PROFIT-SHARING REFORM WITH PARTICULAR REFERENCE TO THE FRENCH LAW OF 1967

INTRODUCTION

> "It is essential that employers and wage and salary earners, who together further the development of firms, should share the reward of their joint efforts . . . Progress, which is achieved by all, must be a source of greater wealth for all, which means that all must take a share in the increase of capital thus produced."[1]

A view strongly held by some is that employees have a fundamental right to share in the profits of a business which they have helped to produce. "It is an expression not of economic or political theory but of practical morality."[2] Advocates of profit-sharing maintain that theirs is a philosophy which does not recognise artificial divisions between men. Labour is not a commodity, it is people; every man therefore has a human right to participate in the increased prosperity to which he has contributed through the teamwork of the company.[3]

Yet despite a philosophy which is both appealing and idealistic "profit-sharing"[4] is not widespread in industrial countries.[5] Few governments in the world have legislated to encourage or to require the implementation of profit-sharing.[6]

France had legislation for compulsory profit-sharing in workers' productive co-operative societies as early as 1915. Since that time France has made numerous legislative provisions relating to profit-sharing, particularly after the post World War II nationalisation of a number of industries. The culmination of these measures was the French Government's Ordinance of 17 August 1967 which for the first time made worker participation in the profits of expansion a recognised right and not just an optional measure to be implemented at the employer's discretion.

The Republic of Venezuela issued a decree in 1939 making profit-sharing compulsory throughout all industry and business. A number of other South American countries — Chile, Bolivia, Ecuador,

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1 Report to the President of the French Republic, preceding the Ordinance No. 67-693 of 17 August 1967 on the Participation of Salary and Wage Earners in the fruits of expansion of enterprises. This legislation will be referred to as "the Ordinance". Journal Officiel, 18 August 1967, pp. 8288-9. The writer's translation from the French.

2 Council of Profit-Sharing Industries, *Profit-Sharing Manual,* Edwards Bros., Michigan, (1949), pp. 3-4.

3 Ibid., pp. 3-4.

4 As defined in Part I, post.

5 For a brief history of profit-sharing see under the reference "Profit-Sharing" in *Encyclopaedia Britannica,* Vol. 18, pp. 600-3.

6 See N.Z. Department of Labour *Profit-Sharing,* a supplement to the Department's 1949 *Report on Incentive Payment Schemes in New Zealand.*

Peru, Argentina and Columbia have made profit-sharing compulsory by law.[7] Various socialist countries such as Czechoslovakia, Hungary, Bulgaria and Yugoslavia have compulsory schemes whereby employees benefit from profits of enterprises in addition to basic wages.[8] The Supreme Court of India, has held that a demand for a bonus can be justified when wages fall short of the living standard or when industry makes "huge" profits, part of which is due to employees' contributions to increased production.[9]

Profit-sharing began to assume major proportions in the United States only after 1942 when the Internal Revenue Code provided that employers' contributions to profit-sharing funds collected and disbursed as specified in the Code were deductible expenses for purposes of taxation.[10]

New Zealand was one of the first countries in which legislation has been enacted designed to remove laws which had hindered the adoption of profit-sharing schemes. The Companies Empowering Act 1924[11] provided for the issue of "labour shares" and enabled a company to issue non-transferable shares, which had no nominal or capital value, to its workers without requiring capital contribution on their part. Similar legislation has been passed in New South Wales.[12]

This article aims firstly to examine the existing profit-sharing legislation in New Zealand and to evaluate whether it has been successful in achieving the goals for which it was introduced. Then the 1967 French legislation on profit-sharing will be examined with a view to determining whether it offers any useful ideas for this country. The French scheme is of vital importance to any inquiry on profit-sharing as it represents the most recent and, indeed, the first instance of compulsory profit-sharing in a major industrial country.[13] This inquiry will be followed by a general discussion as to what benefits can reasonably be expected from legislation which either makes profit-sharing obligatory or offers incentives for firms to initiate profit-sharing schemes.

PART I: DEFINITION OF PROFIT-SHARING

In this article the definition of the Report on Profit-Sharing and Labour Co-partnership in the United Kingdom prepared by the Ministry

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7 Westaway & Jacobs: *Profit-Sharing Experience in Australia and Overseas.* Personnel Practice Bulletin Vol. XV, No. 1 (1959), pp. 27-28.
8 Ibid., p. 28.
9 Ibid.; see also *Some Papers on Wage Policy,* Government of India, Ministry of Labour and Employment, 1957.
10 Note 5, supra, p. 602.
11 Subsequently embodied in s. 59 of the Companies Act 1933, and now s. 67 of the Companies Act 1955.
12 By an amendment to the New South Wales Companies Act 1936.
13 It is still relatively soon to judge the success of the French scheme in terms of results achieved since it only came into effect in 1968.

of Labour[14] has been adopted. "Profit-sharing", according to the Report, applies to those cases in which:

> ". . . an employer agrees with his employees that they shall receive, in partial remuneration of their labour, and in addition to their wages, a share, fixed beforehand, in the profits realised by the undertaking to which the profit-sharing scheme relates."[15]

The relevant agreement between employers and employees should normally be binding in law, though an agreement which has only a moral obligation is sufficient provided that it is honourably carried out.[16]

By a "share" in profits is meant a sum paid to an employee; in addition to his wages, out of the profits, the amount of which is dependent on the amount of these profits.[17]

"Profits", a share in which under a profit-sharing scheme is allotted to the employees, are the actual net balance of gain realised by the financial operations of the undertaking in relation to which the scheme exists.[18] This definition therefore excludes systems under which the amount of bonus depends on the quality or amount of the output or volume of business, irrespective of the rate of profit earned.[19]

The share must be "fixed in advance" to the extent that the employer cannot, at his discretion, determine the fraction of the profits which shall be shared with the employees.[20] The Special Committee did not however consider it necessary that the employees should know all the details of the basis upon which the amount of their share is fixed.

A profit-sharing distribution scheme may exclude persons who are not adults, or have not been in the service of the employer for some reasonable qualifying period, but must, in order to come within the definition of profit-sharing, include not less than 75 per cent of the total number of adult employees who have been in the service of the employer for at least one year.[21] A distribution which is confined to

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14 1920, Cmd 544; Harper, *Profit-Sharing in Practice and Law*, Sweet & Maxwell, (1955), p. 3 also uses this definition.

15 Ibid., p. 3. This definition is in the main identical with that formulated by the International Congress on Profit-Sharing held in Paris in 1889 and subsequently endorsed by the International Co-operative Congresses of 1896 and 1897 and the International Congress on Profit-Sharing in 1900.

16 1920, Cmd 544 p. 3.

17 Ibid., p. 3.

18 For a summary of "What Profit-Sharing is Not" see B. L. Metzger *Profit-Sharing in Perspective*. Profit-Sharing Research Foundation, 2nd ed., Edwards Bros., Illinois, 1966, pp. 1-2. This work will be referred to as Metzger, *Profit-Sharing in Perspective*.

19 E.g. bonus on output, commission on sales, premiums proportionate to savings effected in production.

20 1920, Cmd 544, p. 4. Cf. the requirement for fullest possible disclosure under the 1967 French Ordinance.

21 Ibid., p. 5.

managers, foremen and leading hands, or to any such classes of employees is not profit-sharing.[22]

In this article profit-sharing will include profit-sharing schemes with the characteristics defined above but with the additional feature that there is provision for the employees' shareholding in the company. Where such a scheme carries with it the ordinary rights and responsibilities of a shareholder then it is often described as a "co-partnership"; a principle which is well illustrated in s. 67 of the Companies Act 1955.

PART II: PROFIT-SHARING LEGISLATION IN NEW ZEALAND

Labour Shares

Section 67 of the Companies Act which was first enacted in the Companies Empowering Act 1924 sets up the machinery for an optional scheme whereby a company may issue labour shares to its employees. These shares have no nominal value and are not part of the company's capital yet in most other respects they put the holders in the same position as shareholders, including a right to attend and vote at shareholders' meetings and to share in the profits of the company to the extent authorised by the memorandum or articles of the company. This share in the profits may, if authorised by the articles, be satisfied wholly or in part by the issue of capital shares. In the event of death, retirement or cessation of employment, the value of the shares, which are non-transferable, is computed in accordance with the articles and paid to the holder or his personal representatives.

Expectations

Before inquiring into the success or otherwise of this legislation it is relevant to examine the expectations of the persons responsible for its enactment. The late Mr. Valder of Hamilton, who provided the original impetus for legislation which would facilitate employee shareholding acted on two broad principles. First, that the fruits of extra effort should go to those who contributed such effort and that capital, having received a fair return, was not justifiably entitled to a further return not made by the persons subscribing the capital but by the efforts of the employees. Secondly, the employee should have a secure status in his company. The periodical hand-out of a share in profits was not enough and the workers should be given a permanent claim to company profits through the holding of labour shares and representation on the Board of Directors.[23]

A brief look at the New Zealand Parliamentary debates during the passage of the Companies Empowering Bill through the House of

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22 Ibid.
23 N.Z. Labour Department, *Profit-Sharing* (Supplement to a 1949 Survey on Incentive Schemes), p. 7.

Representatives and the Legislative Council provides a further indication of what the measure was intended to achieve. On the second reading of the Bill the Attorney-General, the Hon. Sir Francis Bell, admitted that the proposal was experimental but that there was reason to believe it would have an influence in dissipating the separation of interests between capital and labour.[24]

Some members considered that the Bill would help remove the cause of industrial strikes and disturbances[25] and result in "better production in the shops and a better spirit among the workers".[26] Other members, although sympathetic with the aims of the new proposal, were sanguine as to its prospects of success on the grounds that certain workers would abuse their new right to participate in their company's affairs[27] or that it was unwise for a business to entrust its employees with a full knowledge of its operations.[28]

Achievements

How then have these expectations and warnings been fulfilled in the light of experience? The words of the member for Buller, Mr. Holland, spoken in the third reading of the Bill give the most accurate prediction:

> ". . . I do not think that this Bill is going to have any material effect . . . for I hold that when it becomes law the ordinary course of events will proceed just as at present, without any revolutionary changes."[29]

In a survey made by the Registrar of Companies in 1940 only eight companies had made some use of the labour shares provisions in the Companies Act.[30] A 1949 Report on a sample of incentive payment schemes in New Zealand[31] prepared by the Department of Labour revealed only one instance of employee partnership under the Companies Empowering Act 1924, occurring in a firm in which the scheme had operated for 21 years. Even in the absence of more precise information it can confidently be asserted that s. 67 of the Companies Act 1955 is a dead letter.

