



The PEPPER IV Report:

Benchmarking of Employee Participation in Profits and Enterprise Results in the Member and Candidate Countries of the European Union

Executive Summary

(updated 2010)

**With a foreword by
the President of the Eurogroup,
Prime Minister of the Grand-Duchy of Luxembourg,
Jean-Claude Juncker**



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PEPPER IV Report

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Executive Summary

This Report summarises and updates the previous PEPPER reports. It is the result of the Commission-funded Project “Assessing and Benchmarking Financial Participation in the EU-27”.

The Summary version of this report is published in French, German Italian and English language and is downloadable on the Inter-University Centre’s website at www.intercentar.de together with the extended versions of the PEPPER III and PEPPER IV Reports which are published only in English. For rights of translation or reproduction, applications should be made to the Director of the Inter-University Centre.

Complying with the concept of the PEPPER reports and building on them it provides a solid basis for leveraging the development of Financial Participation in the European Union in the context of the current reform process triggered by the European Commission and Parliament.

The Project closes the gap between PEPPER I/II (1991, EU-12 / 1997, EU-15) and PEPPER III (2006, 10 new EU Member States / 4 Candidate Countries). Furthermore it implements benchmarking indicators developed by the European Foundation for the Improvement of Working and Living Conditions in all 27 EU Member States and Candidate Countries.

The PEPPER IV Report has been edited by Jens Lowitzsch (Inter-University Centre), Iraj Hashi (Staffordshire University) and Richard Woodward (CASE Foundation, Poland / University of Edinburgh) and written in cooperation with a core-team of experts in the field of Financial Participation, i.e., Milica Uvalić (Perugia University) and Daniel Vaughan-Whitehead (International Labour Organisation). The extended Version of the Report contains 29 country profiles which were compiled by Natalia Spitsa and Stefan Hanisch using information from an international network of legal and economic experts. The European Commission’s Directorate General Employment, Industrial Relations and Social Affairs and the Kelso Institute have supported the Benchmarking Project. The editing was supervised by Patricia Hetter Kelso.

Foreword

Determining wages has at all times been a thorny issue. What is due, what is fair, what is preposterous? How to share profits between capital and labour? Which parts can be variable, which need to be guaranteed? Some of these debates have been led for centuries, others as with too often doubtful compensation schemes of managers, are more recent but equally worthwhile.

Already twenty years ago, Jacques Delors has with characteristic foresight guided the European Commission into a profound analysis of the larger theme of employee compensation in a new world of work that he saw emerging. The present report on 'Promotion of Employee Participation in Profits and Enterprise Results' contributes to feed these reflexions.

Financial participation of employees in the profits of their employer as a complement to monthly wages is nothing else but the practical implementation of the fundamental idea that the wealth creation in an enterprise is first and foremost the result of the labour and know-how of its employees. For employers, it offers the advantage of increasing alignment of interests with employees, of linking part of labour costs to company performance and, if it is well organised, of enhancing motivation.

As this report confirms, financial participation of employees has developed considerably over the last decade. This is to be welcomed. At the same time, we have to keep in mind that it is far from a general trend. Employees in management positions benefit more often from such schemes than those on the shop floor. Smaller firms only rarely develop complex compensation schemes. Working for a company listed on the stock market makes it more likely to be included in some form of an employee stock ownership plan.

One can furthermore witness a significant number of trends in the labour markets that constitute serious challenges to a further broadening the scope of financial participation schemes. A 'hire and fire' mentality is hardly compatible with the long-term motivation financial participation of staff is supposed to achieve. A particular worry lies in the increased recourse to atypical work contracts. While some forms of innovative contracts can be convenient for both parties, it is my firm conviction that the unlimited employment contract has to remain the standard form of employment. Employment is not only about labour needs of companies, it is also about family life, long-term personal projects, the basic assurance that also in three months time, mortgages can be repaid and a week-end trip planned.

As we have been witnessing since late 2008, employees often bear much more than just a fair share of the pain in an economic downturn. Tools allowing them to share the gain when the financial results of their employer are growing are, apart from all other aspects, part of a basic fairness in the relationship between employer and employee. The development of such mechanisms therefore needs to continue.

Fundamentals need at the same time to be respected. Prediction is very difficult, especially about the future, as Niels Bohr put it. Basic principles of prudence therefore demand that financial participation schemes come as a complement to wages. They should also prevent employees to run up significant debt in order to invest in shares, be it in those of their employer. Employee buy-outs, as for example the Employee Stock Ownership Plan (ESOP), can obviously be an attractive way to transfer ownership of a company. But they are the exception, not the rule.

The PEPPER IV report is a further step in developing financial participation in enterprise results in the European Union. Many steps need to follow. But Europe is heading in the right direction.

A handwritten signature in blue ink, consisting of a stylized, elongated shape that resembles a large, thin 'J' or a similar abstract form.

Jean-Claude Juncker

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Jean-Claude Juncker

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I. The Benchmarking Project, the Indicators Employed and the Current Situation in the EU-27

Jens Lowitzsch

1. Introduction

The PEPPER IV Report presents conclusive evidence, regardless of the data source, that the past decade has seen a significant expansion of employee financial participation in Europe. This is true of both profit-sharing and employee share ownership, although profit-sharing is more widespread (for details, see Chapters II and III). This rise is reflected in the data from a survey of thousands of European companies, which show that between 1999 and 2005, the percentage of companies offering broad-based share ownership schemes increased from an average of 13 to 18 per cent; for profit-sharing schemes, the increase was from 29 to 35 per cent (weighted country averages for all countries included in both samples). The percentage of company employees taking advantage of these schemes is also growing.

On the other hand, in spite of 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 increase in all aspects of non-standard employment contracts may exacerbate this problem in future (for details, see Part 3, Chapter II). In order to guarantee the basic Commission principle that financial participation should cover all workers and not only the core labour force, further concrete policy actions to extend broad-based schemes are called for.

A review of the more than 30 years covered by PEPPER Reports indicates that employee financial participation (EFP), though slow to take off, has picked up surprising momentum. Reflecting the two main dimensions of European policy development in this period, that is, integration and enlargement, the reports document several important advances. (1) Economic research has empirically confirmed the positive effects of EFP. (2) The principles and definitions of PEPPER schemes were formally incorporated in the 1992 Council

Recommendation¹. (3) Studies by the European Foundation for the Improvement of Working and Living Conditions from 2000-2004 analysed in depth various aspects of EFP over the course of its evolution and developed the benchmarking indicators. Although the particularly dynamic upturn in some countries (Austria, UK, Ireland) has specific causes, we surmise that the most recent, more general stimulus for the rise of EFP has been the prior Commission activities, that is, the PEPPER Reports as well as the reviewed strategy for growth and jobs in the EU, the Lisbon-Strategy, and the reform of the labour markets.

The different data sources of the PEPPER IV Report, each confirming the positive trend over time, show that actual financial participation of the working population of EU Member States (ECWS) falls short of the opportunities companies offer for such participation (CRANET). The shortfall can only partly be explained by the fact that naturally not all eligible employees participate or that schemes are not well communicated. This discrepancy in the different sets of cross country data can be explained by different definitions and methodology as well as diverse perspectives. None of these surveys specifically dealt with the subject of financial participation per se. It should be clearly understood that in this respect the PEPPER IV benchmarking represents a compromise to cope with the existing data deficit without undertaking a new survey.

How should policy makers implement that part of the Lisbon Strategy calling for broadened employee financial participation? The road to this goal has three clearly marked lanes: Construct a legal framework. Promote. Research.

- Legislate EFP at the EU level with a Council Recommendation on a European Platform utilising the Building Block Approach.

Resting on the principle of voluntariness, the trans-national Building Block Approach reflects the diversity of schemes, while opening national practise to new forms.

- Utilise optional tax incentives to encourage employee financial participation.

While not a prerequisite for EFP, tax incentives clearly have a positive influence in countries which offer them. Making their introduction optional avoids conflict with national law.

- Research the current state of EFP in the EU with a comparative, focused survey.

No cross country data targeting financial participation exists to date. This data vacuum needs to be filled. Policy makers need a clear and precise overview of the *status quo* in order to work towards the goals of the Lisbon Strategy.

a) Recent Initiatives

Both the European Commission and Parliament launched an initiative, manifested in the opinion of the Economic and Social Committee of 26 February 2003,² on the Commission Communication 'on a framework for the promotion of employee financial participa-

¹ Council Recommendation 92/443/EEC of 27 July 1992 'on the promotion of participation by employed persons in profits and enterprise results (including equity participation) in Member States', *Official Journal* L 245, 26 August 1992.

² SOCI 115, Employee Financial Participation, CESE 284/2003.

tion'.³ The European Parliament called on the Commission to submit studies on the issues raised in its Resolution of 5 June 2003⁴. Among these were the feasibility of financial participation in small and medium-sized enterprises and the possibility of implementing in other EU Member States share ownership schemes based on the ESOP (Employee Stock Ownership Plan). In his foreword to a 2008 study published in response to this request⁵, the President of the European Parliament, Hans-Gert Pöttering, stressed the value of the suggested 'Building Block Approach' therein proposed. This approach provides a broad incentive system made up of diverse and flexible alternative components, which correspond to existing national systems, thereby introducing a flexible European concept.

In the European Reform Treaty signed on 13 December 2007 in Lisbon, and – after ratification by all EU member states – entered into force on 1 December 2009, the EU for the first time expressly commits itself to the European Social Model as one of the pillars of its policy. Thus, Art. 3 III of the Treaty on the Functioning of the European Union (TFEU) states that the Union 'shall work for the sustainable development of Europe based on [...] a highly competitive social market economy, aiming at full employment and social progress' and that '[...] It shall combat social exclusion and discrimination, and shall promote social justice and protection [...]'. In 2006, in his foreword to the PEPPER III Report⁶, the Commission's Vice-President Günther Verheugen postulated a stronger link between pay and performance as one possible way to reform the labour markets. Further, in September 2007, Mrs Christine Lagarde, the French Minister for Economy, Finances and Labour, announced that on assuming the Presidency of the European Union in July 2008, France wishes to launch a European Model of financial participation supported by the member countries.⁷ On 21 October 2010, the European Economic and Social Committee adopted the own-initiative opinion SOC 371 on the subject (download at: <<http://www.intercentar.de/en/research/focus-financial-participation-of-employees/eesc-own-initiative-opinion-soc-371/>>).

In the light of these remarkable political initiatives and against the background of the positive dynamic of Financial Participation, we surmise that the conditions for further developing employees' financial participation are now especially favourable. Nevertheless, important challenges remain, both old and new, most urgently, the lack of a European legal framework for Financial Participation but also hardening global competition and the strain it is exerting on Europe's enterprises. While the former is familiar and has been addressed in recent initiatives⁸ the latter has been fundamentally changing the 'world of

³ COM (2002) 364 Final.

⁴ P5-TA (2003) 0253.

⁵ Lowitzsch et al. (2008) *Financial Participation for a New Social Europe* (Rome, Paris, Berlin, Brussels: Inter-University Centre Split/Berlin). The book was distributed in the European Parliament in English, French, German. In autumn 2009, an Italian edition was published. A Polish edition is forthcoming.

⁶ Lowitzsch, Jens (2006) *The PEPPER III Report – Promotion of Employee Participation in Profits and Enterprise Results in the New Member and Candidate Countries of the European Union* (Rome and Berlin: Inter-University Centre Split/Berlin).

⁷ Speech on 12 September at the occasion of the 40th anniversary of FONDACT in the French Senate.

⁸ The European Commission's Directorate General Employment, Social Affairs and Equal Opportunities has supported the project 'A European Platform for Financial Participation' which sets forth both a policy and a detailed proposal for a European concept of employee ownership and profit-sharing; for the project report see Lowitzsch et al. (2008).

work' (see Part 3, Chapter II) leading to a growing demand for flexibility at the level of the individual company.

b) To Address Both Challenges...

Both challenges call for implementation of a European platform for Financial Participation while the role of Financial Participation in the reviewed 'Lisbon strategy' needs to be more precisely formulated. The framework conditions set by legislators are an important factor in enhancing the growth of PEPPER schemes, but only a well formulated policy can fully unleash their potential to boost motivation, productivity, and ultimately economic growth and jobs (see Part 3, Chapter I). To achieve their proclaimed goal of making 'the EU a more attractive place to invest and work in' European policy makers should ensure that the working people who are to bring about these changes also participate in the fruits of this process, that is, in profits and ownership stakes in European firms.

This is the context in which the question of **internal versus external flexibility** becomes of crucial importance. In addition to improving employee motivation and productivity, and thus the competitiveness of European companies, financial participation can play an important role in achieving internal flexibility. Flexibility no longer applies only to the options available to companies for production or other needs.⁹ The Commission's new Flexicurity approach¹⁰ also looks at flexibility in terms of enhanced mobility in the labour market and in work organisation. Table 1 contains a typology of work flexibility. Locational flexibility (or flexibility of place)¹¹ was added to the classical types of flexibility¹², that is, working time, contractual arrangements, variable pay and financial participation as well as functional dispositions. They are grouped into external and internal types; by the internal types of flexibility we mean those that the firm applies to workers within the firm without changing the basic employment relationship, while we use the term external to refer to the interaction between the firm and the external labour market; that is, either to the firm's access to workers outside the company (as, for example, in the case of outsourcing) or to its ability to 'expel' workers and thereby 'externalise' them.

It seems that at the national policy level, up to now, contractual flexibility (external/numerical) has been considered the most important aspect of labour market flexibility. Financial participation as a means of providing internal financial flexibility, on the other hand, has received much less attention. Moreover, in general, most of the flexibility discussion has been focused on specific arrangements or a specific category of flexibility despite the fact that flexibility is multi-dimensional. There are substitutional as well as complementary effects and the type of flexibility that is developed is just as important as

⁹ The European commission in its Joint Employment Report addresses this issue of flexibility, calling for an adequate flexibility for both workers and employers (EC, 2006).

¹⁰ As defined in the recent EC Communication "Towards Common Principles of Flexicurity: More and better jobs through flexibility and security", COM (2007) Final (27-6-2007).

¹¹ See C. Wallace "Work flexibility in eight European countries: A cross national comparison", Sociological Series 60, Vienna, Institute for Advanced Studies, 2003.

¹² The definition of flexibility proposed by J. Atkinson and N. Meager in 1986 distinguishes external numerical flexibility (contractual), internal numerical flexibility (working time), functional flexibility (organisational) and financial flexibility (wages).

its extent.¹³ Increasing internal financial flexibility through financial participation would help to alleviate the pressure on contractual flexibility. This also is in line with many of the general principles of flexicurity held by the heads of states and governments of EU Member States, such as ‘a better balance between external and internal flexibility’, ‘a climate of trust and dialogue’, ‘a better workers’ adaptability capacity’, etc. (see Part 3, Chapter II).

Table 1. A typology of work flexibility

Flexibility Category	Internal	External
Numerical	Working Time (Temporal) – Part time / leave / flexible hours – Overtime / shift / annualisation	Contractual (Employment) – Temporary / Fix-term / Agency work – Relaxed hiring/dismissal regulations
Functional (work organisation)	– Job rotation / Team work / Task rotation – Workers training/options to bring change	– Outsourcing – Restructuring
Locational (spatial)	– Tele work / Home work – Out-workers /Relocation within company	– Relocation – Off-shoring
Financial / Wage	– Variable pay (individual/team related) – Profit-Sharing / Share- Option schemes	– Downsizing – Financial restructuring

Source: compilation by the author.

What gives legitimacy to the current discussion of new forms of financial participation is the fact that the radical reforms of the European legal and economic order in the process of the EU’s eastward enlargement, together with privatisation and globalisation, have led not only to economic progress but also to widening social fissures. While enterprise profits have been on a steep rise for more than a decade, wages have been stagnant¹⁴ and the economic lives of many have been rendered insecure. The ‘society of owners’ must be simultaneously understood as the ‘society of non-owners’. The growing discrepancy between the few who are rich and the many others who are ‘working poor’ needs to be addressed.

c) ...in the Context of the Current Situation in the EU-27

In the EU-15, between 17 per cent (employee share ownership) and 36 per cent (profit-sharing) of employees in the private sector currently participate financially in the enterprise for which they work. These existing schemes constitute a pillar of the European Social Model. In spite of the unsatisfactory results of the PEPPER II Report which followed up the Council Recommendation of 1992 (see footnote 1), the number of share ownership schemes has seen a strong increase during the last decade (see below Chapter II and III). Furthermore, for example in France, the country where PEPPER schemes

¹³ H. Chung, M. Kerckhoffs, P. Ester, “Working time flexibility in European companies” European Foundation for the Improvement of Working and Living Conditions, Dublin 2007.

¹⁴ While from 2003 until 2007 corporate and capital income rose by 37.6 per cent, the average employee income increased only by 4.3 per cent, said Minister of Finance Peer Steinbrück of Germany, cited “Mitarbeiter sollen am Unternehmenserfolg teilhaben” Die Welt Online, 27 August 2008.

have had the longest tradition, there has been a gradual increase in the share of variable pay in recent years.¹⁵ This suggests a tendency in some countries to increase workers' income more and more through variable forms of remuneration. On the whole, a generally favourable attitude within a given country has usually led to some supportive legislation for PEPPER schemes, which in turn has spread their practice. This suggests a clear link between national attitudes, legislation and diffusion (see Part 3, Chapter II). Nevertheless, the European Union still lacks a unified legal foundation on which to build a European system of financial participation.

A quite different situation obtains in the new EU member and candidate countries¹⁶ (see the PEPPER III Report). Very few laws specifically address employee financial participation, and these refer almost exclusively to employee share ownership¹⁷; legislation on profit-sharing is rare¹⁸. Although employees were frequently offered privileged conditions for buying shares of their employer companies, the purpose was not to motivate employees to become more efficient and productive. Nor was there more than mild concern for social justice. Rather, this method was simply an expedient for privatising state-owned enterprises for which at the time there were no buyers. Essentially it was a decision made by default. Given the limited support for PEPPER schemes, it is not surprising that empirical evidence on the effects of schemes is available for only some countries – the Baltic States, Hungary, Poland, and Slovenia. Although much of the evidence is preliminary and refers primarily to the 1990s, when employee ownership played a different role than today, these studies suggest that enterprises with employee ownership frequently performed no worse than firms with other ownership forms. The comparative analysis of the general attitude of governments and social partners shows the lack of concrete policy measures supporting PEPPER schemes, as well as limited interest of both trade unions and employer organisations.¹⁹ Rather than being actively promoted as in some old EU Member States, employee financial participation has most frequently not even been considered, or is viewed with suspicion.

Against the background of the different genesis of PEPPER schemes in the old and the new EU Member States it is surprising, that the data examined in the benchmarking project seem to indicate that a West-East divide exists only with regard to profit-sharing.

¹⁵ Profit-sharing bonuses have increased from 3.1 per cent in 1996 to 4.5 per cent in 2003 of total pay, while 'participation' schemes from 3.8 to 4.6 per cent.

¹⁶ Cyprus, Czech Republic, Estonia, Hungary, Lithuania, Latvia, Malta, Poland, Slovakia and Slovenia which joined the EU on 1 May 2004, Bulgaria, Romania on 1 January 2007 and Croatia, and Turkey as Candidate Countries.

¹⁷ Employee share ownership has largely developed in the course of recent privatisations, with different methods including sales of enterprise shares to insiders on privileged terms; employee-management buyouts; leasing; mass privatisation, and ESOPs and ESOP-type schemes.

¹⁸ Despite the fact that company laws in several countries do refer to the possibility of employees having a share of company profits, Romania is the only country that has specifically legislated a general scheme for cash-based profit-sharing in state owned companies (though implemented in a small number of firms). Among the non-transition countries, only Turkey has legislation on profit-sharing.

¹⁹ Only occasionally have trade unions been supportive of employee ownership, but they remain rather critical of profit-sharing. The employers have been generally indifferent towards financial participation, despite a few cases of active support (as in the case of ESOPs in Hungary).

2. Responding to the Data Deficit: The Benchmarking Project

The PEPPER IV Report is an interdisciplinary legal and economic comparative study. It provides a Comparative Assessment of Financial Participation in the EU-27 and in the candidate countries based on coherent and thus for the first time comparable indicators.

a) Aims

The Project closes the gap between PEPPER I (1991, EU-12), PEPPER II (1997, EU-15) and PEPPER III (2006, ten new Member States and four candidate countries), and utilises the benchmarking indicators developed by the Dublin Foundation in all 27 EU Member States and candidate countries. It consists of three complementary basic components that build on each other:

- Description of the legal environment, fiscal or other incentives and links to participation in decision-making with a specific focus on schemes for SMEs;
- Benchmarking financial participation, that is, the scope and nature of financial participation schemes;
- Comparative analysis of the national policies and characteristics that affect the environment for financial participation.

The final recommendations derived from the comparative analysis, best practise in the member countries and, in the context of the development of ESOPs, that in the United States, set forth both a policy and a proposal for promoting Financial Participation at the European and the National level.

b) Approach

The Benchmarking exercise continues the projects ‘Financial Participation of Employees in the New Member and Candidate Countries’ and ‘A European Platform for Financial Participation’ (both successfully concluded) funded under the same budget line and building on the PEPPER Reports. It digests their results and data from previous studies (EWCS, Eiro, CRANET, EFES).²⁰ The purpose of the project is fourfold:

- To systematically assess similarities and compatibility of the laws and practices governing financial participation in the EU-27 and candidate countries;
- To close information gaps (that is, between PEPPER I, II and III) that currently prevent a full profiling of financial participation policy and practice;

²⁰ EWCS: European Working Conditions Survey and Eiro: Comparative Study on Financial participation in the New Member States (both European Foundation for the Improvement of Working and Living Conditions); CRANET E: Cranfield Survey on International HRM (Cranfield School of Management); EFES: European Employee Ownership Top 100 (European Federation of Employee Share Ownership).

- To discuss individual country's scores on the indicators against the background of comparable scores for the other EU Member States, providing a contextual frame of reference for each single profile;
- To further promote a common platform for financial participation within the European Union, in the context of comparative analysis.

An interdisciplinary conference, with key EU experts presenting preliminary project results, took place in October 2007 in Berlin; preliminary results of the PEPPER IV Report were presented in Brussels and in Strasbourg to the European Commission and Parliament in May 2008; this Final Report was launched in Rome in October 2009.

c) Specific Difficulties to Be Dealt with

In 2004, the European Foundation commissioned a report that developed 16 specific indicators of financial participation policy and practice facilitating like-for-like comparisons of the financial participation situation in each Member State. The second stage of the process, to 'road test' these indicators, was undertaken in 2005. While nine of the European Foundation's 16 benchmarking indicators were supported by existing data, seven of the measures were not supported at all. The Benchmarking project addressed this data shortage not by undertaking a new study dedicated to financial participation; instead, as recommended by the pilot benchmarking study of Slovenia commissioned by the European Foundation, it referred to existing upgraded surveys (that is by the European Foundations 'Eiro Comparative Study on Financial Participation in the New Member States', to whose questionnaire our team contributed input).

Furthermore, the Pilot Study by the European Foundation clearly demonstrated how the Foundation's nine supported indicators can be practically employed to produce a partial profile (in the test case of Slovenia). In order to be independent of new EU-wide surveys, the work programme initially aimed at such a partial profile using those nine indicators. Including the results of the complementary survey of our project partners, additional indicators were added. For individual country's National Sources (see Part 2, Country Profiles) and 'blank spots' (in some cases for single countries and single indicators), our team provided the necessary supplementary information using our EU-wide network from the previous projects.

The Commission and Parliament identified transnational obstacles to the development of a European model for financial participation, which a High Level Group of independent experts had classified at the end of 2003.²¹ Our assessment of the legal environment investigates the possibilities for creating a European legal framework for financial participation. In so doing, the project, as recommended in PEPPER III, builds on the 'Building Block Approach' to combine established schemes in a single program with alternative options and to keep the different elements complementary.

²¹ European Commission (2003a) *Report of the High Level Group of Independent Experts on Cross-Border Obstacles to Financial Participation of Employees for Companies Having a Transnational Dimension*, December (Brussels: European Commission).

3. The Benchmarking Indicators²²

a) Sources

Any benchmarking exercise, especially one involving a large number of countries, relies on the availability of comparable and consistent data. While there are a large number of studies on the impact of employee participation on company performance²³, there are very few sources of information on the availability and take-up of financial participation schemes across countries. Below we briefly present the main sources of information on financial participation (FP) schemes in European countries on which the discussion of this chapter and country reports are based. These sources are very different from each other and need careful interpretation.

(i) CRANET Survey. This is a survey of companies with more than 200 employees²⁴ undertaken by the Cranfield School of Management (Cranfield University, UK) approximately every four or five years since 1992. It is largely a postal survey, sent to the Human Resources Departments of companies with the main aim of investigating the HR characteristics and practices of these companies. One section of the questionnaire is concerned with employees' remuneration and its components. In this section there are questions on whether the company offers any financial participation scheme (specifically, share ownership, profit-sharing or stock option schemes) to various occupational groups of employees (management, professional and technical, administrative, and manual workers). In 2005, the Survey covered 7,914 companies in 32 EU and non-EU countries (the EU member and candidate countries not included were Ireland, Latvia, Lithuania, Luxembourg, Malta, Poland, Portugal, Romania and Croatia).²⁵ Because of the postal nature of the survey, the response rate is rather low (16 per cent in 2005). The CRANET sample is selected randomly from the population of companies with more than 200 employees and is designed to represent the size and sectoral distribution of companies in the population.²⁶ The companies included in the sample are selected separately in each round of the Survey, thus the data is not in the form of a panel. In order to have a more complete picture of FP in all member and candidate countries of the European Union, we undertook surveys in seven of the missing countries (Latvia, Lithuania, Malta, Poland, Portugal, Romania and Croatia).²⁷ The surveys consisted of a smaller number of firms in each country

²² We are grateful to Edvard Orlic, our Research Assistant, for his diligent and dedicated work.

²³ These studies are usually concerned with individual or a small number of countries and use different methodologies in pursuing their objectives.

²⁴ The 2000 Survey covered companies with 100 or more employees. The unit of investigation in CRANET is an 'organisation' or a 'business unit'. While this may include a self-contained subsidiary of a larger company, in general it coincides with the boundaries of 'companies'. For the sake of simplicity, therefore, we refer to them as companies.

²⁵ The number of companies in the countries of interest to this study was 5,214.

²⁶ For more detailed information on the CRANET Survey, see CRANET (2005) and Pendleton, Andrew et al. (2001).

²⁷ The survey conducted in Latvia showed no financial participation scheme in any of 104 companies in the sample. Given the information from other sources (such as EWCS and various research papers) we believe this outcome is unrealistic, caused by a biased sample. As there was no time to repeat the exercise with a random sample, Latvia has been excluded from some of the tables. Luxembourg has been

and covered only those parts of the CRANET questionnaire related to remuneration and the general information about the company, thus were comparable to the CRANET survey.²⁸ It is essential to note that the CRANET Survey does not indicate the incidence of financial participation schemes in companies but only their availability. Furthermore, for the purpose of this research, we have been concerned with broad-based financial participation schemes (that is, schemes covering more than 50 per cent of employees) in private sector companies only, as profit-sharing or share ownership are largely not applicable to public sector organisations (which do not make ‘profit’ as such and do not always have shares to distribute to employees).

(ii) European Working Conditions Survey. This is a large scale survey of working conditions across Europe undertaken by the European Foundation every four or five years to investigate a variety of factors influencing individuals working and living conditions. One section of the questionnaire deals with remuneration and sources of income, asking the respondent whether they receive any income in the form of profit-sharing or any income from the ownership of shares in the companies for which they work. Given that individual subjects may be employed, unemployed, self-employed or retired, the present survey is only concerned with the individuals who are in employment. The 2005 Survey covered some 30,000 randomly selected individuals in 31 countries (including all EU and candidate countries as well as some non-EU countries). These surveys are conducted by face-to-face interviews and, consequently, the response rate is higher (48 per cent in 2005)²⁹. As with the CRANET Survey, only a small part of this investigation is related to financial participation. The previous round of this survey took place in two waves – in 2000 for the EU-15 and a few other European countries and in 2001 for the accession and candidate countries. Unlike the CRANET survey, which only shows the availability of financial participation schemes to employees, the EWCS represents the actual take-up of these schemes. However the data applies to all employees, irrespective of the size of their companies. Given that respondents may be from any category of employee (managers, professionals, clerical or manual), it is not possible to identify whether any financial participation scheme is broad or narrow. Unlike the 2000 and the 2005 survey, the 2001 round did not directly distinguish between employees of the public and private sector.³⁰

(iii) European Federation of Employee Share Ownership (EFES) data. For many years, EFES has been collecting data on the scale of employee share-ownership in large companies in 29 European countries, including all 27 EU Member States. The population

excluded from the benchmarking exercise altogether. Ireland was of course included in the 1999 CRANET.

