration, additional to pay systems, directly linked to the enterprise profits is stipulated in Art. 347 para. 3 and 348 para. 1 CCC for joint-stock companies (*tantiema*[50]). Furthermore, as already mentioned, share based profit-sharing is regulated in the context of conditional capital increases according to Art. 448 CCC, stressing the possibility of transferring shares to employees especially for the case that they have previously acquired claims from profit-sharing. The general type of a scheme linked to enterprise results is referred to in Polish as a '*bonus*' but has no legal foundations.

h) Tax Issues

With the rare - and very limited - exception of LLBOs[51] employee tax incentives for PEPPER schemes do not exist. The most important regulatory acts connected with employee financial participation are the Law on Personal Income Tax[52] and the Law on Corporate Income Tax[53]. There is a uniform 15% dividend tax rate, a uniform corporate income tax rate at 22% (decreasing from 28% in 2002), and a progressive personal income tax ranging from 19%, 30% to 40%.

3. Incidence Now and Over Time

a) Co-operatives

As of 31 December 2001, 411,700 persons were employed in the co-operative sector, which represented 2.9% of employment; this was down from 642,000 at the end of

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47 For details see 'Premie I nagrody dla pracowników' (Pl.), in Rzeczpospolita from Oct. 3rd 2005.

48 See decision of the Supreme Court of Sept. 21st 1990, I PR 203/90, OSP No. 7-8/1991, Pos. 146 and of Jan. 15th, 1991, I PR 382/90 – not published.

49 Such as other forms of remuneration, e.g. gratifications (gratyfikacja, nagrody, nagrody jubileuszowy) or thirteenth salary; see Ciupa (2001).

50 See decision of the Supreme Court of May 5th, 1992, I PZP 23/92, Bibl. Prac. No. 25, p. 96.

51 Allowing the firms to include the interest portion of the lease payments as costs in their accounts, thus reducing their tax liability; see above 2.

52 Law on Corporate Income Tax from February 15th, 1992 (with subsequent amendments).

53 Law on Personal Income Tax from July 26th, 1991 (with subsequent amendments).

1995[54] (CSO, 2003, p. 147). However, employment in workers' co-operatives is certainly much lower: as of 31 December 2002, while a total of 18,682 co-operatives were registered in Poland, only 2,208, or 11.8%, of them were industrial workers' co-operatives (CSO, 2003, p. 613). Although numerically their role in the Polish economy is comparable to that of the employee-owned companies which have been created as a result of the process of privatization of state enterprises (these companies are discussed in the next section), a great deal less research has been devoted to them. This neglect is probably due in large measure to the fact that privatization has occupied a great deal more of the attention of researchers studying the Polish economic transformation than has the evolution of the co-operative sector, and, additionally, to the relatively small significance of workers' co-operatives in comparison with other forms of co-operatives such as agricultural, housing, consumer and credit co-operatives.

b) Employee-Leased Companies

This form of privatization was the dominant one in the early transition period in Poland. Of the state property which had been privatized in Poland through mid-1995, a very high percentage was privatized by the 'leasing liquidation' method. By 30 June, 1995, privatization in accordance with the above-mentioned 1981 and 1990 laws had been completed in 1,457 enterprises, with 140 capital ('indirect') privatizations, 975 Art. 37 ('direct') liquidations, and 342 Art. 19 liquidations (Ministerstwo Przeksztalcen Wlasnosciowych, 1995). Thus, at this point, article 37 liquidations represented 66.9% of all completed privatizations, and since leasing represented about 73% of all article 37 liquidations[55], 48.8% of Polish privatized companies in mid-1995 were employee-leased companies. Later the situation changed, due - among other things - to the implementation of the NIF program and the increasing popularity of other methods of direct privatization. By the end of 2001, privatization had been completed in 3496 enterprises, with 309 indirect privatizations, 512 firms transferred to the National Investment Funds, 1,855 direct privatizations (of which 65.9% were leasing companies) and 820 Art. 19 liquidations (CSO, 2002, p. 22). At this point, therefore, lease-leveraged employee buy-out represented a little over one third of the completed privatizations carried out under the supervision of the Ministry of Ownership Transformation.[56] In terms of the numbers of enterprises privatized, however, leasing still represented the single most frequently used method.

[54] This figure includes not only worker co-operatives but also, e.g. agricultural, housing, consumer, and consumer co-operatives.