Why did s. 67 and its predecessors meet with virtually no response from the management and workers of New Zealand companies? The first and most obvious reason for its desuetude was that it was simply an optional measure which firms were free to adopt or ignore, subs.

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24 201 *N.Z. Parliamentary Debates,* pp. 235-6; ibid., vol. 205, pp. 800-811; pp. 1097-1101.
25 Ibid., vol. 205, p. 803, Hon. Earnshaw.
26 Ibid.
27 Ibid., p. 808.
28 See Mr. Isitt, Member for Christchurch North, ibid., p. 1100.
29 Ibid., p. 1098.
30 *Profit-Sharing* (Supplement to 1949 Report by the Department of Labour on Incentive Schemes in New Zealand), p. 8.
31 Ibid., pp. 37-8.

(1) providing:

> (1) Subject to the provisions of this section, a company may, unless expressly prohibited from so doing by its memorandum, issue special shares (in this section referred to as labour shares) to persons for the time being employed in the service of the company.

In this regard the lack of interest shown by workers, employers and shareholders to the initial French Ordinance of 7 January 1959 is noteworthy.[32] This Ordinance introduced a number of tax and social exemptions for firms that would initiate profit-sharing schemes in some form for the benefit of their workers. The lesson to be drawn from both s. 67 and the French Ordinance would appear to be that there is a certain reluctance on all sides to change the status quo, unless there is a positive incentive or compulsion.

Yet the New Zealand legislation on profit-sharing has never been reinforced with positive incentives for the initiation of profit-sharing schemes. If anything, the present New Zealand tax structure penalises many schemes envisaged under s. 67. Section 88(1) of the Land and Income Tax Act 1954 includes in the assessable income of any person:

> (b) All salaries, wages, or allowances (whether in cash or otherwise), including all sums received or receivable by way of bonus, gratuity, extra salary, or emolument of any kind, in respect of or in relation to the employment or service of the taxpayer.
>
> (c) All interest, dividends . . .

It is submitted that this provision would clearly cover any profit-sharing scheme as defined in Part 1 of this article and also any scheme under s. 67 of the Companies Act.

Section 88C, inserted by s. 14(1) of the Land and Income Tax Amendment Act (No. 2) 1968 adds a further disincentive for profit-sharing in the form of employee shareholding. This section extends the meaning of "allowances" in s. 88(1)(b) to include any benefit conferred on any taxpayer in respect of his present or future employment or service, under any agreement to sell or issue shares in any company to the taxpayer. Subsection (2) of s. 88C sets out the four circumstances in which the assessable benefit is to be determined and when the benefit is to be assessed for income tax. The most unfavourable circumstances from the point of view of employee shareholding is subs. (2)(a) which provides that the amount of the benefit to the taxpayer who has acquired shares under an agreement shall be the amount by which the value of the shares on the date on which he acquired them exceeds the amount paid or to be paid for them. This benefit is deemed to have been received by him in the income year in which he acquired the shares. The effect of this provision is that an employee may be assessable for tax on a benefit, namely shares in the employer

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32 George Lasserre, *La Participation des Salariés* . . . Revue d'Economie Politique (1968) pp. 70-71.

company, which he has not received in terms of cash payment and which he may not be able to dispose of for a number of years depending on the terms of the agreement under which he acquired the benefit. When valuing the benefit the Commissioner is required to take no account of any restrictive provision in the option agreement as to the alienation or transfer of any shares unless those provisions apply for a period of not less than eight years.

Thus the New Zealand taxation laws which relate to profit-sharing reveal that at best profit-sharing schemes are accorded no tax incentives whatsoever and in the case of employee shareholdings there are positive disincentives.

Yet perhaps the most important indications as to why the Companies Empowering Act has never been used to any significant extent can be discerned from the Parliamentary debates on the Bill. A common theme in the debates was the inherent hostility and distrust between employers and workers who were "divided into two antagonistic camps".[33] There is room for conjecture that the unions may have opposed profit-sharing on the ground that it was a ploy to divert the loyalty of their members away from the unions to the employer. Also as profit-sharing schemes are usually introduced at the initiative of the employer, the workers receive benefits which the unions have not won for them. Traditionally, the unions have been most interested in securing permanent increases in wage rates for all their members rather than obtaining uncertain increases of payment for those groups of members who may be fortunate enough to be employed by prosperous firms.[34]

The New Zealand Labour Department on the results of its 1948 survey concluded:

> "The reasons for its non-adoption lie on the one hand in the reluctance of capital to abdicate any portion of its sovereignty and on the other hand in the fear that capital will not be freely invested for a limited reward. In both directions these fears are, it is contended, misplaced . . ."[35]

PART III: THE FRENCH GOVERNMENT'S PROFIT-SHARING LEGISLATION

The profit-sharing legislation introduced by the French Government by the Ordinance of 17 August 1967 represents not only the most recent but also the first instance of a system of compulsory profit-sharing in a major industrial country. The reform is based on four fundamental principles.

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33 205 *N.Z. Parliamentary Debates* (1924), p. 807. Hon. Mr. MacGregor.
34 See *Profit-Sharing, A Study of the Results of Overseas Experience,* Department of Labour. Commonwealth of Australia, (1947), p. 17.
35 Note 30, p. 8.

A. PRINCIPLES OF THE REFORM[36]

1. Profit-sharing becomes a recognised right. For the first time worker participation in the fruits of expansion is recognised as a right, since the system is compulsory, at least for the enterprises which have the characteristics defined by the Ordinance. An earlier Ordinance of 7 January 1959 which was optional in character had introduced certain tax and social security exemptions for firms that would initiate profit-sharing schemes.

> "This met with little response, and only about 300 firms acted on it. The proposal had a lukewarm reception from employers and shareholders alike and aroused many fears. Moreover the workers themselves did not seem to be in favour of the measure."[37]

2. The proceeds of the employee's share must be saved. The amounts appropriated to the employees represent the salary and wage earner's share in the formation of capital within the firm. For this reason it was deemed appropriate that there should in general be a five year period of inalienability during which salary and wage earners could neither sell nor transfer their rights.

3. The system of profit-sharing should result from an agreement between the parties. The head of the firm and employees should be in agreement on the determination of the nature, method of management and the administration itself of the rights instituted by the Ordinance. The institutional framework and the content of agreements may be the object of an extremely wide number of choices. Firms whose management and employees reach an agreement for a profit-sharing system which employs different methods from those defined in the Ordinance[38] may submit such agreement to the C.E.R.C.[39] for confirmation.

4. The procedures are based on dialogue. In a more general fashion the Ordinance aims to create a greater participation by employees in the results of the firm. This consideration is not only true for financial matters because the reform also anticipates the development of a social dialogue within the enterprise between workers and management.

B. THE EXTENT OF THE REFORM

1. An improvement in the overall remuneration of workers. The level of the supplementary remuneration varies greatly from one

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36 The following principles have been extracted and translated from: Ministère de l'Economie et des Finances, *La Participation des Salariés aux Fruits de l'Expansion des Entreprises,* Service de l'Information, No. 12.67.3.

37 *French Worker Participation in Profits,* French Embassy Press and Information Service, No. B/57/4/70, p. 1.

38 "Accords dérogatoires": see Article 5, Ordinance 17 August 1967.

39 Centre d'Etudes des Revenus et des Coûts. The composition and functions of this body are described later.

enterprise to another; in certain firms, running at a loss or low profit there may be not profit to share for a number of years; in others the employees' share may amount to 4, 5 or even 6% of the annual total of salaries.[40] However the Ordinance is in no way intended to create a system of direct remuneration or to have any influence on wages.[41]

2. A more active participation by workers in the life of firms. Participation, although not intended to alter the responsibilities of the head of the firm, should strengthen the right of employees to information and to discussion of such information with management. This is intended to create an active personal interest by workers in the progress of their firms.

3. The promotion of investments. A firm is not taxed on profits which it allocates for productive investments provided that this amount does not exceed the amount allocated as the employees' shares in profits for that year. This tax saving is intended to encourage an increase in self-financing and capital investment by firms.

4. The development of savings. One of the goals of the reform is to develop a savings habit among employees. The legislators considered that the five year period of unavailability of the employees' funds should develop in workers a taste for stable savings over a period of time. To this end, when profit-sharing was introduced the Government created the machinery for company savings plans, intended to absorb any funds released under profit-sharing schemes.

SCOPE OF PARTICIPATION

Article 1 of the Ordinance of 17 August 1967 provides that every firm[42] which usually employs more than 100 employees whatever the nature of its activity and whatever its legal form, is required to comply with the provisions of the Ordinance which guarantees the right of employees to participate in the fruits of the expansion of the firm. For firms employing less than 100 persons the scheme is optional, but if they choose to comply then they will automatically receive the benefits provided in the Ordinance.[43]

Although in principle the Ordinance applies to all enterprises with more than 100 employees, certain special provisions have been found necessary for national corporations to which the concepts of "profit" and "company capital" have no real meaning. Thus corporations whose main purpose is to provide a public service and whose prices and expenditure are controlled cannot make a "profit" in the conventional use of the term. Others operating in the competitive sector which have the freedom to control their prices and general method of operations, must, subject to their special features, follow

40 See the Table "Results of Participation 1968", post.
41 *Notes du Ministère du Travail,* No. 4, 25-31 Janvier 1971.
42 In this article the word "firm" is intended as a generic term to include all the various legal forms of business covered by the Ordinance.
43 Art. 14.

a system similar to profit-sharing as laid down in the Ordinance. Between these two types of national corporations is a whole range of enterprises for which special rules are required.[44]

THE WORKERS' SPECIAL PARTICIPATION RESERVE FUND

Article 2 provides that each year a special worker participation reserve is to be formed by setting aside a portion of the profits, realised in Metropolitan France or its overseas Departments. This amount is calculated on the basis of the firm's taxable profits (net of depreciation). From this sum tax (corporate or personal depending on how the firm is owned) is first deducted and then a further deduction is made of 5% on the firm's capital (including reinvested capital) employed in the business, as determined by the tax inspector.