²⁸ The planned number of firms in each of these countries was 100 in larger and 50 in smaller countries, randomly selected. In practice, the total number of observations in these countries was 533 – in Malta, in particular, the number of firms interviewed was 17 (and for this reason, the information on Malta should be treated with caution). Furthermore, given that the number of large firms in some of these countries (Latvia, Lithuania, Malta, in particular) was small, firms with less than 200 employees were also included in the sample.

²⁹ Of course, given that respondents either ‘did not know’ or ‘refused to answer’ some of the questions in the survey, the effective response rate was lower.

³⁰ However, given that the surveys identify the sector of activity of the respondents, the gap between the 2000 and 2001 surveys has been reduced by the elimination of those respondents working in ‘public services’.

of this database consists of all listed companies with a market capitalisation of at least Euro 200 million and large non-listed employee owned companies (those employing more than 100 people with employees owning more than 50 per cent of shares). The former group consists of 2,270 companies and the latter of some 207 companies. The emphasis of this dataset is not on financial participation schemes in general but only on share ownership and only in large companies. Although the second group of companies do not include all the large, majority-owned companies, this group is only a small part (less than 10 per cent) of the total sample and does not change the overall picture significantly. In this Benchmarking exercise, we use data from 2006 and 2007.

(iv) Country Profiles based on various sources, including the PEPPER I, II, and III Reports, the EIRO Survey and our Project Expert Network in the field. These profiles of all 29 target countries (EU-27 and Croatia, Turkey) cover developments in three areas: Evolution of Financial Participation Schemes, Social Partners' Attitudes and Current Government Policy and Legal Framework.

To sum up, it is clear that the three datasets are not comparable to each other, as they refer to different indicators of financial participation. They should be seen as complementary, each highlighting a different feature of the development of employee financial participation. The diversity of these sources also emphasises the need for a new, comprehensive and consistent large-scale survey of employee participation across the whole of EU and candidate countries.

b) The Indicators and their Link to the Commission Principles

Each of the Benchmarking Indicators selected complies with one of the essential principles of financial participation schemes set forth by the Commission in its Communication seeking 'a framework for the promotion of employee financial participation'³¹. Needless to say, sufficient data was not available for all of the chosen indicators for screening).

- Principle 1: Participation must be voluntary for both enterprises and employees.
- Indicator: Legislative and fiscal support for financial participation.

The Country Profiles provide detailed information on whether specific legislation concerning financial participation exists and whether any tax relief is given. Furthermore, the overview of taxation systems and tax incentives distinguishes between incentives for firms and employees, on the one hand, and for profit-sharing and share schemes on the other.

- Principle 2: Access to financial participation schemes should in principle be open to all employees (no discrimination against part-time workers or women).
- Indicators: Percentage of enterprises offering broad-based financial participation schemes to employees and the percentage of employees covered by such schemes.

CRANET Surveys measured this as the percentage of organisations offering financial participation to each of the four occupational categories (managers and three non-managerial groups). In terms of the all-employees criterion, the assumption is that or-

³¹ COM (2002) 364 Final, 5 July 2002, pp. 3, 10.

organisations that offer financial participation to a particular occupational group do so for all employees within that grade. Furthermore, CRANET Surveys indicate the percentage share of each organisation's workforce that falling into each occupational grade. Putting the two pieces of information together, it is possible to calculate the percentage of employees in each organisation that are offered financial participation.

- Principle 3: Schemes should be set up and managed in a clear and comprehensible manner with emphasis on transparency for employees.
- Indicator: Percentage of employees participating in financial participation.

The 4th EWCS asks whether the remuneration includes payments based on the overall performance of the company (profit-sharing scheme) and/or income from shares in the company the respondent works for.

- Principle 4: Share ownership schemes will almost inevitably involve a certain complexity, and in this case it is important to provide adequate training for employees so as to enable them to assess the nature and particulars of the scheme in question.
- Indicator: Countries with direct/indirect and consultative/delegative participation in decision-making.

The Country Profiles give an overview of the different types of participation in decision-making practised in different countries. Unfortunately, sufficient data for the screening of this indicator was not accessible. The available empirical evidence suggests that incentive effects of financial participation are much greater when accompanied by greater worker participation in decision-making.

- Principle 5: Rules on financial participation in companies should be based on a predefined formula clearly linked to enterprise results.
- Indicators: Percentage of employees whose financial participation is calculated on a predefined formula and the percentage participating in regular ongoing schemes.

The fourth EWCS asks whether profit-sharing payments are calculated on a predefined formula and whether these payments are received on a regular basis.

- Principle 6: Unreasonable risks for employees must be avoided or, at the very least, employees must be warned of the risks of financial participation arising from fluctuations in income or from limited diversification of investments.
- Indicator: European Employee Ownership Top 100 Index.

Sufficient empirical data for the screening of this indicator was not available. However, the information from the European Employee Ownership Top 100 Index permits an assessment of one dimension of risk through matching financial participation in quoted companies with their performance on the stock markets.

- Principle 7: Schemes must be a complement to, not a substitute for, the existing pay system.
- Indicator: Percentage of enterprises in which financial participation and regular salary are kept separate and distinct.

Sufficient empirical data for the screening of this indicator was not available.³² Nevertheless, a good test for this indicator is to examine whether negotiations on the two issues take place separately and at different times; however, there is a danger of respondent bias (employers may be reluctant to give any information which could suggest salary substitution).

- Principle 8: Financial participation schemes should be developed in a way that is compatible with worker mobility both internationally and between enterprises.
- Indicator: Legislative and fiscal support for financial participation.

The Country Profiles look at specific financial participation schemes that are suitable for cross border use. The overview of taxation systems and tax incentives provide complementary information about this dimension of financial participation.

4. Overview of Financial Participation in the EU-27

Table 2. The old Member States of the EU

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Belgium	[A] TU opposed, but relatively more support for PS; EA in favour; [B] Since 1982, legislation for ESO; amendment 1991; since 1999 legislation for SO; since 2001 new law on ESO and PS.	All plans: EmpC up to 20% of after tax profit per annum; up to 10% of total gross salary; ESO: NCL - discounted ES in JSC, financing by firm possible; in capital increases: up to 20% of equity capital, ES discount limit 20%; NTL - (restricted stock grant) value reduced by 16.7%, taxation deferred if 2 years not transferable, 15% tax on benefit, no SSC; (stock purchase plan) benefit tax base 83.33% of fair market value; SO: NTL - since 1999 taxed at grant on a lump-sum basis, no SSC; PS: NTL - tax 15% for PS in an investment savings plan, 25% for other plans.	2005 Cranet: ESO 21%, PS 3.7%; 2005 EWCS: ESO 4.3%, PS 5.9%; firms involved mainly from financial sector, large firms and multinationals; SO 2005 Cranet: 2%; EU-Report 2003: 75,000 employees benefit; most of 20 largest Belgian firms operate plans; 40% of firms with more than 50 employees.
Denmark	[A] TU indifferent to FP; EA opposed to any extension of FP;	ESO: NCL - ES in JSC: discounted, up to 10% of salary per annum, 7-year holding period, free maximum of DKK 8,000 per	2005 Cranet: ESO 36%, PS 7.3%; 2005 EWCS: ESO 2.4%, PS 6.4%;

³² The 2008 European Establishment Survey of the European Foundation for the Improvement of Working and Living Conditions envisages to include questions that could permit an assessment of this indicator.

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
	<p>[B] Employee Funds discussed in 1970-80s, PS popular; later support for ESO and SO; in 2000s Government support for share-based schemes.</p>	<p>annum; financing by firm possible if qualified plan; in capital increases deviation from subscription/pre-emption rights possible; NTL - deferred taxation of benefit; EmplC: discount tax deductible;</p> <p>PS: NCL - SPS; NTL - up to 10% of annual salary;</p> <p>SO: NTL - exemption from PIT/SSC: broad-based if up to DKK 8,000, 5-year holding period; individual if up to 10% of annual salary or up to 15% difference exercise price/market price.</p>	<p>SO 2005 Cranet: 2%; EU-Report 2003: 20% of 500 largest firms by 1999, one third of quoted firms 2000.</p>
Germany	<p>[A] TU partly sceptical/partly hostile because of 'double risk', recently growing interest; EA support individual firms</p> <p>[B] Traditional focus on savings plans (total capital higher than that of ES company plans); FP since 2006 on political agenda of all parties. New law 2009.</p>	<p>ESO: NCL - discounted ES in JSC, financing by firm possible; state savings bonus of 20% of up to Euro 400 (Euro 80 per annum) invested in employer stock; no tax/SSC on up to Euro 360 per annum employer matching contribution; since 2009 Special Employee Participation Fund.</p> <p>PS: None</p> <p>SO: NCL - in capital increase, nominal amount restricted to 10%, that of increase to 50% of equity capital.</p>	<p>2005 Cranet: ESO 11%; PS 45%;</p> <p>2005 EWCS: ESO 0.8%, PS 5.3%;</p> <p>2005 IAB: ESO 3%, PS 12%;</p> <p>2003 WSI: PS in one third of firms;</p> <p>ESO: 2006 AGP, 3,000 firms, 2.3 million employees, Euro 19 billion;</p> <p>SO: EU Report 2003, in over two-thirds of DAX-listed firms.</p>
Greece	<p>[A] TU moved from scepticism to support in 1980s; EA indifferent, low priority not a current topic;</p> <p>[B] Some regulations on CPS (1984) and ESO (1987); since 1999 more attention on SO; not a current issue.</p>	<p>ESO: NCL - ES in JSC discounted or free; within capital increase for 3 years not transferable, up to 20% of annual profit; NTL - no PIT/SSC on benefit;</p> <p>SO: NCL - free/discounted; NTL - taxable at exercise; tax exempt if qualified plan;</p> <p>PS: NTL - up to 15% of company profits, 25% of employees' gross salary; no PIT, but SSC.</p>	<p>2005 Cranet: ESO 23.6%; PS 9.4%;</p> <p>2005 EWCS: ESO 1%, PS 2.8%;</p> <p>SO: 2005 Cranet 2%; SO EU-Report 2003: only a limited number of firms.</p>
Spain	<p>[A] Low priority: TU oppose income flexibility; EA ambivalent, fear information disclosure requirements;</p> <p>[B] Long tradition of social economy: COOPs (new law 1997) and EBO; PS supported in 1994 then shift to ESO/SO; active support.</p>	<p>ESO: NCL - ES/SO in JSC, financing by firm possible; NTL - tax benefits on PIT after 3-year holding period;</p> <p>PS: NLL;</p> <p>SO: NTL - after 2-year holding period 40% reduction of taxed plan benefit;</p> <p>EBO: 'Workers Companies' with more than 51% ESO, 10-25% of profits in Reserve Fund; NTL - if 25% reserve, tax exempt from:</p>	<p>2005 Cranet: ESO 5.7%, PS 17%;</p> <p>2005 EWCS: ESO 0.5%, PS 6.4%;</p> <p>ESO: 2003 CNMV 20% of large firms with share purchase plans;</p> <p>SO: 2005 Cranet: 19%; EU-Report 2003: plans in 40 firms of which 50% in IBEX 35;</p> <p>EBO: 2003 Heissmann, approx. 15,000 'Workers Companies'.</p>

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
		capital transfer tax, tax on formation/capital increase, notary fees.	
France	<p>[A] TU show mixed attitudes: sceptical but actively involved, favour if not substitute to pay; EA generally in favour, especially if voluntary;</p> <p>[B] PS/ESO strong continuous support since 1959; also in privatisations; climate friendly toward FP, focused policy.</p>	<p>ESO: PrivL - 5% ES reserve, up to 20% discount; NCL – discounted ES in JSC, financing by firm possible, also capital increase; SAYE; NTL - flat rate tax of 7.6% and 10% on returns, no SSC;</p> <p>SO: NCL - capital increase; NTL - tax on exercise gain 26-30% after 4-year holding period;</p> <p>ESOP/EBO: Law on Trusteeship 2007; NCL - special reserve for EBO possible;</p> <p>PS: DPS compulsory/CPS voluntary; NTL - flat rate tax 7.6-10% if paid to company savings scheme/fund after 5-year holding period.</p>	<p>2005 Cranet: ESO 34%, PS 92%;</p> <p>2005 EWCS: ESO 5.3%, PS 12%;</p> <p>2004 FONDACT: DPS covered 53% of non-agriculture private sector firms employees (that is 6.3 million);</p> <p>SO: 2005 Cranet 3%; SO EU-Report 2003: approx. 50% of quoted firms and 28% of limited companies, total approx. 30,000 employees.</p>
Ireland	<p>[A] EA strong support; TU support if financial and intrinsic reward to employees; managers/employees pragmatically motivated; Lobby groups/institutions for example banks for ESO;</p> <p>[B] Support in privatisation; improvements in 1995 and 1997; promoting voluntary adoption of SPS, for example Approved Profit-Sharing Scheme (APSS).</p>	<p>ESO: PrivL - 14.9% ESOT stock paid for by loan/by state; NCL - ES/SPS in JSC, financing by firm possible; NTL - New Shares: limited PIT tax base deduction for employees, no SSC;</p> <p>SO: Savings Plan: bonus/interest on savings tax free, no PIT on grant/exercise, no SSC; Approved Plan: no PIT at exercise, no SSC;</p> <p>ESOP: Trust Act - taxed 15% interest / 10% investment; NTL - ESOT: tax incentives as for APSS if ESOT part of APSS;</p> <p>PS: NTL - APSS: at transfer no PIT, no SSC up to limit; salary foregone - up to 7.5% of gross salary deductible.</p>	<p>1999 Cranet: ESO 14%, PS 15%;</p> <p>2005 EWCS: ESO 5.3%, PS,9.2%;</p> <p>SO: 2002 IBEC: 90 firms with SAYE schemes, 15 firms with Approved Share Option Schemes;</p> <p>PS: 2002 IBEC: 400 firms with APPS;</p> <p>ESOP: n.a.</p>
Italy	<p>[A] TU mixed attitudes, recently interested in topic / EA mostly supportive;</p> <p>[B] Trilateral agreement 1993 supported PS; then shift to support ESO/SO; recently discussed on political agenda; new law planned 2010.</p>	<p>ESO: CivC - discounted ES in JSC, financing by company possible; in capital increases deviation from pre-emption rights and preferential 'ES' possible; NTL - PIT & SSC exemption up to Euro 2,065 after 3-year holding period; in limited liability companies free share up to Euro 7,500 tax exempt;</p> <p>PS: NCL - no SSC on up to 5% of total pay;</p> <p>SO: NTL - SSC exemption after 5-year holding period.</p>	<p>2005 Cranet: ESO 13,7%, PS 6.2%;</p> <p>2005 EWCS: ESO 1.4%, PS 3.1%;</p> <p>SO: 2005 Cranet 1%; EU-Report 2003, approximately 6% of employees involved.</p>

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Luxem- burg	[A] TU/EA growing interest in 1990s, not supportive of share schemes; EA support profit-sharing; [B] FP not a current issue.	ESO: NCL - ES in JSC, financing by company possible; SO: NTL – ‘Tradable Option Plans’ reduced tax burden; PS: None.	2005 EWCS: ESO 3.7%, PS 13.5%; PS: PEPPER II, 1995 CPS in 25% of firms, mainly banks; SO: EU Report 2003, estimates 25% of firms - mainly financial sector.
Nether- lands	[A] TU/EA generally in favour; TU support if supplement to pay, prefer PS to ESO; [B] Traditional focus on savings plans; support for SO in 2003.	ESO: NCL - ES in JSC, financing by company possible; NTL - up to Euro 1,226 from pre-tax salary after 4 years in a savings plan 15% flat tax, no SSC; PS: NTL - up to Euro 613 from pre-tax salary after 4 years in a savings plan 15% flat tax, no SSC; SO: NTL – specific tax incentives abolished; IEInt: Qualified Savings Funds.	2005 Cranet: ESO 20%, PS 44.8%; 2005 EWCS: ESO 1.5%, PS 13.8%; PS: 3 million participants (2000); SO: 2005 Cranet 4%; EU-Report 2003, more than 80% of all listed firms.
Austria	[A] TU/EA currently support FP and co-operate; different views about participation in decision-making [B] Legislation since 1974; first tax incentives since 1993; more active support since 2001.	ESO: NCL - discounted ES in JSC; financing by company possible; NTL - PIT/SSC allowance for benefit; CGT or 1/2 PIT for dividends; tax exemption for share sale gain; IEInt: NCL - Employee Foundation: EmpC buys own stock, sheltered in IEInt, dividends paid out; NTL - EmpC: contribution to IEInt, setting-up/operation cost deductible; IEInt: tax allowance on contributions; Employees: CGT on dividends; SO: NCL - capital increase: nominal amount up to 10%, increase up to 50% of equity capital; up to 20% of equity capital for total amount of shares receivable; NTL - 10% of benefit per annum, up to 50% of total benefit tax free and carry forward of taxation for the remaining amount; PS: None	2005 Cranet: ESO 12%, PS 32.8%; 2005 EWCS: ESO 1.2%, PS 5.4%; 2005 WKÖ/BAK: ESO 8%, PS 25%; SO: 2005 Cranet: 2%; 2005 WKÖ/BAK: 1%
Portu- gal	[A] TU/EA Indifferent, low priority: TU prefer PS to SO; [B] ESO mainly supported in Privatisation, especially around 1997; not on the Agenda; FP is generally ignored.	ESO: PrivL - discounted ES; NCL - ES in JSC, financing by firm possible; in capital increase: suspension of pre-emptive right of shareholders for ‘social reasons’ possible; PS: NLL - not considered remuneration, no SSC; SO: NTL – 50% of share sale gain liable to PIT.	2008 PEPPER IV: ESO 5.3%, PS 28%; 2005 EWCS: ESO 0.9%, PS 1.9%; SO: EU Report 2003, from 60 firms listed at Euronext Lisbon Stock Exchange, about 22% have implemented SO.

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Finland	<p>[A] TU/EA generally support FP, especially desire to improve the environment for personnel funds; other forms not discussed;</p> <p>[B] Discussions on FP since 1970s; 1989 law on Personnel Funds (major form until now).</p>	<p>ESO: NTL - discount tax free, no SSC; tax relief for dividends;</p> <p>SO: None; PS: Cash-based none; NCL - share-based 'Personnel funds': in firms with more than 30 employees, if all participate, registration with Ministry of Labour, after 5-year blocking period up to 15% per annum can be withdrawn; NTL - 20% of payments to employee tax free; earnings of fund tax free.</p>	<p>2005 Cranet: ESO 14%, PS 66%;</p> <p>2005 EWCS: ESO 0.7%, PS 11%;</p> <p>PS: 2007 54 Personnel Funds with 126,000 members;</p> <p>SO: 2005 Cranet 5%; 2003 EU-Report: 84% of companies listed at Helsinki Stock Exchange.</p>
Sweden	<p>[A] TU neutral/ opposed, advocated Wage Earners' Funds; EA favour PS for wage flexibility, but no active support;</p> <p>[B] From 1992–97 tax incentives for PS in firms; since then no support.</p>	<p>ESO: NCL - ES in JSC, financing by company possible; in capital increase suspension of preemptive right of shareholders possible;</p> <p>PS: Cash-based none; NCL - share-based 'Profit-Sharing Foundations': one third of employees on similar terms, after dissolution assets to be distributed; NTL - for the employer 24.26% payroll tax instead of 32.28% SSC;</p> <p>SO: None.</p>	<p>2005 Cranet: ESO 16%, PS 26%;</p> <p>2005 EWCS: ESO 1.6%, PS 15%;</p> <p>PS: 2003 Heissmann: 15%; Wage Earners' Funds created in 1983, abolished in 1991.</p>
UK	<p>[A] Climate friendly and supportive toward FP; TU involved, but reservations: prefer SO to PS; EA positive, favour flexibility with regard to form of schemes; employees interested;</p> <p>[B] Long tradition of FP, especially ESO and ESOP; now more active support for SO that is SAYE and Sharesave; 2000 new of Enterprise Management Incentives EMI; very little participation in decision-making.</p>	<p>ESO: NTL - Share Incentive Plan (SIP) discounted: no PIT/SSC; no dividend tax if dividends reinvested in shares, generally no SSC; no CGT if sale immediately after taking shares out of the plan;</p> <p>SO: NTL - Savings-Related SO-Plan, Firm SO Plan: generally no PIT at grant or exercise, no SSC; SAYE: tax bonus on savings; EMI: no PIT, no SSC at grant or exercise; (NCL - Employee Benefit Trust);</p> <p>ESOP: NCL - up to GBP 125 per month shares for pre-tax salary in Trust, EmpC up to 2 matching shares / share worth up to GBP 3,000 per annum; NTL - shares exempt from income tax and SSC after 5 years; EmpC contribution to trust tax deductible;</p> <p>PS: NTL - approved PS; tax benefits abolished in 2002.</p>	<p>2005 Cranet: ESO 19%, PS 13%;</p> <p>2005 EWCS: ESO 1.9%, PS 6.4%;</p> <p>2006 ifsProShare: ESO/ SO approved plans in 5,000 firms, some with ESOPs; SIP in 830 firms; SPS: 2002 1 million employees under approved schemes, average per head less than GBP 700;</p> <p>SO: 2005 Cranet: 2%; 2006 ifsProShare: Savings-Related Plans in 1,300 firms, 2.6 million employees; Company Plans in 3,000 firms; EMI in 3,000 firms.</p>

Table 3. The new EU Member States and candidate countries

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Bulgaria	[A] TU open to FP, EA indifferent; not a current topic on either of their agendas; [B] ESO strong support 1997-2000, then ignored; in 2002 PrivL incentives abolished; FP generally ignored.	ESO: None; NTL - Uniform 7% dividend tax; PS: None; NTL - SPS personal income tax exempt.	2005 Cranet: ESO 38%, PS 5%; 2005 EWCS: ESO 1.8%, PS 6.3%; ESO: 10% Mass Privatisation, 4-5% Cash Privatisation; low, decreasing; MEBO: 1,436, 28% privatisations; managers took over most; PS: AI, few cases survey evidence; SO: 2005 Cranet 14%.
Cyprus	[A] FP not an issue on TU / EA agendas; [B] FP so far ignored.	ESO: NCL - discounted ES in JSC; financing ES by company possible; NTL - dividends/gains from share sale tax-free; PS: None.	2005 Cranet: ESO 10%, PS 7.7%; 2005 EWCS: ESO 1.2%, PS 2.7%; SO: 2005 Cranet: 4%; ESO/PS: AI, insignificant.
Czech Republic	[A] TU / EA indifferent to FP, not a current topic on their agendas; [B] ESOP discussed in 1990; FP ignored after introduction of voucher concept.	ESO: NCL - discounted ES/SPS in JSC; not considered public offering; ES discount limit: 5% of equity capital, financing by company possible; NTL - uniform 15% dividend tax; PS: NCL - CPS/SPS in JSC; NLL: negotiable in collective bargaining agreements.	2005 Cranet: ESO 14%, PS 27%; 2005 EWCS: ESO 1.6%, PS 11%; SO: 2005 Cranet: 3%; ESO: Insignificant; 0.31% of the privatised assets; PS: AI, insignificant.
Estonia	[A] TU indifferent to FP, EA opposed to any extension of employee participation; [B] PrivL supported ESO until 1992; after 1993 FP ignored.	ESO: NCL - rights attached to shares issued before 1995 remain valid; no public prospectus for ES needed; NTL Emp.: no income tax on dividends from resident firms; EmpC: 22% on distributed profit, only 'bonus issue' in capital increase exempt; PS: None.	2005 Cranet: ESO 9.6%, PS 11%; 2005 EWCS: ESO 2%, PS 11%; ESO: 2005 2% (1995 after privatisation 20%) of firms majority employee-owned, 20% minority; PS: AI, survey evidence, very few cases.
Hungary	[A] FP for managers means to avoid external control, for employees to preserve workplace; TU lobbied ES/ESO in privatisation, recently passive; EA indifferent; [B] ESOP/ES strong support in PrivL until 1996; climate friendly toward FP but lack of concrete economic policy decisions.	ESO: PrivL - preferential sale; discount up to 10% firms assets and 150% of annual minimum pay, instalments; Decree 'Egyszerűsített' Credit; NCL - specific 'ES' in JSC, discounted/free, up to 15% of equity capital, financing by company possible; since 2003 tax-qualified stock plans, first HUF 0.5 million free, then 20% tax, 3-year holding period;	2005 Cranet: ESO 15%, PS 15%; 2005 EWCS: ESO 1%, PS 3%; ESO: 1998 1% of assets privatised; preferential privatisation in 540 firms; CS strong decline; now AI, 30% of firms (70% SO, 30% ES), mostly foreign; ESOP: initially 287 employing 80,000, in 2005 151 left; 1.2% of employment by private firms; PS: AI, 20% of firms, mostly foreign, only 10% of entitled receive profit;

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
		<p>SO: NTL – PIT base is value at exercise; ESOP: ESOP Law 1992; preferential credit; corporate tax exempt until end 1996; contribution to Plan up to 20% tax deductible; tax base lowered; PS: None.</p>	<p>SO: 2005 Cranet 27%.</p>
Latvia	<p>[A] TU / EA indifferent to FP, not a current topic on their agendas; [B] Little support for ESO in PrivL; FP so far ignored.</p>	<p>ESO: PrivL - up to 20% ES; specific 'ES' in state / public firms; NCL - preferential ES in JSC free/discounted, in capital increases up to 10% of equity capital non-voting stock; PS: None.</p>	<p>2005 EWCS: ESO 0.6%, PS 8.5%; ESO: PrivL 110.6 million vouchers to 2.5 million people; AI, 1999 16% of 915 firms dominant ESO but falling over time; PS: AI, 7% of firms; mostly IT, consulting, real estate.</p>
Lithuania	<p>[A] Climate FP friendly; TU interested, lack of actions; EA support individual firms; [B] ESOP/ES strong support in PrivL until 1996; now FP not on political agenda of Parliament and Government.</p>	<p>ESO: PrivL - 5% ES deferred paym. up to 5 years; NCL - in corporations ES for 3 years non transferable/non voting, financing by company possible; NTL - uniform 15% dividend tax; after holding period profits from sale of shares not taxed; PS: None.</p>	<p>2008 PEPPER IV: ESO 4%, PS 36%; 2005 EWCS: ESO 0.9%, PS 4%; ESO: low and decreasing; AI, 2000 36% (1995 92%) privatised firms dominant ESO, falling over time; PS: AI; CPS mostly foreign (IT, consulting, advertising, etc); DPS few cases 2005 linked to employee savings plan.</p>
Malta	<p>[A] TU support schemes in practice; FP not a current topic in national tripartite dialogue; [B] FP collateral effect of nationalisation (80's) and privatisation (90's) not a current issue.</p>	<p>ESO: NCL – ES in corporations, exempt from prospectus/investment rules; up to 10% discount, financing by company possible; NTL - SO only taxable at exercise; ESOP: Trust Act refers to FP; taxed 15% interest / 10% investment; PS: mentioned in NLL.</p>	<p>2005 EWCS: ESO 0.7%, PS 3.9%; ESO: AI; banking sector: ES, SAYE scheme, SO; ESOP: AI, Trust Funds in Bank of Valetta / Malta Telecom; PS: AI; 2004 public sector (Shipyard 1,761 employees); private (foreign) firms, mostly reserved for management.</p>
Romania	<p>[A] TU support indiv. cases; EA avoid topic; Tripartite council tackled FP sporadically; [B] ESO supported until 1997 especially MEBO; then support declined; current government gives little support and has other priorities.</p>	<p>ESO: PrivL - aim 30% of privatised assets Vouchers/ES; Vouchers free; 10% discount ES; NCL - ES in JSC, financing by company possible; NTL - 10% dividend tax; ESOP: PrivL on Employee Associations; leveraged transaction, preferential credit, up to interest rate 10%; PS: Ordinance – CPS compulsory in state/municipal firms.</p>	<p>2008 PEPPER IV: ESO 6%, PS 42%; 2005 EWCS: ESO 1.6%, PS 5%; ESO: ES 10% of shares issued at privatisation, decreasing; ESOP: 1998 one third priv., most frequently used single method 2000: 2,632 firms, average 65% ESO, 1,652 majority ESO; PS: estimated 1.2 million employees in public sector covered.</p>

