THE ROLE OF GOVERNMENTS (AND SOCIAL PARTNERS) IN PROMOTING FINANCIAL PARTICIPATION

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Abstract

In article we can submit a proposition, that key influence on nature and range of financial participation exert fiscal and legal frames set up by central authorities, what can be confirmed by results of sectional and national research of financial participation carried out from 1990. What should be underlined, that it is not only a matter of regulation of status of participation programs in labor law and tax system, but it is also connected with company law, capital market, issue of stocks, admittance of financial tools to public turnover, with accountancy rules etc. For example, thanks to legal regulations of relating issue and of purchase of stock by companies, in Germany in 1998 the limitations relating to use option on purchase of stock were suppressed one did away {one put to death} what permitted to German companies to use this tool in financing of firms' growth, in spite of a lack of legislative initiatives and tax encouragements. In Italy, the reforms of corporative governments (e.g. greater protection of smaller investors), became the key factor in further development of financial participation based on share-based financial participation.

1. Introduction

Progress in all areas of functioning of companies, the necessity for satisfying increasing needs of society, growth of competitiveness, will for sustaining the present level of economic growth require changing point of view on previous relation between employees and management. Moreover, they also need changes of work relations and attitudes, which have been stopping all the initiatives up till now, or at least discouraging from engaging workers in the process of production. Therefore, financial participation schemes, which are introduced, are about to include workers in the life of an organization, help to develop mutual engagement, in delegating rights and direct communication within a company. However, implementation of schemes is not possible without an active participation and engagement of key political and social parties which include conferences of trade unions, workers` organizations and government departments. In this case, some steps are taken mainly at state level (although it also comprises activities at self-government level), and it seems that

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organizations at this level have the greatest influence over creating schemes of participation and just legal regulations in this range.

Initiatives which have to broaden financial participation of employees were one of the most significant operations in the context of managing of human resources in the 1990`s. The cabinet of the European Union issued in 1992 a document entitled *Council Recommendation*, in which other countries were called on to take measures promoting implementation of financial participation. This recommendation forced the member states to introduce legal regulations which would make it easier to create various schemes of financial participation and appropriate tax allowances on this grounds (European Council 1992: 53-55).

A recommendation from 1992 was based on the PEPPER report, i.e. "Promotion of Employee Participation in Profits and Enterprise Results"[1]. This report summarized the range, main characteristics and results of participation in profits and participation in properties in countries belonging to the European Union and it proved that, there are significant differences in this field between the member states. In some of the countries, especially in the United Kingdom and France, the schemes of financial participation were quite commonly used and supported by long-term legislative decision, whereas in other countries this phenomenon occurred seldom. In the 1990`s the interest of implementation of financial participation was present in almost all the member states of the European Union. New legal solutions were introduced i.a. in Germany, Ireland and the Netherlands. Active discussions about the role of schemes of participation in property of results of a company (employee share ownership) were especially applied in Belgium, France and Germany. The governments of other states, i.a. Spain and Italy, also supported new participating solutions calling on social partners to introduce the schemes of financial participation (Poutsma 2001).

Apart from legal stimuli and fiscal stimulation, a liberalization of capital markets and changes in systems of corporal governance in some of the member states influenced over the growth of interest in solutions concerning share ownership. The essential element was also the introduction of more flexible scheme of employees` remuneration, which lowered the level of promoting financial participation.

The basic element of the article is an attempt to show the influence of government organizations and central social organizations over the range of financial participation – at company level however, to fully understand the character of functioning related to financial participation at first we have to

[1] The report takes also into account participation in company capital; PEPPER Report, The, *Promotion of employee participation in profits and enterprise results,* Social Europe, Supplement 3/91, Commission of the European Communities, Office for Official Publications of the European Communities, Luxembourg 1991

determine what role these organizations play at the state level in developing financial participation.

In this study there is an attempt to achieve answers to a few crucial questions: do governments of individual countries, associations of trade unions and workers` organizations have strictly determined philosophy or strategies concerning financial participation and if these strategies promote or limit the application of financial participation? What are the potential advantages and disadvantages or deficiencies of financial participation? What kind of efforts are made organizations, mentioned above, to promote or limit the development and application of financial participation? What obstacles can occur in the further development of financial participation schemes and their implementation?