The workers' special participation reserve is equal to half the figure obtained by multiplying the remainder by the fraction of total salaries over the added value[45] of the enterprise.[46] The other half belongs to the shareholders. The legal formula is written as follows:

$$RSP = \left(B - \frac{5C}{100}\right) \frac{S}{VA} \times \frac{1}{2}$$ [47]

Article 3 provides that each worker's share of the reserve is calculated proportionately to the salary received within the maximum limits set by decree. The implementing orders provide on the one hand, the monthly pay figure taken into consideration in calculating the distribution of the reserve is limited to 4,650F; on the other, the amount distributed to any one person may not exceed 6,840F a year.[48] It follows that the highly paid senior and management staffs will not benefit in proportion to their salaries.

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44 The legislation providing for shareholding by workers in the nationalised Renault Car Company is a good illustration of the adaption of the ordinary rules for profit-sharing to an enterprise with special characteristics; see Loi no. 70-11 du 2 Janvier 1970 relative à la Régie nationale des Usines Renault; Journal Officiel, 4 Janvier 1970, p. 145. See also Notes et Etudes Documentaires, *L'Actionnariat des Salariés,* La documentation Francaise, Paris, 1972, pp. 51-54. This will be referred to as *L'Actionnariat des Salariés.*

45 The "added value" is the total economic result realised in the firm's production for that year.

46 "This formula is used to avoid an unearned increment to employees of heavily capitalised firms. A simple division of the 'super-profit' (the balance) between shareholders and employees, without allowing for different degrees of capitalisation, would yield a much higher benefit to employees of, for example, oil firms than to those of firms where labour constitutes a large part of the costs." PEP (Political and Economic Planning) Vol. XXXIII No. 500, October 1967, Appendix to Chapter II.

47 RSP = Workers special participation reserve; B = net profit (after tax and 5% interest on capital); S = Salaries; VA = added value. Georges Lasserre, Professor of Law, University of Paris, *La Participation des Salariés aux Fruits de L'Expansion des Entreprises,* Revue d'Economie Politique (1968), p. 77 and 80 criticises this formula, inter alia, for the reason that the use of a net profit is an artificial concept more likely to hinder workers than to assist them in acquiring a better understanding as to the operations of their firm.

48 Lasserre, *La Participation* p. 78. As at August 1972 one N.Z. dollar is equivalent to about six French francs.

The financial results obtained by employees in 1968 by virtue of the new legislation are shown in the following table prepared by the Interministerial Department of Worker Participation and Interest.[49] In the first year of its operation, of some three million employees covered by the system, more than two thirds were able, by virtue of the results of their firms, to have a share of the profits allocated to them.

RESULTS OF PARTICIPATION (1968)

Nature of Industry or Commerce	No. of employees covered by an agreement	No. of employees having benefited from the distribution	Total of the sums distributed (in francs)	Importance of participation in relation to salaries (%)	Importance of participation in relation to net profit	Total participation per employee (in francs)
1. Extraction — power	54,509	42,750	16,424,000	2.2	6.3	324
2. Metals and mechanic	842,057	574,884	211,627,000	2.8	14.4	386
3. Public works and construction materials	442,815	291,182	64,661,000	1.7	14.4	222
4. Chemistry and rubber industry	193,111	165,201	92,609,000	4.1	14.4	561
5. Textile clothing leather	248,664	156,363	46,184,000	3.2	16.4	295
6. Food wood paper	358,106	227,729	118,941,000	3.4	14.4	428
7. Transport and commerce	524,214	418,851	120,622,000	2.3	13.1	288
8. Banks and other services	279,778	267,506	94,485,000	2.4	9.8	353
Totals or averages	2,943,254	2,167,918	763,553,000	2.7	13.2	353

TAXATION ADVANTAGES FOR FIRMS

The amount distributed to the employees' special participation Since the company tax rate is 50% the firm will save on taxation one half of what it pays into the employees' participation reserve fund. reserve in each year is deductible from that year's taxable profit.[50]

49 Centre d'Etudes des Revenus et des Coûts, *La Participation des Salariés aux Fruits de l'Expansion.* La Documentation Francaise, Paris, 1971. Table 15 p. 20. This text will be referred to as "C.E.R.C. *La Participation*".

50 Article 8, Ordinance 17 August 1967.

A second benefit for firms is that they can make tax-free provision for investments to an amount being equal to that of the participation reserve fund. This results in a further tax saving of 50% on the amount of the reserve. The reason given by the French Government for these substantial tax concessions is firstly to avert the danger that profit-sharing may lead firms to reduce their self-financing margins and secondly to encourage the retention of part of the profits for productive investment and capital expansion.[51]

TAXATION ADVANTAGES FOR EMPLOYEES

The amounts credited to employees by virtue of the participation are not assessable for personal income tax provided that the principle of the unavailability of these sums during a period of five years is respected. It follows that at the time when monies or securities are credited to an employee, if he has an immediate right to dispose of them, they are assessable for income tax.

AGREEMENTS IN DIFFERENT TERMS FROM THE ORDINANCE (ACCORDS DEROGATOIRES)

Article 5 of the Ordinance provides that the participation agreements can depart from certain aspects of the normal system as set out in the other Articles (known as "accords derogatoires") on condition that such changes be approved. The same Article with certain reservations, allows firms which had already implemented a participation scheme before 17 August 1967 to maintain that scheme in force until 1 January 1970. Of the 5,772 agreements in existence at 31 December 1970, 1,860 (32.4%) contained conditions which derogated from the provisions of the Ordinance and thereby came before the supervision of the C.E.R.C.[52] The alterations most frequently introduced by the signatories concerned the method of calculation of the special participation reserve (59% of the employees concerned by the accords derogatoires), the length of service of the employee to determine the beneficiaries of the participation (53%), the methods of sharing the reserve between the beneficiaries (47%) and other derogations (27%).[53]

Where the parties wish to depart from the provisions of the Ordinance their agreement will not qualify for the tax benefits accorded to profit-sharing schemes until the Minister of Social Affairs has confirmed such agreement. This decision is given on the recommendation of the C.E.R.C. and an unfavourable opinion from this body will prevent the confirmation of an agreement.[54]

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51 French Worker Participation in Profit-Sharing, French Embassy Press and Information Service, p. 7. For a criticism of these tax concessions on the grounds that they amount to a subsidy or gift to firms paid for by the taxpayer see Lasserre *La Participation*, pp. 80-86.

52 Centre d'Etudes des Revenus et des Coûts. The composition and functions of this body are described a little later in the text.

53 C.E.R.C. *La Participation*, pp. 17-18; see also Arts. 3 and 4 Ordinance, 17 August 1967.

54 Ibid., pp. 28-29.

The C.E.R.C. was created by a decree of the 18 April 1966. Its task is to assemble and put at the disposition of the Government and the other participants in France's economic and social life the necessary information on which to form a revenue policy for the French economy. To achieve this object it seeks to improve the basis and presentation of statistics relating to revenue, costs and prices. It analyses the growth of productivity in firms as well as the methods of sharing the benefits of such growth between the consumer, the workers, management and owners.

The C.E.R.C., when it meets to examine the accords derogatoires under Article 5, comprises the President and the five members of the Council of the C.E.R.C. plus two employer representatives and two employee representatives. The limited number of these representatives, two for each of the parties, in view of the multiplicity of the union organisations has led to limitation of the term of office of each representative to one year. In this way, the different organisations can turn by turn take part in the C.E.R.C. All the members have speaking and voting rights.

Article 21 of the decree of 19 December 1967 permits the Directors of several Government Departments to participate in the deliberations of the C.E.R.C. in an advisory capacity. These officials include the Director-General of Imports, the Director of the Treasury for the Ministry of the Economy and Finance, the Director of Industrial Policy to the Minister of Scientific and Industrial Development and the Director-General of Work and Employment.

A representative of the General Confederation of Workers' Co-operative Companies takes part in the work of the C.E.R.C. in an advisory capacity when it is dealing with agreements concluded by such companies. A Government Commissioner charged with co-ordinating the opinions of the different departments and with presenting the Government's position delivers his observations, most often oral, on each of the participation agreements submitted to him.

Lastly a reporter (rapporteur), assisted where necessary by special reporters, has the task of analysing and explaining to the C.E.R.C. the contents and any special characteristics of a particular agreement. The reporter in addition to explaining agreements also proposes his preliminary opinion on them to the C.E.R.C.[55]

CONDITIONS OF PRESENCE OR OF LENGTH OF SERVICE

Article 3 of the Ordinance entitles those employees who have been at least three months with the enterprise during a financial year to participate in the profits of that year.

The C.E.R.C., in examining agreements whose signatories sought

55 The above description of the organisation and methods of work of the C.E.R.C. is translated from C.E.R.C. *La Participation,* pp. 27-34.

to alter the length of qualifying service found that many employee representatives, managers and boards of directors held the view that an employee who has not belonged to a firm for more than three months is not really integrated. These people considered that it was somewhat absurd to confer rights locked up for five years to a person who is only passing through the firm and whom one will probably not be able to trace at the end of the period when the funds are made available.[56]

A number of the signatories asserted that employee participation assumes that one has shown a certain interest for the enterprise, a sort of attachment for the social group that it represents and its future development; it was obvious that an employee of three months standing could not be considered as demonstrating this interest or this attachment.

A number of firms endeavoured to justify the derogation they sought on the grounds that in their industry the first months after the beginning of employment corresponds to a period of apprenticeship and that in these circumstances the employee does not really contribute to the firm until after six months or more. Others have emphasised the administrative expenses engendered by the necessity of sharing and of administering for five years sums due to salary and wage earners who have remained little more than three months with the enterprise.

Taking into account the general spirit of the Ordinance, the C.E.R.C. decided on a rather strict position, approving only in exceptional cases clauses which reserved the participation in profits to those salary earners who had been with the enterprise for longer than the three months stated in Article 3. Thus it decided not to approve any agreement stipulating a period which was very much longer than three months; six months constituting the maximum derogation normally authorised by the C.E.R.C.[57]

Arguments based on the necessity of facilitating "integration" of personnel and of encouraging "the spirit of perseverance" were also regarded as insufficient by the C.E.R.C. because the Ordinance of 17 August 1967 did not have for its object the encouragement of the stability of personnel but rather the allocation of a share in the fruits

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56 M. Philippe de Chartre, Secretary of State to the Ministry of Labour, Employment and Population has raised the question whether the three month qualifying requirement in the Ordinance should be modified in view of the fact that a third of all accords derogatoires depart from the normal provisions of the Ordinance only in that they require a longer period of qualifying service. *Bilan et perspectives de l'Ordonnance de 1967 sur la Participation des Salariés aux fruits de l'expansion des entreprises.* Notes du Ministère du Travail. No. 4. 25-31 Janvier 1971.