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
Poland	<p>[A] TU/EA indifferent to FP; managers/ employees pragmatically motivated; lobby groups/institutions (in particular banks) supportive to ESO;</p> <p>[B] FP Supported in early privatisation period; ESO in most privatisations, since mid-1990s more and more ignored; PS increased emphasis in the context of collective bargaining agreements.</p>	<p>ESO: PrivL - 15% ES for free, 2 years non transferable, up to value 18 months minimum pay, <i>National Investment Funds</i> 1995 (NIF), shares for symbolic fee; NCL - ES/SPS in JSC, financing by company possible; NTL - uniform 15% dividend tax;</p> <p>EBO: PrivL - Leverage Lease Buyout (LLBO), anticipated ownership transfer possible; interest 50% of refinance rate; interest part of lease payments are costs; Insolvency Law - buyout right;</p> <p>PS: NCL - CPS/SPS in JSC.</p>	<p>2008 PEPPER IV: ESO 40%, PS 26%;</p> <p>2005 EWCS: ESO 0.7%, PS 5%;</p> <p>ESO: low and declining; AI in privatised firms, 2000 approximately 11.4% (1998 12.7%); NIF adult citizens 1 share in 15 funds;</p> <p>EBO: LLBO 2002 one third of privatisations, most frequently used single method, 1,335 firms employing 162,000, 14% over 250 employees;</p> <p>PS: AI, limited to management.</p>
Slovakia	<p>[A] TU/EA indifferent to FP, not a current topic on their agendas;</p> <p>[B] ESOP discussed in 1990; EBO concept failed 1995; FP now generally ignored.</p>	<p>ESO: NCL - discounted ES and SPS in JSC; up to 70% discount and financing by company possible;</p> <p>PS: NCL - CPS/SPS in JSC.</p>	<p>2005 Cranet: ESO 12.7%, PS 17%;</p> <p>2005 EWCS: ESO 2.3%, PS 28%;</p> <p>SO: 2005 Cranet 10%;</p> <p>ESO: Insignificant; AI, banking sector / new privatisations;</p> <p>EBO: AI, in privatisation, usually management-led.</p>
Slovenia	<p>[A] TU/EA very supportive to FP; Employee Ownership Association lobbies legislation; active support by Works Councils/Managers Association;</p> <p>[B] Strong political support to FP; draft laws 1997/2005 in parliament rejected; new Law on FP in 2008.</p>	<p>All Schemes: since 2008 70% tax relief for PS and ESO with 1-year holding period (100% relief with more than 3-year); up to 20% profits or 10% total salaries per annum and up to Euro 5,000 per employee;</p> <p>ESO: PrivL - up to 20% ES for vouchers; vouchers free, shares for overdue claims;</p> <p>NCL – ES /SPS in corporations; discount / financing by company possible;</p> <p>EBO: up to 40%, shares 4 years non-transferable; Worker association proxy organisation under Takeover Law;</p> <p>PS: PrivL - SPS in internal buyout.</p>	<p>2005 Cranet: ESO 14%, PS 20%;</p> <p>2005 EWCS: ESO 2.6%, PS 18%;</p> <p>ESO/EBO: 90% of privatised firms; CS 1998 60% majority. ESO while only 23% of capital (2004 18% strong decline);</p> <p>PS: CS, in statutes of 32% of firms, but unexploited in 22%; for board members 20% of listed firms;</p> <p>SO: 2005 Cranet 4%.</p>
Croatia	<p>[A] TU recently promote ESO in revision of privatisation; EA indifferent to FP; long tradition of self-</p>	<p>ESO: NCL - ES in JSC financing by company possible; NTL - Dividends tax-exempt; profits from sale of</p>	<p>2008 PEPPER IV: ESO 34%, PS 29%;</p> <p>ESO: 2005 more than 10% of value of privatised firms (1996 20%); 2004</p>

Country	General attitude [A] Social Partners [B] Government	Legislation and Fiscal or other Incentives	Schemes and their Incidence CRANET: Offer in Firms >200 Empl. EWCS: Take-up Rate of Employees
	management; [B] ESO supported until 1995, since then FP ignored; ESOPs planned in new PrivL.	shares not taxed; ESOP: general rules of NCL apply; PS: None.	12% firms with majority ESO; ESOP: Survey evidence, ESOP elements in 9.4% of firms (52 out of 552), completed ESOP approximately in one quarter of them; PS: AI.
Turkey	[A] Climate FP friendly; TU supportive, EA undecided, split; employees interested; [B] FP issue 1968 in Tax Reform Commission; some attention in individual privatisations; 2002 program, lack of concrete measures.	ESO: PrivL decrees for individual firms; discount / instalments; NTL - after 1 year share-sale profits not taxed; for SO limited tax on dividends/profits from sale; IntE: NCL / CivC 'welfare/mutual assistance funds' of firms; financing by company profits/contributions; PS: NCL / CivC both CPS and SPS; up to 10% prior reserve.	2005 EWCS: ESO 1.3%, PS 2.4%; 2005 Cranet: ESO 4.4%, PS 8.9%, SO , 1%; ESO: AI, PrivL 12 cases 9-37% ESO, 1 case majority, up to 15% discount; SO/ESO private firms mostly foreign (26 registered 35 applications) 2007 survey evidence: 3-4% of publicly traded companies; IntE: n.a.; PS: AI, retained profits from dividends widespread; CS 38 out of 50 listed firms; 2007 survey evidence: 20% of publicly traded companies.

Source: PEPPER I-IV and: CNMV 2003; CRANET 2005/1999 (firms with more than 200 employees); EU Stock Options Report 2003; EWCS 2005 (take-up rate); FONDACT 2004; Heissmann 2003; IAB 2005; IBEC 2002; ifsProShare 2006; WKÖ/BAK 2005; WSI 2003; please note that the country data of the different surveys is incoherent due to inconsistencies in methodology and definitions. *Excluded from studies:* Management Buyout, General Savings Plans, Consumer and Housing Cooperatives;

Abbreviations: AI = Anecdotal Information only; CGT = Capital Gains Tax; CivC = Civil Code; CPS = Cash-based Profit-sharing; CS = Case Studies; DPS = Deferred Profit-sharing; EA = Employer Associations; EBO = Employee Buyout; EmpC = Employer Company; ES = Employee Shares; ESO = Employee Share Ownership; ESOP = Employee Share Ownership Plan; FP = Financial Participation; IEnt = Intermediary Entities; JSC = Joint-stock Companies; MEBO = Management-Employee Buyout; NCL = National Company Law; NLL = National Labour Legislation; NTL = National Tax Legislation; PIT = Personal Income Tax; PrivL = Privatisation Legislation; PS = Profit-Sharing; SAYE = Save-As-You-Earn Schemes; SO = Stock Options; SPS = Share-Based Profit-Sharing; SSC = Social Security Contributions; TU = Trade Unions.

II. Availability of Financial Participation Schemes in EU Companies

Iraj Hasbi and Richard Woodward

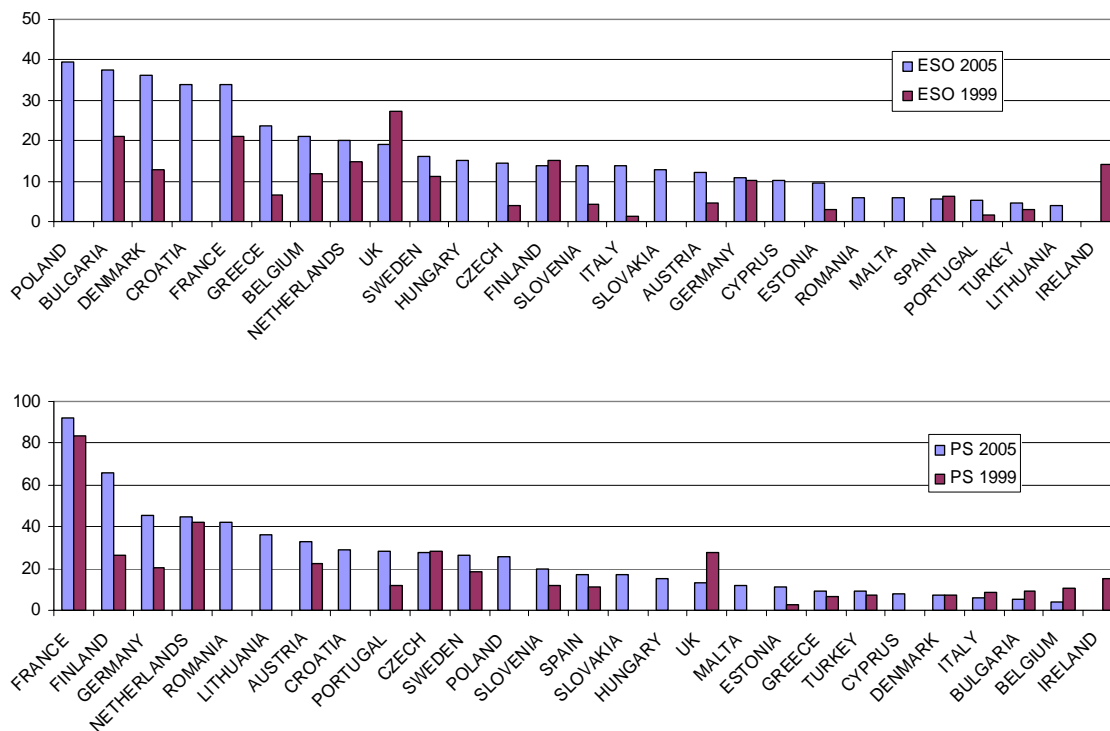
1. Percentage of Firms Offering Broad-Based Financial Participation to Employees

We begin with a look at broad-based employee share ownership (ESO) plans on the basis of data from the CRANET survey of companies (supplemented with data we collected in an independent survey). Figure 1 shows the percentages of companies with broad-based ESO and profit-sharing plans in 1999 and 2005 in 26 European countries (including six in which our surveys were conducted). As we see in Figure 1, between 1999 and 2005, ESO grew in almost every country except the UK and marginally in Spain and Finland (the weighted average for all countries included in both samples grew from 13 to 18 per cent).³³ If we look at the five leading countries in 2005 (with shares ranging from 33 to 40 per cent), we see that three of them (Poland, Bulgaria, and Croatia) are transition countries (indeed, the absence of Slovenia in this group is surprising, as the country's privatisation program generated a large amount of employee ownership); Denmark and France are the other two. The three lowest-ranked countries are Portugal, Turkey, and Lithuania. Estonia is also one of the lowest-ranked countries, indicating the low incidence of ESO in the Baltic States generally. Spain and Portugal's low rankings also indicate the low level of coverage in the Iberian Peninsula. It is interesting that Denmark is far ahead of other two Nordic countries (Sweden and Finland), which might indicate a divergence of that country from at least some aspects of the 'Scandinavian model.' We note that Finland was ahead of Denmark on this measure in 1999, and that Denmark's leadership is thus a recent development owing to what seems to be extremely strong growth of ESO there in recent years. Finally, it is also interesting to note that Hungary, the Czech Republic and Slovenia have such similar levels of coverage (all are middle-ranked) in spite of the very different privatisation methods used in these countries. This is possibly an indicator of convergence of ownership structures in transition countries.

³³ The reader should remember that, as noted in Part 1 Chapter I Section 3, in contrast to the EWCS data presented in the next chapter, Luxembourg was not included in the CRANET surveys, and the following countries were not included in 1999 but were included in 2005 either by the CRANET research team or in our independent survey: Croatia, Cyprus, Hungary, Lithuania, Malta, Poland, Romania, and Slovakia. Ireland is only reported for 1999. Latvia was also included in our survey, but the results are not reported here.

Figure 1 also shows how broad-based profit-sharing (PS) has developed between 1999 and 2005. Again we generally see growth, except in the UK, the Czech Republic, and the lowest-ranked countries (Belgium, Bulgaria, and Italy); the weighted average for all countries included in both samples grew from 29 to 35 per cent. We also note a much wider range of results than in the case of ESO (for ESO, the proportion of firms offering a scheme ranges from 4 to 40 per cent; for PS from under 4 to over 92 per cent). It is not surprising that France is the leading country, far ahead of all others, as deferred PS is mandatory there. The second-ranked country is Finland. Germany, the Netherlands and Romania are fairly similar, with coverage between 40 and 50 per cent. The lowest-ranked countries (with coverage under 10 per cent), in ascending order, are Belgium, Bulgaria, Italy, Denmark, Cyprus, and Turkey.

Figure 1. Proportion of sample firms offering broad-based employee share ownership and profit-sharing schemes in European countries, 1999 and 2005 (in per cent)



Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

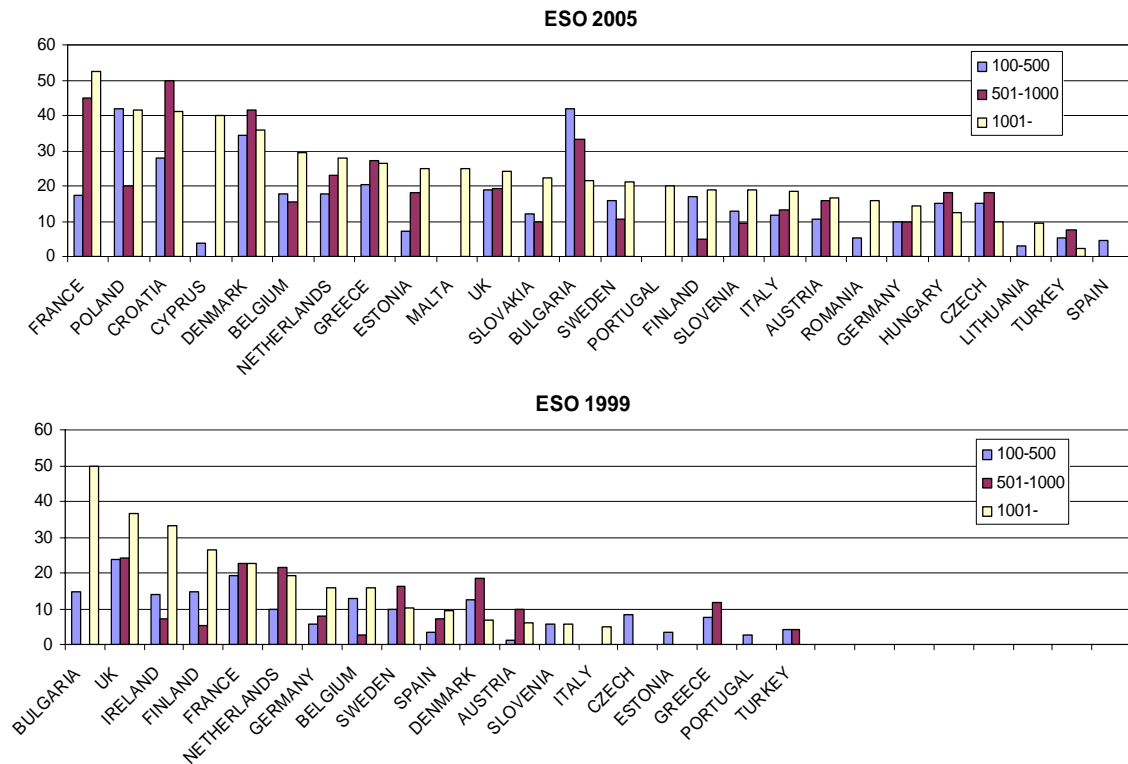
It is interesting to note that two of the countries among the highest-ranked for ESO – Bulgaria and Denmark – are among the lowest-ranked for PS. This indicates that firms and countries choose ESO or PS for different reasons and do not see them as alternative forms of involving employees in the company’s business; thus, there is no correlation between the two schemes.

2. Financial Participation Schemes by Size and Sector

We are also interested in how employee financial participation might differ across firms with respect to company size and sector of business activity.

The breakdown according to size is shown in Figures 2 and 3. The size categories can be described as medium (100-500 employees), large (501-1,000 employees) and very large (1,001 or more employees). For each country, we have calculated the proportion of firms in each size group offering an financial participation scheme. In general, it seems that both forms of employee participation are more prevalent in large and very large companies.

Figure 2. Percentage of firms in each size group offering employee share ownership schemes, 1999 and 2005

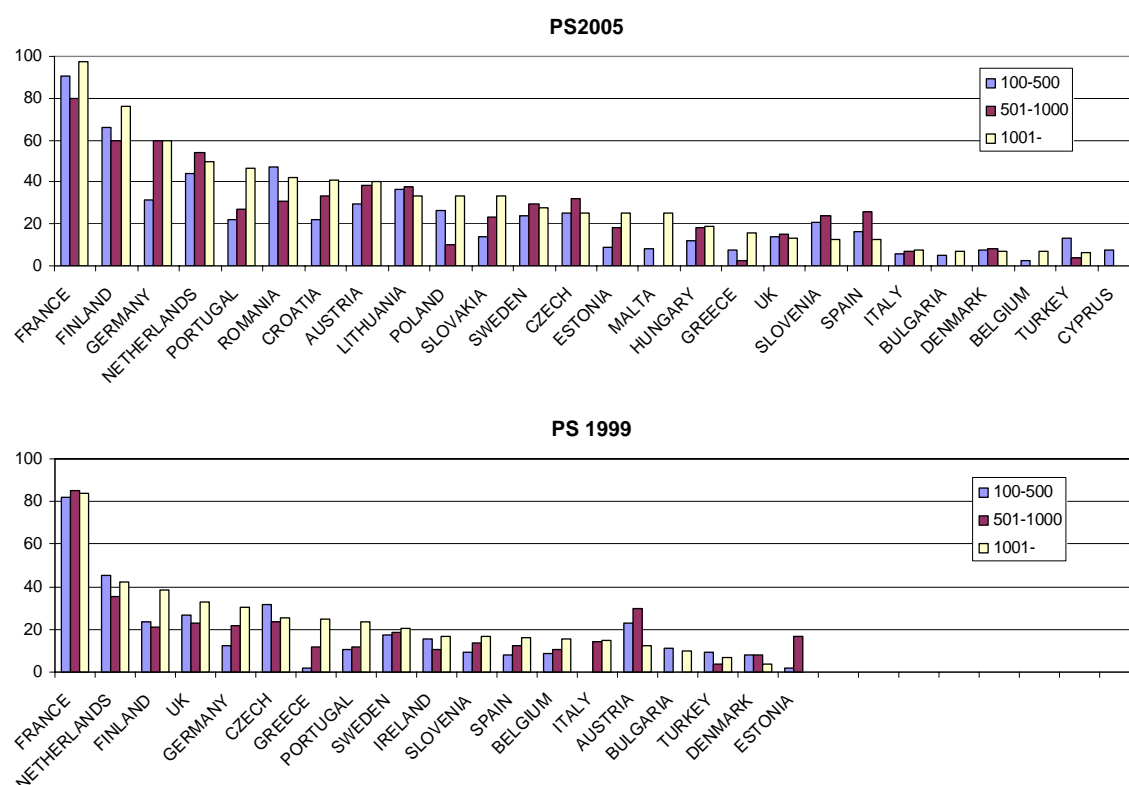


Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

Figure 2 shows the data for ESO. While the highest incidence is generally in the largest firms, we see notable exceptions in Croatia, Denmark, Greece, Hungary, the Czech Republic, and Turkey, where the highest percentages of firms with ESO is found among large (but not the largest) firms, and in Bulgaria, where the medium-sized firms have the highest incidence of ESO. The situation was fairly similar in 1999.

Figure 3 shows the data for PS. There is a much more even distribution across size classes here than in the case of ESO, although here again we see a prevalence (albeit a mild one) of the largest size firms. This situation appears to have changed little between 1999 and 2005.

Figure 3. Percentage of firms in each size group offering profit-sharing schemes, 1999 and 2005



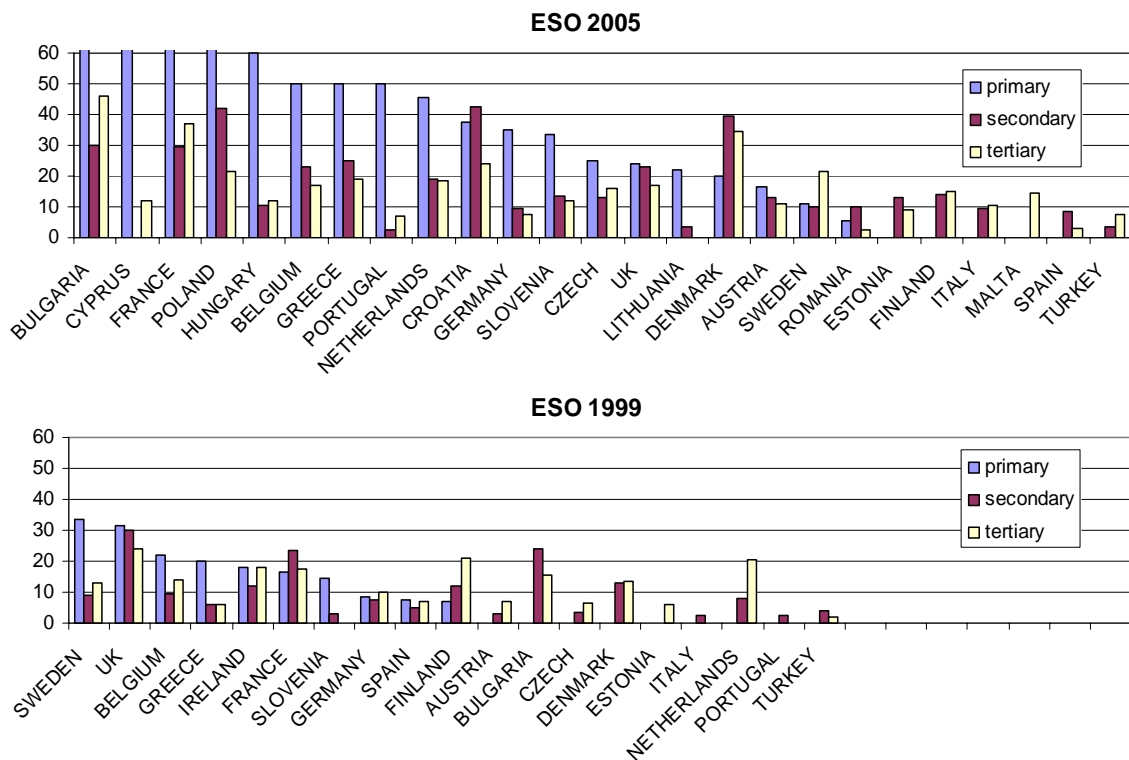
Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

We present a sectoral breakdown of financial participation schemes in Figures 4 and 5, classifying firms into one of three main sectors: primary (agriculture and extractive industries), secondary (manufacturing), and tertiary (services). For 2005, we see a high average rate of incidence of both ESO and PS in the primary sector. However, this is mostly likely a statistical artifact due to the very small percentage of firms in the sample from that sector³⁴, and we see no such pattern for the 1999 data. The really interesting differences would be between the manufacturing (secondary) and service (tertiary) sectors in which the vast bulk of the workforce in a modern economy is found.

³⁴ If, for example, only two firms in a given country sample are agricultural and one is a dairy cooperative, we would have a 50 per cent rate for the primary sector.

With respect to ESO, based on the information contained in Figure 4, there is little differentiation between these two sectors (manufacturing and services) on the whole. In Poland and Croatia (countries for which we lack 1999 data), we see significantly more ESO in the secondary sector, while there is significantly more ESO in the tertiary sector in Bulgaria and Sweden³⁵. In others, the tertiary and secondary sectors are close, with one of the two slightly higher than other, or virtually identical. In 1999, we see strong prevalence of ESO schemes in the secondary sector in France and Bulgaria, and strong prevalence in the tertiary sector in the Netherlands, Finland, Austria and Ireland. It is, however, difficult to say whether the changes between 1999 and 2005 reflect only changes in the sample or broader trends (especially given the generally much lower rates of incidence in 1999). It is perhaps worth noting the significant drops in the share of firms offering ESO schemes in all sectors in the UK (which can also be seen in Figure 1).

Figure 4. Percentage of firms in each sector offering employee share ownership schemes, 1999 and 2005

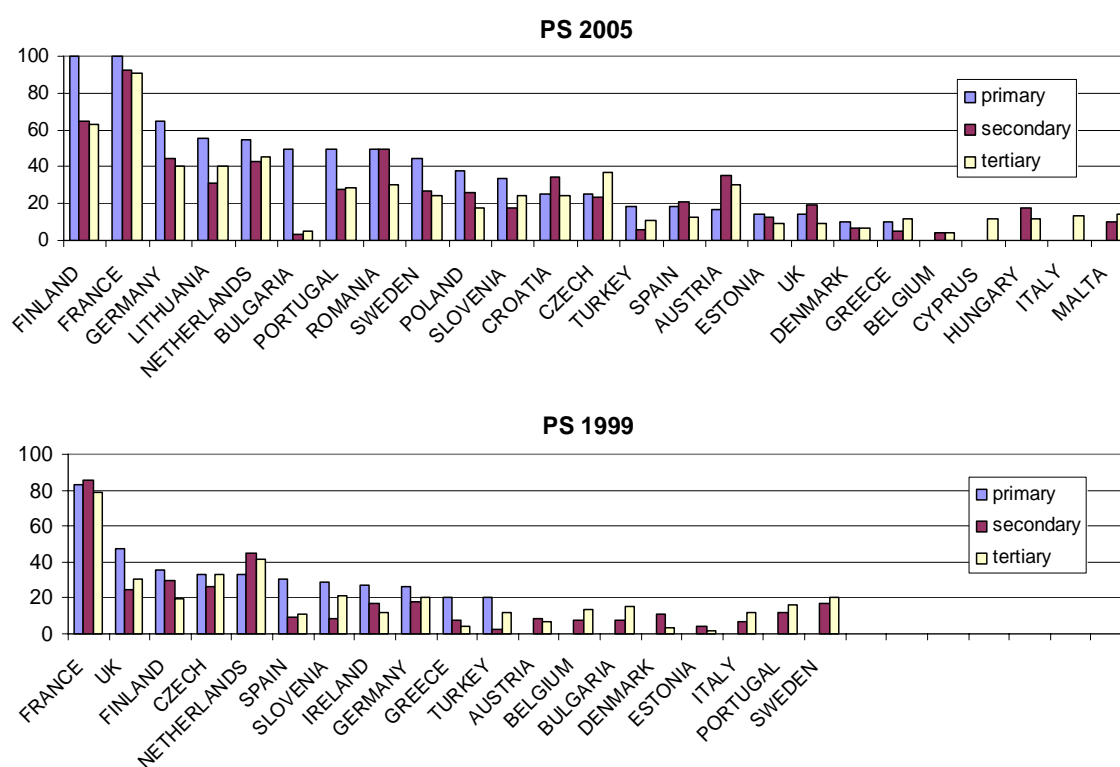


Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

³⁵ This appears to be the case for Cyprus as well, but only because there are no secondary sector companies in the Cypriot sample.

Figure 5 contains information on PS. Again, we generally observe the prevalence of PS schemes in primary sector firms. The number of countries with higher incidence in the secondary than the tertiary sector is roughly equal to that in which the situation is reversed. This was also largely the case in 1999, when overall incidence was lower across the board.