[55] This calculation is based on information contained in CSO (1995), 22, and CSO (1996), 64.

[56] If one considers Central Statistical Office data on employment, however, by the end of 2001 indirectly privatized companies strongly outweighed employee-owned companies, with employment in the former at 269,000 and employment in the latter at 162,000. See CSO (2002), 42.

Size

Most of the firms in this category are small- to medium-sized firms, usually with less than 500 employees. Among enterprises which had initiated or completed privatization by employee leasing by 31 December 2001, only 13.8% employed over 250 persons (CSO, 2002, p. 43).

Distribution of shares and entry of new groups of shareholders

Studies of Polish employee-owned companies have found that they tended to have, on the average, a fairly egalitarian distribution of shares initially, that management began to accumulate shares in a process of concentration that was usually rather slow, and that management shares seemed to have stabilized by the end of the 1990s. Research conducted in the late 1990s on a sample of 110 employee-leased companies privatized between 1990 and 1996 showed that on the average, the share of non-managerial employees in ownership decreased from 58.7% immediately after privatization to 31.5% in 1999. Approximately 32% of leasing-privatized firms were still majority owned by non-managerial employees as of mid-1999. Over time, more and more shares were also found in the hands of outsiders (probably due largely to retention of shares by people whose employment relationship with the firm ceases for any reason), and the presence of strategic outside investors (including foreign investors) had begun to be felt in a minority of firms by the end of the last decade.

Table 1. Transformation matrix

	Had over 20% in 1997									
Had over 20% at time of privatization	No data	SI	M	W	SMW	SM	MW	SW	None	Total at time of priv.
No data	**5**	0	0	1	0	0	2	0	0	8
Strategic investor (S)	0	**3**	0	0	0	0	0	1	0	4
Exec. Bd. memb. (M)	0	0	**4**	0	0	0	1	0	0	5
Non-mg. workers (W)	3	4	2	**48**	0	0	5	3	4	69
All three	0	0	0	0	**1**	0	0	0	0	1
S & M	0	0	0	0	0	**0**	0	0	0	0
M & W	0	0	4	1	0	0	**12**	0	0	17
S & W	0	0	0	0	0	0	0	**1**	0	1
None	1	1	0	0	0	0	0	0	**3**	5
Total	9	8	10	50	1	0	20	5	7	110

Source: Kozarzewski and Woodward (2003).

The transformation matrix presented in Table 1 shows the transformation trajectory of firms grouped with respect to dominant shareholders (defined as shareholders or coalitions of shareholders – for example, top management together with a strategic outside investor – with at least 20% of the firm's shares) at the time of privatization: in the rightmost column, we see the number of firms in each group at the time of privatization, and looking leftward, we see where the firms in these groups ended up in 1997. The diagonal, in which the numbers are printed in boldface, shows firms that remained in the same group in which they started (Kozarzewski and Woodward, 2003).

Polish legislation does not restrict trade of shares in these firms, but the by-laws of the firms often do. The main effect of the restrictions contained in the by-laws is to reduce access of outsiders to shares; however, trade among employees (including members of management, who often have special rights to share acquisition) is largely unrestricted (Gardawski, 1995b, p. 64).

The importance of new share issues is indicated by the results of a 1996 Unia Wlasnosci Pracowniczej survey, as 20.9% of the respondents said that they had had new share issues and 19.8% said that they were preparing such issues. For the latter two categories combined (issue planned or already carried out), 8.1% reported that the issue had been public, and 31.4% reported that it had been closed (Unia Wlasnosci Pracowniczej, 1996). A number of well-known employee-owned companies, including the Bydgoszcz-based cookie and candy manufacturer Jutrzenka, the Krakow-based candy producer Wawel, and the Torun-based mining equipment manufacturer Apator, have issued shares on the Warsaw Stock Exchange, and the number of such cases can be expected to grow fairly rapidly in the near future. On the other hand, a number of employee-owned companies with equally well-known brand names have chosen the option of selling out their holdings to outside strategic investors.