2. The role of governments in promoting financial participation – general characteristic

The interest in financial participation in the European Union has increased during the last several years. Starting from 1990, at the European Union level a number of incentive initiatives have been taken to encourage creating financial participation schemes. Detailed data about this are presented in, already mentioned, the PEPPER report prepared by the European Commission in 1991. In the same year the Cabinet of European Union designed recommendations about promotion of financial participation (European Commission 1991), (Uvalic 1991). One year later a statement issued by the European Commission was presented, which called on the member states to take some steps concerning promotion of financial participation (European Commission 2002). An active role was also performed by the European Parliament, which tried to support initiatives concerning creation of participation schemes through emphasizing the benefits from financial participation.

The most of initiatives which stimulate creation and implementation of participation schemes were taken at the beginning of the1920`s. For example, Belgium adopted new regulations about profit sharing and share ownership; France introduced new laws promoting financial participation in small and medium companies; The Great Britain introduced two new sharing schemes; and Germany took some steps to promote employee share ownership and to reform the current company law which would make it easier to apply share options. In Italy there were changes in company law thanks to which new opportunities for financial participation schemes appeared. It was declared that more understandable legal framework should be created for employee share ownership (Blanpain 2002; see also Mormont and Léonard 2003; "Incomes Data Services" 2001a, 2001b; Weiler 2002; Biagi and Tiraboschi 2002; Limardo and Paparella 2003).

In the literature concerning financial participation it is pointed at three main forms of financial participation: profit sharing, employee share ownership and employee share options (Armstrong 2000), although other authors present different classifications for example, they distinguish four groups of employee participation schemes; cash payments, deferred profit sharing, savings scheme and profit sharing dependent on results (Jacukowicz 1999; see also Poustma 2001; Jędrasik 2007). Of course, these groups are connected with each other, because for example savings scheme on purchase of stocks can be deferred, savings, and based on participation of employees in company capital (Poutsma 2000). The European Commission ("Communication..," 2002), however, distinguished financial participation into "profit sharing" (among the representatives of "capital" and "labour" in a given company) and "employee ownership", whereas schemes which use options are a different kind for the European Commission (because not necessarily they imply a real share ownership of a company)[2].

In this study we present a thesis that the crucial influence on a nature and range of participation is exerted by a fiscal framework and legal regulations of central authorities, which is proved by the result of the most of cross-country researches about financial participation schemes which has been carrying out since 1990 (Uvalic 1991; see also "Profit-sharing in OECD countries" 1995; Vaughan-Whitehead, et al. 1995; "Report from the Commission: PEPPER II: Promotion of Participation by Employed Persons in Profits and Enterprise Results" 1996; Poutsma 2001). It is worth noting, that not only the regulation of a status of participation schemes in the labour law and fiscal system is concerned, but also matters connected with company law, capital market, issuing securities, allowing fiscal instruments to public trading (for example, the legal status of options), regulation of accountancy, etc. For instance, in Germany in 1998 owning to legal regulations of issuing and purchasing shares by a company, the limitations concerning applying options on share purchase were abolished, which allowed powerful German companies to take an advantage of this instrument in financing the development of enterprises, in spite of the lack of any legislative initiatives and tax allowances. In Italy, reforms concerning corporal governance, that is bigger protection of small investors, became a crucial factor in the further development of financial participation based on share-based financial participation. Moreover, the governments of different countries act according to various premises in their policy towards the schemes of financial participation. These can be aims connected with the policy of employment, substitution of payments, flexibility and range of payments, pro-

[2] An employee can have an opportunity to collect a just profit from options (a difference between a price resulting from options and a market price) in the form of cash, or to resell the shares right after taking possession of them during executing options.

investment, redistribution of incomes (to level a disparity of incomes), long-term savings[3], growth of employee`s participation in company business, etc. Promoting the idea of employee participation can also be signed in the logic of political schemes.