Figure 5. Percentage of firms in each sector offering profit-sharing schemes, 1999 and 2005



Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

3. Percentage of Employees Covered³⁶

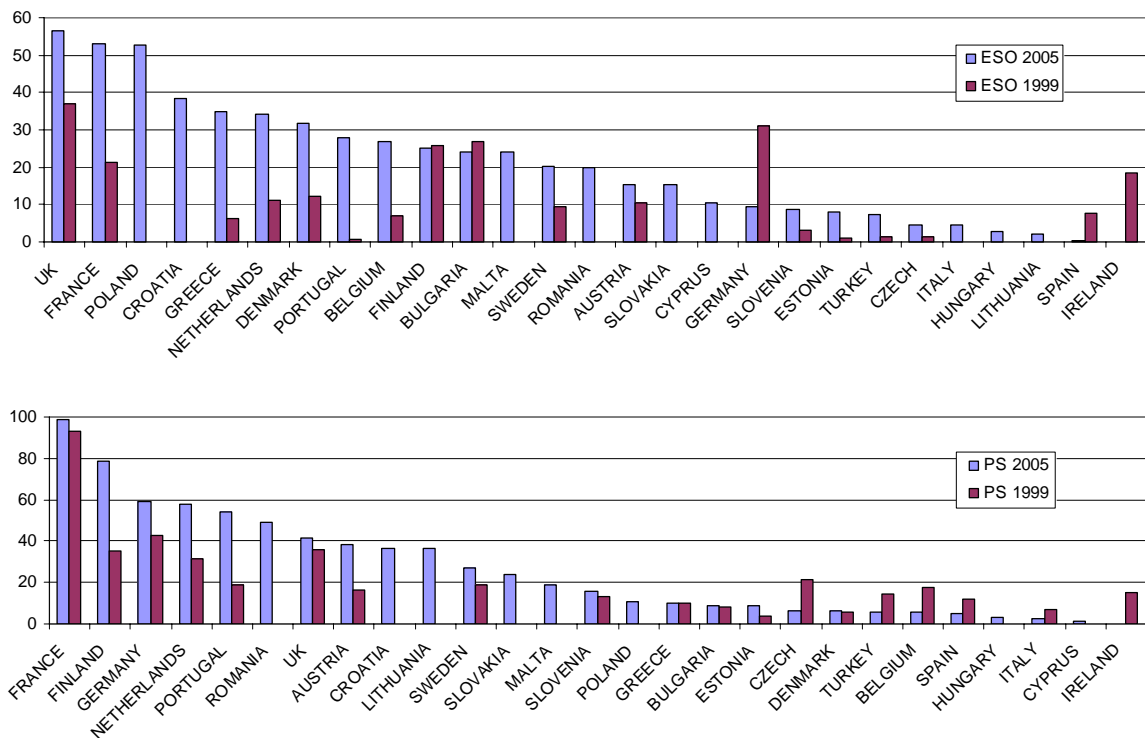
Next, we consider the share of employees in the sample covered by ESO and PS plans. This is an indicator of the extent to which broad-based financial participation plans have been adopted in each country. We present the data on this indicator in Figure 6.

³⁶ The CRANET questionnaire contains questions on the proportion of different categories of employees (managers, professionals, administrative and manual) to whom FP plans are offered and on the share of these different categories in the total workforce of the company. This allows us to calculate the number of employees in each company to whom FP plans are offered (and their share in the total number of employees in the sample for each country).

Looking at employee share ownership, we see that, as with the rise in the number of companies offering ESO plans, the coverage of employees by these plans is also growing in a large majority of countries (the weighted country average of all countries included in both samples grew from 19 to 25 per cent between 1999 and 2005). The three leaders (with employee coverage averaging over 50 per cent) are the UK, France and Poland. There is a fairly long tail of low-ranked countries (with coverage averaging under 10 per cent). In ascending order starting from lowest, these are: Spain, Lithuania, Hungary, Italy, the Czech Republic, Turkey, Estonia, Slovenia, and Germany. Again, Slovenia's position here is surprising, given its privatisation history. It is also interesting to note that Portuguese companies seldom offer a plan, but those that do are large, with many employees (see Figure 2, above).

Turning to PS, we see growth, albeit slower and from a higher starting point (the weighted average for all countries included in both samples rose from 36 to 42 per cent between 1999 and 2005). Here again we have a much wider range, from 100 per cent in France down to under 1 per cent in Cyprus, and again we have a long tail of low-ranked countries. After France, other leading countries (with over 50 per cent) are (in descending order): Finland, Germany, the Netherlands, and Portugal (Romania is just under 50 per cent).

Figure 6. Proportion of employees covered by employee share ownership and profit-sharing schemes, 1999 and 2005 (in per cent)

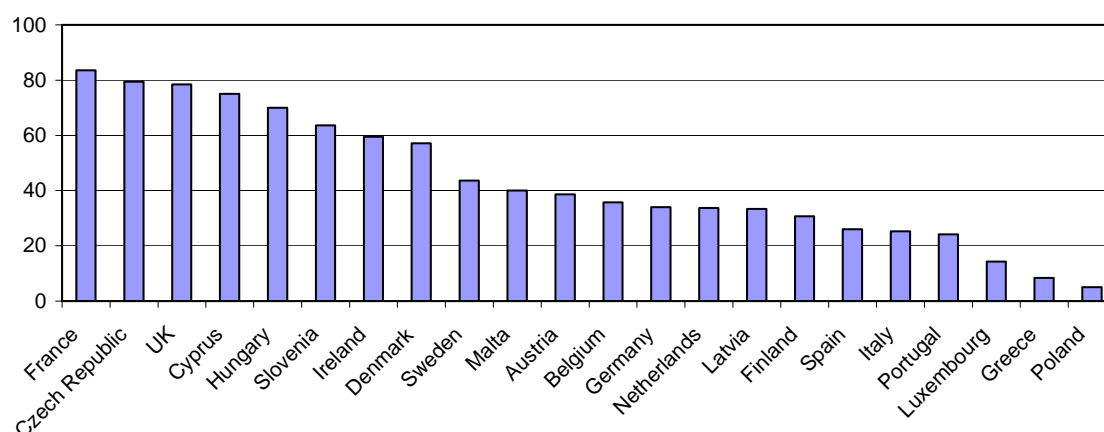


Source: CRANET data and own survey (Croatia, Lithuania, Malta, Poland, Portugal, Romania – for 2007).

4. Percentage of Large (Listed) Firms with Employee Share Plans

The EFES data cover Switzerland and Norway in addition to the 27 EU member countries; however, we ignore the Swiss and Norwegian figures in our discussion). The data on ESO in those companies presented in Figure 7 were gathered in 2007. On the basis of the data contained therein, we arrive at a quite up-to-date picture of the actual incidence of broad-based ESO schemes in the largest European companies, which we can contrast with the picture emerging from the CRANET survey. (Note that five countries – Bulgaria, Estonia, Lithuania, Romania and Slovakia – have values of 0 per cent and are therefore not included in the figure.)

Figure 7. Proportion of large EU companies with ESO schemes, 2007 (in per cent)



Source: EFES.

While it is not surprising to find France, the United Kingdom and Ireland with high rates of incidence of broad-based ESO plans among large companies, the presence of the Czech Republic (represented by 34 companies in the sample), Cyprus (only four companies) and Hungary (20 companies) among the group of leaders is quite surprising. Denmark ranks high, which is consistent with the CRANET data, and so does Slovenia, which is what we expected, but did not find in the CRANET data. Poland and Bulgaria, which were leaders in the CRANET data, are in the rear here. (If the CRANET and our survey data for these countries is reasonably representative, this would tend to indicate that ESO plans are concentrated in smaller and mid-sized companies in those countries, which would be quite unusual, although perhaps consistent with the Polish privatisation program's emphasis on restricting management-employee buyouts to SMEs.) However, the relatively low positions of Romania and the Iberian and Baltic countries in the CRANET data are replicated here and thus seem to provide quite strong corroboration for the CRANET picture of those countries. The high ranking of Hungary and the Czech Republic here and their mid-level ranking in the CRANET data seem to indicate that something

is going on with respect to the dissemination of employee ownership in those two countries which has thus far eluded the attention of researchers, probably due to the low level of employee participation in the privatisation programs of those countries. It would seem that, contrary to the experience of a number of other transition countries, post-privatisation ownership structure evolution has brought more, rather than less, employee ownership to those countries (possibly because of the policies of foreign investors).

III. Take-Up Rate of Financial Participation Schemes in the Workforce

Iraj Hashi and Richard Woodward

1. Percentage of Employees Participating in Financial Participation Schemes

The data from the EWCS survey presented in Figure 8 gives us a picture of the actual extent of employee financial participation in the population of employed persons, as this is a survey of individuals rather than firms. As in the case of CRANET, it covers both ESO and PS schemes as well as the level of participation at two points in time (2000/2001 and 2005), allowing us to draw some conclusions about the rate of diffusion of these schemes in recent years.³⁷

For ESO schemes, as in the case of the CRANET, we see growth in almost all countries (the weighted average for all countries included in both samples rose from 1.5 to 2.4 per cent). The exceptions were the UK, Germany, and Spain (the UK and Spain saw declines in both the CRANET and EWCS surveys). The top countries (with participation rates over 5 per cent) were Ireland, France, Belgium, and Luxembourg (France is the only one of these in both the CRANET and EWCS top country lists, although Ireland also does well in the EFES survey). The lowest-ranked countries (with participation rates under 1 per cent), in ascending order, were: Spain, Germany, the Czech Republic, Lithuania, Hungary, Malta, and Latvia (Spain and Lithuania ranked similarly low in both surveys; when we note that Portugal also has just over 1 per cent, we see these findings to be consistent with the earlier finding of a low incidence of ESO in the Baltic and Iberian countries³⁸). We see strongly contrasting figures for Poland, which ranks highest in our survey data and relatively low in the EWCS survey (and also very low in the EFES survey).

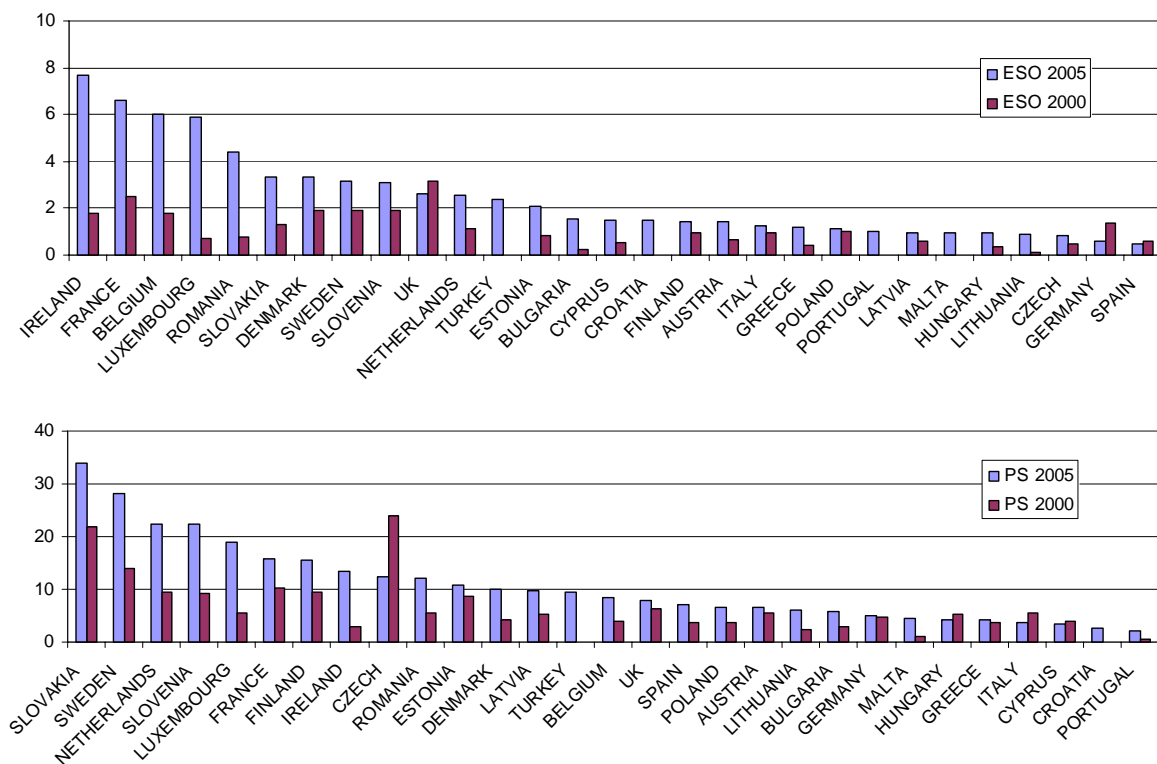
Turning to PS schemes, again as in CRANET, we see a much higher incidence than in the case of ESO (for ESO, the 2005 weighted average for all countries was 2.4 per cent, for PS 9.1, and the range for ESO was 0.5-7.7, whereas for PS it was 2.1-33.9). As in

³⁷ The earlier survey was done in two stages: EU-15 in 2000 and accession and other countries in 2001.

³⁸ Although Estonia does better here than in the CRANET results.

CRANET, we see growth in almost all countries (the weighted average for all countries included in both samples rose from 6.4 to 9.1 per cent). The exceptions were the Czech Republic, Italy, Hungary, and Cyprus (the Czech Republic and Italy saw declines in both CRANET and EWCS). The top countries (with participation rates of over 10 per cent), in descending order, were: Slovakia, Sweden, the Netherlands, Slovenia, Luxembourg, France, Finland, Ireland, the Czech Republic, Romania, Estonia and Denmark (with France, the Netherlands, Finland, and Romania ranking high in both the CRANET and EWCS surveys). The lowest-ranked countries (with participation rates under 5 per cent), in ascending order, were: Portugal, Croatia, Cyprus, Italy, Greece, Hungary, Malta, and Germany (Turkey, Cyprus, Greece and Italy ranked low in both CRANET and EWCS). The high ranking of Slovakia is very surprising, and we suspect that this may be due to the misunderstandings about the nature of profit-sharing schemes and the mistaken treatment of some bonuses as profit-sharing.

Figure 8. Proportion of employees involved in employee share ownership and profit-sharing schemes, 2000-2005 (in per cent)



Source: EWCS.

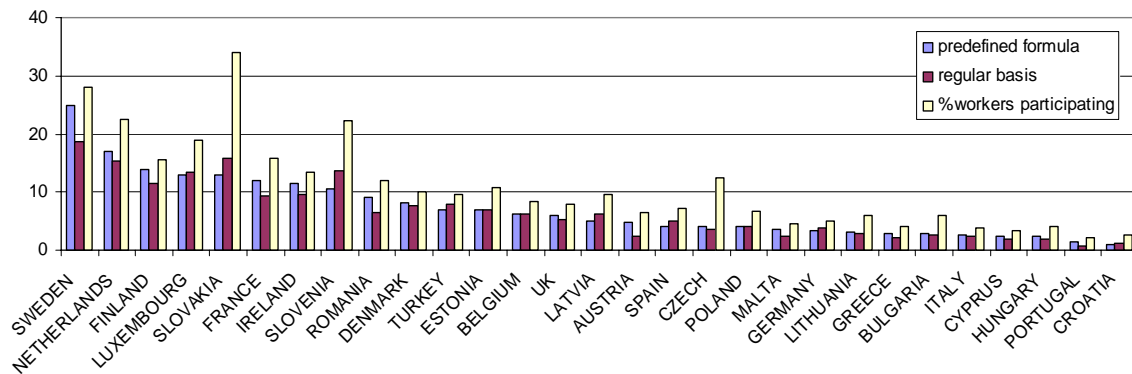
We also see high rates of ESO and PS for two countries for which recent CRANET data were not available: Luxembourg and Ireland. It must be remembered that the EWCS data does not distinguish broad and narrow schemes and, therefore, the high take-up rate of any scheme may only reflect the presence of share-based option schemes for management (which is likely to be the case in Luxembourg).

2. Percentage of Employees Participating in Profit-Sharing Schemes with Pre-Defined Formulas on a Regular, Ongoing Basis

To refine our picture of profit-sharing, we wish to distinguish profit-sharing schemes run according to pre-defined formulas and providing payments to employees on a regular, ongoing basis from those that are dependent on the discretion of employees' superiors and thus do not provide any ex-ante incentives to employees to improve their performance at work. To do this, we present EWCS data for the year 2005 in Figure 9 showing the depth of profit-sharing schemes (that is, the percentage of the workforce participating), of those which are run according to pre-defined formulas, and of those under which payments occur on a regular, ongoing basis. In all cases we see that profit-sharing schemes operating with high-powered incentives cover a smaller proportion of employees than those covered by schemes referred to (possibly incorrectly, that is Slovakia and Czech Republic) as profit-sharing. Using a strict definition of profit-sharing, we see that in the best cases approximately 20 per cent of the workforce is covered. Regardless of which of the three categories is used to rank the countries, there is little difference in the rankings.

The leading countries, independent of the category used to rank them, clearly include Sweden, the Netherlands, Finland, Luxembourg Slovakia, France, Ireland and Slovenia,. At the rear are, equally as clearly: Croatia, Portugal, Hungary, Cyprus, Italy, Bulgaria, Greece, and Lithuania. Given the similarity of results for more precisely defined types of profit-sharing and the general results presented in section 1 above, the comparison with the results from the CRANET survey and our survey here is basically the same as it was there.

Figure 9. Profit-sharing in 2005: A closer look



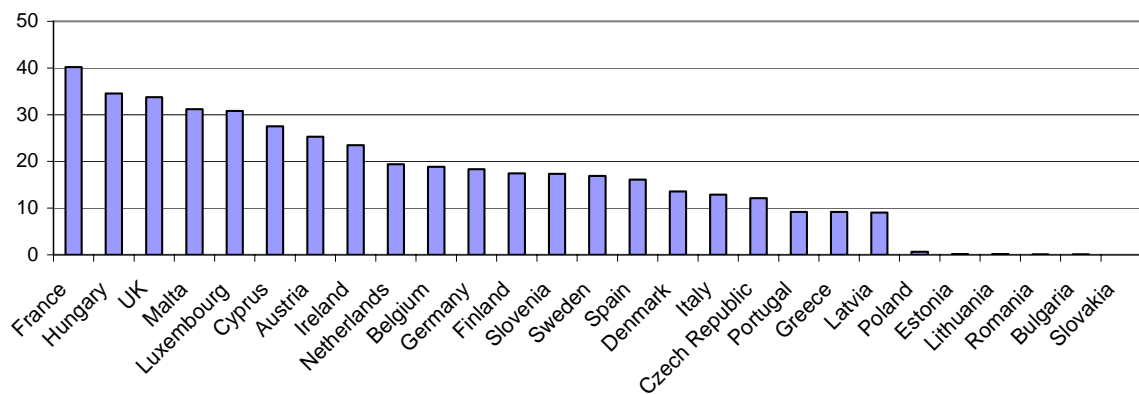
Source: EWCS.

3. Percentage of Employees Holding Shares in Largest (Listed) Firms

Returning to the EFES survey of large European companies, we now consider the question of take-up of ESO schemes by employees – that is, how many employees have actually become owners as a result of the schemes. Figure 10 provides us with information on employee owners as a percentage of the total number of employees in the companies surveyed by EFES. For the entire sample, 26.17 per cent of the total workforce is actually participating in ESO plans (15.05 per cent for the 12 new EU Member States). We can, to some extent, compare this with the CRANET-based information on ESO coverage in Figure 2, although take-up is not the same thing as coverage.

Again, as in Figure 4, France is in the lead, and Hungary and the UK also rank very high (the leading positions of France and the UK are consistent with the CRANET information presented in Figure 6, though Hungary's high position here is in stark contrast to its low position there). Given the small number of Maltese and Luxembourg companies in the sample (5 and 7 respectively), the leading positions those two countries have here can perhaps not be considered as representative (although the high ranking of Luxembourg is consistent with the EWCS survey results). Czech companies do not do as well with respect to take-up as they do in offering schemes, and rank among the last countries here. In Denmark we see a similar discrepancy, though not as large as that in the Czech Republic (in Denmark's case this may be due to the rapid diffusion of ESO plans in very recent times, as noted in Part 1, Chapter II, Section 1 – take-up may not have caught up with the rate of introduction of schemes). Not surprisingly, we again see Romania and the Baltic and Iberian countries in the rear (although Romania was mid-ranked in Figure 6).

Figure 10. Proportion of employees participating in ESO schemes in large EU companies, 2007



Source: EFES.

4. Conclusions

Regardless of the data source used, the evidence presented here shows conclusively that Europe has seen extensive growth of employee financial participation in recent years. This is true for both profit-sharing and employee share ownership, although profit-sharing is more widespread than employee ownership (although Figure 9 suggests that the difference between the two may diminish or even disappear if we adopt a very strict definition of profit-sharing). The percentage of companies with FP schemes of various forms in operation is growing steadily almost everywhere in the European Union, and the percentage of company employees covered by, and taking up, these schemes is also increasing.

On the other hand, on the basis of both company surveys (CRANET and EFES) and surveys of individuals in the workforce (EWCS), it seems that financial participation has extended to a significant proportion of the working population in only a handful of countries. It is therefore clear that, while much has been accomplished, much remains to be done.

Two other broad conclusions are that (leaving aside the recent members and candidate countries), first, the largest companies are more likely to offer their employees any FP scheme, and second, FP schemes are offered to, and have been taken up, on a larger scale by employees in the more developed EU countries – the UK, France, Scandinavian countries – and less so by the less developed members (Greece and Portugal). This implies that employers' recognition of the benefits of employee financial participation grows as economic development progresses and a country's GDP per capita rises.

Related to the above, the depth of FP schemes in most of the new members and candidate countries with a socialist past (the transition countries) is generally low. The ESO schemes, rooted in privatisation programmes, have survived in some countries like Poland but gradually weakened in other countries in the process of secondary privatisation.

Nevertheless, the data examined here seem to indicate that a West-East divide (that is, significant differences between the old EU-15 Member States on the one hand, and at least some of the ten post-Socialist states that have joined the EU since 2004) is less significant than one might have anticipated, or perhaps nonexistent. There seems to be much more variation within those two groups than between them. In fact, according to CRANET data, between 1999 and 2005 the percentage of companies offering broad-based share ownership schemes increased in the old EU-15 from an average of 13 to 17 per cent and in the new EU-12 from an average of 10 to 23 per cent; we observe a slightly different picture for the percentage of companies offering profit-sharing schemes, which increased in the old EU-15 from 29 to 36 per cent and in the new EU-12 from an average of 19 to 26 per cent (all weighted country averages).

There are some discrepancies between data sources with regard to certain countries; however, the overall picture is quite clear. While for most individual countries it would be rather risky to make definitive assertions about the degree of advancement of dissemination of FP schemes on the basis of the data we have examined, we can identify what seem to be some regional trends. For example, we can state with a great deal of confidence that a few regions seem to be much less advanced in the dissemination of FP than others, notably the Iberian Peninsula, the Baltic States, and the Southeastern corner of Europe (including Greece, Turkey and Cyprus).

IV. Taxation and Fiscal Support for Financial Participation

Jens Lowitzsch and Natalia Spitsa

1. The Problem

At the national level, taxation can either inhibit or support the spread of employee financial participation. At the EU level, cross-border migration of employees partaking in financial participation plans, as well as the transfer of such plans by multinational companies to subsidiaries in different Member States, may involve problems caused by conflicting tax regimes.³⁹ Generally, attention is centered on tax incentives, often considered the State's main instrument for promoting employee financial participation. Tax incentives, however, are relative; they need to be analysed in the context of the general taxation system in the given country. National tax systems are not easily compared; it is even more difficult to compare taxation laws governing national financial participation schemes.⁴⁰ Moreover, compulsory social security contributions must be taken into account since they add substantially to the overall burden of state levies, especially on labour; also, in many countries, they influence the tax base of the main income taxes. A systematic overview of the situation in the EU-27 shows, on the one hand, the impact and, on the other hand, the limits of tax incentives in encouraging employee financial participation.⁴¹

The objectives here are:

- To outline general systems of direct taxes as they affect employee financial participation in the EU. National tax systems will be classified as unfavourable, neutral or favourable for employee financial participation schemes.

³⁹ On obstacles to exportation, see European Commission (2003a), pp. 43.

⁴⁰ For the comparison of general tax systems, different types of taxes, different systems of individual taxes, different tax rates, tax bases and taxation moments all must be considered. Tax rates are only comparable if effective tax rates are calculated. However, that is only possible for a specific tax and for a specific personal status and situation. Since most major direct taxes should be examined to determine their effect on employee financial participation plans, effective tax rates cannot be calculated for every possible status or situation.

⁴¹ Due to the complexity of the issue, a discussion on comparability of individual country tax rates of EU Member States cannot be covered in this publication.

- To review specific tax incentives for employee financial participation in order to determine whether specific tax incentives are a prerequisite for employee financial participation and whether some tax incentives are more effective than others irrespective of the country where they are offered.

Tax incentives can be considered efficient if the number of specific financial participation plans supported by these tax incentives increases immediately after the tax incentives have been introduced.

2. General Taxation of PEPPER Schemes in the EU

The following direct taxes are relevant to employee financial participation:

- corporate income tax (CIT),
- personal income tax (PIT),
- taxes on dividends at shareholder level (special rates of personal income tax, ‘investment tax’, ‘dividend tax’, ‘share income tax’, etc.)
- taxes on sale of shares at shareholder level (special rate of personal income tax, capital gains tax, ‘investment tax’, etc.).

According to Articles 3 to 6 TFEU, an EU priority is to prevent the diversity of national tax systems from negatively affecting the development of the Common Market by harmonising national legal codes. As a special case of Articles 3 to 6 TFEU, Art. 113 TFEU (previously Art. 93 ECT) stipulates that indirect taxes (VAT and excises) must be made consistent. Prompted by this provision, numerous directives have been issued and indirect taxation has already been harmonised to a great extent. However, there is no special provision on harmonisation of direct taxes.⁴² Moreover, potential harmonisation in this area is restricted by Art. 5 (2) TFEU (previously Art. 5 (2) ECT). On the one hand, the European Commission supports competition of direct taxes⁴³, regarding tax autonomy as the core component of state sovereignty, closely related to country-specific economic, social and cultural structures. On the other hand, it recognises the importance of preventing unfair tax competition, especially in the area of corporate taxation.⁴⁴ Since there is neither a legal basis nor political support for harmonisation of corporate tax rates, the European

⁴² Only more general provisions of Art. 115, 116 and 117 TFEU on prevention of market distortions and, in cases of substantial discrimination, Art. 107 TFEU on prevention of state subsidies, Art. 45, 49, 56, 63 TFEU (basic freedoms) and Art. 18 TFEU (general anti-discrimination provision) apply. However, these aim at non-discriminatory taxation of physical persons and legal entities from other EU Member States as compared with domestic physical persons and legal entities and at prevention of double taxation. They do not lead to a higher degree of harmonisation.

⁴³ See COM (1980), 139; Weber-Grellet (2005), pp. 28, 152.

⁴⁴ Whereas the issue of unfair tax competition was originally connected with such traditional tax havens as the Channel Islands and Monaco, it has gained even more importance with the accession of new Member States having generally much lower corporate and partially also personal income taxes than Western European EU Member States, except Ireland (see Weber-Grellet, 2005, p. 163).

Commission currently favours the development of the Common Consolidated Corporate Tax Base (CCCTB).⁴⁵ However, even if the CCCTB should be introduced in all Member States, it will not apply to enterprises having no cross-border activities.⁴⁶

Nevertheless, international tax competition is exerting considerable pressure, especially on corporate income tax rates, since the US tax reform of 1986. This is responsible for two persistent tendencies observable worldwide. Firstly, the tax burden has been shifted from direct to indirect taxes (see OECD, 2005a, p. 6) (with some exceptions, for example, France), and from capital to labour (see Weber-Grellet, 2005, p. 30).⁴⁷ Thus taxation of share-based plans may become more favourable over time than that of cash-based plans, since the tax burden on dividends and capital gains is lower than on employment income. Secondly, tax rates are lowered while the tax base is broadened (see OECD, 2005a, p. 6). Although this might lead to the abolishment of specific tax incentives, it does not necessarily mean less favourable taxation: if the rates become sufficiently lower, this may compensate for the loss of tax incentives. The general characteristics of national systems of direct taxes are illustrated in Figure 11 below.