57 See Case H.0017. Company B 22 April 1969. Application by porcelain manufacturing company for a 12 month qualifying period before new employees could participate on the grounds that in their first year by virtue of the long training requirement they did not really contribute to the growth of the company. The C.E.R.C. declined to approve the application because it was not substantiated by sufficient evidence and it was a very significant deviation from the three month period mentioned in Article 3.

of the expansion to all employees who have contributed by their work to the realisation of a firm's expansion, whether or not they have been with it for a long time.[58]

THE DEFINITION OF BENEFICIARIES

In the area of defining these employees who will benefit from the Ordinance, the C.E.R.C. has been particularly strict since it did not wish to interfere with property rights conferred upon employees by statute. The C.E.R.C. found that most agreements which endeavoured to restrict the number of workers who could participate in profits were inspired by perfectly legitimate motives and were often not only accepted but also formulated by the employees' representatives themselves.

The guiding principle used by the C.E.R.C. in examining accords derogatoires was that of non-discrimination. "All the employees who have participated in the realisation of the fruits of expansion have a right, no matter what their legal title or position in the firm, to receive their share of the result".[59] Thus agreements cannot exclude a section of the employees on the grounds that they are foreigners, seasonal workers,[60] part-time workers,[61], hourly,[62] daily workers[63] or on the other hand people who occupy a very important position[64] in the firm. Although most of these categories except senior staff do not have a right to the same sums as the regular staff because the annual salary on which their share is based will vary greatly, no matter how trifling the amount to which they are entitled, they will still be classified as beneficiaries.

Another problem in this area was the case of employees who had been subjected to disciplinary measures. The grounds for excluding such people from the benefits of participation were that they had shown no interest in the advancement of the firm and indeed had sometimes directly impeded or damaged the business. However, the C.E.R.C. refused to become involved in this delicate sphere because certain faults which incur disciplinary measures may not necessarily have prevented the employee concerned from having contributed to the firm's progress. It was considered that since participation is a right granted by law, only a legal authority such as the courts should be able to deprive an employee of this right and that only the courts were competent to judge the substance and seriousness of the alleged faults. Thus in *Case H.0222 S.A.R.L. B, 24 March 1970* the C.E.R.C. held:

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58 See Case H. 0118 — Company D, 27 January 1970. Application for one year seniority requirement refused. C.E.R.C. *La Participation*, p. 102.
59 Ibid., p. 91.
60 Case H. 0690 — Company P, 26 May 1970, ibid., p. 95.
61 Case H. 0744 — Groupe B, 26 May 1970, ibid., p. 94.
62 Case H. 0342 — Company G, 28 April 1970, ibid., p. 95.
63 Case H. 0903 — Company B, 30 June 1970, ibid., p. 95.
64 Case H. 0102 — Company B, 24 February 1970, ibid., p. 99.

> "Article 2 of the Agreement provides that the enterprise committee will be able on a unanimous vote to exclude from the benefits of participation members of the staff who have been dismissed for serious or inexcusable faults. This clause is unacceptable with regard to the principle of the Ordinance according to which the participation is a right open to all employees who have contributed to the expansion of the firm for which they work."[65]

Other borderline cases presented to the C.E.R.C. concerned employees who were undergoing training, those who worked for the subsidiary of a parent company and those who worked in "extensions" of the first such as on committees and social services. Lastly was the rather unusual situation where certain employee-owners, and senior or highly paid management staff had voluntarily renounced their rights because they considered that they already benefitted sufficiently from the profits of the firm.[66]

THE WAYS IN WHICH THE RESERVE IS TO BE USED

The nature and methods of administration of the employees' special reserve are to be decided by collective conventions or by agreements concluded with the most representative trade union organisations, or with the joint production committee.[67]

The reserve must be made over to the employees in one of the following three forms:[68]

1. Allotment of shares in the firm (existing or newly created by capitalising reserves): for this purpose firms will be permitted to buy their own shares.
2. Payment of the sums making up the special reserve into an investment fund with the allocation to each employee of a credit of his individual share of the total fund. These payments constitute debts of the firm such as debentures or blocked current accounts in employees' names. The sums involved must be reinvested in the firm through a fund to be agreed on.
3. Shares or certificates in any investment company external to the firm, or payments into personal accounts opened within an approved firm savings plan.

In the absence of agreement after a year from the closing of the financial year in which the employees' rights commence for the first time, then on the certification of the labour inspector to this effect, the employees' reserve is taken in the form of current accounts in the

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65 Ibid., p. 96.
66 Case H. 0102 — Company B, 24 February 1970, ibid., p. 99 held that such rights can be renounced but only by the individual concerned and such a decision can be reversed at the beginning of each new financial year.
67 Arts. 4 and 10 Ordinance 17 August 1967.
68 Art. 4.

employees' names, i.e. alternative no. 2 above.[69] These funds are blocked for a period of eight years instead of the normal period of five years which applies where agreement is reached.

The most frequently chosen method of employing the participation reserve was that of blocked current accounts and, in exceptional cases debentures, accounting for 56% of all agreements. Investment of funds outside the firm and firm savings plans accounted for 41% and 6% of agreements respectively. Only 0.5% of agreements chose the allotment of company shares to employees.[70] In the light of these figures the whole concept of employee shareholding (described earlier as co-partnership) and its function of involving workers in the progress of their employer companies was called in question.

For this reason the French Government has sought to encourage employee shareholding through special legislation subsequent to the Ordinance of 17 August 1967. President Pompidou on 16 September 1969 made a general policy declaration that legislation relating to shareholding among all or any of the salaried staff of a company would be brought before Parliament in the 1970 autumn session. On 22 September 1969 M. Pompidou stated:[71]

> ". . . worker shareholding . . . is an old idea. It seems to me to be regaining strength. It seeks to involve the workers in the life of the company otherwise than by mere variations in pay. It also constitutes at the same time an endeavour at achieving fairness, a training in responsibility; and this is why I believe that it should be encouraged . . . This form of worker involvement is the most healthy economically and and socially the most satisfying."[72]

The new legislation for employee shareholding plans was introduced in the Law of the 31 December 1970[73] and the Decree[74] of the 7 June 1971. The inspiration for the measures was derived to a significant extent from the "stock option plans employed with success in the Anglo-Saxon countries".[75] Although certain French enterprises had implemented such schemes in the past these were not only exceptional cases but also less extensive and less frequent than those practised in other countries, particularly in the United States.

A Ministry of Finance statement indicated that although the text did not limit the number of eventual beneficiaries it was probable that

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69 Art. 11.
70 These figures are taken from a publication of 10 March 1972 referred to in this paper as *L'Actionnariat des Salariés*, p. 47.
71 Statement made at a press conference on the announcement of the shareholding project for Renault workers. *L'Actionnariat des Salariés*, p. 47.
72 Ibid., p. 54.
73 Loi no. 70-1322 relative a l'ouverture d'options de souscription ou d'achat d'actions au bénéfice du personnel des sociétés. Journal Officiel du 30 Janvier 1971.
74 Décret no. 71-418 du 7 Juin 1971.
75 President Pompidou, 16 September 1969, quoted in *L'Actionnariat des Salariés*, p. 47.

the legislation would be used rather as a means of involving the managerial and controlling staff, whereas the procedures of the 1967 Ordinances were more particularly reserved for the employees as a whole. By giving an additional motivation to the management staff the intention was to recruit and maintain good personnel and to reward them for the results of their competence and effectiveness.[76]

The reform[77] provides companies with the right to increase their authorised capital and offer the shares thereby created to the staff. The beneficiaries have a period of five years in which to exercise the option. Except for some general principles, the law imposes no obligation on either the companies which give the options or the beneficiaries which receive them. All the employees are able to benefit from the option but the company has the right to limit the range of persons so entitled. In order to adapt the share option plan to their structure and objectives companies are permitted to make their own special rules such as the qualifying length of service and the period for which the shares must be kept.

In principle no limit is placed on the employee's right to resell his shares immediately after the exercise of the option, although the option agreements themselves may impose a minimum period during which the shares must be held. For taxation purposes the benefit corresponding to the difference between the market value of the share at the date of exercising the option and the price of the option constitutes additional salary. However, this benefit is exempted from income tax if the shares thus acquired are registered and the beneficiary undertakes not to dispose of them for a period of five years from the date on which the option is exercised.

FIVE YEAR PERIOD OF INALIENABILITY OF WORKERS' SHARE IN THE PROFITS

Exceptions to the Rule

Article 6 of the Ordinance lays down that except as provided by decree the rights constituted for the benefit of the employees by virtue of the provisions of the present Ordinance cannot be negotiated or demanded until the expiration of five years starting from the commencement of these rights.

Exceptional cases provided by decree are the marriage, dismissal, retirement of the beneficiary or the disability, serious illness or death of the beneficiary or of the beneficiary's spouse.[78] Another exception to the rule of inalienability is that firms are authorised to pay directly to salary and wage earners the sums due to them when these do not amount to 20 francs per person.[79]

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76 *L'Actionnariat des Salariés*, p. 48.
77 The following two paragraphs are a very brief outline of some of the more important provisions of the Law of 31 December 1970.
78 Décret no. 67-1112 du 19 Décembre 1967, Art. 16.
79 Art. 62-IV, Loi No. 68-1172 du 27 Decembre 1968.

The rights of the salary and wage earners are immediately liquidated in cases of dismissal but not of resignation.[80]

REVENUES PRODUCED

Whatever the method of administration used, the C.E.R.C. has held that the employees' credits in the special participation reserve must be income producing.[81] Although there is no provision in the Ordinance which imposes such a principle the C.E.R.C. has taken into account three factors. Firstly, Article 11 of the Ordinance provides a rate of interest of 5% on employees' credits placed in the current accounts of the employer where the parties have failed to agree on the method of investment to be used. Secondly, because the employee is forbidden to dispose of the credits for a period of five years the legislature must for this reason have intended that these funds should be income producing, since during this space of time no capital gain can be hoped for. Lastly it would not be fair that the enterprise and the shareholders should benefit by these methods of financing at no cost to themselves.