We can suppose that the mentioned aims of government can influence over the company business through:

1. Legislation and connected legislative instrument, supported by fiscal initiatives. Separate legislation concerning financial participation is not the only instrument owning to which governments can influence over applying financial participation: stock exchange law, labour law, and general taxation system can also influence over a shape of financial participation. In some cases there is a need to apply changes in existing law to promote the development of participation.
2. An influence of the ideology and outlook of a government, which can shape a general attitude towards financial participation.
3. Strategies of enforcing laws. At a central level it seems important not only to enact legal framework of participation (and let the way of putting it into practice to companies), but also more active participation of a government in applying the legislation.

The crucial influence over the range and nature of financial participation is exerted by legislative framework, which results from the policy and government`s attitude towards the problem of financial participation. Activities at a company level are also shaped from below by "business systems", which comprise i.e. the issue of accountancy standards, agreements within the corporal governance and ownership structures which have got very important meaning. Social partners can also have got the influence (direct or indirect) over the shape of financial participation at a company level.

Direction of influence can be different. Trade unions as well as employers` organizations can also, in some way, shape or direct the government ideology and policy in matters concerning financial participation. It is certainly connected with their being engaged into promoting or limiting different kinds of participation solutions. Social partners` ability to influencing over a government fundamental orientation in the case of financial participation will be dependent on how close the relations between different partnership organizations and political parties are. The crucial circumstances in this case are the presence of tripartite organizations at the state level and a range and relations between social partners` organizations and political parties (or even membership of members of these organizations in political parties) The activity of social partners can result

[3] In a „cash based" scheme an employee can (however it is not obligatory) at the beginning allocate a given share in profits for consumption, whereas in deferred schemes due shares for a longer period of time are, from the point of view of economy, savings of households.

from government legislation or regulating initiatives. It can be described as a reactive approach, which may be manifested as attempts to obstruct government initiatives concerning the promotion of participation solutions or attempts to change some propositions presented by a government. Social partners can also influence over taking participation initiatives by the means of collective labour agreements at the state or sectoral level. This influence is mostly dependent on whether and in what degree financial participation will be a part of collective labour agreements mentioned above. Trade unions and employers` organizations can also have direct influence over a shape of participation solutions through specific relations with companies and their workers, which will be dependent on i.e. a range of collective bargaining at the company level and a range in which financial participation is a part of these bargaining agreements.

Apart from authorities and social partners the influence over the range and participation schemes also is also made by factors connected directly or indirectly with companies and conditionings of an external nature. As far as only companies are concerned we can also include in the factors: the organizational culture (Hofstede 2000), types of running activities, organizational structure, management system, size of a company[4], etc. External factors are, for example, trends connected with globalization (foreign investors who use participation in their companies can encourage other companies to do the same thing, or even lobby for appropriate legal reforms), the development of capital market, or a situation on the labour market.

The importance of influence of factors connected with companies` behaviour and external environment depends mostly on activity of organizations associating employees and employers, trade unions, branch agreements, etc. These organizations can influence over government`s decisions, however in real life they limit only to bargaining at the employee-employer level and they are rather passive beneficiaries of government policy. In fact, a government also decides about results of employee and employer bargaining, of which businesses are not really convergent. It can, for example, make some of its decisions obligatory (compare with France), but most of all it influences over a subject of bargaining (for instance, tax allowance can be more attractive so that employees may want participation even though it may bring about some risk connected with some of its forms). Of course the differences between countries are also caused by tradition and culture.

[4] Some participation schemes are better to introduce in big companies, because it is connected with high overheads or they rather seem cost-effective on the assumption that we will reach a scale of a large employment rate.

3. Employee financial participation in selected European countries - legislation

Countries which are going to be the subject of study has been selected in such a way to include countries where financial participation is mostly promoted and supported by authorities (France, the Netherlands and Great Britain), countries with medium range of central initiatives on for the benefit of financial participation (Germany and Belgium) and others where little decisions are made in favour of participation at the central level. One of the criteria is also a differentiation of participation forms.