A common feature of all direct tax systems of EU member and candidate states is that only income and not expenditure is taxable.⁴⁸ Accordingly, as affecting the relationship between the respective tax burden on capital and labour, income tax systems can be divided into flat tax, dual tax and differentiated tax systems; all these systems have advantages and drawbacks from an economic standpoint and are currently present in different EU Member States. In a genuine flat tax system, represented, for example, by Romania and Slovakia, the tax burden falls equally on all sources of income, flat and relatively low, since the basic tax rate to which other tax rates are adapted is the tax on capital income. This system is generally equally favourable to all forms of employee financial participation. The same is true of tax systems, which impose different tax rates on labour and capital income, but levy a flat personal income tax (for example, Estonia, Latvia, Lithuania).⁴⁹ Dual tax systems represented, for example, by Sweden and Finland, are characterised by a highly progressive personal income tax as opposed to a flat tax on capital income. This combination is, theoretically, negative for cash-based profit-sharing and positive for share-

⁴⁵ See COM (2001) 582 of 23 October 2001; COM (2003) 726 of 24 November 2003; CCCTB/WP/046 of 12 December 2006; COM (2007) 223 of 2 May 2007; the proposal, due in 2008, has not yet been completed, but it seems probable that the CCCTB could be introduced in several years. Seven Member States with relatively low tax rates are opposed to the idea, but no unanimous decision is required in this case. The EU Tax Commissioner declared that the initiative can, if necessary, be implemented by eight Member States through enhanced co-operation.

⁴⁶ Moreover, the usefulness of this instrument for harmonisation of corporate taxation is considered to be questionable if no limits for corporate tax rates are set at the same time, see Bundesministerium der Finanzen [Federal Ministry of Finance] (2007), p. 73).

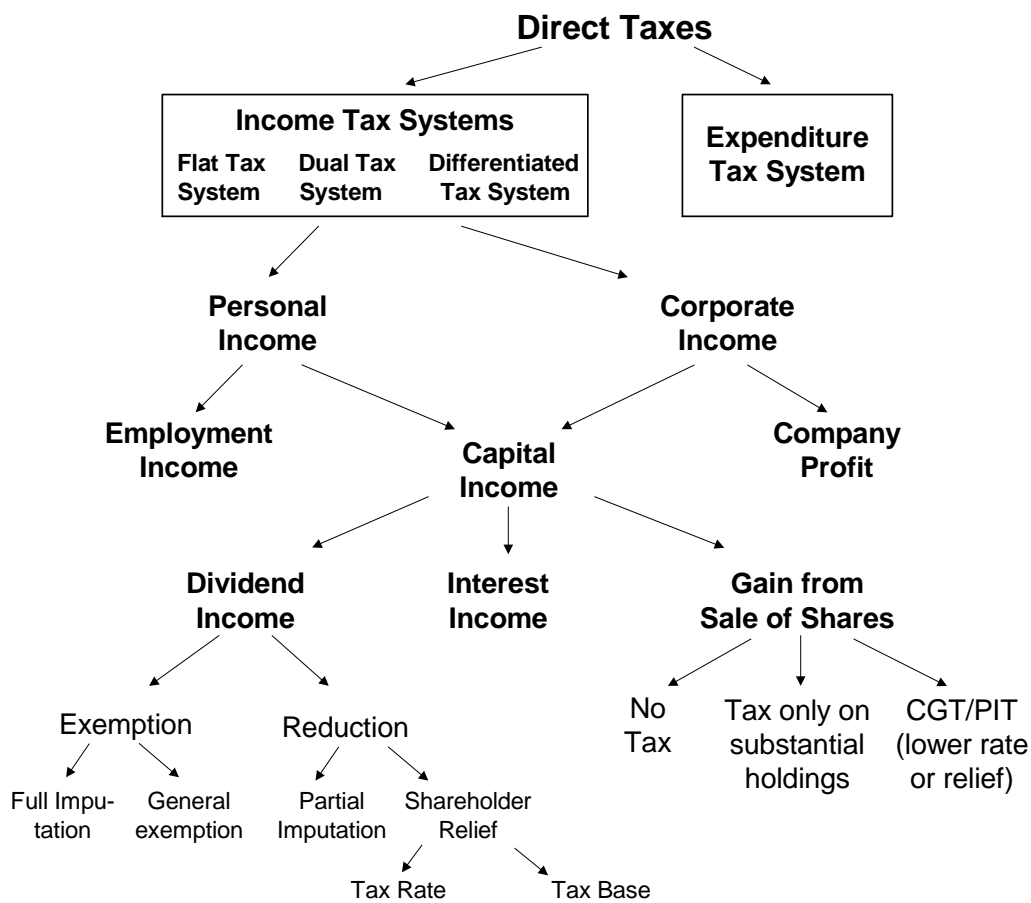
⁴⁷ There is no theoretical basis and/or empirical evidence for the assumption that the tax burden on capital should be lower than on labour, although the practice is based on it (see Ganghoff, 2004, p. 35).

⁴⁸ However, Croatia has had an expenditure tax system from 1994 until 2000. For example, Bulgaria, Estonia and Hungary have an expenditure tax on fringe benefits payable by the employing company. The quite unusual Estonian corporation tax system (replacement of corporate income tax by the tax on distributed profits) could also be connected with the idea of expenditure tax.

⁴⁹ These systems give more leeway to share ownership since tax rates on capital income are usually lower than those on labour. However, in practice the advantage of flat tax systems may not be so substantial since often relatively high compulsory social security contributions will be levied additionally.

based schemes. Most EU Member States have a differentiated tax system which generally favours employee share ownership if taxes on capital are flat and relatively low. As far as tax systems are concerned, no common tendencies can be observed. Taxation traditions and goals of EU Member States are different and none of the prevailing systems can be considered the best objectively.⁵⁰

Figure 11. General characteristics of national systems of direct taxes



As far as the system of corporate income tax (taxation of dividends at the corporate and shareholder level) is concerned, no EU Member State provides relief for corporations, but many mitigate double taxation by providing relief for shareholders.

⁵⁰ Most Western European countries cannot introduce a flat tax system because of the potential loss of revenue (see for Italy OECD, 2005b, p. 4).

Table 4. General taxation and compulsory social security contributions

Country	Type of dividend treatment	CIT ⁵¹	Taxation of dividends at shareholder level ⁵²	Taxation of share sale at shareholder level ⁵³	PIT ⁵⁴	Compulsory SSC ⁵⁵
Belgium	Shareholder Relief: reduced tax rate	3%	15%	Generally 0%	Progressive 25-50% central+0-9% sub-central; SSC deductible	Empl.: overall rate 13,07% EmpC: overall rate 35%
Bulgaria	Shareholder Relief: reduced tax rate	10%	7%	Shares of public firms listed at Bulgarian Stock Exchange 0%	Flat 10%, voluntary SSC deductible	Empl.: (cumulative) 12.10-25.74% EmpC: (cumulative) 29-29.7 %
Croatia	Dividend tax exemption for shareholders	20%	0%	0%	Progressive 12-40%+city surtaxes 0-18%; SSC deductible	Empl.: 20% to pension fund EmpC: 17.2% to health, unemployment, injury funds
Cyprus	Shareholder Relief: reduced tax rate	10%	15% special contribution to the defence fund	15% special contribution to the defence fund	Progressive 20-30%; SSC deductible	Empl.: overall rate 6.8% EmpC: overall rate 8.5%+2% to Social Cohesion Fund
Czech Republic	Classical system	19%	15% withholding tax at source	General PIT for sale of shares within 6 months	Flat 15%; SSC deductible	Empl.: (cumulative) 11% EmpC: (cumulative) 34%
Denmark	Classical system	25%	28% Share Income Tax up to DKK 48,300, 42% above; not for professional traders	27-42%	Progressive 3.67-15% central+8% labour market tax+average 24.9% sub-central; ceiling 51.5%	Empl.: 8% health tax EmpC: 0%

⁵¹ Data on corporate tax for 2010 stem from the 2010 edition of the EU Report “Taxation trends in the European Union” (European Commission, 2010b) or has been downloaded from the database at <<http://www.dits.deloitte.com/DomesticRates/domesticRatesMatrix.aspx>>, Log-in: 25 September 2010. The generic term ‘corporate tax’ includes in this context all central and sub-central statutory taxes and surcharges on corporation profits.

⁵² Data source for dividend taxation (2010), see footnote 51.

⁵³ Data source for capital gains taxation (2010), see footnote 51.

⁵⁴ Data on personal income tax rates for 2010 stem from the 2010 edition of the EU Report “Taxation trends in the EU” (European Commission, 2010) or has been downloaded from the database of the European Union <http://ec.europa.eu/taxation_customs/taxinv>, Log-in: 25 September 2010.

⁵⁵ Data source for social security contributions (2010), see footnote 54.

Country	Type of dividend treatment	CIT ⁵¹	Taxation of dividends at shareholder level ⁵²	Taxation of share sale at shareholder level ⁵³	PIT ⁵⁴	Compulsory SSC ⁵⁵
Germany	Shareholder Relief: reduced tax rate	34.5%	25%+ solidarity surcharge 5.5%; no SSC	25%+ solidarity surcharge 5.5%; no SSC	Progressive 14-45% +solidarity surcharge 5.5%; limited by an absolute amount; pension and health care contributions partly deductible	Empl.: (average) 19.93-21.5% EmpC: (average) 19.03-19.43% Both limited by an absolute amount
Estonia	Tax exemption for shareholders; exemption of retained profits from corporate tax	21% on distributed profits	0%	General PIT	Flat 21%; mandatory SSC deductible	Empl.: contribution to the unemployment fund 2.8% EmpC: 'social tax' 33% + contribution to the unemployment fund 1.4%
Greece	Shareholder Relief: reduced tax rate	24%	10%	Generally 0%; 20% on sale of shares of LLC or partnerships	Progressive 18-45%; SSC deductible	Empl.: 16% EmpC: 28.06% Both limited by an absolute amount
Spain	Classical system	30.75%	General PIT	General PIT	19% up to EUR 6,000, 21% above	Empl.: 6.35% EmpC: 29.9%
France	Partial Imputation	33.33%	CGT 18% + social levies (CRDS, CSG) 12.1%	CGT 16%; on stock options 30-40%	Progressive 5.5-40%	Empl.: average 20%; limited by an absolute amount EmpC: (aggregated) 29.72- 34.22 %
Hungary	Shareholder Relief: reduced tax rate	10% up to HUF 500 mln, 19% above	30%	20%	Progressive 17-32%; voluntary SSC deductible	Empl.: 17% limited by an absolute amount EmpC: 29%
Ireland	Classical system	12.5%	20%	25%	Progressive 20-41%; voluntary SSC deductible	Empl.: 5-8% EmpC: 10.75%
Italy	Shareholder Relief: reduced tax base and tax rate	31.4%	Qualified holdings – tax base reduced to 49.72%, tax rate general	12.5% for small shareholdings; general PIT on substantial;	Progressive 23-43% + surcharge 0.9-1.4%; SSC deductible	Empl.: (cumulative) 9.2-10.2% EmpC: (cumulative) 23.05%

Country	Type of dividend treatment	CIT ⁵¹	Taxation of dividends at shareholder level ⁵²	Taxation of share sale at shareholder level ⁵³	PIT ⁵⁴	Compulsory SSC ⁵⁵
			PIT; not qualified holdings – full tax base, tax rate 12.5%	tax base reduced to 49.72% of the added value		
Latvia	Shareholder Relief: reduced tax rate	15%	10%	15%	Flat 26%	Empl.: overall rate 9%; EmpC: overall rate 24.09%, both from after-tax income
Lithuania	Classical system	15%	20%+6% health care contribution	Generally 15%; 0% if held more than 1yr and no substantial shareholding for last 3 years	Flat 15%	Empl.: 9% EmpC: 30.98-31.7%
Luxembourg	Shareholder Relief: tax base reduced	28.59%	15%; tax base reduced to 50% of the dividend income;	General PIT for short-term holdings; high allowance and 1/2 PIT rate for long-term holdings	Progressive 8-38%	Empl.: 12.14-14.45% EmpC: 12.14-19.07%
Malta	Full Imputation	35%	General PIT and tax credit for CIT	stamp duty 2-5%; shares quoted on Malta stock exchange tax exempt	Progressive 15-35%	Empl.: overall rate EUR 13.24-65.82 weekly; EmpC: overall rate EUR 13.24-65.82 weekly
Netherlands	Shareholder Relief: reduced tax rate	25.5%	15% for small, 25% for substantial holdings	0% for small, 25% for substantial shareholdings	Progressive 33.45-52%	Empl.: 5.2-31.15% EmpC: 19.43%
Austria	Shareholder Relief: reduced tax rate	25%	25%; optional: general PIT at a half rate; generally no SSC	0% for small long-term holdings; for substantial shareholdings 25%	Progressive 36.5-50%; statutory and voluntary pension contributions partly deductible	Empl.: (cumulative) 17.8-18.2% EmpC (cumulative): 21.7-21.9% deductible Both limited by an absolute amount
Poland	Shareholder Relief: reduced tax rate	19%	19%	19%	Progressive 18-32% ; SSC deductible	Empl.: average 13.71% EmpC: average 14.66-23.38%
Portugal	Partial Imputation	26%	20%; imputation credit of 50%	Generally 10%; tax exemption if shares are	Progressive 10.5-42%	Empl.: overall rate 11% EmpC: overall rate 23.75%

Country	Type of dividend treatment	CIT ⁵¹	Taxation of dividends at shareholder level ⁵²	Taxation of share sale at shareholder level ⁵³	PIT ⁵⁴	Compulsory SSC ⁵⁵
				held more than 12 months		
Romania	Classical system	16%	'Investment Tax' 16%	'Investment Tax' 16%; 1% for long-term investment	Flat 16%; voluntary contributions to private pension funds deductible	Empl.: (cumulative) 10.5-17% EmpC: average 20.8-29%
Slovakia	Dividend tax exemption for shareholders	19%	0%	General PIT	Flat 19%; SSC deductible	Empl.: 13.4% EmpC: 35.2%
Slovenia	Shareholder Relief: reduced tax rate	20%	20%	0-20% according to the holding term	Progressive 16-41%; contributions to private pension funds deductible	Empl.: 22,1% EmpC: 16.1%
Finland	Full Imputation	26%	'Investment Tax' 28%; generally no SSC; tax base reduced to 70%	28%	Progressive 6.50-30% central+ 18.49% (average) sub-central; SSC deductible	Empl.: average 7.3%; EmpC: average 23% Both limited by an absolute amount
Sweden	Shareholder Relief: reduced tax rate	26.3%	'Individual Capital Income Tax' 30%	30%	Progressive 20-25% central + 31.6% sub-central	Empl.: 7% EmpC: 31.42%
Turkey	Partial Rmputation	20%	15%; imputation credit of 50%	0% if held more than 2 years, otherwise general PIT	Progressive 15-35%	Empl.: 16%; EmpC: 21.5%; both limited by an absolute amount
UK	Partial imputation	28%	10% up to the basic rate limit; 32.5% above; 42.5% above GBP 150,000; imputation credit	CGT 18%; taper relief	Progressive 20-40%	Empl.: overall rate 11% EmpC: overall rate 12.8%

Abbreviations: CIT = Corporation Tax; PIT = Personal Income Tax; CGT = Capital Gains Tax; SSC = Social Security Contributions; EmpC = Employing Company; Empl. = Employee; IC = Intermediary Company.

Within the EU, classical, imputation, shareholder-relief and exemption systems are all represented. From the point of view of employee financial participation, classical systems (double taxation of dividend income, for example, Ireland, Latvia, Romania) are generally unfavourable.⁵⁶ Partial imputation generally leads to a higher tax burden at shareholder level than full imputation and shareholder-relief (see Spengel, 2003), p. 23) and is, therefore, relatively unfavourable. Most countries presently offer shareholder-relief, but it is difficult to assess the effect on employee financial participation without comparing effective tax rates.⁵⁷ The best system for share-based plans is undoubtedly one that exempts dividend income from taxation by law (for example, Croatia, Cyprus, Estonia, Slovakia) or through full imputation (for example, Finland).

Taxation of capital gains from sale of shares is of great importance for employee share ownership. In this context, three concepts can be distinguished within the EU: exemption from taxation (for example, Belgium, partially Bulgaria); taxation only on substantial holdings (defined differently in different countries, for example, Austria, Italy, Luxembourg, Netherlands) and taxation by capital gains tax or by personal income tax at a lower (and usually flat) rate. Obviously, tax exemption is the most advantageous for employee financial participation. Taxation of substantial holdings is also favourable, since employee shareholdings are usually small. There is no common tendency for the taxation of capital gains.

Compulsory social security contributions⁵⁸ can either reduce the tax base of corporate and personal income tax or be calculated on after tax income (for example, Latvia). Otherwise, they impose an additional burden on gross income and are thus very unfavourable for cash-based profit-sharing, even when general taxes are low as in Slovakia. Further, social security contributions can be levied on capital income as in France (this would have had negative consequences for share-based schemes had France not introduced specific tax incentives). Generally, no common tendency in the development of social security is discernable, since in most countries contributions are connected to long-term insurance and thus are not as easily altered by the state as are taxes.

Tax and social security rates and deductions are interdependent within a national tax system, therefore each national system has to be analysed separately as a whole; details are presented in Table 4, above.

In the context of taxation, it is only relevant whether a financial participation scheme is cash-based or share-based and whether an ‘intermediary entity’⁵⁹ is used as a vehicle. The

⁵⁶ However, it depends on the personal income tax rate. For example, the income tax rates in Ireland, Latvia and Romania are relatively low.

⁵⁷ Due to globalisation of business and to the requirements of the EU law, there is a tendency to exchange imputation for shareholder relief systems. See Spengel (2003) p. 25.

⁵⁸ Whether social security is levied as a tax, for example, as in Denmark and Estonia, or takes the form of social insurance contributions merely means that in the case of taxes there is no corresponding claim against a social insurance institution.

⁵⁹ The generic term used for intermediary companies, funds with a separate legal personality and trusts (in common law countries UK, Ireland and Malta), which accumulate distributed profits, hold, allocate and transfer shares, options or certificates of the employer company for employees, sometimes pay out dividends or returns, administrate dividends, and make investments.

same taxation rules apply to employee share ownership schemes and share-based profit-sharing schemes, both direct and deferred.

a) Employee Share Ownership

Employee Shares

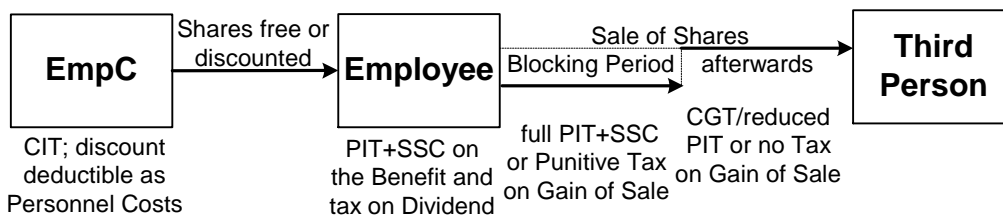


Figure 12: Taxation of employee shares

The benefit in value from transfer of discounted shares is generally deemed employment income and correspondingly subject to full personal income tax and compulsory social security contributions at the employee level. The employer company can generally deduct the discount as a personnel cost. However, valuation rules, especially for non-quoted shares, differ considerably between countries.⁶⁰ Taxation of dividends depends on the country-specific type of dividend treatment. Since there is no tax relief for the employing company in any EU Member State, full corporate tax generally is to be paid by the employer company on the entire profit, including the part to be distributed.⁶¹ The Different systems of dividend taxation at shareholder level are explained above. Taxation of gains from sale of shares depends on whether the shares are sold during or after the end of the blocking period. If the shares are sold during the blocking period, there are no major differences between EU countries: either full personal income tax and social security contributions or a special (high) punitive tax will be imposed. If the shares are sold after the end of the blocking period, taxation depends on the system of taxation of capital gains presented above. If there is no general exemption, or exemption for small shareholdings, other forms of tax relief usually apply.

Stock Options

Taxation of employee stock options is complex due to differences in the taxation moment and valuation methods, which depend on the taxation moment. In most EU Member

⁶⁰ The valuation of the same shares for the purpose of taxation of employees or employers may follow different rules and lead to different taxable amounts as in Austria. The moment of valuation of shares may also be different in different countries and lead to differences in value and in the tax base derived from it.

⁶¹ However, in one EU Member State, Estonia, corporate tax is replaced by the tax on distributed profits. This original system may have a positive economic effect on accumulation of funds, but it constitutes a strong disincentive for the employer company in relation to share-based employee participation plans as well as to cash-based profit-sharing.

States, taxes are imposed at exercise; taxation at grant or optionally at grant or exercise, as well as taxation at sale of shares, are also practiced.

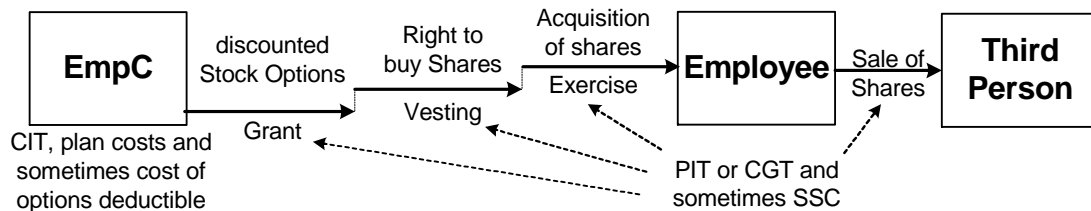


Figure 13: Taxation of stock options

Upfront taxation at grant is connected with considerable risks, so that special tax relief such as reduced tax rate or tax base and exemption from social security contributions are necessary as compensation. Although it could be argued that stock option benefits should be considered as capital gains, it is deemed to be employment income in most EU Member States; as such it is usually charged as personal income tax and partly also subject to social security contributions. The employer company can generally deduct setting up and operating costs of the plan as well as cost of options if the shares are repurchased (with the exception of, for example, Belgium). In some countries (for example, Denmark, Ireland, Luxembourg, Portugal), both the employer company and the employee are exempted from social security contributions (for details, see European Commission, 2003c; PriceWaterhouseCoopers, 2002).

b) Profit-Sharing

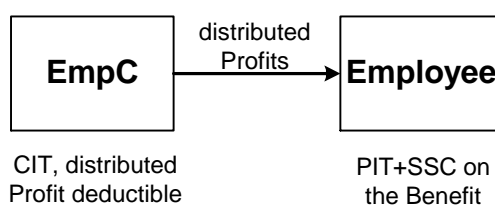


Figure 14: Taxation of profit-sharing

As far as cash-based profit-sharing is concerned, no major discrepancies exist between different EU Member States. Distributed profit is generally deductible for the employer company as a personnel cost (with the exception of Estonia, where it is instead subject to the tax on distributed profits), and it is subject to full personal income tax and social security contributions for the employees. The same taxation rules as for employee share ownership apply to share-based profit-sharing (see above).

c) Intermediary Entities

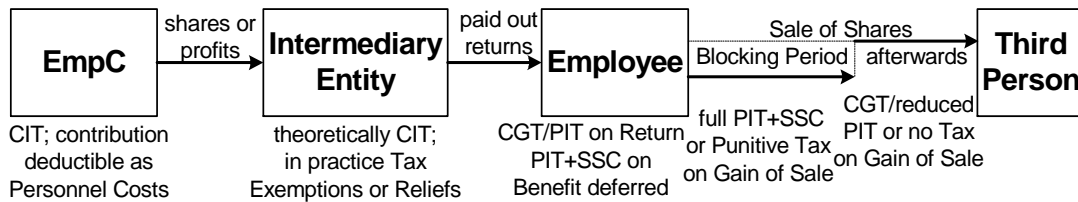


Figure 15: Taxation of share ownership plans and profit-sharing plans using intermediary entities

Share ownership plans and profit-sharing plans using a vehicle for the holding of shares and the investment of accumulated funds exist in many varieties in different EU Member States, especially because of substantial differences in company law. However, there is a similar basic logic: the employer company can usually deduct contributions to the intermediary entity, as well as set up and operating costs, from the tax base of the corporate income tax; the intermediary entity is usually established in a tax-friendly form. Taxation of employees would be the same as for simple share-based plans (see above) if it were not for specific tax incentives (for example, deferred taxation of the benefit), which in most cases are granted.

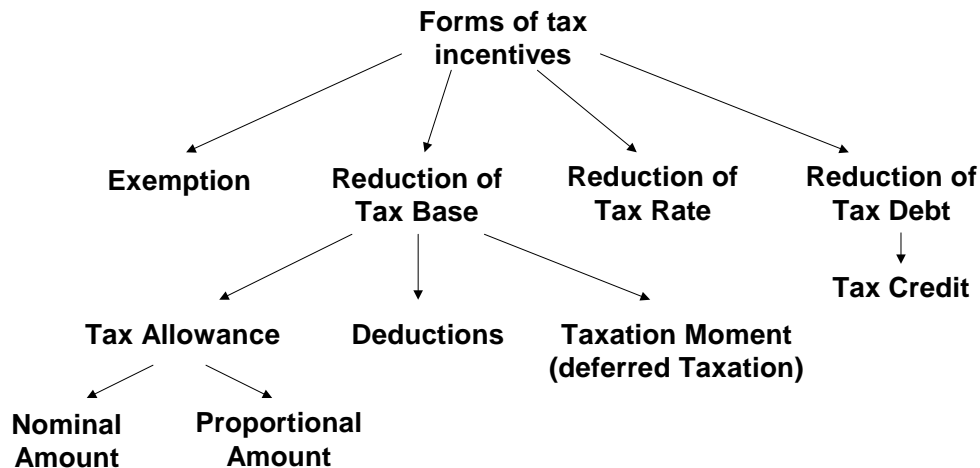
3. Specific Tax Incentives for PEPPER Schemes in the EU

Aside from specific tax incentives, most national taxation systems are more or less favourable to financial participation. The only tax system which actually hinders the development of financial participation is that of Estonia, due to taxation of distributed profits at company level instead of general corporate income tax.⁶² National taxation systems which exempt dividends and capital gains from taxation and social security contributions are especially advantageous to share-based schemes. Although details differ, generally in most countries the same taxes apply to similar plans so that the important difference is the general level of the tax burden of standard income taxes and compulsory social security contributions determined by tax rates and tax bases. As mentioned above, comparable effective rates cannot be calculated for all possible situations. Nevertheless, a substantial difference in tax rates implies a difference in tax burden. Thus it can be argued that low-tax countries generally have more favourable tax regimes for financial participation so that specific tax incentives are not necessary. The example of Ireland, however, shows that the government of a low-tax country can have a strong political interest in promoting employee financial participation; it can offer additional tax incentives even though the low

⁶² For this reason, it is contrary to the financial interests of the employing company to distribute profit to employees in cash-based profit-sharing schemes or as dividends to employees who have become shareholders. However, the Estonian tax system is to be changed in 2009 to comply with the EU Parent-subsidiary Directive (see KPMG, 2007, p. 15).

level of general taxation limits their impact.⁶³ Therefore the different instruments used to create specific tax incentives are important. Incentives may take the different forms diagrammed below.

Figure 16. Forms of tax incentives



Tax rate reductions and exemptions, although most effective because they are based on law rather than arbitrary judgments of tax authorities, and confer the same advantages to all categories of income, are seldom utilised (see Spengel, 2003, p. 28). One reason for this neglect is that such tax incentives result in heavier losses of revenue; also tax authorities have virtually no discretionary power over their use.⁶⁴ Deductions favour higher incomes under a progressive system of taxation, like the personal income tax in most EU Member States; tax credits (direct reduction of tax liability), on the other hand, are non-discriminatory and usually more valuable than an equivalent tax deduction or tax allowance.⁶⁵ Tax allowances benefit lower incomes whereas nominal tax allowances benefit the taxpayer less and therefore involve smaller revenue loss than would a proportional determination of the tax allowance. Deferred taxation favours share ownership schemes avoiding otherwise necessary additional liquidity at the moment of acquisition.

Specific tax incentives for employee financial participation are currently in effect in 16 (mainly Western) countries out of the 29 Member States and candidate countries; these differ substantially in type and size. Details are presented in Table 5, below.

⁶³ See Irish Department of Finance, TSG 98/12.

⁶⁴ To compensate for revenue losses caused by lowering the tax rate, either rates of other taxes are increased or the tax base is broadened. Thus, a lower tax rate does not necessarily lower the total tax burden. It is not surprising that countries with low statutory tax rates like Ireland have fewer tax concessions than countries with high statutory tax rates like France, Italy and Spain. See Spengel, (2003), p. 29.