The parties are free to agree on an appropriate rate of interest provided that this is not too low with reference to the current money market rates. As a general rule 5% has been considered by the C.E.R.C. to be the minimum rate.[82] Provided this minimum is observed the parties may set a formula for fixing the rate which varies from year to year, with reference, for example, to the official index or an index of rates agreed by the parties which follows the fluctuations of the money market. However, any such agreement must be decided and set out in a precise formula and if there is to be an annual variation this cannot be left to the unilateral decision of management.[83]

INFORMATION FOR THE EMPLOYEES

The collective and individual information to be given to employees whether there is an agreement or not must be at least the equivalent to that required under the Decree of 19 December 1967.[84]

(a) Collective information

The staff are to be informed of the formula which has been used to calculate their rights in a financial year in which there has been a sharing of profits. This is done in accordance with the terms of the agreement between the parties or, in default of such agreement, by the posting of notices at the place of employment.[85]

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80 Case H. 0018 Company A — 24 June 1969; C.E.R.C. *La Participation*, p. 128.
81 See Case H. 0189 — Company V, 24 February 1970, C.E.R.C. *La Participation*, p. 140 where a clause in an agreement stipulating that "the parties acknowledge that the current accounts will not earn interest" was held to be contrary to the principles of the Ordinance.
82 C.E.R.C. *La Participation*, p. 140.
83 Case H. 0384 Establissement E., 28 April 1970, ibid., p. 140.
84 Décret no. 67-1112 du 19 Décembre 1967, titre III, Arts. 24-27 .
85 Ibid., Art. 24.

Within six months after the closing of the financial year the employer must present to the delegates of the staff or other approved body a report which comprises:

— the elements which serve as a basis of calculation of the total of the participation reserve for the last financial year
— precise information on the administration and use of the sums appropriated to this reserve[86]

(b) Individual information

On every occasion in which shares in profits are allotted amongst employees a card must be delivered to each beneficiary indicating

— the total amount of the participation reserve for the last financial year
— the amount of the rights attributed to the individual concerned
— the method of administration of the rights in cases where these have been entrusted to an organisation
— the date on which the rights may be demanded or transferred
— the circumstances in which the rights can be liquidated or transferred before the expiration of the five year period.

EVALUATION OF THE ORDINANCE

Like any major reform affecting the interest of workers and employees the Ordinance of 17 August 1967 has attracted its share of controversy. Professor Lasserre[87] is perhaps one of the more outspoken critics of the measure. He has said:

> The reform was imposed on the country when it had been wanted by almost nobody . . . And yet, when the Ordinance appeared, it was evident that it completely failed to answer the great intentions expressed by the Head of State.[88] It was a curious result of the obstinacy of a man who is not a specialist in these questions and who sees them from a distance, and on the other hand of alarmist campaigns and pressure of big business . . . which obtained an extraordinary metamorphosis of the reform in a supplementary financial advantage[89] for itself, without any sacrifice on its part.

Lasserre criticises the scope of the application of the reform on the grounds that it will apply to less than half of the 4.9 million employees who work for firms employing more than 100 workers. This he says would make approximately two million beneficiaries out of 13 million workers in commerce and industry.[90] He feels that the system created by the Ordinance is not a valid system of worker

86 Ibid., Art. 25.
87 Georges Lasserre, Professor of Law and Economic Sciences at the University of Paris.
88 I.e. General de Gaulle.
89 He refers to the tax advantages given to firms under Art. 8 discussed earlier.
90 Lasserre, *La Participation,* p. 77.

participation and interest, capable of modifying the attitudes and behaviour of workers, able to make them consciously stalwarts of the firm and to stimulate their zeal and their goodwill. The period of 5 or 8 years before the receipt of the benefit in a disposable form, plus the extreme smallness of the benefit, would in his view suffice to deprive it of any efficacy.

Criticism is also made of the base on which the special workers' participation reserve is calculated[91] because it substitutes the actual profit for an artificial notion of "fiscal" profit.

> "The workers are therefore going to be placed in a situation, not of participation, but of passive dependence, with regard to arbitrary figures, over which they can have practically no power".[92]

His most serious criticism is that the burden of meeting the tax exemptions granted to the firms falls upon the taxpayer:

> "It is no longer the firm which shares its enrichment with the workers in order to make them true associates: it keeps the benefit completely for itself. It is the entire nation which gives the firms a subsidy, a gift . . ."[93]

The legislation is further criticised on the grounds that its benefits go only to a small minority of workers, not on the grounds of their need or merit but simply to those who happen to work in the most profitable enterprises. For those people the reform represents a small supplementary "private benefit". If the share going to this minority of workers remains as insignificant as it appears it will be, then Lasserre considers that the reform will be met with indifference and a great many complications will have been introduced for nothing. But if the workers' share takes on a more important aspect then the 85% of those who are excluded, through no fault of their own, will want their share.

> "It is there that the danger of the unlucky Ordinance lies, and not in the prophesies of doom voiced by management and the stock exchange."[94]

Nevertheless the official view of the French Government is that the measure does appear to be operating successfully. The Secretary

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91 Art. 2, discussed earlier.
92 Lasserre, *La Participation,* p. 80.
93 Ibid., p. 81.
94 Ibid., p. 83. Although Lasserre is particularly severe in his criticism of the provisions, application and aims of the Ordinance he does offer a constructive alternative, namely workers' co-operatives. In these co-operatives the workers own the means of production or the goods which are produced and are totally responsible for the success of the operation; *Fonctions du profit et participation des travailleurs,* Economies et Sociétés, Vol. V. No. 12, December 1971. See also, by the same author, *La réforme de l'entreprise et la participation.*

of State for the Ministry of Labour Employment and Population, M. Phillippe de Chartre, in a report on the operation of the Ordinance up to the beginning of 1971 stated:

> "In all objectivity, and at the present moment, one can conclude, I think, in the success of the application of the Ordinance of 1967, taking into account the different objectives which it includes. This success is owed, of course, to the decisive action of those who have been the promoters and the pioneers of this reform and also to the progressive understanding and to the profound intuition of the work force. From the present time . . . it is incontestable that, by the application of the participation agreements, the partners in the company have found, within their enterprises, the possibility for concrete and objective discussions, taking place in a climate of free co-operation. I add . . . that the Ordinance of 1967 has well-defined objectives, and that it is fundamental, in particular, that it does not have an influence on salaries, it introduces a participation by employees in the fruits of company expansion . . . We have a feeling that beyond the initial reservations, a large agreement is developing and that beyond even today's results, one will perceive, as the President of the Republic noted, in his last press conference, the capital importance of the Ordinance of 1967 in three or four years."[95]

No doubt, as in most controversies, the truth of the situation lies somewhere between the two extremes and the Ordinance, though proving moderately successful, may require certain important modifications if it is fully to achieve its purpose. At any event, it is probably too early to pass judgment on the scheme which will not give the great majority of employees any tangible cash benefit until it has been in operation for 5 to 8 years.

PART IV: THE ADVANTAGES OF PROFIT-SHARING LEGISLATION

We have now considered profit-sharing legislation in New Zealand and France. From the experience of nearly half a century it is clear that s. 67 of the New Zealand Companies Act 1955 is moribund. On the other hand the French profit-sharing legislation commencing with the Ordinance of 17 August 1967 has not yet been in operation long enough for a reasonably conclusive judgment to be made on its success. For this reason the following pages will consider the views of some of the commentators on profit-sharing in an endeavour to assess what benefits can reasonably be expected from the enactment of legislation designed to require or encourage profit-sharing.

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95 *Bilan et perspectives de l'Ordonnance de 1967 sur la participation des Salariés aux Fruits de l'expansion des entreprises.* Notes du Ministère du Travail, 25-31 January, 1971.

THE INCENTIVE ASPECT OF PROFIT-SHARING

Does a profit-sharing scheme in fact act as an incentive to individual employees to make a greater effort and thereby increase production?

> "The value of profit-sharing and co-partnership cannot be assessed solely by reference to the amount of the financial benefit accruing to the participants, and, moreover for some kinds of schemes this financial benefit cannot be identified for precise measurement."[96]

In 1946, a report from the National Industrial Conference Board of the U.S.A. doubted whether the amounts distributed to individual employees were usually large enough to induce employees to put more effort into their work.[97] At that time in the U.S.A. the maximum tax deduction allowed to companies for profit-sharing bonuses was 15 per cent of the wages bill. A survey of 264 schemes showed that slightly less than half the schemes distributed amounts in excess of ten per cent of annual wages.[98] In the United Kingdom a survey in 1955 by the Ministry of Labour reported that, of 259 active profit-sharing plans, 163 paid amounts to employees of less than ten per cent of wages and the average paid to all participants in profit-sharing schemes was 6.3 per cent of wages.[99] In Australia, amounts varying from 0.6 per cent to 16 per cent of the annual wages bill of their respective firms were distributed to employees in 1951.[100]

In New Zealand Dr. Lau has calculated the possible effect of profit-sharing here in terms of increased benefit for employees. He says that according to Reserve Bank statistics for 1971 the average company income in New Zealand was approximately 9 per cent tax paid. If 8 per cent were set aside for dividends and reserves and if the balance were shared 50:50 between the labour force and shareholders the average profit shared bonus would be about 70 million or about 3.2 per cent, i.e. still less than two weeks' wages if all employees participate and that is a relatively good year.[101] He concludes:

> "The monetary reward resulting from profit-sharing alone will

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96 *Profit-Sharing and Co-Partnership Schemes,* Ministry of Labour Gazette (U.K.), May 1956, p. 166. Referred to as "Labour Gazette, May 1956."

97 Brower, Beatrice F., *Experience with Profit-Sharing,* The Conference Board Management Record, New York National Industrial Conference Board, Vol. VIII, No. 2, February 1946, pp. 33-38.

98 Flippo, Edwin B., *Profit-Sharing in American Business,* Bureau of Business Research, College of Commerce and Administration, Ohio State University (1954), p. 41.