3.1. Belgium

Employee financial participation has been regulated in Belgium law relatively recently, though initiatives in this field has been taken since the end of the 1980`s (Mormont and Léonard 2003). A crucial importance for the development of participation had two reforms: in 1999, which regulates legal problems concerning options and in 2001 which concerns employee share ownership and profit sharing. Since 1999 value of options subject to taxation has been estimated when options are given to an employee and not when options are executed[5], however social insurance premiums are not deducted from an income gained from options. The law does not limit a number of options which an employer can offer to an employee or even possibility to choose a group of workers to which options will be given. Other tax allowances are also expected depending on a period of possessing share by an employee before possible resale.

A bill of 2001 concerning employee share ownership and profit share schemes had to sort out the rules of financial participation. The main element of the bill is the tax allowance scheme (especially advantageous in case of schemes based on employee share ownership). Moreover, the bill states that participation cannot be a substitute of a salary which means that it can only be a bonus which is added to a company remuneration scheme. Additionally, a bill of 2001 allows collective managing of employees` shares (a form of employee co-operative), and also introducing in small companies deferred profit sharing scheme in the form of savings fund which would invest money. Moreover, an interesting solution is to assign part of current taxes from incomes of participation system by Belgium government (for instance, taxation of employee options) on

[5] Value of employee options raises together with a growth of value of basis instruments (in the case of using options in participation schemes the shares of employer`s company are basis instruments) so that while executing options it is higher than when it is issued (of course when the situation is advantageous in the case of share value)

compensation of losses in the social security system caused by excluding benefits of participation from obligation to pay a premium (Blanpain 2002)[6].

3.2. France

France has got a broad system of legal and fiscal regulations determining the rules of employee financial participation (Schmidt and Regnaud 2002). In France among applied forms of participation the most common is profit sharing in two forms: deferred (called just participation) and cash based (interessment). The first form is obligatory for companies which employ more than fifty workers. Profit sharing is done according to rules stated by the government (the authorities set up such a system) or according to rules negotiated by collective labour agreement. A share in profits given to an employee is paid into RSP fund (reserve speciale de participation). For holding his funds on the RSP account for at least 3 years an employee can make a use of tax allowances. The second form is not obligatory. It has a form of cash bonus of which amount can be dependent on different indicators of efficiency of company`s progress, and not only on the profit. There is a possibility of participating in company savings scheme (saving funds which are given to an employee within the framework of bonuses from funds on the account of specially created fund), for participation in which employees can benefit from tax allowances. Introduction of such a scheme in a company may be done only according to an agreement with trade unions, the representatives of trade unions at the company level, works councils or on the basis of the majority of two-thirds of all employees in a given company.

The crucial elements of participation schemes present in France are employee savings schemes. Such schemes can be prepared by employers through their own initiative or in an agreement with representatives of trade unions, works councils or the majority of two-thirds of all employees working in a company. Participation of employees in savings schemes is on voluntary basis and employee`s premiums go along with premiums from the employer (these can be premiums dependent on the amount of income). Such funds form so-called *Fonds Communs de Placement d'Entreprise* (FCPE) that is company investment fund. FCPE is assigned to buy participation units in investment funds (usually mixed, diversified) or shares of copmany-employer. In France thanks to assigning FCPE to purchase employee`s shares (it is a coommon condition in case of almost half of existing FCPE) the capital form of employee financial participation became more common (Incomes Data Services London 2001a).

[6] More details concerning taxation of shares can be found in the PWC report for Directorate General for Enterprise, 2002. The report concentrates on the fact that option schemes are usually intended for directors and managers, but at present they are commonly used in bigger enterprises in Belgium

Capital participation is also supporte by the law: recently, there has been introduced a new legal requirement concerning increase of the pool of available shares to buy by FCPE during each increase of the company capital if the share of emlployee owneship in a company is less than 3%.