⁶⁵ However, more value for taxpayers means higher revenue losses for the state. In addition, tax credits generally cause higher tax administration costs. Recently, tax credit systems have been replaced by tax allowances in France and Italy (see Tipke and Lang, eds, 2005, pp. 799, 802).

Table 5. Tax incentives for employee financial participation

Country	Employee	Employer Company
Belgium	ESO ES: Since 2001: 15% tax on benefit, no SSC if 2-5 years blocking period; tax base: quoted shares market value-costs, non-quoted shares purchase price-net asset value of shares; Sale of shares: tax-free up to 25% of equity; sale during blocking period 23.29% punitive tax; SO: Since 1999: taxation moment – at grant; taxation base: lump sum value = 15% of stock value at grant + 1% for each year before exercise, value reduced by half (7.5% + 0.5%) if options cannot be exercised within 3 years from grant, exercise period within 10 years from grant, no guarantee against fall in value, strike price determined at option offer; no SSC; IntE: Do not exist.	ES: Discount deductible from tax base of CIT; SO: Difference between market price of stock and exercise price of options deductible from tax base of CIT only if not EmpC, but a foreign company provides shares for employees at exercise and cross-charges the cost to EmpC; IntE: Do not exist.
	PS General: Since 2001: 15% tax for participation in the framework of an investment savings plan; 25% tax in other cases; but full SSC; IntE: Do not exist.	General: No SSC; IntE: Do not exist.
Denmark	ESO ES: Since 1987 (broad-based plan): no PIT, no SSC on discount, if value does not exceed 10% of annual salary, 5-year blocking period and shares deposited on trust with a bank; SO: (1) Broad-based plan (since 1987): no PIT, no SSC if value of options does not exceed 10% of annual salary and 5-year blocking period; (2) Individual plan under § 7H (since 2003): no PIT, no SSC if value of options does not exceed 10% of annual salary or exercise price less than 15% lower than market price of underlying shares; (3) Individual plan under § 28: no incentives; IntE: Do not exist.	ES: Discount deductible from tax base of CIT; SO: (1) Option costs deductible from tax base of CIT; (2) No; (3) Option costs deductible from tax base of CIT; IntE: Do not exist.
	PS General: (1) Broad-based plan (since 1987): up to DKK 8,000 tax-free if blocking period 7 years and shares deposited on trust with a bank (2) Individual plan under § 7H (since 2003): no PIT, no SSC on benefit if value does not exceed 10% of annual salary; IntE: Do not exist.	General: (1) Costs of shares deductible from tax base of CIT; (2) No; IntE: Do not exist.
Germany	ESO ES: No PIT, no SSC on benefit, if not exceeding 50% of the share value and Euro 360 annually; savings bonus of 20% on investment up to Euro 400 annually if annual income up to Euro 20,000 and 6-year blocking period; SO: No; IntE: Do not exist	ES: No; SO: No; IntE: Do not exist
	PS General: No; IntE: Do not exist	General: No; IntE: Do not exist.
Greece	ESO ES: Since 1987: (only for JSC) no PIT, no SSC on benefit – if shares issued in a capital increase 3-year blocking period; Dividends: tax on movable assets (10%);	ES: Discount deductible from tax base of CIT, no SSC; SO: (1) No; (2) Costs of distributed shares deductible from tax

Country	Employee	Employer Company
	<p>SO: (1) Since 1999 ‘Qualified plans’: no PIT, no SSC at grant or exercise; (2) Since 1988 ‘non-qualified plans’: gift tax can be applied instead of PIT at discretion of tax authorities;</p> <p>IntE: Do not exist.</p>	<p>base of CIT;</p> <p>IntE: Do not exist.</p>
PS	<p>General: (only for JSC, usually cash-based) no PIT, but SSC on benefit if not exceeding 25% of annual gross salary;</p> <p>IntE: Do not exist.</p>	<p>General: Distributed amount deductible from tax base of CIT, but SSC;</p> <p>IntE: Do not exist.</p>
Spain	<p>ES: (1) Since 2003: no PIT, no SSC on benefit up to Euro 12,000, if plan regular, each employee and his family own not more than 5% of equity capital, 3-year blocking period; (2) Since 1997 Sociedades Laborales, if reserve for loss compensation 25% of annual profits tax credit of 99% on transfer tax and following tax exemptions on: no tax on company formation and tax credit of 99% on transfer tax, levies for notarial deeds on transfers to the company, debts, bonds and debenture bonds;</p> <p>SO: 80% tax relief on up to 2 x (annual medium wage x number of years before vesting), if vesting period not exceeding 2 years, options granted not annually, 3 years between option grant and share sale, plan broad-based;</p> <p>IntE: Do not exist.</p>	<p>ES: No;</p> <p>SO: No;</p> <p>IntE: Do not exist.</p>
PS	<p>General: No</p> <p>IntE: Do not exist</p>	<p>General: No;</p> <p>IntE: Do not exist.</p>
France	<p>ES: No;</p> <p>SO: No;</p> <p>IntE: Do not exist.</p>	<p>ES: Training of employees on EFP: tax relief Euro 75 per hour and person, up to Euro 5,000 per company for 2 years (2007);</p> <p>SO: No;</p> <p>IntE: Do not exist.</p>
PS	<p>General: Since 1986/1994 (intéressement – gain sharing): no SSC, but full PIT, if transferred immediately; tax incentives only if combined with savings funds (PEE, PPESV); Since 1967/1986/1994 (participation – profit-sharing): no PIT, no SSC, special flat tax of 7.6% on benefit if blocking period 5 years, the amount does not exceed 25% of gross salary up to Euro 14,592; returns tax free if accumulated, 10% special flat tax if paid out during blocking period;</p> <p>IntE: Since 1986/1994 (PEE - short-term savings plan): no PIT, no SSC, flat tax of 7.6% if blocking period 5 years and EmpC match does not exceed the ceiling; Since 2001: (PPESV - long-term savings plan): like short-term, but 10-year blocking period; if EmpC match exceeds the ceiling for short-term, but is under the ceiling for long-term - flat tax of 8.2%; Returns: flat tax of 10%.</p>	<p>General: Since 1986/1994 (intéressement – gain sharing): no SSC; tax incentives only if combined with savings funds (PEE, PPESV); Since 1967/1986/1994 (participation – profit-sharing): no CIT, no SSC, special flat tax of 7.6% on benefit if blocking period 5 years, the amount does not exceed 25% of gross salary up to Euro 14,592; returns tax free if accumulated, 10% special flat tax if paid out during blocking period;</p> <p>IntE: Since 1986/1994 (PEE - short-term savings plan): no CIT, no SSC, flat tax of 7.6% if blocking period 5 years and EmpC match does not exceed the ceiling; Since 2001: (PPESV - long-</p>

Country	Employee	Employer Company
		term savings plan): like short-term, but blocking period 10 years; if EmpC match exceeds the ceiling for short-term, but is under the ceiling for long-term - flat tax of 8.2%; Returns: flat tax of 10%.
Hungary	<p>ES: Since 2003 ‘Approved Employee Securities Benefit Programme’: no PIT and tax relief for voluntary insurance on benefit, if not exceeding HUF 50,000 annually and programme approved;</p> <p>SO: Since 2003 ‘Approved Employee Securities Benefit Programme’: incentives as for ES;</p> <p>IntE: Since 1992 ESOP: no PIT on shares transferred via ESOP; contributions to ESOP deductible from tax base of PIT.</p>	<p>ES: No;</p> <p>SO: No;</p> <p>IntE: Contributions to ESOP deductible from tax base of CIT.</p>
	<p>PS</p> <p>General: No;</p> <p>IntE: Do not exist.</p>	<p>General: No;</p> <p>IntE: Do not exist.</p>
Ireland	<p>ES: (1) Purchase of new shares: at sale of shares no PIT, no SSC, only CGT on issue price, if full price paid, 3-year blocking period and not exceeding lifetime ceiling of Euro 6,350; (2) Restricted Stock Scheme: deduction from tax base of PIT on benefit from 10% for 1 year blocking period to 55% for 5-year blocking period;</p> <p>SO: (1) Since 1999 SAYE: no PIT, no SSC at grant or exercise, if plan broad-based, SAYE contract with a bank for 3, 5 or 7 years, exercise price of shares up to 25% under the market value of underlying shares at option grant, plan approved by tax authorities; (2) Since 2001 APOS: no PIT, no SSC at grant or exercise, if plan broad-based, 3-year blocking period, plan approved by tax authorities;</p> <p>IntE: ESOT enjoy incentives only if combined with APPS (see below).</p>	<p>ES: (1) No SSC; (2) No;</p> <p>SO: (1) No SSC; (2) No SSC;</p> <p>IntE: ESOT enjoy incentives only if combined with APPS (see below).</p>
	<p>PS</p> <p>General: No;</p> <p>IntE: (1) Since 1986 APSS: no PIT, no SSC on benefit not exceeding Euro 12,700, if plan broad-based, 3-year blocking period in trust, plan approved by tax authorities Sale of shares: CGT; sale during blocking period PIT at top rate on proceeds of sale less market value and CGT on increase in value; (2) Since 1997 ESOT: incentives only if combined with APSS trust.</p>	<p>General: No;</p> <p>IntE: (1) Costs of setting up and operating the plan deductible from tax base of CIT, no SSC; (2) EmpC: incentives only if combined with APSS trust; IntE: no tax on dividends if dividends used for qualifying purposes.</p>
Italy	<p>General: sale gain taxed with 12,5 CGT instead 40%;</p> <p>ES: Since 1999: no PIT, no SSC on benefit up to Euro 2,066 if 3-year blocking period ; in limited liability companies free share up to Euro 7,500 tax exempt</p> <p>SO: Since 1999: no PIT, no SSC if 5-year blocking period between option grant and sale of shares, unless proceeds of the share sale invested in securities with the value equal to the difference of shares value at option grant minus share purchase price; PIT exemption abolished in 2008;</p>	<p>ES: Discount deductible from tax base of CIT;</p> <p>SO: No;</p> <p>IntE: Do not exist.</p>

Country	Employee	Employer Company
	IntE: Do not exist.	
PS	General: Since 2007: 23% deduction of PIT up to Euro 350 annually, no SSC; max bonus value Euro 6,000 with income ceiling of Euro 35,900 annually; IntE: Do not exist.	General: Since 1997/2007: 5% tax exemption for contributions distributed to employees, 25% deduction of SSC; IntE: Do not exist.
Netherlands	ES: Since 1994, usually JSC: tax incentives only in combination with a savings plan – no PIT, no SSC, instead 15% flat tax, if plan broad-based, 4-year blocking period, annual ceiling of the savings plan Euro 1,226; SO: No; IntE: Since 1994, usually LLC: regulation of tax incentives as for direct employee share ownership.	ES: No; SO: No; IntE: No.
PS	General: Since 1994/2003: tax incentives only in combination with a savings plan – no PIT, no SSC, instead 15% flat tax, if plan broad-based, 4 years blocking period, annual ceiling of the savings plan Euro 613; IntE: Do not exist.	General: No; IntE: Do not exist.
Austria	ES: Since 2001: Amount free of taxes and SSC up to Euro 1,453.46 annually, if 5 years blocking period, plan broad-based, shares deposited with a domestic credit institution; SO: Since 1999: tax allowance (10% of the benefit per year, but not more than 50% of the total benefit tax free) if options non-tradable, plan broad-based, value of underlying share at option grant not exceeding Euro 36,400 + carry forward of taxation for the remaining amount (taxation optionally at sale or at termination of employment, but at the latest at the end of the 7 th year after grant) if options deposited with a domestic credit institution; IntE: Since 2001: up to Euro 1,453.46 annually CGT; if more PIT; no SSC.	ES: The book value of transferred shares deductible as personnel costs; SO: Costs of share purchase or the amount not contributed to the equity in the case of capital increase deductible from CIT; IntE: payments to IntE and costs for IntE deductible from CIT; up to Euro 1,453.46 per annum and per person tax-free; if more CGT; dividends on shares tax free.
PS	General: No; IntE: Do not exist.	General: No; IntE: Do not exist.
Poland	ES: No; SO: No; IntE: Do not exist.	ES: Leverage Lease Buyout (LLBO), Corporate income tax law allows to include interest part of lease payments as costs reducing the tax base; SO: No; IntE: Do not exist.
PS	General: No; IntE: Do not exist.	General: No; IntE: Do not exist.
Portugal	ES: No; SO: No SSC; IntE: Do not exist.	ES: No; SO: No SSC; IntE: Do not exist.

Country	Employee	Employer Company
PS	General: Since 1969 (usually cash-based): no PIT, no SSC, if individual agreement concluded and effective; IntE: Do not exist.	General: Profit distributed to employees deductible from tax base of CIT; IntE: Do not exist.
Slovenia	ES: Since 2008: 70% deduction from PIT on benefit not exceeding Euro 5,000 annually per employee, if 1 year blocking period, 100% deduction, if 3 years blocking period; SO: No; IntE: Do not exist.	ES: Value of distributed shares deductible from tax base of CIT in the year, when the blocking period ends; SO: No; IntE: Do not exist.
PS	General: Since 2008 (for share-based PS): same as for ES; IntE: Do not exist.	General: same as ES; IntE: Do not exist.
Finland	ES: Since 1992: no PIT, no SSC on discount, if it does not exceed 10% and plan broad-based; Dividends: in public companies 30% tax free; in private companies 100% tax free if earnings per share less than 9% and the total amount less than Euro 90,000; SO: No; IntE: Do not exist.	ES: Discount deductible from tax base of CIT; SO: No; IntE: Do not exist.
PS	General: No; IntE: Since 1989/1997: Personnel Funds no PIT, no SSC on 20% of pay-outs from the Fund, if 5-year blocking period.	General: No; IntE: EmpC: no CIT, no SSC on profits transferred to IntE; IntE: earnings tax free.
UK	ES: No; SO: (1) Since 1980 SAYE: no PIT, no SSC at grant or exercise, if plan broad-based, exercise price of shares up to 20% under market value of underlying shares at option grant, SAYE contract with a bank, plan approved by tax authorities; (2) Since 1984/1996 CSOP: no PIT, no SSC at grant or exercise, if value of outstanding options up to GBP 30,000 per employee, exercise price not lower than market value at grant, exercise period 3 to 10 years after grant, plan approved by tax authorities; (3) Since 2000 EMI: no PIT, no SSC at grant or exercise, if value of options granted annually not exceeding GBP 100,000 per employee and GBP 3 million per company, tax authorities notified; IntE: Since 2000 SIP: no PIT, no SSC on benefit, if plan broad-based, 5-year blocking period in trust, value of shares up to GBP 3,000 (free shares), up to GBP 1,500 (partnership and dividend shares) annually per employee, plan approved by tax authorities; Sale of shares: no tax, no SSC if sold immediately after withdrawal.	ES: No; SO: (1)-(3) Costs of setting up and operating the plan; since 2003: costs of providing shares to the plan deductible from tax base of CIT, generally no SSC; IntE: Costs of setting up and operating the plan; since 2003: costs of providing shares to the plan deductible from tax base of CIT, generally no SSC.
PS	General: No; IntE: Do not exist.	General: No; IntE: Do not exist.

Abbreviations: APOS = Approved Share Option Scheme; APSS = Approved Profit-Sharing Scheme; CIT = Corporate Income Tax; CGT = Capital Gains Tax; CSOP = Company Share Option Plan; EMI = Enterprise Management Incentives; EmpC = Employing Company; ESOP = Employee Share Ownership Plan; ESOT = Employee Share Ownership Trust; IE = Intermediary Entity; JSC = Joint-stock Company; LLC = Limited Liability Companies; PIT = Personal Income Tax; SAYE = Approved Savings-Related Share Option Scheme, SIP = Share Incentive Plan; SSC = Social Security Contributions.

Although at first impression, the table seems to suggest unbridgeable diversity, the analysis of the data leads to the conclusion that pre-conditions as well as forms of tax incentives are generally similar, but differ substantially in size. The table columns correspond to the classification of employee financial participation forms in country profiles, but, as explained above, a different classification should be used for purposes of the following tax analysis: employee share ownership plans and share-based profit-sharing plans belong to one category (with certain specific features of indirect plans), stock option plans to a second category, and cash-based profit-sharing plans to a third category.

a) Share-Based Plans

Tax incentives in most countries apply to direct share-based plans, share-ownership as well as share-based profit-sharing. The most common pre-condition is a blocking period between one and seven years, the most common being 5 years (for example, Austria, Belgium, Denmark, France and Italy for some plans). A blocking period can be combined with an obligation to deposit shares with a bank. In indirect share-based plans, shares must be deposited with an intermediary entity (intermediary company, fund or trust) and cannot be withdrawn within a certain period of time (up to 10 years), which practically corresponds to the ‘voluntary’ blocking period in direct plans (for example, Austria, Finland, France, Ireland, UK). In some cases, tax incentives apply only if the primary plan is linked to a savings contract or scheme (for example, France, the Netherlands). In many countries, tax incentives apply only if the plan is broad-based (for example Austria, Denmark, Finland, Hungary, the Netherlands, Ireland, UK, France). However, some countries introduced broad-based as well as individual plans with partly different pre-conditions and tax incentives (for example Denmark). In some countries, where the plans are pre-defined in the law, approval of tax authorities is necessary (for example Hungary, Ireland, and UK).

The most common form of tax incentives for employees on the benefit in share-based plans (excluding stock option plans) is an allowance of tax and social security contributions, but the absolute amount differs significantly, from Euro 360 per employee annually in Germany to Euro 12,700 in Ireland. In Finland and Denmark, where the amount is given as a percentage of annual salary, the allowance might be even higher (10 per cent in Denmark and in Finland for direct share ownership plans and 20 per cent in Finland for indirect share-based profit-sharing). The tax-free amount in indirect plans is often larger than in direct plans. Another possibility is a special, relatively low flat tax instead of personal income tax and social security contributions (for example, 15 per cent in Belgium, 7.6 per cent in France). In France, the special tax is imposed on the employees as well as on the employing companies. Relatively rare tax incentives for employees are deduction from the tax base of personal income tax (Ireland for restricted stock schemes, Slovenia for a short blocking period) and a savings bonus (Germany for very low incomes). Tax incentives on dividends are also applied quite seldom (for example, Finland, France), since taxation of dividends is always lower, and social security contributions are not levied. Since the employer companies usually can deduct the value of distributed shares as personnel costs under general taxation rules and since they are not subject to social security contributions on that amount, special incentives are not required. However, in France it was necessary to exempt the employer companies from social security contributions, which are usually imposed, and to introduce a special flat tax of 7.6 per cent on the bene-

fit and of 10 per cent on the dividends, which also apply to employees. Specific tax incentives exist for intermediary entities in indirect plans: all earnings (for example, Finland) or at least a certain amount of contributions and dividends (for example, Austria, Ireland, France, UK) are either tax exempt or levied by a special low tax.

b) Stock Options

The greatest variety of tax incentives occur in connection with stock option plans. In addition, it is difficult to compare pre-conditions and incentive forms in different countries, since several stock option plans often exist in a single country. At a higher level of abstraction, the most common pre-conditions are blocking and exercise periods (for example, Belgium, UK, Ireland); restrictions on the difference between the market price of underlying shares and the exercise price (for example, Belgium, Denmark, Ireland, UK, Austria); the existence of a broad-based plan (for example, Austria, Denmark, Ireland, UK), and approval by the tax authorities (for example, Hungary, Ireland, UK). In the so-called SAYE plans in Ireland and UK, combination with a savings contract is required. As far as tax incentives for employer companies are concerned, eligibility often depends on whether the shares are to be purchased on the market or issued in the course of capital increase (for example, Austria, Greece).

The most common tax incentive forms for employees are an allowance of personal income tax and social security contributions, whereby the amounts are either the same as for shares, for example, Denmark, Hungary, or much higher, for example, CSOP (GBP 30,000) and EMI (GBP 100,000 !) in the UK. Such forms as deferred taxation (for example Austria) or taxation at grant (for example Belgium) are country-specific. Tax incentives for employer companies is the deductibility of costs of share purchase or option costs from the tax base of the corporate income tax.

c) Cash-Based Profit-Sharing

Only two countries (Greece and Portugal) have tax incentives for cash-based profit-sharing; in both cases these were introduced several decades ago. These tax incentives were obviously inefficient; the incidence of employee financial participation in Greece and Portugal is still the lowest among Western European countries. A possible reason for this inefficiency is restricted eligibility of – otherwise quite generous – tax incentives: in Portugal, tax incentives become applicable only on the basis of an individual contract limited in time; in Greece, tax incentives are applicable only to joint-stock companies.

4. General Principles

Two general principles may be drawn from the combined data on tax incentives and the incidence of financial participation from the various countries:

– **Tax incentives are not a prerequisite to financial participation**

Financial participation schemes without tax incentives (for example, profit-sharing plans in Austria and Germany) sometimes have a higher incidence than those with tax incentives (for example, share ownership plans in Austria and Germany).⁶⁶ Therefore tax incentives are not to be considered a prerequisite to the development of financial participation. Furthermore, in low-tax countries (for example, Ireland), tax incentives are less important and, in any case, cannot be as large as in high-tax countries.⁶⁷

– **Tax incentives effectively promote the spread of financial participation**

Countries with a long tradition of employee financial participation (for example, UK, France)⁶⁸ universally confirm this experience, but so do countries where tax incentives are quite recent, for example, Austria,⁶⁹ where a substantial increase has been observed, even though total numbers are still relatively low.

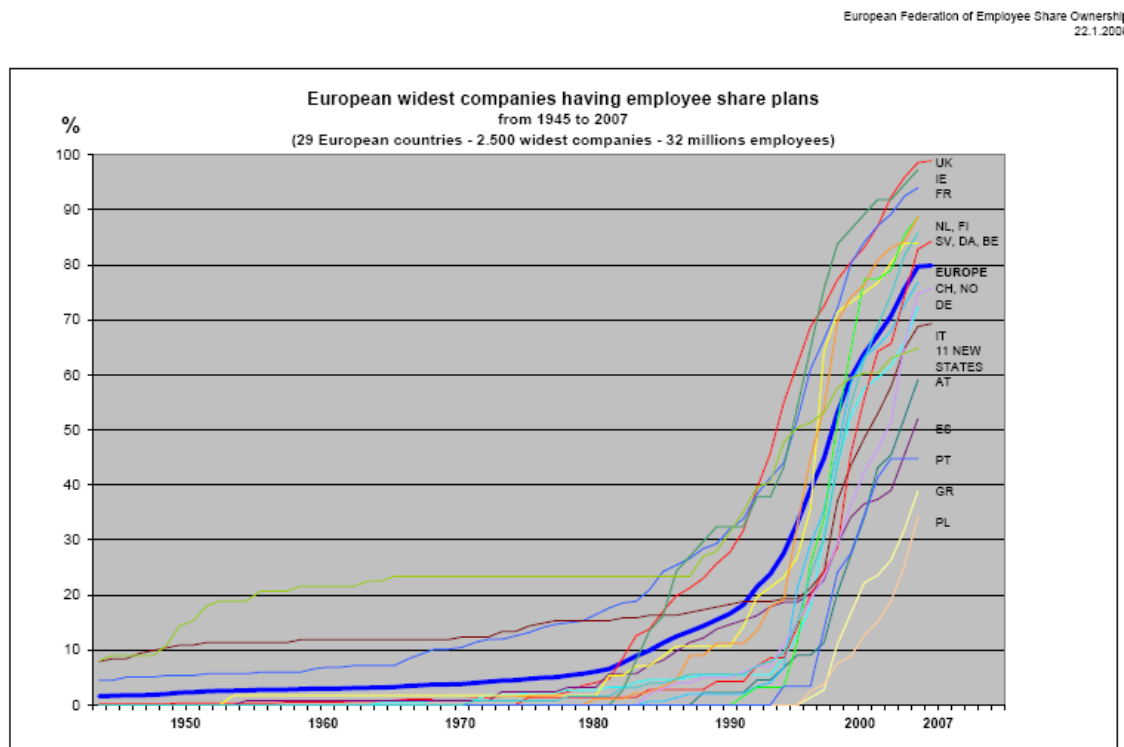
⁶⁶ In Austria, only 8 per cent of enterprises and 6 per cent of the workforce participated in employee share ownership plans in 2005, tax incentives for which were introduced in 2001, whereas 25 per cent of enterprises operated profit-sharing plans without tax incentives (see Kronberger et al., eds, 2007, pp. 11, 17, 162). In Germany, 2.4 per cent of enterprises had an employee share ownership plan in 2001, supported by (marginal) tax incentives, whereas at the same time 8.7 per cent of enterprises operated profit-sharing plans without tax incentives (see Würz, ed., 2003, p. 59).

⁶⁷ It should be noted that in countries which are considered low-tax, not all statutory taxes are necessarily low; the statement refers only to low statutory taxes. For example, in Ireland, corporate income tax is exceptionally low (12.5 per cent), whereas personal income tax is close to the EU average (20-42 per cent). Therefore, most tax incentives for employee financial participation in Ireland concern employees and not employer companies. The Irish Government declared that no tax relief which reduced the revenue from corporate income tax can be introduced because the low tax rate leaves very little leeway (Irish Department of Finance, TSG 98/12).

⁶⁸ In France, legislation on voluntary employee financial participation without tax incentives of 1959 and even legislation on compulsory employee financial participation without tax incentives of 1967 did not lead to a significant number of plans in operation. Only in 1986 when the first tax incentives were introduced did the number of plans increase rapidly; this upward tendency has been supported by the introduction of new tax incentives (see Würz, 2003, p. 39). In the UK, although profit-sharing has existed since the 19th century and share ownership since the early 1950s, the number of plans remained small until the first tax incentives were introduced in 1978. Since then, the system of tax incentives and economic efficiency of incentives and plans are regularly reviewed by the government, and the number of plans is steadily increasing, especially Revenue Approved plans (see Würz, 2003, p. 130); <<http://www.ifsproshare.org>>, Log-in: 20 July 2007.

⁶⁹ In Austria, only 8 per cent of employee financial participation plans were implemented before first tax incentives were introduced in 1993, while 45 per cent of plans were introduced in four years after more substantial tax incentives became effective in 2001 (see Kronberger et al., eds, 2007, p. 32).

Figure 17. European largest companies having employee share plans



According to the graph by EFES (see Figure 17, above) representing the increase in the number of European widest companies offering financial participation plans from 1945 to 2007, introduction of tax incentives in most Western European countries has led to a significant increase in the number of plans in the short-term and a steady growth in the long-term. In most countries, the angle of the graph representing increase becomes steeper following the years in which tax incentives were introduced (for example Denmark 1987 and 2003; Finland 1996; France 1986 and 1994; Ireland 1986 and 2001; the Netherlands 1994 and 2003; UK 1980, 1984 and 2000). However, in some countries there is no correspondence between the introduction of tax incentives and the increase in the number of plans (for example Greece (increase since 1999, although tax incentives since 1987; Portugal (increase 1993 until 2000, although tax incentives since 1969); Austria (increase since 1997, although tax incentives since 2001). In each deviating case it can be explained by country-specific circumstances. It is common to all deviating countries that they have (or have had until recently) only insignificant tax incentives and a small number of financial participation plans. In Portugal, a vast majority of plans emerged as a result of privatisation in the 1990s, because in this procedure substantial incentives, not only concerning taxes, were granted to the workers of privatised enterprises; all these incentives were abolished after privatisation procedures were completed at the end of the 1990s. In Greece, complexity of regulation and lack of information about financial participation prevented the companies from introducing broad-based plans, although tax incentives were introduced quite early; since 1999, tax incentives for stock options were introduced and utilised generally by executives. In Austria, profit-sharing, although not linked to tax incentives,

traditionally makes up the major part of financial participation plans. However, the increase of originally almost non-existent share ownership plans was substantial after the introduction of tax incentives in 2001 according to national statistics; it can only not be seen on the graph due to the still low percentage of share ownership as compared to profit-sharing plans.