99 Labour Gazette, May 1956.

100 Hurley, W. M., and Wickham, O. P., *A Review of Australian Profit-Sharing Practice.* Personnel Practice Bulletin Vol. VII, No. 3, September (1951), pp. 3-10. See also Westaway & Jacob, *Profit-Sharing Experience in Australia and Overseas* (1959), Vol. XV, No. 1, Personnel Practice Bulletin, pp. 22-33.

101 *Aspects of Profit-Sharing,* N.Z. Commerce, Vol. 27, No. 3, September 1971, pp. 11-12.

> not be large enough to influence the employee's attitude. Therefore a profit-sharing scheme should never be introduced as a substitute for good wages and good working conditions."[102]

Even if profit-sharing did significantly increase a New Zealand worker's earnings would this guarantee better industrial relations? Howells and Woodfield[103] in their survey of worker, union and management preferences in two firms in the freezing industry concluded, inter alia:

> "Union officers followed management in exaggerating the motivation value of money, but seemed to deny that it applied to themselves — their predictions for this one item were considerably in excess of their own preferences. This settled conviction by management and officers that workers are 'wage-pursuing automata' motivated mainly by the dollar has been revealed by other writers. Though the pay packet theory, as C. A. Mace describes it, is not a bad place to start from, the real danger is that it stifles thought at precisely the point where thought should begin."[104]

The theory has recently been advanced that most unrest and conflict between workers and management in industry is not because of financial rewards, even if these are the apparent or superficial cause of conflict. In an attempt to answer the question "what motivates men? Not simply to go to work, but more importantly to work to the best of the ability", recent studies in the behavourial sciences:

> ". . . have challenged the view that workers are by nature lazy and work shy and have argued that what motivates men to achievement is the chance to exercise the skills and capacities which are denied in many jobs. Job enlargement and job enrichment are among the indicated remedies.[105]
> . . . money is seldom a source of positive satisfaction, that what motives achievement is the chance to realise some aspect of the self, some skill or capacity."[106]

The writer suggests that the conclusion to be drawn from the above discussion is that any additional financial advantage to the worker by virtue of a profit-sharing scheme should not be relied on in itself to achieve harmonious industrial relations.

IMPACT ON INDUSTRIAL RELATIONS

What contribution is profit-sharing likely to make towards improving industrial relations?

A particularly thorough study of the effect of profit-sharing plans

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102 Ibid., p. 12.
103 Associate Professor and Lecturer respectively in the Department of Economics at the University of Otago.
104 *The Ability of Managers and Trade Union Officers to Predict Workers' Preferences* (1970), 8 B.J.I.L. 249-250.
105 Cotgrove, Dunham and Vamplew, *The Nylon Spinners*, p. 8.
106 Ibid., p. 28.

on labour and management relations was undertaken by Helburn in 1965.[107] His findings were based on the responses to questionnaires by management and/or unions in a representative sample of American companies. The following table indicates the impact of profit-sharing upon industrial relations as seen by management and unions in Helburn's study.

MANAGEMENT AND UNION: THE IMPACT OF PROFIT-SHARING UPON INDUSTRIAL RELATIONS[108]

Industrial Relations	Management		Union	
	Number	Per Cent	Number	Per Cent
Improved	115	55.6	34	33.0
Worsened	2	1.0	7	6.8
No effect	35	16.9	34	33.0
Can't evaluate	55	26.6	28	27.2
Total	207	100.1	103	100.0

The large number of "no effect" or "can't evaluate" answers emphasises the fact that profit-sharing is but one of a number of factors influencing a labour-management relationship. Therefore it is not easy to isolate and evaluate with any precision the influence of profit-sharing in any given situation.

In a further questionnaire respondents were asked to rate in order of importance undesirable occurrences which profit-sharing might have helped to reduce. Six occurrences were listed:

MANAGEMENT AND UNION: THE EFFECT OF PROFIT-SHARING ON THE REDUCTION OF SPECIFIC FACTORS IN INDUSTRIAL RELATIONS[109]

Factors	Overall Score[110]		Number of Times mentioned as a per cent of response[110]	
	Management	Union	Management	Union
Turnover	562	219	69.0%	49.4%
Reject and salvage	231	131	36.9%	32.3%
Work stoppages	145	89	22.0%	25.3%
Absenteeism	119	88	23.8%	25.3%
Written grievances	89	50	18.5%	20.7%
Tardiness	69	40	17.3%	12.6%

107 This study and its results are published in Metzger, *Profit-Sharing in Perspective,* pp. 163-177.

108 Ibid., p. 168, Table 28A.

109 Ibid., p. 168, Table 30A.

110 The overall score was derived by assigning a value of six points for first ranking, five points for second ranking, etc., through six ranks, and adding total points assigned. Some respondents simply checked factors rather than ranking them. If only one factor was checked, it was given six points. If more than one factor was checked, there were no points assigned to any of the factors, but the checks were counted in the "number of times mentioned".

Despite the rather encouraging results of Helburn's survey the writer considers that one should not place too much reliance on an improvement in industrial relations solely as a result of the introduction of a profit-sharing scheme. The reasonable expectations of profit-sharing are well expressed by Westaway & Jacobs as follows:

> "There is general agreement among writers that no plan can be successful where relations between union and management are poor or where the general atmosphere is filled with mutual distrust. Profit-sharing should emerge as a tangible expression of existing healthy industrial relations; it has little chance of altering existing poor industrial relationships."[111]

EMPLOYEE SHAREHOLDING AS A TYPE OF PROFIT-SHARING

Two important reasons are often given by the advocates of extended share ownership. Firstly the economic well-being of a country requires that as average earnings rise, an increasing number of people should retain some money for investment after immediate needs have been met. Although these savings may individually be small, in total they can amount to a considerable sum which wisely invested, could contribute substantially to the rate of the national growth. Secondly the fact that the ownership of industry is often concentrated in relatively few hands can give rise to a socially undesirable situation and can lead to unnecessary divisions and hostilities.[112]

A report, completed in 1963 by Guy Naylor, Barrister-at-law, commissioned by the British Wider Share Ownership Council investigated whether there was any enthusiasm in British industry for providing facilities for employee ownership of shares, either in the employing company or outside it. This report contained the following conclusions on employee shareholding.

Companies which had not adopted such schemes often did so for several main reasons. Some felt that if a company provides opportunities to buy its own shares it may appear to be inducing or encouraging its employees to do so, but that if it provides opportunities to buy other shares it may appear to be recommending them. In either case, if anything goes wrong, the employee may expect to be rescued by his employer. Moreover an employee with shares in the company in which he works has too many eggs in one basket. This however could be circumvented by encouraging employees to become shareholders in unit trusts rather than the employer company.

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111 *Personnel Practice Bulletin* (1959), Vol. XV, No. 1, p. 32.

112 "The 1965-6 Survey of Share Ownership by the London Stock Exchange gave an estimated 2½ million share owners, or about 7% of the U.K. adult population. The 1965 census of share owners conducted by the New York Stock Exchange shows that there are 20 million share owners in the U.S. adult population of 119 million or nearly 17%." *Sharing the Profits* Acton Society Trust and Guy Naylor (ed. Garnstone Press Limited) (1968) p. xvii.

Another argument was that the average employee should not invest in equities at all until he has got some readily realisable savings, has made provision for life assurance, has completed or almost completed any mortgage payment commitments, and has his hire-purchase obligations under control. The study found that it was difficult to devise a scheme which is fair, certain and explicable to employees. The average employee is uninterested in shareholding and would always prefer money. It is doubtful "whether possession of a stock certificate turns an employee into a capitalist".[113]

The most prevalent motives for starting schemes were to give an employee a sense of identification with the company. A minority view was that it would stimulate an interest in how the capitalist system works, and consequently lessen the appeal of nationalisation of industry. Other motives were to create an interest in the business in general, to stimulate loyalty, to encourage, attract and keep good employees, to provide incentive and a stake in the business, to encourage saving and provide for retirement.

Naylor includes in his report a "glancing reference" to what he was able to gather about the viewpoint of the employees from talking to employers. He did not find the view that employee shareholding encourages incentive and loyalty was widely held by employers. On the contrary some companies felt that better results were obtained from providing other benefits of a benevolent nature. It was also felt that profit-sharing (whether it takes the form of shares or not) which is based on the profits of the year is intrinsically unfair to the employee because within certain limits what he does or does not do has little effect on the year's profits or dividends.[114]

A further important question discussed by Naylor is that "Even if loyalty, incentive, identification, integration into the capitalist society, instinct for saving and many other laudable methods can be achieved by employee shareholding" is this the best method and if so, can the average employee afford it?[115] An average employee may already have many financial obligations both connected with and apart from his place of work. The large number of potential demands on a worker's pay packet can at least raise a prima facie doubt as to whether the average employee is well advised to become a shareholder at all.

In Italy legislation has provided for the distribution of company shares either free or at specially favourable prices for employees of a company, but the general experience has been disappointing because the shares were sold immediately the employees were entitled to do so.[116] West Germany allows a maximum amount of 624DM (about $NZ163.00) a year to be attributed to employees in the form of shares

113 Ibid., pp. 105-6.
114 Ibid., p. 109.
115 Ibid., p. 110.
116 *L'Actionnariat des Salariés*, p. 26.

in their employer companies. These shares are given at preferential rates but must not be sold for a period of five years. In Belgium also there is legislation giving employees certain tax benefits on the attribution to them of shares in their employer companies.[117]

On the New Zealand scene Dr. Lau's suggestion for a successful profit-sharing scheme is that co-partnership or the holding of shares in the employer company by allocating the profit share in the form of shares in the company is generally speaking not desirable.