As far option schemes are concerned they are not popular, even though the transactions with the use of these financial instruments have been regulated in French law since 1970. Until recently companies have been giving options only to the representatives at the highest level of management. However, recently there have been introduced tax preferences for granting options, including allowances for employees who after executing options (taking possession of company shares) for appropriate long period of time do not get rid of their shares. It favours the development of employee share based schemes (Schmidt and Regnaud 2002; see also Rojot 2002; Mabile and Fakhfakh 1997).

3.3. Germany

In Germany financial participation means most of all employee`s share in company`s capital (capital participation) (Weiler 2002). There is a conceptual difference between this form of participation and the idea of profit sharing, however in practice employee`s share in capital is usually connected with share in profits. In most of German companies the employer puts up a certain amount of money for a worker each month and sometimes an employee decides to increase a saved amount through deducting a part of his salary. These funds are assigned for different kinds of investment, of which possible range is listed in the bill. An employee can take an advantage of tax allowance with reference to saved income and if these savings are assigned for capital investments he can also be given a bonus which is paid out by the government. Tax benefits which encourage to save were about to motivate people who earn little to save means for the future, however after the last reform which increased a threshold allowing to use the tax allowance, it is used by most workers. Government savings bonus encourages to allocate savings for capital investments and since 1999 its structure has favoured the purchase of stocks and shares by employees (because the amount of bonus in dependent on type of investment).

Participation schemes based on options began to be introduced only after liberalization of regulations concerning the control over the market in 1998. In 2002 the capital income tax was decreased that is why we may expect the growth of interest in this form of participation. Schemes which are based on options need approval from workers council. Such schemes usually refer to possibly broad group of employees (they are not confined to e.g. only management) (Senne 2002; see also “Incomes Data Services” 2001b; Carstensen et al. 1995).

3.4. Italy

Italy did not develop legal solutions to financial participation, even though we can observe that since the beginning of 1990`s there has been increasing interest in this matter (Limardo and Paparella 2003). The constitution of 1946 gives employees the right to co-participate in managing of a company and access to capital investments in the main branches, however this rule does not represent any particular legal rules. Just in 1996 a percentage of changeable part of remuneration was excluded from the duty to deduct premiums on social security. Tax allowances for shareholders of a company were also introduced but they were applicable only if for three years they would not sell of their shares. Employee options are subject to income tax when they are executed. The basis of taxation is a difference between a price of execution of options and a current market price of a basis instrument. The reforms of Italian company law means a stimuli to take up steps to promote employee financial participation, however any particular solutions have not been developed yet (Biagi and Tiraboschi 2002; see also Tiraboschi 2002; Boca et al. 1999: 9-50).

3.5. The Netherlands

Just as in France and Germany the crucial role here is played by employee savings schemes (Poutsma and Voets 2002). In 1994 two types of such schemes were introduced. The first one, called bonus scheme, is based on the fact that an employee assigns a part of his net pay for the savings fund and an employer put asides the same amount for him. In the second type of the scheme savings premiums are paid totally by an employee to the amount of fixed percentage of his gross salary. In both cases if an employee withdraws saved amount of money after four years of joining the programme, it will be exempt from taxation.

In the Netherlands there are also option schemes which are functioning apart from employee savings fund systems. They are subject to two different fiscal regulations however the right to choose a way of taxation is given to an employee: before 2001 the tax duty emerged just when options were issued and now it is possible to pay the tax when options are executed ("Incomes Data Services" 2002).

3.6. Portugal

Portuguese legal frameworks of financial participation are more humble than in already mentioned European countries (Ramada 2002). Despite the lack of direct solutions concerning participation, Portuguese market regulations and tax system at the worst do not present any obstacle for further development. In Portugal profit sharing is not considered as a payment for work that is why granted amounts of many to employees in such a form are not subject to pay premiums on social insurance. Till 2000 the taxation of options had not been regulated by the law, but now half of capital income, from selling purchased shares as result of execution of options, is subject to taxation. The process of ownership changes was in the favour of employee share ownership of which prices were advantageous for groups of workers in privatized companies. Employee ownership does not seem to be a permanent phenomenon, because employees usually prefer to sell their shares immediately to get some profits rather than to consider them as a long-term investment.

