



**Eurofi 2008 - Thursday
11/09/08 Session [4D]
FINANCIAL PARTICIPATION
AND EMPLOYEE SHARE-
HOLDING, ISSUES AND
PERSPECTIVES IN EUROPE:
What are the workers
expectations and company**

needs? How can long term retail savings (employee saving schemes, defined-contribution schemes...) contribute to financing retirement in the EU and to the european economy? Towards further convergence of european tools and players...

The Panel

Moderator: **Daniel Lebègue**, Co-Chairman, Eurofi

Panellists: **Elemer Terták**, Director, Financial Institutions, DG Internal Market & Services, European Commission

Ieke van den Burg, MEP, Member of the Committee on Economic and Monetary Affairs, European Parliament

Jens Lowitzsch, Assistant Professor, Inter-University Centre at the Institute for Eastern European Studies, Free University of Berlin

Augustin de Romanet de Beaune, Director General, Caisse des Dépôts et Consignations

Alain Leclair, Chairman, French Asset Management Association (AFG)

Philippe de Buck, Secretary General, BusinessEurope

Paul Maillard, Vice-president, FONDACT, French Specialist in Participation and Employee Stock Ownership

George Tuthill, Senior Business Development Manager, Computershare Investor Services and President, International Association for Financial Participation

The Debate

Moderator **Daniel Lebègue**, Co-Chairman, Eurofi, introduced the debate, noting that nearly 20 years after the first Pepper report, the promotion of financial participation and employee shareholdings was once again on the agenda of the European Union.

“The Commission, the Parliament, the Economic and Social Committee, recently announced a new initiative for developing financial participation. This movement is warmly welcomed by professionals of the financial industry and we are here today to discuss how to implement this project.”

Mrs Lagarde, the French Minister of Finance had also publicly supported the development of such schemes recently.

The objective of the discussion was to explain the main potential benefits of Financial participation for the different stakeholders, the issues faced at present and to define how to make further progress at the EU level.

I. Van den Burg, MEP, Member of the Committee on Economic and Monetary Affairs, European Parliament clarified the scope of Financial participation which comprises profit sharing in cash dividends and investment in the shares of the company by its employees. She explained that the EU Parliament had been supporting for many years the work done at EU level in the context of the Pepper reports. Some warnings were nevertheless expressed by the Parliament: shareholding or option plans solely invested in the shares of one company were riskier than diversified pension plan systems and should not represent a majority of the savings of company workers and ways should be found to involve employees in the governance of the company eg through work councils or broader employee participation.

Mrs Van den Burg also pointed out that taxation differences across EU member states were a major barrier to cross-border schemes for companies operating in several EU states and for mobile workers wanting to transfer financial participation plans. She therefore thought that DG Tax should be more active in engaging plans to solve these problems.

J. Lowitzsch, Assistant Professor, Inter-University Centre at the Institute for Eastern European Studies, Free University of Berlin, first summarized the major results of the Pepper IV report which benchmarks Financial participation across Europe over the past 10 years and assesses the attitude of social partners and the impacts of different tax regimes. The benchmark shows positive results with an increase of the % of firms offering various Pepper schemes: between 1999 and 2005 the % of companies offering broad-based share ownership schemes rose from 10 to 18% on average and the % of companies offering profit sharing schemes from 19 to 26%. The number of employees taking advantage of these schemes is also growing. But financial participation plans are only extended to a significant proportion of the workforce in a handful of countries. A new initiative would be required to improve this situation in accordance with the principles put forward by the EU Commission that financial participation plans should cover all workers.

J. Lowitzsch then commented on the link between financial participation and long term investment particularly in SMEs. He considered that developing an alternate LBO (Leverage Buy Out) tool possibly based on ESOP like vehicles (employee stock ownership plans) similar to those used in the US was of strategic importance for the EU to facilitate successions

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in European SMEs. 1/3 of EU entrepreneurs, mainly those running family businesses, will indeed retire within the next ten years, representing around 690,000 SMEs which could affect up to 8 Mio jobs per year. Developing such tools would be a way to avoid many companies being sold to foreign investors and to make sure the income of these companies remains in Europe. The proposal was made to the Commission by the team in charge of the Pepper report to develop a European ESOP like vehicle applicable across EU Member States that would refer to the main legal traditions existing in Europe. This initiative gathering 15 partners from more than 10 countries has the support of the Economic and Social Committee. He concluded by stating that he believed the conditions for further development of financial participation of employees in Europe were there and wished that Eurofi and the Ecofin took an active role in this enterprise.

