European ESOP: The main structural features and pilot implementation in Slovenia

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GLOSSARY

"**European ESOP**" – Employee ownership model based on the US ESOP, which defines generic structural features that can be readily implemented in national settings with minor adaptations.

"**Slovenian ESOP**" – Principles behind the European ESOP applied through the national pilot projects in Slovenia.

"**Employee Ownership Cooperative (EOC)**" – A counterpart to the Employee Stock Ownership Trust (ESOT) in the US, that is, a holding entity that holds shares in the name of employees.

"**Individual Capital Accounts (ICA)**" – Personal accounts in EOC that hold shares in the name of employees in the EOC. The ICAs are a version of ownership capital that mimic equity in the way that they "measure" the individualized value of reinvestment for each member. The ICA structure is adopted by ESOPs in the US and Mondragon in Spain.

"Suspense Account" – A capital account in EOC, which holds unindividuated shares – shares that are not yet paid for and hence are not yet distributed to ICAs. The value of a suspense account also indicates the value of the outstanding debt (to owners selling the shares or to a bank providing a loan).

"**Roll-over**" – The technical solution to the problems of repurchase liability and accumulation of capital value on ICAs in US ESOP. It uses cash-flow from a company to constantly purchase the oldest shares on ICAs and distribute them to all the active accounts.

"**Distribution key**" – The criterion for the capital distribution of profits to the ICAs. The distribution key can be egalitarian, based on wage differences, can take into account the tenure at the company, or the combination of both.

INTRODUCTION

In Europe, employee ownership (EO) is increasingly identified as one of the most operational and effective economic alternatives to the dysfunctional economic system of the 21st century.[1] This is understandable since the Western counterparts are exemplary cases of excellent practice in the field of EO. Over the Atlantic, the American Employee Stock Ownership Plan (US ESOP) was introduced already in the late 1970s and now there are about 7.000 ESOPs in the US covering about 10 % of the private workforce. More recently and closer to the EU, the UK has passed the Employee Ownership Trust (EOT) law, which offers very similar buyout mechanism and has very similar features with some notable exceptions.[2] Just last year, the Canadian government committed part of the national budget to establish employee ownership based on the US and the UK examples in order to address the business succession problem in small-and-medium-sized enterprises (SMEs); and it seems that it is only a matter of time until an appropriate law follows.[3]

There has been a great variety of employee ownership models in Europe. Some of the best examples are Marcora in Italy, Sociadades Laborales in Spain, Le FCPE de Reprise in France, and many unregulated *ad hoc* models set up by individual owners without any institutional support. None of those models, however, offers an effective and systematized tool for business succession. And while the European Commission has been touting ownership succession at the top of the challenges list for the SME sector for the past decade,[4] Europe continues to lack a universal and functional model for large scale ownership transfers to employees.[5]

Since 2018, the Institute for Economic Democracy in Slovenia has been developing a model based on existing best practices. Influenced by the structural and institutional analysis of EO models globally - particularly the US ESOP - main features have been generalized by using

1 EFES, "Employee Share Ownership: European Policy" (European Federation for Employee Share Ownership, 2019); Jens Lowitzsch and Iraj Hashi, "The Promotion of Employee Ownership and Participation" (European Union, 2014); Graeme Nuttall, "Sharing Success: The Nuttall Review of Employee Ownership" (Great Britain: Minister for Employment Relations, Consumer and Postal Affairs, 2019); Lorena Lombardozzi and Adriano Cozzolino, "European Economic Democracy A New Path out of the Crisis," 2019, https://www.academia.edu/39727140/European_Economic_Democracy_A_new_path_out_of_the_crisis; Antonio Fizi, "Pan-European Cooperative Law: Where Do We Stand?" (Euricse, 2013), https://www.socioeco.org/bdf_fiche-document-4018_en.html.

2 One of the majort shortcomings of the UK EOT is that they lack one of the most functional inventions in the co-operative and employee-centred companies, the individual capital accounts (ICAs) used by ESOPs in the US, Mondragon co-operatives, and proposed for the European model.

3 Accessed on 21st of April 2022 on the website https://theconversation.com/new-budget-offers-canada-a-chance-to-get-employee-ownership-right-181019

4 Jasmin Schiefer et al., "Obstacles and Challenges of Business Succession in Central Europe," *Journal of International Business Research and Marketing* 4, no. 5 (July 30, 2019): 24–29, https://doi.org/10.18775/jibrm.1849-8558.2015.45.3004; European Commission, "Entrepreneurship and Small and Medium-Sized Enterprises (SMEs)," Text, Internal Market, Industry, Entrepreneurship and SMEs - European Commission, July 5, 2016, https://ec.europa.eu/growth/smes_en; Dijana Močnik et al., *Slovenska Podjetnška Demografija in Prenos Podjetij: Slovenski Podjetniški Observatorij 2018*, 2019.