3.7. Sweden

Relatively small commonness of employee financial participation in this country is definitely connected with the fiasco of the campaign promoting employee ownership, which was started as an initiative of trade unions (Gergils and Gergils 2003) in the 1980`s. Employee funds, which were administered by trade unions, invested a part of companies` profits in their shares. At the beginning of the 1990`s funds were liquidated because of political reasons. It does not mean a total disappearance of participation forms in Sweden. Currently there have been profit sharing funds, which in the period of 1992-1996 were completely exempted from paying premiums on social insurance. In 1997 the duty to pay premiums on social insurance from allocated part of profits to employees (but at a discount rate) were introduced once again which caused a decrease in the interest of participation schemes.

3.8. Great Britain

In Great Britain employee financial participation has got long traditions: in 1978 savings-capital deferred schemes were regulated by the law (Pendleton et al. 2002b). The supply of possibilities was broadened in 2000 when *Share Incentive Plan* was introduced. Companies which use legal solutions and their workers take advantage of fiscal benefits. The range of these solutions is broad, and its offer includes schemes for big companies and small ones, which are open for general use and for selected groups of workers. The most important of English financial participation schemes is SAYE (*Save As You Earn*, which means “Save while working”), which is also called *Sharesave* (it is a neologism that means saving with the purpose of purchasing shares). As the name shows, employees save funds to purchase stocks within the framework of execution of a very advantageous option (at execution price lower to 20% than the price of market basis instrument in the day of issuing option) issued by an employer. The interest from saved funds (the interest rate of savings account) is not subject to capital income tax. The capital income tax is paid by an employee only from the income coming from the sale of stocks possessed as a result of execution of options, when he decides to sell his shares of a company.

Share Incentive Plan introduced a range of tax benefits facilities for employees and employers. The amount of money assigned to savings for the purchase of stocks is deducted from the basis of taxation of personal income tax. Within the framework of savings scheme a company can add up to a doubled sum of amounts saved by an employee. An employer can also hand stocks over to employees for free. According to the range of participation schemes which are entitled to use tax allowances, a range of solutions dedicated to small companies was developed. Since 1987 in England there has also been cash-based profit sharing, with favourable fiscal rules, however in 2000 tax allowances entitled to its members were abolished because of common practice to avoid taxation through a fiscal implementation of the system in companies. However, profit sharing is still used in companies in England which find such solutions attractive for example, from the point of view of flexibility of remuneration system. In England participation in such systems is totally voluntary as well as for an employee and an employer. The decision on introduction and selection of a type of a system belongs to company`s management and the consultation with employees is not required.

4. Conclusions

• The taxation and legal frameworks established by the authorities are of crucial importance to the range and types of applied forms of employee participation.
• The influence over the development of participation is not only made by the rules which regulate it in the direct way but also by the taxation system, labour market regulations, capital market law, accountancy laws, etc.
• Popularization of the use of employee participation forms by a country may serve as a realization of different kinds of political, economic and social targets.
• The use of some employee profits sharing forms (e.g. employee options) is connected with the level of development of capital market.
• The commonness of employee participation schemes does not seem to be dependent on the socio-economic doctrines or even active participation of a country in its economy. The leaders of participation are "the liberal" United States, but also France which has got relatively developed social system.
• The availability of information about participation schemes which are used in individual countries seems to be dependent on the level of direct regulation this matter in the legislation.
• The data concerning other then described here types of extra-salary remuneration of employees are hardly available, because in most cases in this matter companies have got a total freedom.

• Significant question connected with employee profit sharing are, in the face of globalization processes, the practices of transnational corporations in the field of participation: they are dependent on the culture of a given organization, practices which are functioning in the country of origin and the rights of the countries which are the seat of business of company`s branches.
• The lack of data about the share of participation in different companies is in more or less degree caused by the treasury, whereas the use of mechanism of participation in privatization is a separate question, because employee participation can be short-term, or even fictitious.
• It seems that the understanding of the meaning of employee participation and the reasons of domination of their specified forms in individual countries could also be considered in the context of pensions systems which are functioning there.

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