E. Tertak, Director, Financial Institutions, DG Internal Market & Services, European Commission focused his intervention on the issue of the regulation of pension options and particularly occupational pension funds which is at present being debated in the context of Solvency II. Rules need to be defined, according to E. Tertak, to ensure that pension funds are safe enough and are able to provide stable revenue in the long term.

The Commission is trying to define the most appropriate way to ensure this through a prudential risk oriented regulation and to maintain a level playing field between occupational pension funds and other companies eg insurance companies providing pension products. A document was published by the Commission this week. He concluded by saying that the Commission was looking seriously at the pension matter to try and solve the problems arising from the present landscape which is fragmented with different pillars and different regulations.

A. de Romanet, Director General, Caisse des Dépôts et Consignations started by stressing the importance of financial participation from a social, economic and political point of view but regretted that this issue was not better known and taken into account in present EU policies, maybe because of its complexity. EU institutions had been discussing this issue for many years without being able to reach an agreement. Financial participation indeed has many positive features: it improves the purchasing power of workers, contributes to future pensions, better involves employees in the conduct of companies and can potentially strengthen the capital base of corporations and the development of SMEs. He then explained that the Caisse des Dépôts et Consignations strongly supported this concept considered as a major driver of the economic development of Europe and of its companies and a "modern response" to their challenges. Financial participation can indeed:

- Enhance the competitiveness of EU companies: studies show that companies with ESOP type plans perform better and financial

participation can help to strengthen the European roots of companies

- Contribute to bring the benefits of globalization to EU workers and to better accept it
- Help to cope with issues raised by the ageing EU population.

The challenge ahead is to renew the interest for this subject in the EU. This requires a debate at the EU level involving all the economic and social stakeholders. It also requires comparing the different national experiences to identify best practices. Many European countries indeed have a strong tradition of financial participation and some of them have recently introduced new bills: France, the UK, Belgium, Ireland, Finland, Austria, the NL, Germany... The French system introduced in 1967 and recently extended to SMEs for example is well developed and benefits to more than 5 Mio workers at present. But the objective should not be to promote a specific system since all of them have advantages and drawbacks.

A. de Romanet considered that the EU calendar was favourable for relaunching the topic of financial participation and concluded by quoting some words of General de Gaulle: "Our civilization must build a system that governs human relations so that everybody shares the fruits of the enterprises to which they contribute their efforts to and so that they enjoy the dignity of being responsible for their part in the success of the collective effort on which their own destiny depends".

A. Leclair, Chairman, French Asset Management Association (AFG) thought that the Parliament and the Commission could agree in the coming months on launching a strong initiative around financial participation at an EU level if all stakeholders worked together. Defining a common target among many different stakeholders was indeed the main challenge. One point that was striking was that there was no political debate about financial participation. It was a "trans-political matter" cutting across political parties as illustrated by the support brought in France to such proposals successively by L. Fabius (member of the socialist government) and F. Fillon (French right wing Prime Minister). It is therefore a complex but feasible objective.

There are many supporters of these schemes according to A. Leclair. Employees (eg in France more than 5 Mio people benefit at present from this system and 5 Mio additional workers could be covered if it was extended to the public sector), but also large corporations operating within and outside Europe. Many companies indeed want to reinforce links with their employees working in different countries by putting in place common profit sharing or company share ownership schemes. But solutions must be found as mentioned previously to reduce the complexity of putting in place such systems for the company management and to facilitate the transfer of financial participation plans across Europe for mobile workers. The respective merits of employee shareholding and profit sharing should

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also be closely considered: shareholding by employees is very positive but company saving schemes also increase the commitment of employees towards their company.

A. Leclair considered that developing financial participation should be a priority of the Commission in the coming months. One of the potential difficulties to be overcome is that several DGs need to be involved (DG Markt, DG Social affairs, DG Enterprise...). He concluded by saying that there was an urgent need to improve the situation at a European level with a strong interest expressed by the different parties involved. He was very eager to work with the group Eurofi would put together at the EU level to deliver some guidance and suggestions on this issue.