5 Fizi, "Pan-European Cooperative Law"; Niels Mygind, "Trends in Employee Ownership in Eastern Europe," *The International Journal of Human Resource Management* 23, no. 8 (2012): 1611–42; Lowitzsch and Hashi, "The Promotion of Employee Ownership and Participation"; Rado Bohinc, "Why Poor Employee Ownership Progress in the EU? A Comparative EU - US Overview," *Dr. Rado Bohinc* (blog), April 17, 2019, https://radobohinc.si/en/dr-rado-bohinc-an-eu-approach-to-employee-ownership-progress-a-comparative-eu-us-overview/; Johann Brazda, Marckus Dellinger, and Dietmar Rößl, "Tax Treatment of Co-Operatives in Europe under the State Aid Rules," *Genossenschaften Im Fokus Einer Neuen Wirtschaftspolitik , Teilband IV*, 2012, 1091–1104.

the *good features* and resolving the *flawed features*. The outcome is a generic model with a set of universal features, which we call the "European ESOP" or the "Cooperative ESOP". These features are open-ended enough to be used in devising the national models in Europe but are also narrow enough that the system accounts for the main challenges of the historical and contemporary employee ownership models. The first publication of the model dates back to 2019, when the technical concept was described in a paper published by the European Federation for Employee Share Ownership in Brussels.[6]

Our purpose in this paper is to provide a more concise description of the European ESOP, to compare the European model against the US ESOP, and to give an overview of the pilot implementation in Slovenia, where the Slovenian ESOP - as the national adaptation of the general principles behind the European ESOP – has been implemented for the first time.

THE DESCRIPTION OF THE EUROPEAN ESOP

The European ESOP (or just "ESOP" hereafter unless otherwise specified) is a separate legal entity associated with a company (hereafter "Company"). That separate legal entity could be a new type of cooperative (Employee Ownership Cooperative or EOC), which can distribute profits to its members and where membership is administered with low transaction costs and simplified red-tape. Each Company employee is a member of the EOC and has a personal capital account in the EOC to hold their individuated capital shares in the Company – the personal accounts are called Individual Capital Accounts (ICAs).

The ESOP is a vehicle for the employees in the associated Company to acquire, over a period of time, some percent (up to 100%) of the Company's ownership. The shares owned by each employee are kept in the ESOP in an individual capital account so the employees will enjoy the rights to the income and capital appreciation rights of the shares, but they may not individually sell, mortgage, or bequeath the shares. Thus, the employee ownership is individualized but indirect since the employees cannot sell their shares to others or bequeath them to their heirs. The shares will eventually be bought back by the ESOP and redistributed to the current employees.

The *individuated indirect* EO addresses two problems: first, it provides individual incentive for investment and addresses the problems of underinvestment present in the "social," collective, or common ownership EO models (e.g., the UK EOT model), and second, it solves

6 David Ellerman and Tej Gonza, "A Generic ESOP: Employee Share Plan for Europe," *European Federation for Employee Share Ownership*, 2020, http://www.efesonline.org/LIBRARY/2020/A%20Generic%20ESOP%20Employee%20Share%20Plan%20for%20Europe.pdf

the succession problem – and eventual degeneration - since workers do not directly hold shares and cannot sell them to outsiders.[7]

The US and the European ESOP are *not* based on employees personally making share purchases out of their salaries or other income. One of the central features of the ESOP model is that the Company makes periodic ESOP contributions, much like a form of tax-favored profit-sharing, in cash to the ESOP which then passes the money through to buy out the shares of an existing owner (and eventually to buy back employee shares).

Most of the US ESOPs have been established to address the succession of family firms or SMEs where the founders wanted to retire or exit to pursue other opportunities with no family members who want to take over the business. Selling to a competitor usually means a slow death of the enterprise as the competitor moves the customer list, some key employees, and eventually all the business to their main facilities. Family firms are also benefactors in the local community by providing jobs, income, and taxes to support the community — so selling out to a competitor may eventually be seen as a betrayal of the community and the local employees who, for the most part, will lose their jobs. That is not a good legacy for a family firm. The ESOP provides the alternative of rewarding the employees who helped build up the company and keeping the jobs, incomes, and taxes in the local community, while also awarding the founders and owners for their lifelong efforts.

Other ESOPs in the US have been set up because owners wanted to access cheap debt capital (leveraged ESOPs) or owners wanted to motivate and reward employees by making them owners. While most US ESOPs are in the SME sector, some US ESOPs are part of large companies.[8]

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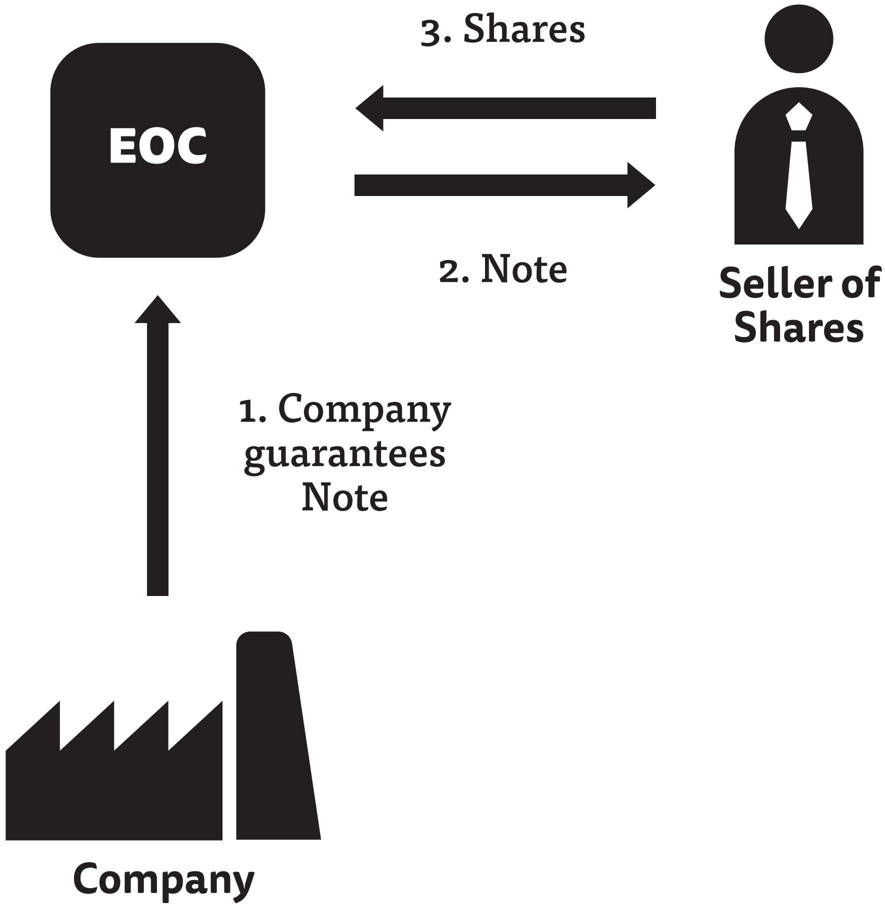
7 One of the common problems with internal and employee ownership was the lack of an effective mechanism for preventing the degeneration through sell-out of the shares to outside biders. If employees are direct owners of shares there is an incentive for each individual employee to look for a better price on the market for that share, if the legal structure allows that. Degeneration happens when shares are brought with employees into their retirement (and are than inherited) or when sold to outside investors, which gradually shifts ownership outside of the company and ''degenerates'' the employee-owned structure.