Employee participation in governance

Employee attendance at shareholder meetings was found to be high on the average in the firms surveyed by Unia Wlasnosci Pracowniczej: 75 to 100% of the employees attend in between 45 and 50% of the firms and 51 to 75% attend in about 20% of the cases. Attendance seems to be much higher in companies privatized in 1991, 1992 and 1993: the majority of employee shareholders attends meetings in over 84% of companies privatized in 1991, in over 77% of companies privatized in 1992, and in about 60% of those privatized in 1993, but only in 37.5% of companies privatized in 1994 and 50% of companies privatized in 1995.[57] Nevertheless, given the facts that these meetings occur only once a year and are often dominated by a core group of shareholders, usually from middle and top management, holding the largest blocks of shares, and that management is usually uninterested in facilitating information flows to the work force, it is not surprising that several researchers have concluded that the dominant management style in Polish employee-owned companies is more autocratic than democratic (Dabrowski et al., 1992, p. 50; Dabrowski et al., 1993, p. 49; Gardawski, 1995b, pp. 60-63).

c) The Mass-Privatization Programme (MPP)

All adult citizens received certificates which entitled them to one share in each of the 15 funds, thus becoming indirect shareholders of privatized companies. The distribution of certificates started on Nov. 22nd, 1995, ended a year later and reached a

[57] It is possible that the results for 1994 and 1995 are not representative, as the sample includes only about 9 of the former (9.3% of the sample) and 3 of the latter (3.5% of the sample). See Unia Wlasnosci Pracowniczej (1996).

total of 25,657,090 certificates, i.e. about 95% of all certificates, creating revenues of 350 million PLN for the state treasury. Before trading the certificates were valuated at about 144 PLN.[58] On December 31st, 1996 already 9.8 million certificates, i.e. about 38%, were dematerialised. At that time the certificate price had reached seven times that of the issuing fee, i.e. 142.5 PLN.

d) Employee Shares

No systematic data are collected regularly on employee shareholding in private companies or companies privatized in Poland by commercial methods. However, a study of ownership and governance patterns in over 80 of Poland's 500 largest companies which have been privatized in the years 1990-2001 found that employee shareholding was marginal in this group of firms. Insiders possessed only 12.7% of shares at the beginning of 1998, and this fell to 11.4% two years later. In two thirds of the companies, managers held no shares at all, and non-managerial employees held no shares in almost half of the companies in the sample. Managers and other employees had majority stakes in only 5% of the firms (Kozarzewski, 2002).

e) Stock Options

Due to the widespread use of stock options in venture capital financed information technology firms in the United States, interviews with representatives of Poland's private equity and venture capital industry about the extent of such schemes in Poland were conducted for this report. The common reply was that options were used in Poland only for top management, and that broad-based options schemes were only known in Hungary and Russia.

f) Profit-Sharing

Other forms of employee financial participation in profits are sanctioned by Polish law. However, while no empirical research has been conducted in Poland to determine the extent of their use in practice, the opinion of experts is that they remain largely unused except for managerial employees. The so called Tantiema as a form of profit-sharing in practice seems to be used exclusively for managerial employees. The one bonus scheme linked to results, referred to in Polish as a '*bonus*' is not a widespread practice.

[58] Of the 60% shares transferred to NIFs only 85% were foreseen for holders of certificates; thus 51% of the total value of the participating companies (7,228 milliard PLN) was divided by 25,675 million Certificate holders.

4. Empirical Evidence on Effects of Employee Ownership

In Section 4.a), in addition to certain information available from the Central Statistical Office, the relevant results of two research projects conducted by the interdisciplinary team headed by Maria Jarosz of the Institute of Political Studies of the Polish Academy of Sciences – the first in carried out in June 1993 and June 1994 and the second from 1997 to 2000 are discussed.[59] Section 4.b) sums up an econometric analysis Woodward carried out using the data obtained by the Jarosz team in its studies. Concerning the Mass-Privatization Programme Section 4.c) refers to a study by Iraj Hashi and Tadeusz Kaminski in the context of an ACE-project.

a) General Results of Studies in the 1990s

Profitability

In the first half of the 1990s, employee-leased companies were, on the whole, financially sound in spite of the burden of lease payments and the effects of the general recession which affected the country in the first three years of the economic transformation.

Table 3. Gross profitability (ratio of gross profit or loss to total revenues)

	1994	2001
Employee-owned companies	6.4	1.7
State enterprises currently undergoing Art. 37 liquidation	3.2	1.7
Capital-privatized companies	4.9	1.4
Commercialized companies participating in NIF program	4.2*	-4.0

* Companies designated for participation in the program. **Source:** CSO (1995), p. 66, CSO (2002), p. 47.