Ph. de Bück, Secretary General, BusinessEurope explained that Business Europe represented all businesses across Europe and had national confederations as its members. He shared the views of A. de Romanet and pointed out a certain number of issues that should be taken into account in the debates around financial participation.

The increasingly global scale of economies and of labour markets, especially for executives should be considered. The EU is indeed facing demographic challenges not only related to pensions but also to the need for sufficient and skilled workforce, which is necessary to maintain growth in the economy and transform EU economies into knowledge-based economies. This requires new HR management approaches, which can be supported by financial participation plans in particular, to attract and retain employees and also to make sure they participate in the activities of the companies they work for and prepare adequately their retirement. There is also a strong push within SMEs, which are becoming increasingly private equity companies, for results and performance and remuneration systems encouraging employees to participate in the results of the company which can also be facilitated by financial participation. A positive feature of Financial participation systems is therefore that they contribute to making workers participate more actively in the capitalistic system, which is the basis of the EU economic system. This of course requires also dealing with the difficulties created by possible downturns of the economy.

Finally the cross-border issue is very important according to Ph. de Bück. There is indeed an ethical issue involved when it comes to remuneration since advantages should be provided in a balanced way across the company. Most significant EU companies being cross-border in one way or another at present must face up to 27 different tax systems, social security systems or labour relation systems. Finding ways to solve this is a priority, without necessarily going towards harmonization or regulation, particularly in the fiscal and social areas which require unanimity.

There are two major issues to be solved for cross-border companies:

- Reducing the administrative burden and costs of companies facing many different systems
- Facilitating the free movement of workers and companies across Europe particularly with the issue of the portability and comparability of rights.

Ph de Buck concluded by saying that financial participation and complementary pension systems were major drivers of the performance and growth of EU economies in terms of developing entrepreneurship in particular which was less widespread than in the US in particular and should therefore require specific attention in the coming years.

P. Maillard, Vice-president, FONDACT, first explained that FONDACT was a not for profit association dedicated to the development of financial participation in France and abroad. He agreed that financial participation was very positive both for companies and for workers and required to be promoted in Europe as an unparalleled incentive for workers and management alike. The concept was first developed in the US, the UK and France. One of the most important contributions of financial participation, according to P. Maillard, is to help building stronger economies through a more active involvement of workers in their company.

He recalled the objective defined by the Commission in July 2002 to develop financial participation in Europe as a significant contribution to achieving the goals set during the Lisbon summit.

Among the actions proposed by the Commission he thought a particular focus should be put on "European convergence" to solve the cross-border issues pointed out by the previous speakers and recalled the two main options underlined in 2004 in the report of the expert group requested by the Commission and steered by JB de Foucault:

- Creating a new optional EU system, a 28th regime, applicable to all 27 EU countries. A system that respects this framework would automatically benefit from all the economic incentives offered by the countries where the plan is put in place. This system could propose potentially different options or features enabling firms to adapt to the context of the different member states.
- Favouring mutual recognition through which a plan set up by a EU company respecting a given country regulation could apply automatically to all its subsidiaries and workers without any modifications required.

G. Tuthill, Senior Business Development Manager, Computershare Investor Services and President, International Association for Financial Participation explained that the IAFP is a worldwide organization promoting and facilitating the introduction of financial participation and

has recently been supporting Central and Eastern European countries eg Slovenia in the development of financial participation schemes.

He agreed with many points developed previously. Many companies recognize the benefit of sharing their wealth and success with their employees. This is an incentive for employees, a good way of further stimulating the development of companies and more broadly of making economies more productive without increasing their cost base. Still there is a need for governments to remove barriers to employee financial participation through consolidation of tax legislations and regulations and a more adapted administrative environment.

Legislation indeed acts in some cases as a negative impetus. For example following the introduction of the Prospectus Directive some employees are unable to invest money in their own company shares. G. Tuthill therefore considered that EU governments need to reconsider their approach to these issues, simplify rules and bring together more practices existing throughout the EU.

He then highlighted different points that are important in the employee financial participation debate:

- Education and research are important issues. More education is needed. Research would also help to better understand why some companies had not introduced financial participation schemes.
- Best practices. G. Tuthill considered that performance related rewards could be considered as best practice. For broad based employee financial participation, best practice would be a performance related bonus with potential measures from corporate performance, divisional team performance and personal performance. The performance objective should be measurable and objective, easily understandable and achievable. Some US multinational in particular are going in this direction.