8 The largest ESOP is a supermarket chain Publix Supermarkets with 207.000 employees. The list of biggest US ESOPs here - https://www.nceo.org/articles/employee-ownership-100

ILLUSTRATION OF THE EUROPEAN ESOP TRANSACTION

One way to understand the European ESOP structure is to follow the steps in all the transactions. In our example below, there are four different entities – Employee Ownership Cooperative (EOC), Company, Seller of Shares, and Employee-Owners in EOC. The illustration describes the main mechanism of partial buyout of shares from the Seller.

Initial transaction

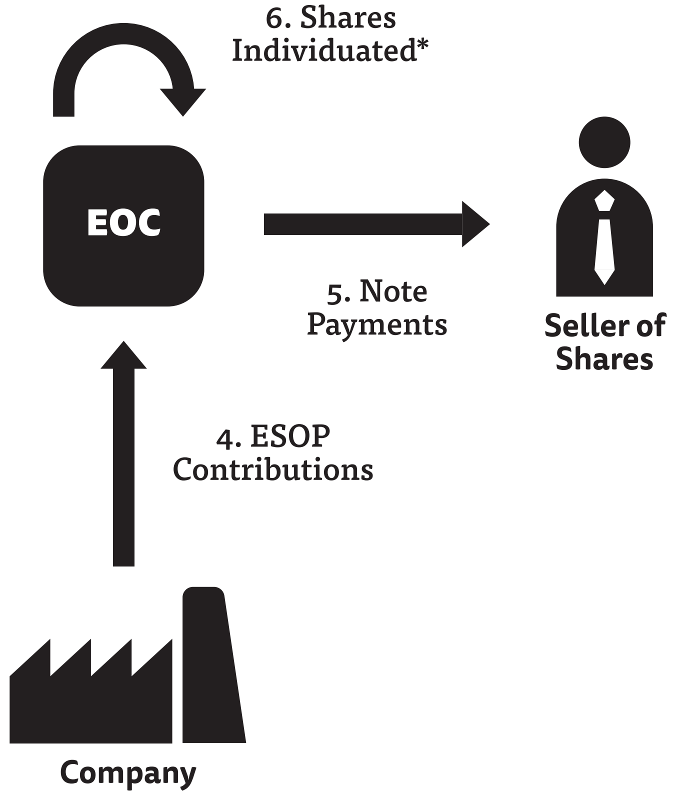


Step 1: The seller of shares (owner selling part of the shares or anything up to a 100% to EOC) gets a guarantee from the Company, which ensures that contributions will be made to the EOC to eventually pay off the note in return for a certain percentage of the shares going to the EOC.

Step 2: Share is valuated, and the EOC issues the guaranteed note to the Seller, which states that EOC owes the value of shares to the Seller.

Step 3: The shares pass to the EOC. The shares are not individuated to the employees at this stage but are held in an unindividuated Suspense Account, which holds the unindividuated shares.

Paying out the Seller

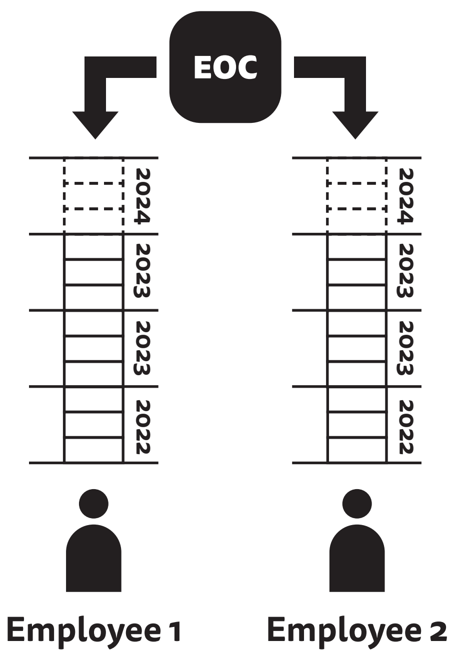


Step 4: The Company makes regular (e.g., monthly, or annual) cash contributions to the EOC. Before any special legislation is passed, the contributions will probably be taxed on the level of the Company with corporate income tax and transferred to the EOC as dividends.