Table 3 shows that profitability indices for the average Polish employee-owned company have been close to or better than the average indices for firms privatized by other methods (including commercial methods). Similarly, the Jarosz group found that total profitability (ratio of gross profit to costs) in its sample of employee-owned companies was higher than the national average for 1992 and 1993 and net (after-tax) profits were rising. On the other hand, they also found that gross (pre-tax) profits were

[59] The sample used in the first Jarosz research project research (1993-1994) was a group of 110 companies selected from the population of companies privatized by the leasing method through the end of 1991 (constituting 56% of the entire population of firms privatized by this method by that date). The second project, entitled 'Direct Privatization: Investors, Managers, Employees' and financed by the Polish State Committee for Scientific Research (contract No. PBZ-014-11), utilized a sample which included 110 firms privatized by the leasing method between 1990 and 1996. This constituted 12.9% of the total number of companies privatized by that method through the end of 1996. For detailed discussions of the results of these studies, see Jarosz (1994, 1995, 1996, 1999, 2000).

falling, whereas the national average was rising (Pietrewicz, 1995, pp. 24-26). It is worth noting that profits were highest among those types of enterprises which were least typical among the group of employee-owned companies; i.e., among large industrial enterprises employing over 300 persons (Pietrewicz, 1995, p. 54).

In the second half of the 1990s, the Jarosz group found gross profitability (gross and net) to be declining among the employee-leased companies in their sample of privatized companies. This is illustrated in Table 4.

Table 4. Gross and net profitability and losses in Jarosz sample of leasing companies, 1993-1998

	Gross profitability	Net profitability	Percentage of companies with losses
1993	7.7%	4.2%	5.5%
1994	7.5%	3.8%	6.0%
1995	6.5%	3.1%	6.5%
1996	6.9%	3.8%	8.5%
1997	6.1%	3.7%	20.4%
1998	3.2%	1.6%	37.9%

Source: Krajewski (2000), 132.

Investment

In the early 1990s, the claim was frequently made that employee-owned companies in Poland were characterized by exceptionally low levels of investment activity. Indeed, one study found a tendency to low investment and de-capitalisation in employee-owned companies compared with the enterprise sector of the national economy as a whole (Pietrewicz, 1995, pp. 39-40). However, as Maria Jarosz emphasized, Polish employee-owned companies formed on the basis of a lease contract were obligated to make regular - and rather burdensome - lease payments, to which a large portion of profits must be dedicated, thus limiting the possibilities for using retained earnings to finance investment; additionally, during the leasing period these firms had exceptional difficulty (in comparison with other privately-owned firms) in obtaining bank credits, since they did not own, but only leased, their physical capital and thus possessed inadequate collateral.[60] It should also be noted that the leasing method of privatization was explicitly intended for firms which were considered to require little investment.[61]

[60] See Jarosz (ed.) (1995), p. 16. Generally speaking, the burden of leasing payments had to be carried by the employee-owners themselves without help from outside, as most banks were very reluctant to finance employee leasing privatization. One early 1990s survey of the nine largest banks operating in Warsaw found that, when assessing the risk associated with various privatization methods on a scale of AA to CC (i.e., from no risk to prohibitive risk), employee leasing was assessed as a C risk (unless a foreign investor was involved, in which case the assessment was improved to A). See Solarz (1994), pp. 86-87.

[61] See Najwyzsza Izba Kontroli (1993), p. 9, *Uchwala Sejmu Rzeczypospolitej Polskiej z dnia 12 lutego 1993 r. w sprawie podstawowych kierunków prywatyzacji w 1993 r.* (M. P. 1993, No. 9,

In spite of this, by the late 1990s the situation in employee-owned companies had improved noticeably. A 2000 State Treasury report lists these companies along with foreign-owned companies, publicly listed companies, and companies with domestic strategic investors in the group of companies with relatively high and stable rates of investment, contrasting them with state-owned enterprises, state-owned companies and companies privatized under the National Investment Fund program, which had poor investment performance. However, the authors did note that investment per employee and the ratio of investment to sales revenues was much lower in employee-owned and other domestically owned companies than in foreign-owned companies (Ministerstwo Skarbu Panstwa, 2000, p. 52). The relatively high investment propensity of these companies is illustrated by statistics concerning investment of profits in the Jarosz sample of employee-owned companies in the years 1996-1998. If we compare Tables 3 and 4, we see that 30-40% of the companies in the sample did not pay dividends in spite of having made profits, and among those companies which did pay dividends, the percentage which paid out less than 60% of profits in dividends was consistently over 70% in the years 1996-1998.