5. Conclusions

Firstly, tax incentives should (and in most countries actually do) target those taxes which constitute the heaviest burden in the national taxation system. Usually (with the exception of countries with flat tax systems which at present do not offer specific tax incentives) these are the progressive personal income tax and social security. Many countries therefore provide:

- exemptions from social security contributions for certain plans (for example, France, Belgium, UK, Ireland, Finland),
- levying a capital gains tax (for example, UK, for dividends Belgium),
- levying a special low tax (for example, France) in lieu of personal income tax, and
- tax allowances for personal income tax (for example, Austria, Finland, Ireland).

Secondly, tax incentives should be provided for both employees and the employer company, inasmuch as participation is voluntary for both parties in all EU Member States except France. However, this requirement is relative: in most countries the employer company has already been granted tax incentives in the form of deductions under general taxation law and only tax incentives for taxes involving the cost of shares and stock options are needed. In most countries, the only important incentive for the employer company is the exemption from social security contributions; this has actually been introduced in many countries (for example, France, Ireland, Finland, Belgium). The employee is usually more in need of direct incentives as the heaviest burden of progressive taxes falls on him or her.

Thirdly, even substantial tax incentives may prove inefficient when the pre-conditions of eligibility are too restrictive, complex or inflexible. This is the case (for example, in Greece) for cash-based profit-sharing and in Germany and Belgium for schemes of all types (see European Commission, 2003a, pp. 17, 24). The flexibility problem can be solved, as in Ireland and the UK, by allowing the employer company to choose between less flexible approved schemes combined with substantial tax incentives and more flexible unapproved schemes combined with minor tax incentives. Another interesting approach was presented in the EC Report on Stock Options (see European Commission, 2003b, pp. 42, 43): Since direct taxes cannot be harmonised under the effective EU Treaty, as shown above, it might be reasonable to harmonise the pre-conditions for the application of tax incentives where they exist in a particular country. National legislators would be authorised to introduce additional national plans and to decide the size and the form of tax incentives for these as well as for those plans encompassing all of Europe. Harmonisa-

tion can only be accomplished if the existing pre-conditions in different EU Member States are at least comparable for all types of employee financial participation schemes, as is apparently the case for stock options.

Fourth, some forms of tax incentives are more favourable for certain types of plans and also lead to higher efficiency:

- For share ownership and stock options as far as benefit taxation is concerned: generous valuation rules combined with a favourable taxation moment (for example, deferred taxation, often linked to holding period), and, if possible, exemption from SSC for both the employer company and the employee.
- For dividends and sale of shares: a special tax rate or capital gains tax in lieu of personal income tax and, if necessary, exemption from SSC.
- For ESOPs and Intermediary Entities: exemptions from income tax on share acquisition⁷⁰ or on share sale if the profit is realised after a holding period or within a retirement program; the company may qualify for tax relief on both interest and principal payments on the loan; sale of stock to an ESOP on a tax-deferred basis if the proceeds of the sale are reinvested in securities of other domestic corporations (tax-free rollover).
- For profit-sharing: a special tax rate in lieu of the progressive personal income tax as well as exemption from SSC for both the employer company and the employee.

However, the most effective forms of tax incentives do cause revenue losses. Therefore, efficiency should be weighed against the revenue requirements of each country independently. Should a government wish to introduce specific tax incentives, it might well begin with ‘soft’ tax incentives which do not cause substantial revenue losses, for example, tax allowances defined by nominal amount (as in Austria). Later, depending on revenue needs and the political climate, it may proceed to more effective measures: tax allowance as a proportional amount, deductions, tax credits, introduction of special low tax rates, and, finally, full exemption from taxation.

Fifth, in spite of the difficulty of their implementation at the European level (because of the exclusive jurisdiction of national legislation over tax law), tax incentives remain powerful tools for enhancing and broadening financial participation. This is especially true when they remain optional for the member countries and not subject to a unanimous vote of approval. Countries could voluntarily offer tax incentives singly or in groups. Such a step would create an increasingly favourable environment in which countries having an advanced tradition, such as France or the United Kingdom, would encourage emulation. Optional preferential treatment as part of the Building Block Approach requires distinguishing between profit-sharing schemes, share ownership schemes and employee stock ownership plans.

⁷⁰ In Ireland this is the case only where the ESOP comprises an ESOT working in tandem with an Approved Profit Sharing Scheme.

V. The Path to a European Regulation

Jens Lowitzsch

The basic conception of civil society as a society of private property owners has not (yet) been sufficiently recognised in European law.⁷¹ Since the adoption of the European Charter of Fundamental Rights (as part of the Treaty of Nice in 2001) ownership has been more precisely defined in Art. 17 of the Charter. But not until the ratification of the European Reform Treaty and the inclusion of the European Charter of Fundamental Rights as part of it, the Charter became binding European Law.

So far the only explicit support for a framework for financial participation is to be found in the Council Recommendation of 27 July 1992⁷² and in Part 7-II of the Action Programme for Implementing the Community Charter of the Fundamental Social Rights of Workers.⁷³ Title XI (Social Politics) of the additional protocol of the European Human Rights Convention of 1952, however, contains no recognition of the financial participation of employees. It merely states principles of protection of labour, equal opportunities and co-determination, although Art. 139 (former 118b) ECT permits agreements between social partners on a community level. A rare exception to the general silence is the second Council Directive on Company Law.⁷⁴ In summary, the community law appears deficient in regard to employee participation in general, and financial participation in particular.

⁷¹ One reason is that Art. 295 (former 222) of the Treaty of Amsterdam excludes private property as a legal institution from the law of European contracts. But de facto the treaties do deal with the subject of private property, especially by regulating derived rights and related areas.

⁷² Concerning the promotion of participation by employed persons in profits and enterprise results (including equity participation), 92/443/EEC, *Official Journal* L 245, 26 August 1992, p. 53-55.

⁷³ The Charter of 9 December 1989, which was also signed by the United Kingdom in 1998, is neither a binding legal act nor is it a treaty among the signatory states. It is merely a solemn declaration which should nonetheless serve as an aid to the interpretation of the provisions of the EC Treaty, since it reflects views and traditions common to the Member States and represents a declaration of basic principles which the EU and its Member States intend to respect. Together with the Action Programme, which has also been approved by the Heads of State or Government, it is therefore used by the Commission as a basis for justifying many of the Directives it proposes.

⁷⁴ See Art. 19 para. 3, 23 para. 2, 41, para. 1 and 2 of the Directive, 77/91/EEC, dating back to 13 December 1976 which allow derogations from the European legal framework for Joint-stock Companies designed to encourage the financial participation of employees.

1. Key Issues and Obstacles to Creating a European Concept

The American experience in institutionalising techniques for broadening the ownership of capital, valid in all of the 50 American states, provides a model for such a trans-jurisdictional framework. In its communication⁷⁵, the Commission refers to this experience by stressing the ‘important impact financial participation can have in terms of economic growth, fostering industrial change and making sure that all workers participate in this growing prosperity’. Furthermore, the Commission states that ‘especially when compared to the experiences in the US, there exists still a huge, largely unused potential for the further development of financial participation as part of an overall strategy aimed towards stimulating the growth of new, dynamic companies’. Two relevant issues are currently under consideration in the European Union:

- Can broadened ownership of capital through ESOPs or similar vehicles help EU companies become more competitive in the world market? One field of action already identified in this context, in the Council Recommendation of 7 December 1994,⁷⁶ are transfers of businesses to employees as a way to facilitate business succession in SMEs.⁷⁷
- Assuming that broadened ownership of capital is desirable from a social and economic standpoint, what is the best way to amend legal structures in the EU so as to create a legal foundation for employee share ownership as part of property rights legislation, and thus the ‘acquis communautaire’ itself?

a) Focus: Legislating Financial Participation Schemes

Although tax incentives are the most common way of encouraging financial participation schemes, a common European legal framework imposing such tax incentives would collide with the national legislative sovereignty over taxation. Under the European Union, each Member State retains exclusive power over all matters involving taxation; any Directive involving taxation requires the unanimous consent of the Member States. Therefore, a European approach to the problem must provide a broad incentive system going beyond the classical instruments of tax legislation. Establishing such schemes through legislation is of primary importance, as it gives companies a distinct legal entity and provides them with a clear framework for company decisions and actions. At the same time, establishing a legal framework delineates what is possible for companies without inviting sanctions from regulatory, legal or taxation authorities (see Pendleton et al., 2001, p. 9).

⁷⁵ COM (2002) 364 Final, 5 July 2002, pp. 3, 10.

⁷⁶ On the transfer of small and medium-sized enterprises, 94/1069/EEC, with explanatory note, Official Journal No. C 400, 31 December 1994, p. 1.

⁷⁷ One of the key areas defined in the Final Report of the MAP 2002 Project, *European Commission Enterprise Directorate-General, ‘Transfer of Businesses – Continuity Through a New Beginning’* (European Commission, 2003b).

b) Unanimous Decision vs. Majority Vote

Diverse national approaches to both financial participation and participation in decision-making constitute further impediments to change. For obvious reasons, it is very difficult to reach a unanimous supranational compromise either in the Commission or in the Council. The law of European Treaties in general permits majority vote decisions in a limited number of cases, already extended by the Treaty of Nice.⁷⁸ The Reform Treaty further extends the the qualified majority voting for the adoption of regulations to 32 additional policy areas. “Joint adoption” as per Art. 289 Treaty on the Functioning of the European Union – referred to as TFEU – (previously Art. 251 ECT) will now become the norm and the European Parliament will equal status with the Council as co-legislator. As to taxation (Art. 113, 114 II and 173 TFEU; previously Art. 93, 94 and 175 ECT), however, the requirement of unanimity for all measures is maintained across the board.⁷⁹ In the field of social policy (Art. 48 and 153 TFEU; previously Art. 42 and 137 ECT), the decision-making process has remained essentially unchanged. Despite maintenance of the status quo, the Council, acting in unanimity, may, as before, make the co-decision procedure applicable to those areas of social policy, which are currently still subject to the rule of unanimity (Art. 115 and 153 II 3 TFEU). Therefore, the search for a legal foundation at the Directive level has to focus on those ‘majority vote’ regulations if it is to be successful. This is further true because the position of the governments in relation to the social partners, their role in society and their relation to each other varies significantly in the different member countries.⁸⁰

c) Different Contexts, Different Approaches – The Building Block Approach

A strict distinction concerning suitable options and legal procedure to create solutions at the European level has to be made between participation in decision-making and financial participation of employees. Participation in decision-making, whatever its form at the national level, is as a rule obligatory for enterprises in the given country.⁸¹ Since community law would be equally binding, a supranational compromise can encompass only the smallest common features of the diverse national regulations.⁸² Financial participation on the

⁷⁸ No less than 27 provisions were changed completely or partly from unanimity to qualified majority voting. Furthermore, the Treaty of Nice has extended the scope of co-decision. This procedure became applicable to seven provisions which changed over from unanimity to qualified majority voting. Accordingly, most of the legislative measures, which after the Treaty of Nice required a decision from the Council acting by qualified majority, were decided via the co-decision procedure.

⁷⁹ There are still 112 cases, in which the European Parliament does not contribute to creating legislation. The number of instances using the co-decision procedure has increased from 15 to 85 cases since its introduction (see Lieb Maurer and von Ondarza, eds, 2008, p. 37).

⁸⁰ For example, the consensual continental contrasts with the Anglo-American confrontational model; likewise the strong position of the state in France contrasts with the powerful role of the German ‘Tarifpartner’ (collective bargaining parties, such as trade unions and employer associations) (see Pendleton and Poutsma, 2004).

⁸¹ As, for example, the German ‘Mitbestimmung’ and the Works Councils in France and the Netherlands.

⁸² This problem is well illustrated by the prolonged controversy over the so-called European Workers Council, and as a consequence the rather minimal compromise of the regulation in the European Company Statute.

other hand is traditionally an optional instrument for improving company performance and corporate governance; enterprises are therefore free to introduce financial participation schemes.⁸³ Thus, provided that they are granted voluntarily on the national level, a supranational concept can offer a variety of incentives from which to choose.

A European Regulation should thus encompass a broad incentive system, which provides different and flexible solutions, compatible with those already established in the Member States. An adaptable scheme can provide for a solution suitable for use throughout the European Union, comprising best practises of national legislation and customs (compare White and Case, 2001, p. 4). Combining them in a single program with alternative options leads to a 'Building Block Approach', with the different elements being mutually complementary.⁸⁴

These building blocks consist of the following three basic elements:

- Profit-Sharing (cash-based, deferred and share-based);
- Individual Employee Shareholding (stock options and employee shares);
- Employee Stock Ownership Plans (ESOPs) as collective schemes.

While profit-sharing schemes, stock options and employee shares are relatively widespread in the European Union, Employee Stock Ownership Plans (ESOPs) are predominantly to be found in countries with an Anglo-American tradition, for example, the United Kingdom and Ireland.⁸⁵ Originated in the United States as a technique of corporate finance, the ESOP, using borrowed funds on a leveraged basis, has the capacity to create substantial employee ownership and can be used to finance ownership succession plans, an important feature, especially for European SMEs.⁸⁶ Furthermore, it can be used to refinance outstanding debt, to repurchase shares from departing plan participants, or to finance the acquisition of productive assets.⁸⁷ The last two functions are also both possible on an unleveraged basis. In the unleveraged case, of course, less stock can be acquired in any given transaction.

2. Options for Creating the Legal Foundations of a European Concept

a) Recommendation According to Article 288 and 292 TFEU

The European Concept could be framed as a Recommendation according to Art. 288 sentence 1, alternative 4 and sentence 5 TFEU (previously Art. 249 ECT). The downside

⁸³ A rare exception exists in France where enterprises with more than 50 employees are required to establish a participation fund. See European Commission (1997), p. 19-20.

⁸⁴ For a detailed technical description of the different mechanisms and schemes see Lowitzsch et al. (2008).

⁸⁵ For Ireland, see Shanahan and Hennessy (1998), p. 9.

⁸⁶ One of the key areas defined in European Commission (2003b).

⁸⁷ From an entrepreneurial point of view, see Ackermann (2002).

of such a solution, however, is that Recommendations according to Art. 288 sentence 5 TFEU are not legally binding and thus implementation in the Member States would be far from certain. On the other hand, legislation of such schemes in any form whatsoever is a major step forward, as it sets up a distinct legal entity for companies to refer to and provides a framework for company decisions and actions in those countries that approve the European Concept.

One possible solution to the problem of national implementation would be a recognition procedure by Member States for financial participation similar to that proposed by the High Level Group of Independent Experts (European Commission, 2003a, pp. 52). As a result of this procedure, single Member States would recognise single elements from the European Concept drawn up in the Recommendation as equivalent to a plan drawn up under its own laws and provide equivalent benefits. In this way, they would provide companies operating under their legislation with a legal framework that delineates what is possible without invoking sanctions from regulatory, legal and taxation authorities. Recognition is nonetheless a major step and would require considerable co-operation between the Member States and the Commission.

b) Directive Level: Amending Existing European Company Law

Considering the difficulties in passing and implementing European Directives, especially in sensitive areas where unanimous decisions may be required, it seems preferable to amend existing European legislation. Since employee share ownership fits into the framework of company law, rules to implement it could be proposed as an amendment of the ‘European Company’ legislation. Like the European Company Statute⁸⁸ (ECS), which provides an option for forming a supranational company, there could be an amendment to the ECS permitting such companies to create ‘European Employee Shareholding’ as an option.⁸⁹ This option could be easily extended to other companies, which do not fall under the ECS, provided that national legislation would then be adapted to the requirements of the supranational statute.

The EU Member States would have an incentive to implement legal rules pertaining to the ‘European Employee Shareholding Statute’ as an amendment to the ECS, choosing from a variety of incentives, possibly including tax breaks as well as other preferential treatment:

- Unlike the supplementary rules to the ECS concerning participation in decision-making, those on ‘European Employee Shareholding’ would be totally voluntary; they would apply only if the company decides to adopt one of the existing models of financial participation.

⁸⁸ Council Regulation (EC) No. 2157/2001 of 8 October 2001 on the Statute for a European company (SE); OJ, L 294/1.

⁸⁹ As proposed in the report of the Committee on Employment and Social Affairs of 5 May 2003 (A5-0150/2003), p 11 and 14 and expressed in the European Parliament Resolution of 5 June 2003 (P5-TA (2003) 0253), 31. IV; like the Council Directive 2001/86/EC of 8 October 2001, ‘supplementing the Statute for a European company with regard to the involvement of employees’ but with regard to financial participation.

- As in the case of the supplementary rules to the ECS on participation in decision-making,⁹⁰ the scheme would be, at first hand, proposed by the employers to their employees; in other words, a negotiated proposition. If the proposed scheme does not correspond to a catalogue of minimum requirements, or the parties so decide, a statutory set of standard rules would apply as a ‘safe harbour’.

The mechanism of the ‘default standard rules’ concerning participation in decision-making, foreseen in the ECS for resolving potential conflict while at the same time not imposing a solution, would even be suitable in the field of financial participation:

- As for the ‘standard rules’ for private and/or unlisted SMEs, an ESOP-trust would be feasible since it may provide a relatively non-controversial solution to the question of employee voting rights and may buffer potential risk more easily, while at the same time solving the problem of business succession.
- As for the ‘standard rules’ for quoted medium-sized and large enterprises, a restricted broad-based employee stock option or stock purchase scheme (as practised in the United Kingdom) seems to be feasible since there has already been substantial development in European harmonisation on the one hand (see below), and a remarkable initiative put forward by the Enterprise Directorate-General on the other (European Commission, 2003c).

c) National Level: Building on Existing National Company Law

Given the above-described difficulties in arriving at a supranational compromise either in the Commission or in the Council, in order to reach a regulation at the Supranational level, the simplest solution is to build on existing national legislation originating in the *Acquis Communautaire*. A rare example of such legal ‘common ground’ are some of the national rules on listed and unlisted joint-stock companies originating in the implementation of European Law that is, the second Council Directive on Company Law 77/91/EEC, dating back to 13 December 1976. Art. 19 para. 3, 23 para. 2 and 41, para. 1 and 2 of the Directive allow Member States to deviate from the European legal framework of joint-stock companies in order to encourage employee financial participation. Although primarily referring to share ownership schemes these – optional – regulations also leave room for combination with profit-sharing schemes.

Art. 19 para. 3 allows Member States to deviate from the restrictive rules governing exemptions from the general prohibition against a company acquiring its own stock. When the shares acquired by the company are earmarked for distribution to that company’s employees or to the employees of an associate company, a general shareholders assembly decision is not obligatory although such shares must be distributed within 12 months of acquisition.⁹¹

⁹⁰ Here it is the result of negotiations between employer and employee representatives.

⁹¹ The general rules that (i) require that the acquisitions may not have the effect of reducing the net assets below the amount of the subscribed capital plus those reserves which may not be distributed under the law or the statutes and (ii) require that only fully paid-up shares may be included in the transaction still apply across the board.

Member States may lift the limit of the nominal value of the acquired shares of 10 per cent of the subscribed capital (including shares previously acquired by the company and held by it, and shares acquired by a person acting in his own name but on the company's behalf) though, according to Art. 41 para. 1.

As an exception to the general prohibition against a company leveraging the acquisition of its own shares, Art. 23 para. 2 allows Member States to permit companies to advance funds, make loans, and provide security (financial assistance), with the intention of selling these shares to company employees. Art. 41 para. 1 further allows for deviations from general rules and restrictions to encourage employee financial participation during the process of raising additional capital. An example is the financing of the share issue from the companies' own funds or through a profit-sharing scheme. Finally, the opening clause of Art. 41 para. 2 of the Directive providing for the possibility of suspension of Arts. 30, 31, 36, 37, 38 and 39 for companies under a special law issuing collectively held workers' shares, has not been used except in the case of France⁹².

Table 6. Implementation of the Second Council Directive on Company Law 77/91/EEC

Country	Art. 19 III permission to acquire companies own shares for its employees	Art. 23 permission to advance funds, make loans, provide security (financial assistance), with a view to acquisition	Art. 41 I derogation to encourage financial participation in case of capital Increases	Other general provisions in Company Law to promote financial participation
EU-15				
Belgium	Without decision of General Assembly	Value of financial assistance within distributable reserves; net assets mustn't become less than subscribed capital; also firms founded by employees who hold more than 50% of voting rights	5 years not transferable, limit: 20% of equity capital; up to 20% discount	No
Denmark	Limit: equity capital exceeds distributional dividend; share capital less own shares held must amount to not less than DKK 500,000	If qualified stock purchase plan; also acquisition from employees; to extent that shareholders' equity in company exceeds amount of not distributable dividends	According to Articles of Association issue of new/bonus shares; also subsidiary employees; authorisation up to 5 years each; also other than by cash payment	Deviation from subscription/pre-emption rights by decision of General Assembly (two thirds of votes and equity capital) for benefit of employees
Germany	Without decision of General Assembly; also (former) employees or	Yes	Stock options for firms/affiliated firms employees; General	In firms with individual share certificates num-

⁹² See Art. L.225-259 to L.225-270 of the French Commercial Code: Employee shares collectively owned by paid personnel in a workers' commercial co-operative.

Country	Art. 19 III permission to acquire companies own shares for its employees	Art. 23 permission to advance funds, make loans, provide security (financial assistance), with a view to acquisition	Art. 41 I derogation to encourage financial participation in case of capital Increases	Other general provisions in Company Law to promote financial participation
	of affiliated firms; reserve fund necessary without reducing equity capital or reserve funds		Assembly decision; nominal amount of options restricted to 10%, that of increase to 50% of equity capital	ber of shares to be increased to the same extent as equity capital is increased
Greece	Also personnel of ancillary firms	No	Shares / stock options, free / discounted; 3 years not transferable without General Assembly approval	No
Spain	Also for stock options	Yes	No	No
France	In context of share-based profit-sharing scheme, share savings plan or stock option scheme	Also in subsidiaries or companies included in a group savings scheme	For all schemes; General Assembly decision required; no public offering;	Employee stock options; Share-based deferred profit-sharing; Save-as-you-earn schemes
Ireland	Not specific for employees, generally possible	Firm / group firm; provision of money / loans under share scheme; present / former employees and members of families	No	Finance Acts: Share-based profit-sharing; Save-as-you-earn / Share purchase schemes
Italy	No	Value of financial assistance within distributable reserves	Pre-emptive right of shareholders can be suspended for up to 25% of new shares with majority General Assembly vote; more than 25% require majority of capital held	Special 'Employees shares' can be issued in capital increase with specific rules for form, tradability and rights
Luxembourg	As minimum requirements of Directive	Limit: net assets of company not lower than amount of subscribed capital plus reserves	No	No
Netherlands	Also employees of group firm; without decision of General Assembly, if Articles provide; equity capital reduced by acquisition price not less than amount paid for shares plus reserve funds	Yes (but restrictions for closed JSC)	No	No

Country	Art. 19 III permission to acquire companies own shares for its employees	Art. 23 permission to advance funds, make loans, provide security (financial assistance), with a view to acquisition	Art. 41 I derogation to encourage financial participation in case of capital Increases	Other general provisions in Company Law to promote financial participation
Austria	Also employees of affiliated firms; reserve fund for own shares to be established without reducing of equity capital or other reserve funds; Stock options without decision of General Assembly, but consent of supervisory board	No	Stock options for firms /affiliated firms employees; General Assembly decision; nominal amount of options restricted to 10%, that of increase to 50% of equity capital ; limit of 20% of equity capital for total amount of shares receivable	In firms with individual share certificates the number of shares has to be increased to the same extent as equity capital is increased
Portugal	Not specific for employees, generally possible, if partnership contract does not provide for anything else	Also to employees of affiliated firms; liquid assets mustn't become less than subscribed capital plus not distributable reserves	General Assembly may limit/abolish pre-emptive right of shareholders for 'social reasons'	No
Finland	Not specific for employees, generally possible	Yes, if interest rate is less than the reference interest rate, difference is taxable benefit and subject to social tax	No special regulation with a view to employees	Act on Personnel Funds
Sweden	Not specific for employees, generally possible	employees of firm/ group firm; total value limited; at least 50% of firms' employees covered; advance/loan to be repaid within 5 ys	General Assembly can suspend shareholders pre-emptive right of; also group firm; also wife / husband / children	No
UK	Not specific for employees, generally possible	Firm/group firm; provision of money / loans under share scheme; present/former employees/ family members; net assets mustn't become less than subscribed capital; value of financial assistance within distributable reserves;	No	Finance Acts: Share-based profit-sharing; Save-as-you-earn / Share purchase schemes

New Members

Bulgaria	Not specific for employees, generally possible	No	No	No
Cyprus	Without decision of General Assembly	Advance funds, make loans to employees	No	No

Country	Art. 19 III permission to acquire companies own shares for its employees	Art. 23 permission to advance funds, make loans, provide security (financial assistance), with a view to acquisition	Art. 41 I derogation to encourage financial participation in case of capital Increases	Other general provisions in Company Law to promote financial participation
Czech Republic	Without General Assembly decision provided for reserve	In accordance with Articles of Association	Financing from company profits or profit-sharing; not considered public offering	Discount limit: 5% of equity capital, covered by firms own resources
Estonia	Not specifically for employees, generally possible	No	No	No
Hungary	Not specific for employees, generally possible	Also employees of controlled firms or organisations founded by employees	Both, free / discounted special 'Employee Shares', not considered public offering	Spec. free/discounted 'Employee Shares'; limit: 15% equity capital; not transferable; obligation to sell back
Latvia	Firm may fully pay up stock, not transferable; for up to 6 months	No	Non-voting shares, max 10% of equity capital, covered by firms profit; no public offering	'Employee shares' in municipal/state firms; not transferable; obligation to sell back
Lithuania	Not specific for employees, generally possible	Advance funds or loan paid back by deductions from employees' salary	Non-voting shares for up to 3-year period in which share sale only to other employees	No
Malta	Without decision of General Assembly	For employees of firm/ group firm; provided it does not endanger firms own funds	No	Free/discounted shares of mother firm for employees; no prospectus needed
Poland	Also retired employees/ affiliated firms; reserve needed	Reserve needed, also employees of affiliated companies	Financing from firms' profits / profit-sharing; not considered public offering	No
Romania	Financed by profits and/or distributable reserves	Yes	No	No
Slovak Republic	In accordance with Articles of Association	Provided it does not endanger company's own funds	By General Assembly decision	Discounted share offers, discount up to 70% covered by firms' own resources
Slovenia	Also retired employees and of associate firms	Also employees of associate companies	Financing from profit-sharing possible	No

Country	Art. 19 III permission to acquire companies own shares for its employees	Art. 23 permission to advance funds, make loans, provide security (financial assistance), with a view to acquisition	Art. 41 I derogation to encourage financial participation in case of capital Increases	Other general provisions in Company Law to promote financial participation
Candidate Countries				
Croatia	Also employees of associated firms; reserve from profits needed	Reserve needed; must not endanger equity capital	Among others to fulfil employees' claims to acquire shares	No
Turkey	Not specific for employees, generally possible	No	No	No

As the table above illustrates, a surprisingly large majority of Member States have adopted national legislation permitting a company to acquire its own shares in order to transfer them to its employees (implemented in 17, possible in 25), and to facilitate this acquisition by financial assistance (implemented in 23). Despite the fact that this legislation has rarely been used in some countries, the existence of corresponding regulations across the EU may serve as a foundation for a European concept.

3. Compliance with the Postulates of the European Policy Makers

a) Achieving Competitiveness While Maintaining Diversity

Financial participation of employees is closely linked to the objectives of the Lisbon summit for making the European economy ‘the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion’.⁹³ Our proposed European Concept refers – as does the Commission – particularly to the experience in the US that demonstrates the impact such a model can have ‘in terms of economic growth, fostering industrial change and making sure that all workers participate in this growing prosperity’⁹⁴. Therefore, in order to harness the potential – still largely unexploited in Europe – of the further development of financial participation as part of an overall strategy for stimulating the growth of new, dynamic companies as the Commission requires, we advocate the development of ESOPs.

Although the thesis that democracy requires a broad distribution of wealth is widely accepted, present social policy has not yet responded to the growing concentration of

⁹³ See point 1.5 of the Presidency Conclusions of the Lisbon European Council (No. 23 of 24 March 2000).

