BUSINESSEUROPE

SPEAKING NOTES

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Financial participation and employee shareholding, issues and perspectives in Europe

- First and foremost, it is important to note that there are many different financial participation schemes and supplementary pension systems across Europe. This diversity reflects different companies and workers needs across EU Member States and the different national frameworks in which they are operating;

- There is a danger of confusing financial participation schemes with supplementary pensions; a clear distinction must be made between the two. A supplementary pension scheme provides deferred compensation on financial contributions. It aims to provide workers with an income after retirement. In contrast to financial participation schemes, a supplementary pension does not make an employee a shareholder in the company and it does not give a right of access to the company's profits and/or results. Whereas supplementary pensions are linked to wages/salary, financial participation schemes are not, they act in a complementary way. If a distinction is not made between the two, this can lead to a lack of clarity in the relationship between the employer and the employee and the employee's respective rights vis-à-vis the company;

<u>What are the workers expectations and company needs?</u>

- Financial participation schemes intend to give, usually to all employees, access to the enterprise's profits and/or results. They may be divided in two main categories:

    - <u>participation in profits</u>: sharing of profits between those providing the capital and those providing the labour by giving employees a variable income, in addition to their fixed pay, linked with the profits or another measure of the enterprise's results, e.g. annual bonuses;

    - <u>employee shareholding</u>: offers employees indirect participation in the enterprise's results in the form of dividends and/or appreciation of the value of the capital they hold, e.g. share purchase;

- By involving employees more closely in the life of the business, allowing them to share in the success of their company, aligning their interests with those of the

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company's shareholders and, thus, linking employees to the company over the longer term, these schemes are very important tools to motivate employees.

- Worker participation models in the form of share purchase or share savings schemes (employee shareholding) also have the advantage that they make share ownership accessible to the workforce and support wealth creation;

- This applies also to SMEs: a large number of SMEs have introduced financial participation schemes, fully conscious of their potential and usefulness. However, account needs to be taken of the fact that many SMEs are not in a position to generate the financial resources for worker equity participation or broad profit-sharing schemes, over and above already high wage costs;

- Financial participation schemes must be voluntary. The introduction of financial participation schemes is a decision for the individual company or employer, in the light of existing national law and practice, and depending on the financial situation of the company;

- Companies make use of both share purchase or share savings schemes broadly, and narrowly based financial participation schemes depending on their specific circumstances. Sometimes these two forms may even co-exist within the same company. Employers will choose the schemes deemed to be best suited for the pursuit of their human-resource-oriented goals and in that respect differentiation between groups of employees based on legitimate criteria such as qualification or responsibility may be necessary;

- The role of the social partners, and whether financial participation will be an issue for collective bargaining, will depend on national practice. Where this corresponds to national practice, financial participation schemes may allow for greater flexibility in collectively agreed remuneration systems, with fixed wage levels supplemented by pay components to reflect the success and performance of the company. This flexibility, beneficial to both employees and companies, should be promoted.

- Important obstacles to wider use remain: not all EU Member States provide a legal and tax environment that sufficiently encourages companies to introduce such schemes;

- Problems arise in a cross–border context:

    - Different legal provisions, tax schemes and differences with regard to social security contributions generally prevent companies operating in two or more EU Member States from being able to apply one single corporate financial participation model to employees in different Member States. This generates high administrative costs;

    - In addition, the divergent and complicated fiscal treatment of financial participation models in cross-border situations has become an obstacle to the free movement of employees and a source of distortion within the

Single Market for employers. As regards, for example, stock options, major problems for employees arise from the difference in timing of taxation and from the risk of double taxation. Distortions for employers may arise from no or double deductibility of related costs for corporate taxes;

- Within the EU, better coordination of national tax arrangements is necessary to overcome these obstacles. This could be achieved by taxing exclusively in the Member State where the employee pays income tax when the financial participation is granted regardless of where and when a cash-flow occurs.

- Finally, Member States should provide a favourable fiscal and legal framework that encourages equity participation and profit-sharing schemes and avoids putting financial and administrative burdens on companies that wish to introduce such schemes.

<u>How can long term retail savings (employee saving schemes, defined-contribution schemesé) contribute to financing retirement in the EU and to the European economy? Towards further convergence of European tools and playersé</u>

- Second pillar supplementary pension schemes should not be seen in the same light as financial participation schemes. Both may be characterized by investment and return, however, they differ considerably in terms of their aim and the link between the employer and employee;

- The aim of a supplementary or company pension scheme is that financial contributions are made throughout the employeeơs career to provide some kind of remuneration once he has retired. The pay out is only made once the employee reaches retirement;

- Whereas in financial participation schemes, employees are linked directly to the company finances, with company pension schemes, the financial contributions are often invested externally in shares or bonds, through a contract with a life insurance company or with a pension fund. In many cases, the employer simply acts as a sponsor for the pension, not as the guarantor for the benefits that will eventually be paid to the employee;

- Company pension schemes contribute a great deal to financing retirement and provide an important supplement to 1st pillar state pensions. With demographic change, their importance is likely to increase in the future. They must therefore remain a viable and cost-effective option for companies. EU level convergence of rules and conditions for operating company pensions would be a danger to this;

- Since supplementary pension schemes and the role they play in providing an income for retirement differs considerably across Member States, setting of rules and conditions should be left to the appropriate level (interprofessional, sectoral/industry or company level) in the Member States without interference at EU level;

- Similarly to financial participation schemes, member states should provide the necessary fiscal and legal framework and avoid putting financial and administrative burdens on companies that wish to provide supplementary pension schemes for their employees. Member states should deal with fiscal obstacles and social security issues at national level to support financing of retirement;

- The commission will be consulting on whether harmonized EU level solvency rules for life insurance undertakings (which often offer pension products) should be extended to pension funds (also referred to as IORPs ï Institutes for Occupational Retirement Provision). Solvency rules for pension funds would be a danger to the financing of retirement, as they could make the running of supplementary pensions more costly for employers, possibly deterring employers from offering them;

- Extending EU level solvency rules for life insurance undertakings to pension funds is not necessary or appropriate, as they offer pensions plans in very different ways. Pension funds are associated with a sponsoring employer ï an employee can only enter into a pension fund if he is the employee of the sponsoring employer. Therefore, pension funds do not have the same position or possibilities to gain clients on the market as life insurance companies do. Different solvency rules can therefore apply without causing unfair competition in terms of pension provision.