Table 5. Dividends in Jarosz sample of leasing companies, 1996-1998

	1996	1997	1998
Percentage of companies paying dividends	50.0%	48.7%	32.0%
Of which: Percentage which paid out 60% or less of profits in dividends	78.0%	72.7%	75.8%

Source: Krajewski (2000), pp. 113-115.

Restructuring

It is true, however, that in the early to mid-1990s restructuring and adjustment activity in firms privatized by the employee leasing method tended to be concentrated in increased promotional activity and adjustments of a simple, cost-reducing nature (e.g., employment reductions), involving little in the way of introduction of new products or significant improvement in the level of technology (Pietrewicz, 1995, 51-52).

In the early transition period, opponents of privatization by employee ownership often expressed fears that it would tend to stimulate efforts to maintain employment at the inefficient levels of overstaffing typical in the command economy. In fact, employees themselves often expressed hopes that share ownership would be a guarantee of employment (Gardawski, 1995a, p. 184). In reality, however, employee-owned companies showed a great deal of elasticity in their employment policies, often engaging in significant layoffs (in firms that were on the average relatively small to begin with). Average employment in the first Jarosz sample fell from 285 at the end of 1991 to 242 at the end of 1992 (i.e., a 15.1% decrease) and to 213 at the end of 1993 (a 12.0% decrease), stabilizing somewhat in 1994 (average employment in mid-1994 was 209) (Pietrewicz, 1995, p. 29). Employment restructuring was no longer needed in the

Pos. 64), and *Kierunki prywatyzacji majatku panstwowego w 1995 r.* (Dz. U. 1995, No. 27, Pos. 142).

second half of the 1990s, and greater economic prosperity brought increased employment: in the second Jarosz sample, average employment fell from 211 at the end of 1993 to 182 at the end of 1995, but then grew to 190 at the end of 1996 and 204 at the end of 1997 before dropping slightly again (to 198) at the end of 1998 (Krajewski, 2000, p. 127).

Wages

Those who feared overmanning and a continuation of the hidden unemployment characteristic of the Communist period as a result of employee ownership also feared excessive wage growth. Indeed, wage growth was found to be fairly high in the period immediately following privatization but slowed down considerably thereafter, even failing at times to keep pace with productivity growth. Thus, for example, in 1993, average productivity growth in the first Jarosz sample was about 2.9%, but real earnings decreased by about 1.9%, and by mid-1994 average earnings in the sample were below the national average (Pietrewicz, 1995, pp. 30, 34). In the second half of the 1990s the situation changed again. In the second Jarosz sample, the average monthly earnings in employee-owned companies were well above the national average in the period 1995-1998.

b) Econometric Results on Productivity Effects of Employee Ownership

Woodward has carried out two econometric studies of the effects of employee participation on productivity, using data from the two Jarosz samples. Measures of employee ownership included the percentage of the company's shares held by non-managerial employees, the percentage of the work force holding shares in the company, and measures of the degree of equality of share distribution. There was also one measure of the participation of employees (or rather their representatives) in corporate governance; namely, the percentage of the supervisory board members who had been non-managerial employees prior to privatization.

In the first study (Woodward, 1999), using data from the first Jarosz project and applying an Ordinary Least Squares (OLS) framework for five different sectors (manufacturing of wood products, manufacturing of machines and certain other products, construction, trade, and non-material services), I found neither employee ownership nor employee representation to be related to productivity in any statistically significant way (with the exception of one estimation in which I found a significant and negative coefficient for a dummy variable indicating a relatively high degree of equality of share distribution). In the second study (Woodward et al., 2004), estimates were made on data from the second Jarosz project using both OLS and panel (fixed effects) methods, with industry dummies rather than separate regressions for various sectors. As in the case of the first study, the only significant relationship was found in one (OLS) estimation in which there was a significant and positive relationship between productivity and the concentration of shares in the hands of the single largest shareholder.