⁹⁴ Commission communication seeking ‘a framework for the promotion of employee financial participation’, COM (2002) 364 Final, 5 July 2002, pp. 3, 10.

wealth; no regulations have come into force either at a national or a European level. Social attention so far has been focused on the growing wealth of the few (for example, anti-monopoly legislation). Given this context, an open, modular concept ideally responds to the need for developing regulations at the supranational level in order to support financial participation more actively and to overcome national differences in taxation policy. At the same time, such a legal framework, while providing a broader incentive system, delineates what companies may do without inviting sanctions from regulatory, legal and taxation authorities.

A legal foundation at the European level has to focus on ‘majority vote’ regulations if it is to be successful. Thus, it should encompass a broad incentive system which provides different and flexible solutions compatible with those already established in the Member States:

- Relatively widespread in the European Union are profit-sharing schemes, stock options and employee shares.
- In countries with an Anglo-American tradition, for example, the United Kingdom and Ireland, ESOPs are also to be found;
- Central and Eastern European countries have developed share ownership systems (rather than profit-sharing schemes) with shares being distributed for free or sold at the market price or under preferential conditions.

The apparent difference in legal and political priorities between East and West is due to the fact that the first priority of post-socialist legislators is to change the socialist economic system through privatisation and re-privatisation. Therefore, the development of these schemes does not necessarily constitute a progressive evolution of their pay system or their work organisation process.

The Building Block Approach reflects this diversity, while opening national practise to new forms of financial participation.

b) The Building Block Approach: Meeting Essential Principles...

The proposed Building Block Approach fully complies with the essential principles of financial participation schemes, which the Commission sets forth in the cited Communication:

- All elements of the building blocks are voluntary for both enterprises and employees (this does not, however, conflict with the French compulsory regulations at the national level).
- The building blocks can be put together in any combination depending on the specific needs of the given enterprise so as to produce individually tailored, clear and comprehensible plans.
- Discrimination, for example, against part-time workers or women, would exclude any national company scheme from being integrated into the supranational European Concept.
- The proposed share ownership schemes that have been established in the United States and the United Kingdom for decades include adequate training programs and

educational materials, which allow employees to assess the nature and details of the schemes.

- Unreasonable risks for employees are buffered by the diversity of the concept. The dissemination practices for employee information aim at, among other objectives, raising the awareness of the risks of financial participation resulting from fluctuations in income or from limited diversification of investments.
- By collecting the best practise of national legislation and customs, the rules on financial participation at the company level are based on a predefined formula clearly linked to enterprise results.
- Each building block is a complement to, not a substitute for, existing pay systems.
- It is the explicit aim of the Building Block Approach to be used throughout the European Union and as such to be compatible with worker mobility both internationally and between enterprises.

c) ...and Overcoming Transnational Obstacles

At the same time, the Building Block Approach seeks to address transnational obstacles identified by the Commission and Parliament (European Commission, 2003a, pp. 17) as imposing barriers to the development of a European model and to cross-border plans for financial participation:

- By providing a broad incentive system going beyond the classical instruments of tax legislation, the modular approach neither relies on nor excludes tax incentives.
- In spite of the difficulty of implementing tax incentives, these still remain a powerful tool for enhancing and broadening financial participation. They could be voluntarily granted by countries singly or in groups, creating in the process an increasingly favourable environment. The pro-activism of countries with an advanced tradition like France or the United Kingdom would at the same time encourage others to emulate them.
- The PEPPER IV benchmarking across the EU provides the first ever complete overview of employee participation in all member and candidate countries of the European Union and thus facilitates the avoidance of transnational obstacles, for example, blocking periods when employees may not dispose of their shares.
- Our project, by providing information in a systematic way with reference to the experience of the EU-15, is also helping to overcome the cultural differences in the social partnership as well as raising the new member countries' awareness of employees.

VI. Summary and Recommendations

Jens Lowitzsch

The PEPPER IV Report presents conclusive evidence, regardless of data source, that the past decade has seen a significant expansion of employee financial participation in Europe. This is true of both profit-sharing and employee share ownership, although profit-sharing is more widespread. Against the background of the different genesis of PEPPER schemes in the old and the new EU member countries it is surprising, that the data examined seem to indicate that a West-East divide exists only with regard to profit-sharing. Throughout the European Union, the percentage of enterprises offering various PEPPER schemes is on the rise. Between 1999 and 2005, broad-based share ownership schemes increased from an average of 13 to 18 per cent and profit-sharing schemes from 29 to 35 per cent (weighted country averages for all countries included in both samples). On the other hand, 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.

Analysis of the legislative framework in the 27 EU members and the two candidate countries has shown that PEPPER schemes vary widely, reflecting the recent history of the countries under consideration and their different approaches and attitudes toward the role of employees. There are important differences between the former socialist countries and the mature market economies of the EU-15, and within the former group between those in which employees enjoyed a privileged position (such as the former Yugoslavia and Poland) and those which were managed along the more orthodox Soviet model (such as Czechoslovakia). The apparent difference in legal and political priorities between East and West stems from the fact that the first priority of post-socialist legislators was to change the socialist economic system through privatisation and re-privatisation; thus the development of PEPPER schemes does not necessarily represent a progressive evolution of their pay system or their work organisation process, as it does in the EU-15. A rare exception of legislation found in the majority of the countries under consideration are rules permitting joint-stock companies to acquire their own shares in order to transfer them to their employees, and to facilitate this acquisition with financial assistance. This phenomenon has its roots in the Second Council Directive on Company Law⁹⁵ and in the new

⁹⁵ See Art. 19 para. 3, 23 para. 2, 41, para. 1 and 2 of the Directive 77/91/EEC, dating back to 13 December 1976 which allow derogations from the European legal framework for joint-stock companies designed to encourage the financial participation of employees (see Part 3, Chapter IV, Section 3).

Member States, as part of the *acquis communautaire*, corresponding legislation was adopted in the context of accession to the EU.

In the past, the comparative analysis of the general attitude of governments and social partners has shown a lack of concrete policy measures supporting PEPPER schemes and limited interest both by trade unions and employers organisations in about half of the countries. Instead of being actively promoted as in some old EU Member States, employee financial participation in the new member countries has (with some exceptions) most frequently not been considered, or has been viewed with suspicion. During the last decade across the EU, however, a general, positive shift in attitude could be observed, with the number of passive countries decreasing to about a third.

Based on these principal findings of the PEPPER IV Report, suggestions for future initiatives, which could contribute to a more widespread diffusion of employee financial participation in the enlarged EU, are being made to the EU Member States as well as to the Commission.

1. Promoting PEPPER Schemes at the National Level

A growing body of empirical evidence⁹⁶ shows that financial participation can substantially benefit not only employees but also business enterprises and the national economy. This potential, however, remains largely under-utilised in most Member States, while financial participation within the EU itself is unevenly diffused.

– **The challenge: Legislating PEPPER Schemes**

In conformity with much of the Western experience, a major obstacle to introducing employee financial participation in the new member countries is the lack of specific legal provisions on employee financial participation offering specific fiscal incentives to encourage it. The absence of specific legal provisions may also account for the decrease in financial participation in those countries, which earlier utilised it as a tool of privatisation. Western experience shows that profit-sharing and employee share ownership are most prevalent in those countries which have legislated PEPPER schemes and offer a variety of well-designed tax incentives that encourage its use and spread. Therefore, the promotion of PEPPER schemes in new member and candidate states might well begin with action in the policy area.

– **Share Ownership Schemes: Developing a long-term perspective**

Given the prevailing economic conditions in Central and South Eastern Europe, the new member and candidate countries could discover that financial participation is even more important to them than to the EU-15. Although these countries introduced share ownership as a one-time incentive to employees during privatisation, they did not follow up with

⁹⁶ Financial participation has been statistically linked with greater productivity and with higher profits (profit-sharing, see Festing et al., 1999; share ownership, see Blasi et al., 2003). Furthermore, these effects appear to be strengthened by the presence of other kinds of employee involvement (Kim, 1998).

policies and measures that would make employee share ownership a permanent component of their new private property, free market economies. By contrast, a number of Western governments, as well as the EU itself, have actively promoted employee financial participation precisely because of its beneficial long-range effects.

– **Profit-sharing: Strengthen incentives and increase productivity**

Profit-sharing in particular, despite its limited diffusion in the new Member States in Central and Eastern Europe⁹⁷, is likely to play a more prominent role in these countries, stimulated by the rich experience of the EU-15 with these schemes. The need to strengthen incentives and increase worker productivity in the future should generate more favourable attitudes towards flexible remuneration schemes like profit-sharing. Furthermore, profit-sharing enhances loyalty and motivation among employees by ensuring them employment security in exchange for wage flexibility.

– **Internal versus external flexibility: Profit-sharing and flexicurity**

The political desire to reduce unemployment figures has led government to favour the process of entry and exit from the labour market and an ‘external flexibility’ model. Profit-sharing schemes are an element of ‘internal flexibility’ that allows wages to fall in a period of economic downturn thus allowing the employer company to maintain its margins by automatically decreasing its labour costs without reducing its labour force. Several studies show that profit-sharing can provide wage flexibility and employment stability. This is in line with the common principles of ‘flexicurity’ sustained by the European Commission and Council, among them ‘a better balance between external and internal flexibility’, ‘a climate of trust and dialogue’ and ‘a better workers’ adaptability capacity’. Thus, especially given the changes occurring in the world of work and the need to achieve internal flexibility (as opposed to external flexibility), profit-sharing can play an important role in the flexicurity approach.

– **Financial crisis, state intervention and participation**

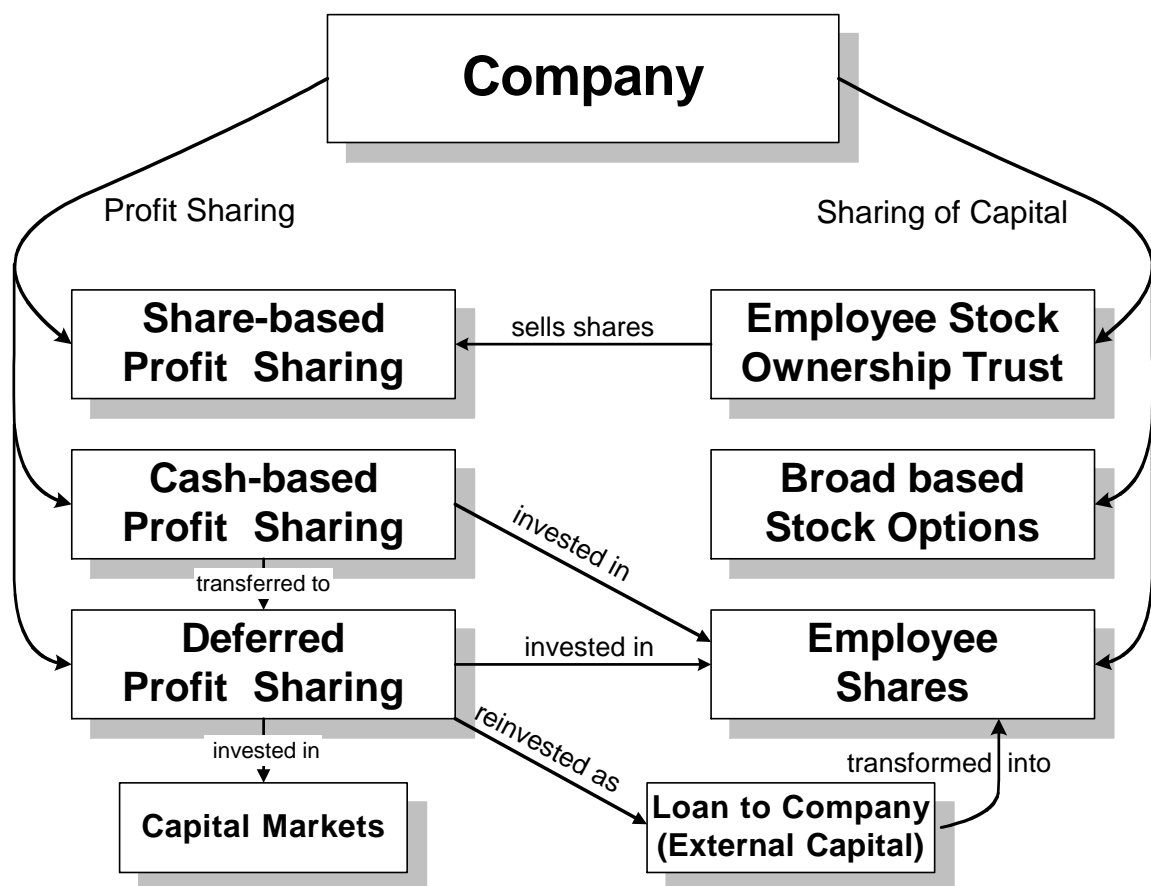
‘As we have been witnessing since late 2008, employees often bear much more than just a fair share of the pain in an economic downturn. Tools allowing them to share the gain when the financial results of their employer are growing are, apart from all other aspects, part of a basic fairness in the relationship between employer and employee. The development of such mechanisms therefore needs to continue’ (see foreword to this volume by Jean-Claude Juncker). In the context of the massive and unprecedented state intervention, one solution could be to increase employee financial participation in subsidised companies as a quid pro quo for state help. Subsidies to prevent bankruptcy as well as those that aim at stimulating the economy may, for example, be channelled through an Employee Stock Ownership Plan (ESOP) or a similar scheme. Furthermore, banks that receive state guarantees could be obliged to support financial participation of employees through their lending activities, for example, financing employee buyouts.

⁹⁷ In the early 1990s, the general economic conditions – recessionary trends, falling wages, low or negative profits – have not favoured the adoption of profit-related remuneration schemes. Changes in the area of labour relations have usually provided laws based on the standard wage employment contract, which together with rigid tax provisions, do not allow much flexibility in payments systems.

2. The Building Block Approach: Developing a Common Model for Financial Participation across the EU

The 'Building Block Approach' as a flexible platform model ideally meets the need to developing schemes at the European level in order to more actively support financial participation and overcome national differences in taxation policy. At the same time this framework both provides a broader incentive system and delineates what companies may do without inviting sanctions from regulatory, legal and taxation authorities.

Figure 18. The Building Block Approach



– Providing a broad incentive system with flexible solutions

A European model must be compatible with those existing models in the Member States. Relatively widespread in the EU-15 are profit-sharing schemes, stock options and employee shares. In countries with an Anglo-American tradition, for example, the United Kingdom and Ireland, but also in some transition countries, such as Hungary, Croatia and Romania, ESOP models are also found. The Building Block Approach reflects this diversity, while opening national practise to new forms of financial participation. The building

blocks consist of the three basic PEPPER elements:⁹⁸ (1) Profit-Sharing (Cash-Based, Deferred and Share-Based); (2) Employee Share-holding (Stock Options and Employee Shares); (3) Employee Stock Ownership Plans as Collective Schemes.

– **A future EU Recommendation: Implementing the legal foundations of a European Model**

The European Platform composed of the proposed Building Blocks could be framed as a Recommendation addressing the problem of national implementation by a recognition procedure by Member States. As a result of this procedure, each Member State would recognise individual elements of the European Platform as drawn up in the Recommendation to be the equivalent of a plan drawn up under its own laws and conferring equivalent benefits. This establishes a distinct legal entity for the chosen Building Block, which companies in those countries that decide on recognition can refer to.

– **Building on existing national legislation originating in the *acquis***

Given the above-described difficulties in arriving at a supranational compromise, the shortest path to a regulation at the supranational level, the simplest solution is to build on existing national legislation originating in the *acquis communautaire*. A rare example of such legal ‘common ground’ is found in some of the national rules on listed and unlisted joint-stock companies originating in the implementation of European Law, that is, the Second Council Directive on Company Law 77/91/EEC. Further investigation of other common existing regulations in this field is needed.

3. PEPPER Schemes for SMEs: Employee Stock Ownership Plans (ESOPs)

In addition to well known forms of financial participation (for example, employee shares and profit-sharing), the Building Block Approach introduces a lesser known but flexible form of collective share ownership: the ESOP. While, for example, share-based profit-sharing schemes have only one source of funds (that is, direct contributions from the employer company), the ESOP can obtain financing from such different sources as: (1) a loan from the employer company, a selling shareholder or a financial institution such as a bank; (2) dividend earnings; (3) sale of shares to its related share-based profit-sharing scheme; and (4) contributions from the employer company.

While share ownership generally involves additional risk for employees, the ESOP avoids this consequence. Although employees, as in other share ownership schemes, are encouraged to invest a part of their wealth in shares of their own companies rather than in those of other companies, thus concentrating rather than diversifying risk, there is this fundamental difference: ESOP debt is funded by appropriately timed contributions from the company to an employee trust (ESOT). Thus the scheme provides a benefit additional to basic wages. The employee’s salary is unaffected. Further, ESOPs motivate employees to

⁹⁸ For a detailed technical description of the different mechanisms and schemes, see Lowitzsch et al. (2008).

become more productive, while at the same time making enterprises more competitive.⁹⁹ Finally, there is an additional advantage to the company: shares are not sold to outsiders; thus, there is no risk of loss of control while the company itself remains local. This makes ESOPs an important tool for solving the problems of business succession in family-owned enterprises, one that strengthens bonds between enterprise and community, keeping jobs local and resulting in more wage income being spent at home.

– **Heads of family enterprises will be retiring en masse in the next ten years**

A recent Commission Communication from 2006¹⁰⁰ stated that with the aging of Europe's population, 'one third of EU entrepreneurs, mainly those running family enterprises, will withdraw within the next ten years'. This portends an enormous increase in business transfer activity, which could affect up to 690,000 small and medium-sized enterprises and 2.8 million jobs *every year*. It is anticipated that as a consequence of the new forms of business finance now coming into use, transfers within the family will decrease, while sales to outside buyers will rise. The entrance of international investors into what used to be primarily domestic markets will broaden the range of potential buyers for European small and medium-sized enterprises. This process is likely to threaten the successful regional structure of European (family-owned) businesses and will profoundly affect the European Community itself. This field of action was highlighted as a main objective of the Council Recommendation of 7 December 1994¹⁰¹. Recently the European Commission stressed the importance of ownership transfers to employees as a specific measure for facilitating business succession in SMEs.

– **ESOP as a vehicle for business succession**

A full or partial ESOP buyout provides an ideal vehicle to facilitate transitions in ownership and management of closely held companies. The ESOP creates a market for retiring shareholders' shares, which is of major importance to unlisted SMEs having no other ready source of liquidity. ESOPs may easily buyout one or more shareholders while permitting other shareholders to retain their equity position. This is a major advantage from the shareholders' perspective. At the same time, ESOPs give business owners the opportunity to diversify their investment portfolios without the costly process of going public. Furthermore, there is no dilution in equity per share of current stockholders since no new shares are issued and all shares are bought at fair market value. If the ESOP borrows money to buy shares, the company repays the loan by combining any dividend income of the trust with its own tax-deductible contributions to the plan. As the loan is repaid, a number of shares equal to the percentage of the loan repaid that year is allocated to employee accounts, usually on the basis of relative compensation. In this way, the ESOP creates a market for retiring shareholders' shares at a price acceptable to the owner - a

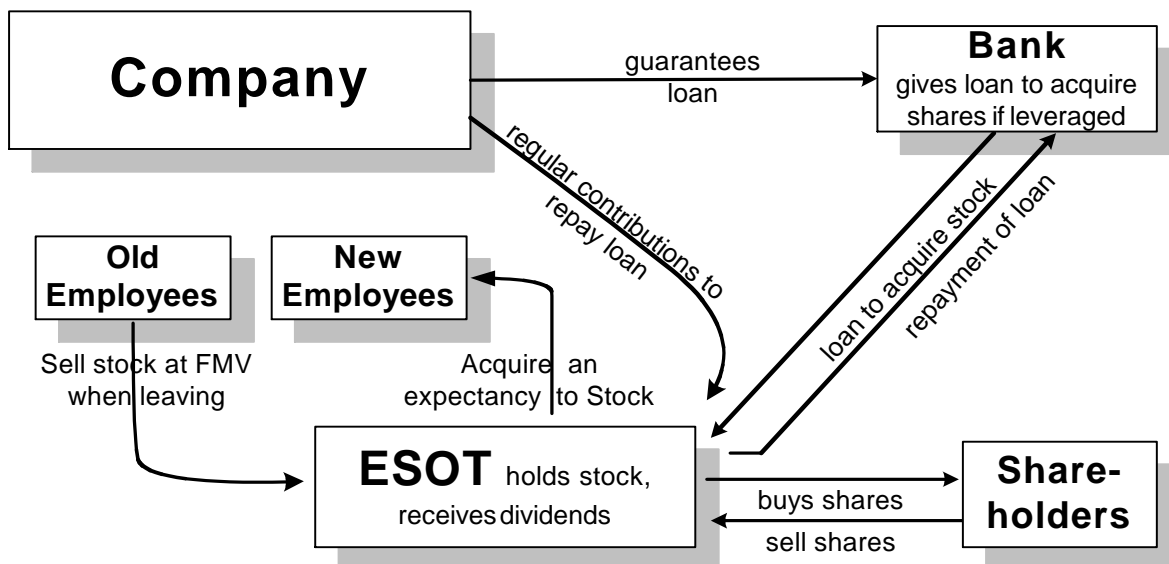
⁹⁹ For a recent, comprehensive overview of the positive economic evidence (in particular for ESOPs) see Blasi et al. (2003); they find an average increase of productivity level by about 4 per cent, of total shareholder returns by about 2 per cent and of profit levels by about 14 per cent compared to firms without PEPPER schemes.

¹⁰⁰ Implementing the Lisbon Community Programme for Growth and Jobs, on the Transfer of Businesses – Continuity through a new beginning, from 14 March 2006, COM (2006) 117 Final.

¹⁰¹ On the transfer of small and medium-sized enterprises, 94/1069/EEC, with explanatory note, Official Journal No. C 400, 31 December 1994, p. 1; reiterated in the Communication from the Commission on the transfer of small and medium-sized enterprises, OJ C 93, 28 March 1998.

market which otherwise might not exist. At the same time, when a change of control is appropriate, ownership is transferred to motivated employees who have a vital interest in the company's long-term success.

Figure 19. ESOP as a vehicle for business succession



Thus, the ESOP may be an attractive alternative to selling the business to outsiders, especially when there is a desire to keep control of the business within a family or a key-employee group.¹⁰² As a trusteed plan, the ESOP is designed to separate control over the shares in the trust from the 'beneficial owners'. The trustee exercises voting rights while the employees are the financial beneficiaries. The trustee may, in fact, be the very person who has just sold some or all of his shares to the trust. For smaller firms especially, it is much easier to contemplate a gradual transfer of ownership by creating a market for the shares of those who wish to sell at the present moment, while enabling those who wish to hold their shares to retain their equity interest permanently or at least until some later date. The result is the opportunity to gradually cash out without giving up immediate control.¹⁰³

– ESOP as an alternate leveraged buyout tool

The growing number of Private Equity firms targeting Europe's small and medium-sized enterprises¹⁰⁴ makes a comparison of an alternate leveraged buyout tool of immediate strategic importance. This alternate vehicle is the Employee Stock Ownership Plan. Al-

¹⁰² The ESOP may also be used to buy out dissident shareholders.

¹⁰³ Once the loan is paid off, of course, most companies make some arrangement for the presence of employee representatives on the plan committee.

¹⁰⁴ The part of LBOs in the total funds raised in Europe reached over 68 per cent in 2005. In contrast the amount of venture capital investments only represents 5 per cent (see PSE Socialist Group in the European Parliament, 2007, p. 69).

though the ESOP and the Private Equity fund have some features in common¹⁰⁵, the two markedly differ in one crucial respect: they benefit different constituencies and have different economic and social effects. The Private Equity buyout concentrates ownership of productive enterprises and the income they produce, while the ESOP broadens both the economy's ownership base and the distribution of income. The Private Equity buyout increases the wealth of its own narrow constituency, while the ESOP improves the material well-being and economic security of working people and their families. The Private Equity buyout is a short-term transaction aimed at restructuring and selling the target company to a third party that, in turn, may be just another Private Equity Fund. The ESOP is a long-term commitment, which ensures the continuity of the enterprise.

Quick profits for a few investment consortiums whose participants are already well-capitalised, or incomes rising over time for employees motivated by the ESOP to make their enterprises more profitable and competitive? This is the choice confronting the European Union as it prepares for a massive transformation of ownership of the business enterprises that generate its economic prosperity.

4. Promoting PEPPER Schemes through Tax Incentives

In spite of the difficulty of implementation at the European level (due to the exclusive jurisdiction of national legislation over tax law), tax incentives remain powerful tools for enhancing and broadening financial participation. This is especially true when they remain optional for the member countries and not subject to a unanimous vote of approval. Countries could voluntarily offer tax incentives singly or in groups. Such a step would create an increasingly favourable environment where countries having an advanced tradition, such as France or the United Kingdom, would encourage emulation. Optional preferential treatment as part of the Building Block Approach requires distinguishing between profit-sharing schemes, share ownership schemes and employee stock ownership plans.

- **Tax incentives are not a prerequisite to PEPPER schemes but they effectively promote financial participation where they exist**

On the one hand, financial participation schemes without tax incentives sometimes may have a higher incidence than those with tax incentives. Therefore, tax incentives are not to be considered a prerequisite to the development of financial participation. On the other hand, the experience of countries with a long tradition of employee financial participation as well as that of countries where tax incentives are quite recent, universally confirm their positive impact.

¹⁰⁵ The ESOP, invented in 1956, is the prototype leveraged buyout; the Private Equity form originated in the seventies to utilise tax advantages, which the US Congress had passed to encourage the ESOP.

- **Tax incentives should (and in most countries do) target those taxes which constitute the heaviest burden in the national taxation system**

The heaviest taxes are usually the progressive personal income tax and social security contributions. Many countries therefore provide: (1) exemptions from social security contributions for certain plans (for example, France, Belgium, UK, Ireland, Finland); (2) levying a capital gains tax (for example, UK and on dividends Belgium); (3) levying a special low tax (for example, France) in lieu of personal income tax, and (4) tax allowances for personal income tax (for example, Austria, Finland, Ireland).

- **Some forms of tax incentives are more favourable for certain types of plans and also lead to higher efficiency**

For share ownership and stock options as far as benefit taxation is concerned: generous valuation rules combined with a favourable taxation moment (often linked to holding period), and, if possible, exemption from SSC for both the employer company and the employee.

For dividends and sale of shares: a special tax rate or capital gains tax in lieu of personal income tax and, if necessary, exemption from SSC.

For ESOPs and Intermediary Entities: exemptions from income tax on share acquisition¹⁰⁶ or on share sale if the profit is realised after a holding period or within a retirement program; the company may qualify for tax relief on both interest and principal payments on the loan; sale of stock to an ESOP on a tax-deferred basis if the proceeds of the sale are reinvested in securities of other domestic corporations (tax-free rollover).

For profit-sharing: a special tax rate in lieu of the progressive personal income tax as well as exemption from SSC for both the employer company and the employee.

5. Informing Governments and Policy Makers about the PEPPER Initiatives

The development of financial participation schemes across the EU is strongly influenced by national policies, in particular by the availability of an appropriate legal framework, tax incentives and other financial advantages. As a result, different laws and sometimes mandatory rules in different countries often require specific forms of financial participation, forcing companies to tailor the design of an international plan accordingly. Here the EU has an important role to play in promoting employee financial participation throughout the newly enlarged EU. It could disseminate information and proposals on this subject as a continuation of earlier initiatives in this area.

In line with prior Commission activities, a Community initiative should launch an EU-wide, comparative, focused survey of financial participation. Since no cross-country data focussed on financial participation is available at present, the PEPPER IV benchmarking

¹⁰⁶ In Ireland this is the case only where the ESOP comprises an ESOT working in tandem with an Approved Profit Sharing Scheme.

is a compromise intended to cope with the existing data deficit without undertaking a new survey. There were inconsistencies between different data sources, which showed different scales of financial participation, for example, a much larger offer (CRANET) than the actual take-up rate by employees (EWCS). This discrepancy in the cross-country data can probably be attributed to diverse definitions and methodologies employed as well as a diverse emphasis of the surveys. To facilitate a discussion of individual country scores on different indicators vis-à-vis comparable scores of other EU members, and to obtain a reliable overall picture, a more comprehensive and consistent database is indispensable. The Commission should support additional research specifically designed to fill this gap.

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