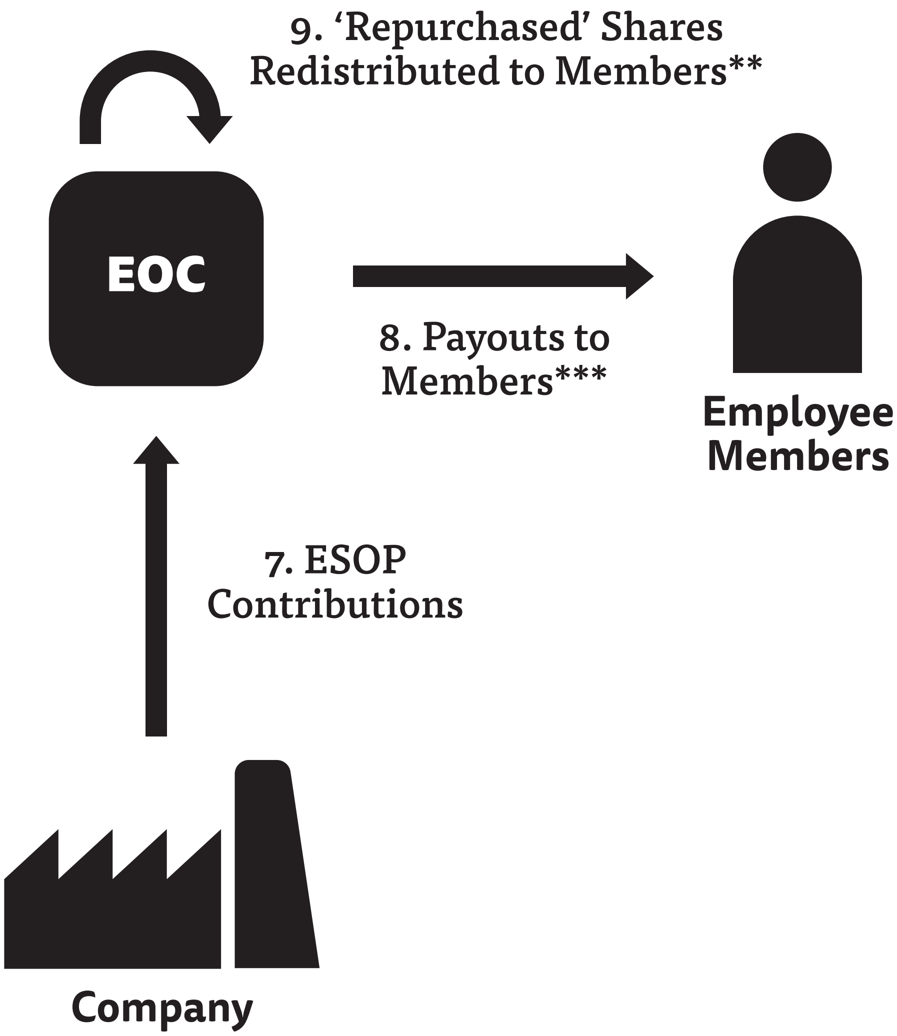
Step 5: The cash is passed through the EOC to pay down the note from the seller.

Step 6: Shares equal in value to the principal portion of each note payment are taken out of the Suspense Account and divided between the Individual Capital Accounts, usually according to salary. Each year, the shares that are paid off are distributed to ICAs -shares are allocated to ICAs in bundles designated by a date, which is important for the roll-over (see below).

*** Step 6.: Shares Individuated (YEAR 2024)**



Roll-over system



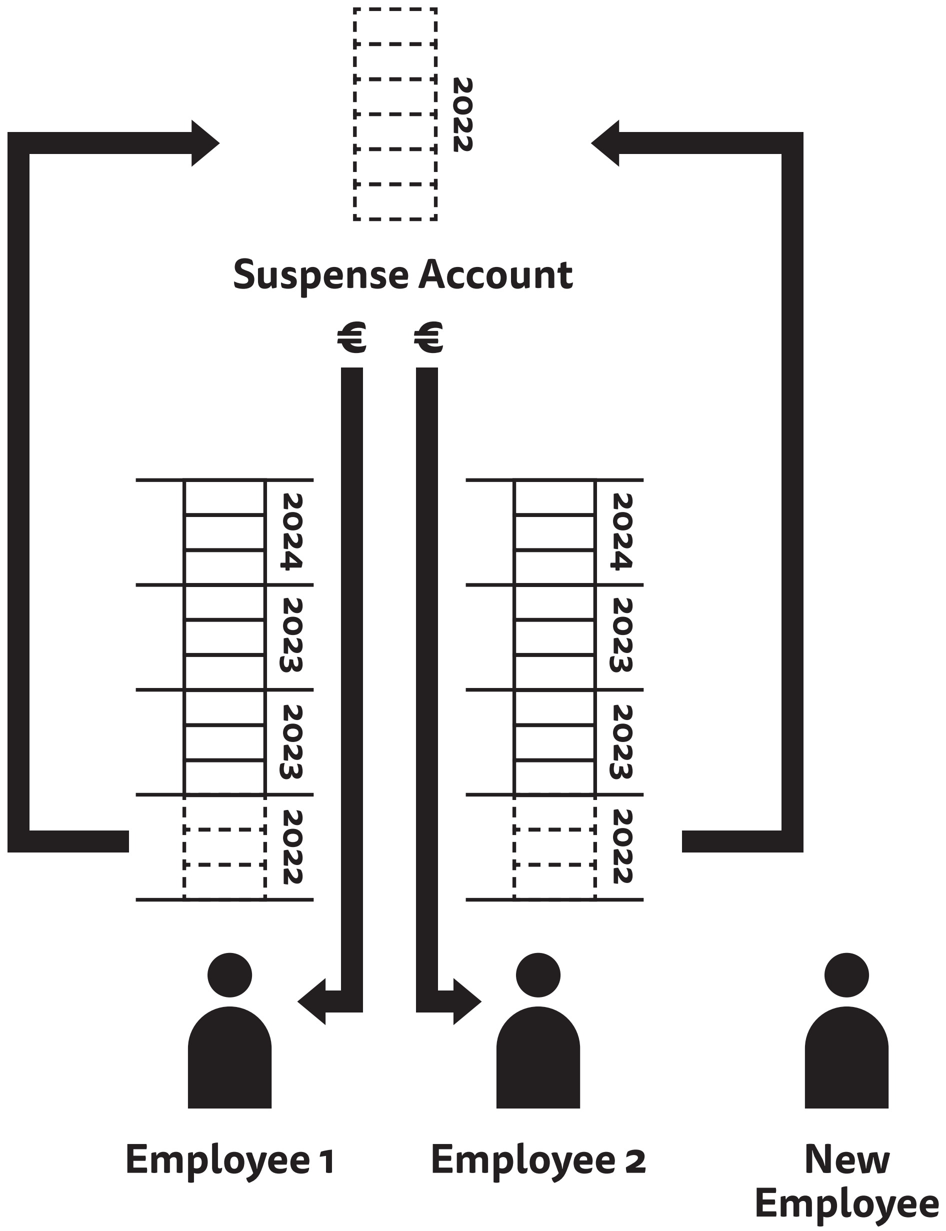
Step 7: The ESOP contributions continue on a regular basis after the note to the Seller has been paid fully. In that moment, all the shares are individuated to ICAs and there are no shares left in the Suspense Account.