In both cases it would be justified to conclude that in Poland the failure to observe a strong relationship between employee participation and productivity is due to the managerialist culture of Polish enterprises and the resulting extremely limited scope for employee participation in decision-making, especially on the shop-floor level.

c) The Mass-Privatization Programme (MPP)

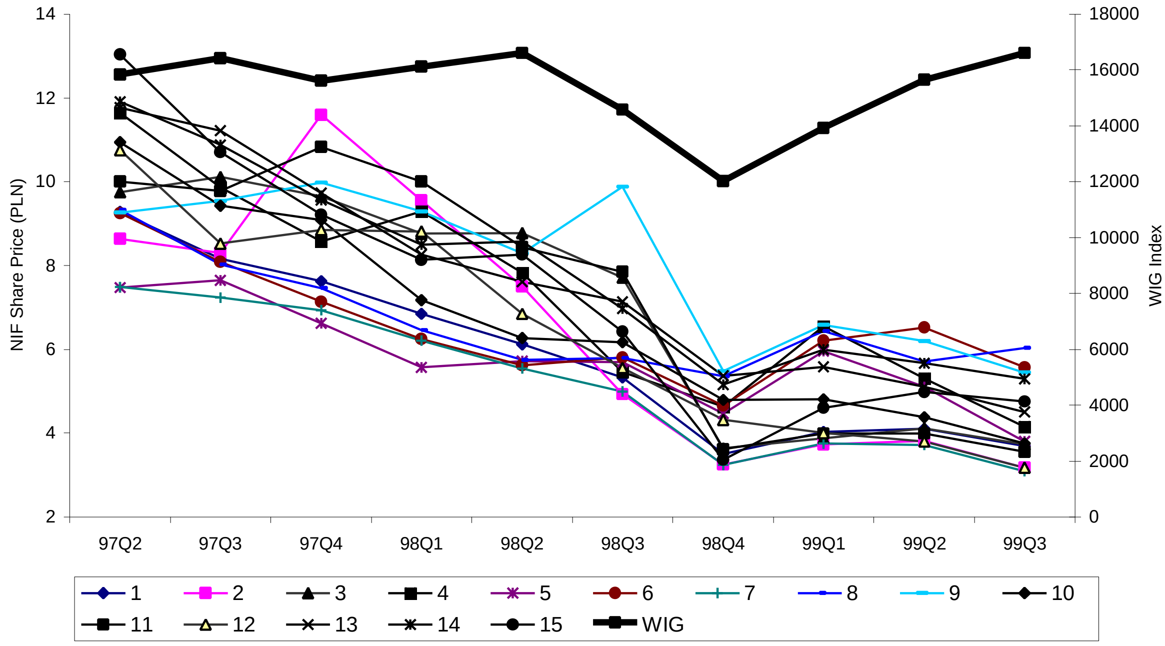
All National Investment Funds took advantage of their legal powers and reorganised the supervisory boards of their portfolio companies. While, in general, asset disposal was not a major problem facing the new management, employment reduction took place fairly slowly in all portfolio companies and is also expected to continue at a slow pace. Many companies have been floated on the stock market or sold to strategic investors, and some of the loss making enterprises liquidated or entered into the bankruptcy process. Despite restructuring efforts and improvements in profitability in the majority of NIFs, their performance in the 1995-1998 period has been, on the whole, rather disappointing.

NIF's shares began trading in a buoyant market in 1997, then gradually a general long term decline began. The fall in share prices continued throughout 1997 and 1998, though recovering somewhat in the first quarter of 1999.

It is now recognised though, that irrespective of their balance sheets, most of the companies in the scheme were in poor shape in late 1995 and early 1996 when they were transferred to NIFs (see Hashi, 1999, p. 7).[62] Although NIFs regarded themselves as agents of change, embarking on policies aimed at changing the management structure, strategy, operations and, more importantly, the dominant culture of their portfolio companies, their success remained little visible. In most cases, both the net assets values and the return to NIF shareholders (measured by the change in share prices) have not increased in line with inflation.

[62] The uncertainty about future ownership and the absence of new investment in the preceding 2-3 years had resulted in a serious deterioration of their position.

Figure 1 - Average Quarterly NIF Share Prices (PLN) and WIG Index



Source: Warsaw Stock Exchange data base; Hashi. (1999).

Portfolio companies of the Polish Mass-Privatization Programme

In spite of the weaknesses of the MPP since the end of 1998 Poland witnessed a process off ownership accumulation in the hands of financial institutions. Other than in the Czech Republic this development is to be seen as a reaction to the partly dispersed ownership structure resulting from the much regulated Polish model and aims on the overcoming of corporate governance problems on the fund-level.

Not until the restructuring activities of the NIFs on the level of the portfolio companies came to effect the companies started to attract institutional investors. As can be seen from table 6 above the stock exchange, OTC market as well as individual investors and employee owned companies are involved.