> In times of adversity when employees need their savings most the value of shares fall. Also in listed companies there is the undesirable incentive to sell when share prices rise. Finally when employees are shareholders there may be a conflict between them and outside shareholders as to the amount which should be distributed and the amount which should be retained for reserves and such conflict could have the opposite result from that for which the scheme is designed to attain.[118]

INCREASED EFFICIENCY AND PRODUCTION

Is the assumption that profit-sharing will lead to increased efficiency and production justified? In the Profit-Sharing Research Foundation Supplementary Survey of March-April 1963[119] managements were asked to rate the effectiveness of their profit-sharing programmes relative to specific benefits. The following ratings were given:

	Per cent of companies rating profit-sharing programme "moderately effective" or "very effective" relative to specific benefit	
Specific Benefit	**Cash Plans**	**Deferred Plans**
e. In furthering employee interest in company, loyalty, feeling of partnership, sense of belonging	93%	94%
a. In improving morale, teamwork and co-operation	93%	84%
i. As a means of recognising and rewarding individuals for their contributions to growth of company	82%	72%
f. In improving quality, pride in workmanship, sense of responsibility	82%	65%
d. In increasing productive efficiency	81%	50%

117 Law of the 27 June 1970, Art. 3: see *L'Actionnariat des Salariés*, p. 26.
118 Note 101, ante, at p. 12.
119 Metzger, *Profit-Sharing In Perspective*, p. 129.

c. In attracting and holding desirable employees (reducing turnover)	79%	84%
j. In giving employees a better understanding of factors entering into business success (economic education)	74%	52%
h. In facilitating the introduction of new methods and equipment	64%	24%
b. In reducing wasted time and materials (cutting costs)	62%	55%
g. In providing economic security for employees	60%	93%

The majority of cash plans were considered effective in helping the companies realise all ten enumerated benefits.

The same survey obtained management comments on deficiencies in profit-sharing schemes. It was found that profit-sharing cannot be very successful unless in most normal years there are profits to share. Profit-sharing far from being a substitute for competent management, had in fact challenged management to greater competence because profit-sharing employees expected and responded to dynamic leadership. Communication of the philosophy and benefits of profit-sharing must be continuously and persuasively presented to employees. Very few plans were considered "very effective" in achieving the goal of "reducing wasted time and materials".

> "This highlights the facts that employees will not automatically cut costs and save on materials just because they will share in the profits. They must be told how much things cost, how savings can be achieved; and be shown how these costs reductions and/or savings affect their profit shares before they will be able to contribute effectively in this area."[120]

Recent English studies have cast some doubt on the value of financial incentives to stimulate and maintain increased efficiency over a period of time. Strictly speaking these investigations relate to payment by results schemes rather than profit-sharing as defined in this paper. Nevertheless it is considered that their findings offer some assistance in assessing the relation between profit-sharing and increased efficiency.

Behrend[121] comments that the usefulness of payment by results schemes is being doubted by many industrialists who have become aware that the effectiveness of their incentive schemes is wearing off while in some cases changes in industrial technology have led to the abandonment of incentive schemes by some firms.[122] Behrend suggests that it is almost impossible to find direct and objective statistical evidence

120 Ibid., p. 122.
121 Of the University of Edinburgh.
122 Hilde Behrend, *An Assessment of the Current Status of Incentive Schemes* (1963-4), Vol. 5-6, Journal of Industrial Relations, p. 96.

to support the widely held belief that there is a direct relationship between the application of incentive schemes and the raising of standards of effort. Therefore one is obliged to fall back on the evaluation of behaviour and opinions by workers and managers as to whether the schemes they use work satisfactorily. However this evidence may not be conclusive because even where a scheme is working badly management who have faith in it will excuse its scant earnings by attributing lack of success to the improper use of the scheme.

Looking more specifically at the question raised by Behrend as to the inappropriateness of incentive schemes in view of changes in industrial technology, the view has been expressed that such schemes will decline where the work pace is set by the machine and the output limited by the capacity of the equipment. Bean[123] and Garside[124] have found that the experience in a number of European countries and the U.S.A. is that:

> "The net effect of recent technological changes seems to have been expansion rather than abandonment of incentive coverage. With increasing capital per worker the spreading of overhead costs via capacity utilisation of equipment becomes an important consideration. This leads Bolle de Bal to distinguish a "stimulation" function of payment by output, encouraging workers to increase production, and a 'regulation' function aimed at 'the maintenance of a certain minimum level of production necessary to ensure the profitability of ever more costly technical investments', i.e. to prevent operatives from neglecting production and allowing output to fall below a certain threshold level. He postulates, as an adaption of payment methods to new technical conditions, a future decline in the stimulation function in favour of the regulatory."[125]

Bean and Garside concluded that in the medium term payment by results schemes of a regulative type aimed at the maintenance of certain minimum level of production necessary to ensure the profitability of ever more costly technical investments could well become central to the whole concept of incentives.[126]

QUALIFYING PERIOD

As far back as 1922 the U.K. Ministry of Labour reported that although a profit-sharing scheme may exclude persons who are not adults or who have not been in the service of the employer for some

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123 Lecturer in Economics, University of Liverpool.
124 Assistant Industrial Relations Officer, British Steel Corporation, Scunthorpe.
125 *Payment by Results Systems: Some Indicators of Incidence and Relevance to Capital Intensive Operations* B.J.I.R., July 1971, p. 182. Bolle de Bal, *The Psycho-Sociology of Wage Incentives* B.J.I.L., Vol. III, No. 3, November 1969, p. 390.
126 B.J.I.L., July 1971, p. 197.

reasonable qualifying period, it should include not less than 75% of the total number of adult employees who have been in the service of the business for at least one year.[127]

Seear and Copeman in their introduction to an inquiry into the "Habits, Attitudes and Problems of Employees' Shareholding Schemes" consider it may be reasonable to exclude short-term employees from a scheme, since it is an administrative nuisance and uneconomic to have to take into a scheme those who are not staying long and have little real interest in the company. Moreover, the scheme should be mainly concerned with providing some extra reward for those who invest their working lives with a company.

B. L. Metzger comments[129] that the decision on eligibility requirements will depend on the composition of the work force, e.g. seasonal, part-time or full-time permanent workers, and also on the company's objectives of the profit-sharing plan. Exclusion of transient workers from a deferred plan through a waiting period simplifies plan administration and accounting and maximises the benefit for the smaller number who are eligible.

Dr. Lau considers that it is better to reduce the number of staff who participate and to pay them individually a higher share in the profits than to distribute the percentage to be allocated among all the employees and thereby arrive at a lower benefit for each of them. A further reason for imposing a qualifying period is that it is:

> "generally speaking, the staff which has been with a company for a number of years which makes the most contribution to its profitability. I would say therefore that a scheme could well provide that before a member of the staff qualifies for the profit-sharing scheme he must have been in the employment of the company for not less than two years. This would increase substantially the profit-sharing bonus of those who participate and it should also be an incentive for the newer staff to remain with the company and not for negligible reasons change employment, as happens so often."[130]

EMPLOYEE INFORMATION

The Profit-Sharing Research Foundation considers that effective communication to employees is the "life blood" of any profit-sharing scheme.[131] A common fault is that firms fail to maximise the incentive potential of a profit-sharing programme through lack of sufficient employee communication.

"Successful profit-sharing is directly linked to kindling the

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127 1920 Cmd. s. 44, p. 4; "Sharing the Profits", Note 112, p. xxi.
129 Metzger, *Profit-Sharing in Perspective*, p. 55.
130 *N.Z. Commerce*, Sept. 1971, p. 12.
131 Metzger, *Profit-Sharing in Perspective*, p. 184.

> profit motive in your employees, to making them feel they are partners with management in creating profits . . . Employees must constantly be reminded that out of profits and only out of profits do they get good jobs, good pay, good benefits, good working conditions, good service, good equipment. And a profit-sharing plan brings all these factors into immediate focus for them — if the company is profitable and the plan is properly communicated to them."[132]

The type of communication recommended by the Profit-Sharing Research Foundation includes:

(a) Thoroughly informing management about the purposes of the profit-sharing plan.
(b) Informing the employees when the plan is installed.
(c) Selecting the appropriate media to accomplish (b), whether by meetings, letters, booklets, statements of account, posters, charts, slides or films.
(d) Important communications on the programme should come from the top of the organisation.
(e) Communication should be made when employee interest in profit-sharing is highest.
(f) Profit-sharing should be used as an incentive to develop interest, loyalty, enthusiasm, cost-consciousness, profit-mindedness and a spirit of co-operation among employees.

The justification for this effort is the:

> "impressive relationships between successful profit-sharing communication programmes and successful plans, between unsuccessful plans and inadequate profit-sharing communication programmes."[133]

Dr. Lau in commenting on the success of profit-sharing in certain companies states that an important factor was the communication by management to the staff of as much of the company's business policy as results as could be done without adversely affecting the business.

> "Keeping the staff informed of future planning, of orders on hand, of results of trade conditions, etc., has in the view of many managers been the main reason for the success of the profit-sharing scheme and the long term success of their company. Some went so far to say that good communication was a more important feature than the profit-sharing scheme."[134]

The writer therefore concludes that the emphasis placed on worker management communication and dialogue in the 1967 French profit-

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132 Stanley D. Noble — President of the Council of Profit-Sharing Industries. Address before the Mid-Continent Trust Conference, 1963, Metzger, *Profit-Sharing in Perspective*, p. 192.
133 Metzger, *Profit-Sharing in Perspective*, p. 191.
134 *N.Z. Commerce*, September 1971, p. 11.

sharing legislation is well justified. Therefore any country intending to introduce profit-sharing legislation should give close and careful consideration to providing for a reliable system of employer-employee communication.

TAXATION ASPECTS OF PROFIT-SHARING

The cost of a profit-sharing scheme to a firm depends to a large extent on whether the share allocated for the employees is taxable especially if the firm's profits are taxed at a high rate. At the same time the provisions concerning personal income tax affect the amount which an employee actually receives and thereby influences the effectiveness of the scheme. As discussed earlier in this paper the taxation legislation affecting profit-sharing in New Zealand is a positive disincentive for the adoption by firms of profit-sharing schemes.

In the United Kingdom payments made by a company under a profit-sharing scheme are generally allowed in the company's assessments to income tax and profits tax, being allowed as an expense of carrying on the business and treated in the company's accounts as an addition to wages and salaries; however the employee's benefits are treated as earned income and taxed under P.A.Y.E. If distribution is made otherwise than in cash, the individual employees will probably find their income tax liability increased without their cash resources being increased to meet it, with the result that until the benefits are converted into enough cash to compensate for this increased liability, their immediate net cash income position will be worse than if there had been no profit-sharing scheme at all.[135]

The taxation position in Britain and New Zealand compares unfavourably with that in some other countries. In the United States the employer's contributions to a deferred profit-sharing programme are deductible as a business expense up to 15% of the annual compensation of participants. The employee participant is not currently taxed on his share of the company's contribution. The fund earnings such as dividends and interest are not currently taxed and therefore compound much more rapidly. Tax on a participating employee's profit-sharing trust account is deferred until the employee actually or constructively receives benefits (usually at retirement, death, disability or severance of employment). Employer securities, distributed to a terminating fund member as part of an immediate settlement are computed for tax purposes at average acquisition cost rather than at market value. Any appreciation on such security above the acquisition cost is excluded from tax and is taxed only when the stock is sold. If such stock is held until the death of a member the appreciation is never taxed.[136]

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135 Harper, *Profit-Sharing in Practice and Law*, pp. 28, 29.
136 Metzger, *Profit-Sharing in Perspective*, pp. 200-201; see U.S. Internal Revenue Code of 1954 for the rules for qualifying a deferred profit-sharing trust.