Step 8: EOC maintains liquidity through controlled cash flow from the company, which it uses to repurchase the oldest ICA shares from the employees on a first-in-first-out basis. In the example below, in 2025, the first bundle of shares was repurchased from Employee 1 and 2 (shares 2022). They are momentarily placed in the Suspense Account.

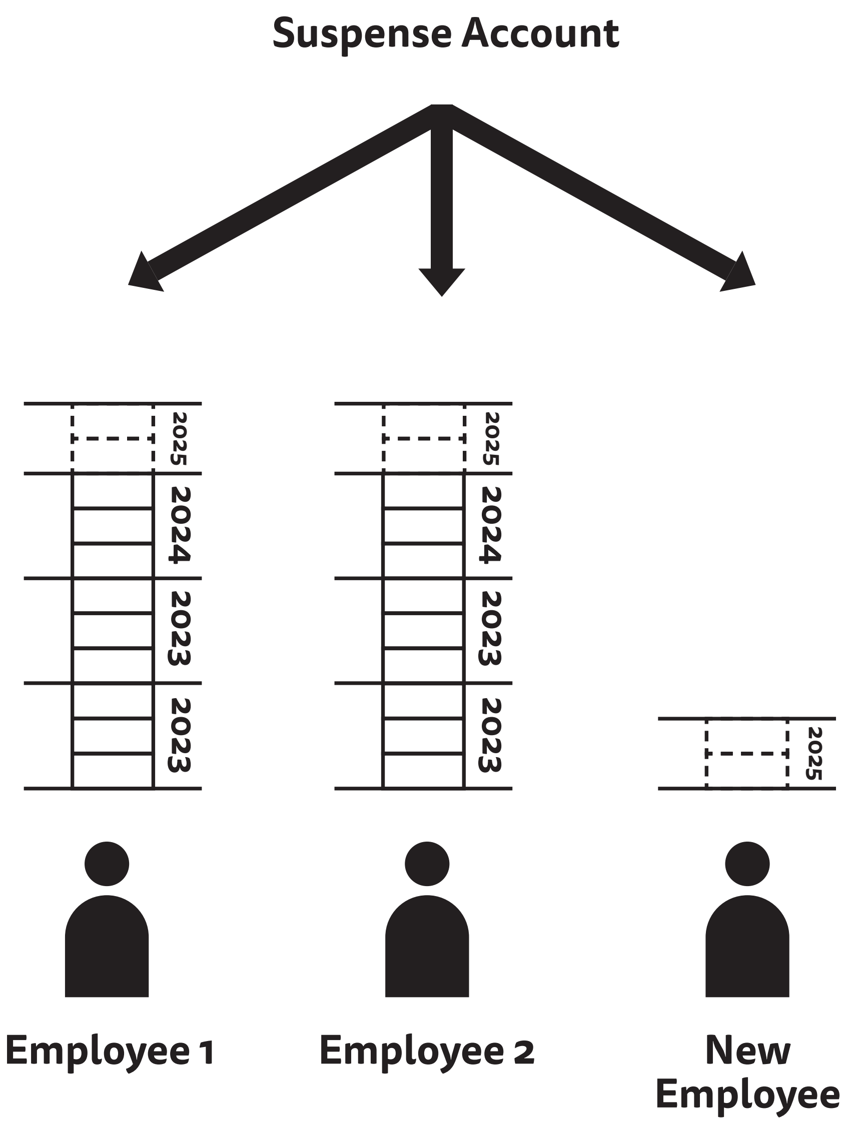
Step 9: As the oldest shares are repurchased from the member (whether still an employee or not), those shares are redistributed to the active ICAs – active ICAs are held by employees who are still with the company. Employees who left the company do not get new shares redistributed and are gradually paid out within the roll-over system. When a new employee joins, as in the picture below, he or she also receives the shares reallocated (now with the new date on the bundle) – redistributed shares also go to new members.