Table 6 - New owners of the NIF firms on December 31st, 1999

NIF	Firms with new owners	Domestic investors	Foreign investors	Private entre-preneurs	Employee owned firms	Stock ex-change*	OTC market *	Bankruptcy / liquidation
1	18	11	2	4	1	1 (2)	3	5
2	16	8	2	4	2	1	- (1)	3
3	20	12	2	4	2	2	1	5
4	16	10	3	1	2	- (1)	-	1
5	18	10	2	3	3	-	- (1)	2
6	16	7	5	4	-	- (1)	-	4
7	5	2	1	1	1	-	-	4
8	17	10	4	3	-	-	2	4
9	16	7	7	2	1	- (3)	1	4
10	9	3	3	3	-	1 (2)	3	1
11	16	10	5	1	-	4 (5)	- (1)	4
12	14	11	1	1	1	-	-	-
13	15	8	3	4	-	1 (3)	-	4
14	11	7	4	-	-	3	-	4
15	17	7	6	4	-	- (3)	-	1
Total	225	123	50	39	13	13 (26)	10 (13)	46

Source: *T. Kaminski* 'Secondary Ownership Changes in Companies Participating in the NIF-Programme', ACE Working Paper, Warsaw 8/2000, p. 13; *(Minority shareholding).

5. Summary and Conclusions

In summary, the current level of development of employee participation in Poland could be characterised as intermediate, at least in comparison with other post-Communist countries. The only observed forms of employee financial participation in Poland consist in shares in the ownership of co-operatives and privatized enterprises; on the other hand, Poland's privatization program was characterized by significant incentives for employee participation, and ownership structures in companies privatized by the employee leasing method have, on the whole, been relatively stable, with non-managerial employees retaining, on the average, a significant portion of enterprise shares. However, it must be borne in mind that financial participation hardly extends beyond these companies and the small worker co-operative sector, and the significance of these groups of firms in the Polish economy is a shrinking one. No incentives have been provided by policy makers for the extension of employee financial participation. All forms of participation are available for use in employee compensation schemes; however, there are no tax incentives to do so, and no interest in development of such schemes can be observed either in political or trade union circles. Moreover, the development of non-financial participation (i.e., participation in decision-making) has been very limited, even in those companies where employees hold significant share packages: Poland remains dominated by an elitist and managerialist corporate culture which minimises opportunities for participation.

Although it seems that the development of both direct and indirect (representational) employee participation in decision-making processes in employee-owned companies is in a very primitive stage at best, there are signs that some potential for development of genuine employee involvement could be resting latent in these firms. In many Polish employee-owned companies, for example, no dividends have been paid out - even after two to three years of functioning as a private firm - due to decisions to plough back profits in the form of investment or not to pay dividends until the lease is paid off. The fact that employee shareholders can be convinced to vote in favour of such 'austerity' plans provides some evidence that the entrepreneurial attitudes characteristic of genuine ownership and participation may be present among the work forces of certain employee-owned companies.

The influence of the European Union on the development of financial participation in Poland can be described as negligible, since efforts by the Commission (in terms of the *acquis communautaire*) in this area have focused on non-financial, indirect participation (i.e., employee representation in corporate governance organs such as the supervisory board and executive board). Almost all progress which has been made in the area of decision-making participation in Poland can, however, be ascribed to the European Union.

The economic performance of employee-owned companies in Poland is certainly satisfactory in comparison with most other ownership groups in the country's economy. However, econometric evidence provides little or no support for the hypothesis that employee ownership is related – either positively or negatively – to performance. This is due, I believe, to the organizational culture which is dominant in Polish companies regardless of their ownership form. The sort of identification with a firm which is the cornerstone of genuine ownership and the associated entrepreneurial spirit does not result automatically from mere shareholding. Ownership must imply not only a claim on a portion of the firm's revenues, but also participation in decision-making and responsibility for the firm's development. Studies of employee ownership in developed economies indicate that employee participation is more effective in generating such attitudes among employees the closer it is to the individual employee; that is, direct participation of each employee in decisions affecting his or her daily work is much more effective in generating the motivational effects that lead to productivity growth than is, for example, the presence of trade union representatives on supervisory boards. If employee ownership is mere share ownership without such participation in decision-making processes, it is likely to be hollow and fail to yield positive effects on productivity.

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