He considered that share ownership was the fullest form of participation since the share in capital creates a powerful and enduring company / employee link with employees becoming a strong part of the company life and investors there for the long term. Several countries have for example developed pension plans linked to employee share systems and with tax relief eg the UK. However this greater involvement goes hand in hand with greater risk taking with the possible fluctuation of share values. He therefore recognized that a certain level of diversification was required to avoid employees "putting all their eggs into the same basket" and that ways of overcoming this and helping people should be proposed.

G. Tuthill considered that profit sharing was "capitalism in its best and truest form" with profits continuing to be made but with those making the profits sharing the rewards. He concluded by stressing that employee financial participation would contribute to the objective of making Europe

the most competitive and dynamic knowledge based economy in the world by 2010 and was very much in favour of stimulating discussion and promoting research about employee financial participation.

A representative of the CFDT, the French trade union, explained that the concept of financial participation which consists in providing advantages either through profit sharing or employee shareholding in addition to the salary had existed for a long time. This additional remuneration had positive characteristics: it obliges employees to follow more actively the evolution of the company they work for and should lead them to be more involved in the conduct of the business. On the other hand the rights of the employees should be preserved and this additional remuneration should not impact the base salary of employees and make them bear an exaggerated entrepreneurial risk. Trade unions are not against these systems so long as this is preserved.

P. Bérès, MEP, Chairwoman of the Econ Committee of the European Parliament who was in the audience said that her main concern was to make sure that the right balance was struck between the right economic policy and the smooth running of the financial markets. She considered that employee financial participation was an important topic to be raised for EU financial markets and thought that it should be quite high on the agenda of the next European Parliament. She considered that three topics particularly important were to be looked at:

- Governance and the issue of employee participation in boards of companies that have put in place financial participation schemes
- The role of employee financial participation in fighting short term activism in the capital of companies in the context of the debates around private equity, hedge funds or sovereign wealth funds... Employees have an interest in preserving their working tool and company, although they cannot be expected to keep their shares in all circumstances.
- The possible role employees could play in the oversight of the strategy of pension funds they invest in with pension funds potentially making decisions that could go against their interests.

A certain number of additional remarks were made by the speakers and participants in the audience relatively to the fiscal treatment of financial participation and to the risks associated with these schemes.

Dr Kees Vos, President of EFES (European Federation of Employee Shareholding) insisted on the importance of the fiscal advantage and hoped that EU countries would make serious efforts to go towards a common fiscal approach. He also thought the Commission could be more cooperative in lifting unjustified barriers and should work in closer cooperation with the associations promoting financial participation to do so.

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Charles Cronin from the CFA institute commented on the risks associated with employee financial participation schemes with reference to the Maxwell Communications case and the related corporate governance issues.

J. Lowitzsch agreed that there were risks associated with these plans but this depended on the type of scheme and on the amount of money invested. He thought that the key question was whether employees invested their own money in the scheme or if investment was made on top of their salary. He gave the example of US ESOPs which do not impact the salary and where employees do not lose any money even if the company runs into difficulty, contrary to share purchase plan where employees invest their own money with a matching contribution. **I. van den Burg** thought that a reinsurance concept would be possible to mitigate risk with a collective system funded by the share plans of different companies to back financial participation schemes up to a certain level of investment.

Ph de Bück was pleased to hear the big interest expressed for financial participation by the different participants in the panel despite the variety of systems across Europe and considered there was room for work for

Eurofi. Responding to some remarks made previously, particularly by the trade union representative he explained that financial participation had never been considered by companies as an alternative or substitute to regular remuneration. He also argued that issues had to be addressed step by step. The priority was facilitating the setting up and management of financial participation plans for cross-border companies and their use by mobile workers. A 28th regime could be a solution but would probably not solve all problems. He also thought that questions around corporate governance or a broader participation of employees in boards should be addressed separately.

D. Lebègue concluded by pointing out that this had been a very fruitful discussion with a strong consensus among the different stakeholders and political will expressed at the EU level. There appeared to be strong commitment in major EU countries such as UK, Germany, France. He therefore considered the conditions were there at the EU level to promote a new initiative favouring financial participation and announced that Eurofi would work in the next months to facilitate the decision on a European package for this question with a representative panel of stakeholders.

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