** Step 8. Payouts to Members

(YEAR 2025)



*** Step 9. 'Repurchased' Shares Redistributed to Members (YEAR 2025)



COMPARISON WITH THE US ESOP MODEL

The good features

The experience in the US shows that the US ESOP has been one of the most successful inventions in relation to practical implementation of employee ownership schemes in a private market-based economy. We measure success along two dimensions: firstly, the US ESOP has been studied in detail and the empirical research indicates superior productivity, growth, and resilience of ESOP companies.[9] At the same time, the sheer numbers, where ESOP is implemented in 7.000 firms employing over 12 million American workers (ca. 10% of the private workforce), indicate that the right institutional support can be very productive in promoting EO. The logical conclusion is – there are features of the US ESOP that make it a remarkable social invention. In this section, we summarize the main features of the US ESOP that are captured by the European ESOP:

1) The ERISA (Employee Retirement Income Security Act) law requires that *all* permanent employees[10] are part of the ESOP employee ownership program *without* the employees risking any of their own assets or savings. Since all permanent employees are included, at least when ESOP contributions are made, the US ESOP creates a company of owners, which helps the workplace culture. One of the more important features of the US ESOP is inclusivity – when everyone is in the same boat, everyone is motivated to help rowing faster and safer across the rough seas.[11]

2) The ESOP buyout can be leveraged with bank or seller-supplied credit, so a significant number of shares may be purchased at one time from a retiring owner. In the case of debt leverage by external financier, the company guarantees the loan by securing a note promising regular ESOP contributions on a monthly or annual basis. This solves the "finance problem" in so many other worker ownership schemes (e.g., cooperatives) since it is the existing standard parent company guaranteeing the loan. The seller's credit option is usually cheaper and less complicated; however, it requires the owner

9 Anis Jarboui, "ESOPs, CEO Entrenchment and Corporate Social Performance," *International Journal of Business and Economics Research* 2, no. 6 (n.d.): 116; Douglas Kruse, "Does Employee Ownership Improve Performance?," *IZA World of Labor*, 2016, https://doi.org/10.15185/izawol.311; Douglas L. Kruse, Richard B. Freeman, and Joseph R. Blasi, *Shared Capitalism at Work: Employee Ownership, Profit and Gain Sharing, and Broad-Based Stock Options* (University of Chicago Press, 2010); Fidan Ana Kurtulus and Douglas L. Kruse, *How Did Employee Ownership Firms Weather the Last Two Recessions? Employee Ownership, Employment Stability, and Firm Survival: 1999-2011* (W.E. Upjohn Institute, 2107), https://doi.org/10.17848/9780880995276; E. Han Kim and Paige Ouimet, "Broad-Based Employee Stock Ownership: Motives and Outcomes: Broad-Based Employee Stock Ownership," *The Journal of Finance* 69, no. 3 (June 2014): 1273–1319, https://doi.org/10.1111/jofi.12150; Joseph Blasi, Douglas Kruse, and Dan Weltmann, "The Response of Majority Employee-Owned Firms during the Pandemic Compared to Other Firms," *Journal of Participation and Employee Ownership* 4, no. 2 (January 1, 2021): 92–101, https://doi.org/10.1108/JPEO-09-2021-0014; Jared Bernstein, "Employee Ownership, ESOPs, Wealth, And Wages," *Commissioned by the Employee-Owned S Corporations of America*, 2016; Joseph Blasi, Douglas Kruse, and Dan Weltmann, "Firm Survival and Performance in Privately Held ESOP Companies," in *Sharing Ownership, Profits, and Decision-Making in the 21st Century* (Emerald Group Publishing Limited, 2013), 109–24.

10 Contractual workers and seasonal workers are excluded from the US ESOP scheme.

11 There are examples where ESOP did not cover all employees because one or more collectives bargained out of the deal – usually leading to disasterous results. This was the case with United Airlines ESOP - https://www.forbes.com/sites/fotschcase/2017/04/17/uniteds-troubles-could-have-been-avoided/?sh=44e155e7c062 .

to agree on being paid out over a period of several years, depending on cash flow to the ESOP trust.[12]

3) The ESOP has a system of individual capital accounts so that employees have individualized ownership that will be cashed out when they exit or retire, if not sooner under the roll-over plan (see the explanation of the roll-over below).

4) Once the shares are 'in' the individual capital accounts of the ESOP, they are eventually bought back by the ESOP. Because shares are anchored with the workers of the Company, owners are also members of the local communities, which means that the interests of these communities is generally considered by the ESOP companies.

5) The US ESOPs are also incentivized by favorable tax treatment (favorable in US terms) of 2 main transactions: a) if the seller sells more than 30% of the Company's shares to the ESOP and invests the received purchase price back into the US economy, the received purchase price is not taxed; and b) accumulated wealth of beneficiaries in the US ESOP is not taxed until it is paid out. Even then it is taxed only if it is not invested in a recognized pension scheme.

The flawed features

The US ESOP was established as a pension fund; at the time, the simplest way to establish an EO model was to carve out the private pension legislation so that the trust could hold more than 10% of the company's shares. While this was the pragmatic way to establish EO in the US, it has brought about some legal artifacts that are arguably detrimental to the ESOP model. The European ESOP model is an *improvement* over the US ESOP in several respects.

1) The US ESOP was implemented as a special type of retirement plan, so the ESOP does not need to buy back the share until the employee exits or retires. There are some provisions that some shares can be repurchased after the beneficiary reaches the age of 55, and there were individual and isolated cases where the ESOP was structured in a way that employees could access ICA liquidity before retirement.[13] In the generic European ESOP model, the employees can already "see some ownership money" in Step 8.[14]

2) In the US ESOP, the contributions to ESOP are only made when there is a loan to be paid off or shares to be repurchased (either the existing owner sells more outstanding shares on employees retire and sell ESOP shares). It is only *then* that the new employees get the

12 All of the Slovenian ESOP projects in the pilot phase are based on sellers' credit since financial institutions need a functional example and/or a law before they are willing to participate.

13 https://www.fiftybyfifty.org/2022/03/central-states-manufacturing-gives-workers-early-access-to-esop-wealth/

14 Roll-over usually "kicks in" when the outstanding debt is paid off – when the Suspense Account is emptied, and all shares are individuated to the employees. There is also an option that roll-over is initiated while the Suspense Account shares are still being paid out – an agreement can be reached, usually at the risk for the owner or the creditor, to share the ESOP contributions between servicing the outstanding debt and financing the roll-over, so that employees already "see some money" in the first years.

shares to their ICAs, which means that no shares are individuated until there are more ESOP contributions. In the European ESOP, the ESOP contributions are regularized to repay the loans/notes or to start the share roll-over so new workers are automatically included in the ownership, and exiting workers are automatically bought off without imposing an unpredictable repurchase liability.

3) Since the ESOP contributions are determined based on annual financial capabilities of the underlying company, and since the contributions determine the size of the roll-over, this solution addresses the repurchase liability that has been discussed as one of the problems of the US ESOP. At the same time, the roll-over tends towards equalizing the ICAs among younger and older members, distributing the risk more equally. Finally, if US ESOP motivates people to leave the company to "see the money", the European ESOP corrects for that incentive. At the same time, it gives the younger workers more tangible motivation since they start receiving payments sooner.

4) In the US ESOP, the ESOP is a trust, and the employees are only "beneficiaries" as if they were minors. The democratic governance of the European ESOP is the first step towards building an ownership culture in the Company since the employees are treated as partners. In the European ESOP, the ESOP is an ownership vehicle that is democratically governed by its members (i.e., the Company employees beyond some probationary period). All members have one vote, which grants them a say in the (annual) general assembly of the EOC when discussing high-level corporate decisions, and one vote in delegating their representative (and the EOC board). The representative votes on the block of shares held by EOC at the shareholder assembly of the Company. The governance structure of the European ESOP provides both voice and influence to the employee-owners. Empirical research confirms that employee participation is the central and most important factor behind the superior business performance results of the employee-owned firms.[15]

The European ESOP model should be implementable in any private property market economy and does not require any special legislation. Nevertheless, to incentivize, support (tax benefits, financial instruments, subsidies, building of supporting infrastructure etc.), and regulate national models of the European ESOP, the legislation should immediately follow the pilot examples.

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15 Niels Mygind and Thomas Poulsen, "Employee Ownership – Pros and Cons – a Review," *Journal of Participation and Employee Ownership* 4, no. 2 (January 1, 2021): 136–73, https://doi.org/10.1108/JPEO-08-2021-0003; Sherry Jueyu Wu and Elizabeth Levy Paluck, "Having a Voice in Your Group: Increasing Productivity through Group Participation" (PsyArXiv, April 27, 2020), https://doi.org/10.31234/osf.io/vm4hu; Roberto Frega, "Employee Involvement and Workplace Democracy," *Business Ethics Quarterly*, October 7, 2020, 1–26, https://doi.org/10.1017/beq.2020.30; Imanol Basterretxea, Chris Cornforth, and Iñaki Heras-Saizarbitoria, "Corporate Governance as a Key Aspect in the Failure of Worker Cooperatives," *Economic and Industrial Democracy*, February 4, 2020, 0143831X19899474, https://doi.org/10.1177/0143831X19899474; Joseph Blasi, Douglas Kruse, and Richard B. Freeman, "Broad-Based Employee Stock Ownership and Profit Sharing: History, Evidence, and Policy Implications," *Journal of Participation and Employee Ownership* 1, no. 1 (January 1, 2018): 38–60, https://doi.org/10.1108/JPEO-02-2018-0001.\\uc0\\u8221{} {\\i{}Business Ethics Quarterly}, October 7, 2020, 1\\uc0\\u8211{}26, https://doi.org/10.1017/beq.2020.30; Imanol Basterretxea, Chris Cornforth, and I\\uc0\\u241{}aki Heras-Saizarbitoria, \\uc0\\u8220{}Corporate Governance as a Key Aspect in the Failure of Worker Cooperatives,\\uc0\\u8221{} {\\i{}Economic and Industrial Democracy}, February 4, 2020, 0143831X19899474, https://doi.org/10.1177/0143831X19899474; Joseph Blasi, Douglas Kruse, and Richard B. Freeman, \\uc0\\u8220{}Broad-Based Employee Stock Ownership and Profit Sharing: History, Evidence, and Policy Implications,\\uc0\\u8221{} {\\i{}Journal of Participation and Employee Ownership} 1, no. 1 (January 1, 2018

THE SLOVENIAN ESOP AND THE PILOT IMPLEMENTATION

Since 2020, the Institute for Economic Democracy has been implementing the principles behind the European ESOP into the Slovenian economy. In the pilot phase, we have collaborated with 30 private enterprises and have worked closely with about 5 companies. By the beginning of 2022, three pilot ESOPs have been established and we expect at least three more companies to transform into ESOPs by the end of the year. In this section, we describe the Slovenian ESOP as the national adaptation of the European ESOP and the process of implementation in private firms.

The Slovenian ESOP model is based on Employee Ownership Cooperative (EOC) as the ownership trust for employees. The EOC is a membership organization, which means that inclusion and exclusion of employees into ownership through EOC is based on predefined rules and conditions. This severely decreases transactions costs and simplifies the red tape. At the same time, cooperatives have the possibility of paying out profits to their members, which is something that other legal forms such as a foundation ("*stiftung*") or non-profit company may not allow.

The Slovenian ESOP is founded by the employees of the Company. In the process of incorporation, the employees themselves actively participate in the formation of the specific rules of their ESOP. While the general features are defined by the model itself, certain features may depend on the culture of the company and a democratic requirement of the employees.[16] If the company has more than 10 employees, the practice is that informal democratic elections take place where the employees' representative group is delegated, to actively participate - through experts' guidance - in establishing the rules of the system.

Typically, to minimize the cost and administrative burden, just a few employees (at least 3 but usually more, often the representative group) are founders of the EOC. Once the EOC is registered, all other employees who are eligible for membership can become members by paying in a mandatory share.[17] By paying the mandatory share, an employee becomes member and receives two sets of rights: voting rights and financial rights (the right to profits and the right to the value of the underlying assets, i.e., shares in the Company, which is indicated by the ICAs).

After the EOC is established, the cooperative proceeds with the purchase of shares from the exiting owner – or any owner that is selling a share of the Company. The recommended valuation for internal buyouts, which use the internally generated capital to purchase the shares, is based on the net asset value (NAV) of the Company. We consider NAV as the most objective value of Company's past financial achievements, the most transparent since it is reported annually and regulated by accounting standards, and the most appropriate, since

16 E.g., the rules on voting, different majorities required for decisions (high majority of 75% + for decisions to terminate ESOP plan), rules on length of probation period before an employee is eligible to become an ESOP member, the distribution key that determines capital distribution to ICAs etc.

17 The mandatory share is a standard obligatory one-time contribution that grants the rights to membership in a cooperative. We should emphasize that mandatory share in European ESOP does not provide claim to capital of the cooperative but is simply a "ticket" to membership and can be as low as 10€ or 100€. This is decided by the employees or their representatives, who set up the rules of the system. The membership share is not revalued when the Company share value changes (that is the role of the ICAs) and is paid back upon exit.

it is not based on guess-estimates of the future profits (that might be used in an arms-length sale to an outside buyer).

The selling owner has two general options of payment of the purchase price: onetime payment and the seller's credit option. If the selling owner insists on a onetime payment, the EOC needs to acquire a loan. The loan can be provided by the Company itself, which can borrow its own cash assets or receives the loan from a bank and lends it over to the EOC. Another option is that the Company guarantees the loan for EOC, which receives it from the bank directly. In either option, the selling owner receives the purchase price immediately. Finally, the owner can decide to be paid out gradually - which is the seller's credit option – in this case, the Company contributes to the EOC on an annual basis, and the cash is used to pay off the owner's note.

In the Slovenian ESOP, which is not yet legislated and is currently in the pilot phase, the most affordable financing option is paying the profits to the EOC as a part owner of the Company. The EOC receives annual contributions, which are taxed once as corporate income at the Company level, and then personal capital income tax is applied to the seller (and in the roll-over phase to the employees) when he or she is paid out by the EOC.

As the debt is being paid off – either to the selling owner or to the external creditor -, those amounts are distributed to the members of the European ESOP in accordance with internal rules (distribution key) and the accumulated wealth of their individual capital accounts. The distribution key is the measure of capital distribution to the ICAs in the EOC. It is calculated based on the share of individual wages in total members' payroll.[18]

One of the crucial elements of the European ESOP – and the Slovenian adaptation – is that only current employees are members of EOC. Persons who are no longer with the Company lose their membership, whereas the value of their ICAs is gradually paid out (according to roll-over rules) until their personal capital account is empty. This is a crucial element that prevents ownership succession problems and keeps the ownership perpetually in the hands of the ongoing generation of employees.

In 2022, we established three Slovenian ESOPs – three companies that are pioneers in the European employee-ownership context. These are engineering and software companies: Inea (80 employees, 100% ESOP), Inea RBT (10 employees, 100% ESOP), and Hudlajf (15 employees, 10% ESOP).[19]

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18 The distribution key is usually tied to the wage-differences in the Company but it can also be more equal or completely egalitarian. In the US ESOP, the largest differences within ESOP can be determined by wage-differences – the ESOP law proposal that we prepared for Slovenia considers the same limitation. Some of the pilot groups in Slovenia also decided to include the tenure with the company as the additional variable of the distribution key.

19 We are currently working to establish Slovenian ESOP with more industrial companies, other start-up companies, and larger companies between 200 and 1.400 workers.

CONCLUSION

The work we have conducted with business owners and managers of Slovenian companies has indicated that there are different possible motives for establishing employee ownership. There is a general and objective need for ownership succession tools, and ESOPs have proved themselves as an effective tool for addressing this issue. Owners may also want to reward employees for the past work, motivate them for the future work, they may want to increase employee retention, enhance productivity, improve crisis resilience, or simply help workers and local communities by guaranteeing that their business will remains viable and socially responsible.

In Europe, there has been a lack of a unified front on employee ownership. There is a great diversity of models, some more and some less successful. The purpose of this paper was to isolate the most important structural features of the potential generic European ESOP model, which could be widely adopted at both the EU level and in individual European nation states.

We have also described shortly how the principles behind the European ESOP have been implemented in pilot projects in Slovenian companies. We hope that this will set a trend; already, the model has been recognized by some of the international stakeholders and institutions, and the European ESOP model has served as the basis for the special piece of legislation proposal for Slovenia that is going to be tried with the new government in 2022.

The European ESOP could unify the employee ownership front in Europe. It certainly provides the universal principles for addressing the business succession problem and for including employees in the ownership of profitable companies.

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