In West Germany tax exemptions are given up to 624 DM[137] (about $NZ163.00) per worker per annum alloted by a company for an approved scheme of employee saving and investment. In the case of profit-sharing or bonuses such a scheme requires that the sums be retained by the employer at interest for a period of not less than five years.

It is obvious that a country's taxation laws will have a vital effect on whether a company will decide to implement a profit-sharing scheme as opposed to an alternative form of employee benefit. The writer therefore considers that the total absence of any tax incentives for profit-sharing in New Zealand must be critically examined in the light of overseas experience.

PART V: CONCLUSION: PROFIT-SHARING REFORM IN NEW ZEALAND

There are two principal reasons for which a Government might wish to enact legislation to require or encourage profit-sharing. Firstly it may hold the view that profit-sharing is an expression of social justice and is therefore a desirable end in itself. This social justice consideration appears to have been a crucial element in the French legislation on profit-sharing. The second reason is that profit-sharing may be justified in hard economic terms by the apparent benefits which companies with such schemes have obtained. The merits of this argument were examined in the last section of this paper where certain of the studies referred to suggested that profit-sharing may, where properly administered, act as an incentive to increased production and efficiency and can even result in improved industrial relations. It was apparent, however, that because profit-sharing is but one of a number of factors influencing any given labour-management relationship, it is difficult to specify with any degree of certainty just how great a role profit-sharing plays in the overall situation. For this reason the writer does not express an opinion on the desirability of profit-sharing reform in New Zealand. Such a decision is not a legal one but rather of an economic, political or social nature. It is appropriate however to consider the ways in which experience already gained elsewhere in the field of profit-sharing could be usefully applied in this country.

On the assumption that profit-sharing reform is considered desirable in New Zealand, the question arises as to the best method of implementing reform. Using the French Ordinance of 17 August 1967 as a point of reference, the writer sets forth his views on the subject.

a. Should profit-sharing be compulsory?

Should worker participation in company profits be made compulsory for all firms employing more than a certain number of staff? As we saw earlier, the initial French profit-sharing legislation of 1959

137 Laws of 12 July 1961, 1 July 1965, 27 June 1970. See *L'Actionnariat des Salariés*, p. 27.

was optional in character and aimed to encourage firms to implement profit-sharing schemes by means of tax and social security exemptions. It was not a success. Despite this failure, the writer suggests it would be quite inappropriate to contemplate compulsory profit-sharing in New Zealand at this stage. Rather, taxation incentives should be rendered sufficiently attractive to entice firms and their employees to take advantage of such measures. It is considered unwise to impose a profit-sharing scheme on a firm whose profit may be so low as to render the return to the worker insignificant. Such an arrangement would probably fail completely as an incentive to workers and may do more harm than good to the concept of profit-sharing.[138] Alternatively in such a situation an incentive based on output may be a fairer way of rewarding individual effort because the failure to make a profit may be a factor beyond the worker's control.[139] By leaving profit-sharing a matter of choice depending on its appropriateness for any given firm the invidious distinctions which are referred to by Lasserre as arising under the French legislation[140] could be either avoided or at least not attributed to the legislation.

b. Investment and period of unavailability of workers' funds

The five year period during which the French worker is unable to dispose of the share of the profits distributed to him is of course vital to the policy of encouraging savings aimed at by the Ordinance of 17 August 1967. Since profit-sharing should not be used as a substitute for an adequate wage there may be considerable merit in tying up this additional source of the worker's ready cash. New Zealand, which must rely heavily on overseas capital, could by this method attain a greater degree of self-financing in the development of its economy. The worker also stands to gain in some important respects by a period of unavailability of his share in the profits. During this period his compulsory savings will be profitably invested and compounding interest. Moreover this total amount will be free of tax. For these reasons the temporary unavailability of these funds should be more than compensated for by the increased amount which the worker ultimately receives.[141]

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138 "Fluctuating profits means that the lottery element in profit-sharing is more pronounced. It has sometimes been claimed that profit-sharing can be introduced in firms which are not making profits, as the incentive provided by the scheme will provide profits in the future. Such cases seem to be rare in practice . . ." *Profit-Sharing,* Department of Labour and National Service (Australia), (1949), here referred to as *"Profit-sharing"*.

139 "Profits are effected by many factors other than the efforts put forth by the employees, such as business fluctuation, overseas trade, the efficiency of management, the efficiency of competitors, etc. There is no certainty that increased effort will result in increased financial reward through a profit-sharing plan." Ibid., p. 19.

140 Note 87, ante, and text.

141 Dr. Lau shares this view. Discussing the West German legislation granting tax exemption for approved profit-sharing schemes he says: "While normally employees would be reluctant to wait six years for their profit share, if they know they will receive it tax free with interest I suggest it would be most acceptable to them and of course they would receive the statement each year showing how their profit-sharing bonus is accumulating." *N.Z. Commerce,* September 1971, p. 12.

The ways in which the workers' profit-sharing fund should be invested during its period of unavailability has been well explored in the French legislation and should be suitable for adoption in New Zealand allowing for local modifications. However, it was seen that since so few participation agreements chose employee shareholding as a method of investment, additional legislation was required in 1970 and 1971. New Zealand could therefore gain the benefit of this experience by enacting from the outset especially favourable conditions for this type of investment. The writer considers that employee shareholding should be encouraged because it is probably the purest application of the spirit of profit-sharing in that it identifies the interests and prosperity of the workers with those of their company.[142]

c. Length of qualifying service

A most important consideration in a profit-sharing scheme is the length of service an employee should have with a firm before becoming entitled to share in its profits. The French Ordinance lays down a period of at least three months to qualify. As mentioned earlier in this paper one third of all agreements which came before the C.E.R.C. seeking to derogate from the Ordinance did so only insofar as they sought approval for a longer period of qualifying service than three months. The report of the French Ministry of Labour of 25-31 January 1971 suggested that the three month period might require modification in view of the widespread wish to alter it in the agreements concluded between the parties.

This whole question raises an important point as to the underlying purpose of the French Scheme. In one case the C.E.R.C. held that the Ordinance did not have for its object the encouragement of the stability of personnel but rather the allocation of a share in the fruits of expansion to all employees who by their work had contributed to such expansion irrespective of their length of service.[143] This approach is sharply in contrast to the American view which looks to profit-sharing to assist in such factors as reducing labour turnover and retaining good personnel.

In the writer's opinion the French three month qualifying period has little to recommend it apart from giving an almost immediate company-wide incentive. It fails to capitalise on the benefit which a longer qualifying period may give in reducing labour turnover. By making short-term workers eligible, the cake to be shared among the entire staff must be divided into smaller pieces and therefore its value as an incentive is diminished. Lastly it is not unreasonable to give some greater reward to those who invest their working lives or a significant part thereof with the company in preference to those who are just passing through.

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142 The problems which this identification of interests may give rise to have already been discussed.

143 See note 58.

It is therefore recommended that for a profit-sharing agreement to be eligible for favourable taxation provisions a minimum qualifying period of at least one year's service should be required.

d. The definition of the beneficiaries

The French rule of non-discrimination[144] in defining the beneficiaries of a profit-sharing scheme is, it is submitted, a sound approach and one which could be adopted without significant alteration in the requirements for a profit-sharing agreement in this country.

e. The profit-sharing formula

The writer considers that the parties should be free to adopt their own formula for the profit-sharing benefit to be received by participants. This formula should be simple and not subject to the criticism of the French formula which Lasserre considers is more likely to bewilder the workers than to enlighten them. Any formula should in normal years give a result which will be of some financial significance to workers in relation to their annual wage. To achieve the latter object it may be desirable to load the tax exemptions accorded to registered profit-sharing schemes in favour of those companies which in normal years can average a profit-sharing payout equivalent to about two weeks wages a year.

f. Agreement as to the type of scheme

Integral to the French system is that the method and administration of the profit-sharing scheme should be agreed upon between the parties. The concept of full worker awareness, understanding and involvement in the scheme seems to be regarded as highly desirable[145] and should therefore be embodied in any New Zealand reform in this field. This requirement could most conveniently be dealt with by an agreement between the parties, registered at the Companies Office. Such an agreement, if approved as conforming with the requirements which are recommended in this section of this article, should automatically entitle both the firm and its employees to the taxation concessions referred to above. No doubt such an agreement would have to conform to a provision similar to the 1953 Regulations under the United States Fair Labour Standards Act.[146] These regulations require, inter alia, that the plan must be a definite written programme communicated or made available to the employees and established in good faith for the purpose of sharing profits as additional remuneration over and above the employee's wage or salary and the latter must be independent of the profit-sharing plan.

g. Tax incentives

It is considered the best method to implement successfuly profit-

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144 Ibid., and text.

145 "There is widespread agreement that profit-sharing will not be fully effective unless the employees are fully consulted in the formulation and administration of the plan." *Profit-Sharing*, p. 25.

146 Section 7(d)(3), Amendment Act, 1950.

sharing legislation is to encourage profit-sharing through tax incentives in favour of those firms and their employees who implement approved profit-sharing schemes. An approved scheme could be one passed by a body equivalent to the French C.E.R.C. provided that it embodies the basic various requirements described in this section. Once approved and registered, the scheme would automatically entitle the company and its employees to the tax benefits accorded to profit-sharing.

What then should these tax benefits be? Firstly it is considered that employee's profit-sharing distribution for each year should be tax free to a certain maximum level. Although it is outside the scope of this article to suggest the exact figure, this maximum level should be sufficient to act as a positive encouragement for profit-sharing schemes, while at the same time striking a fair balance with other sections of the tax-paying community.[147]

Secondly, companies should be given some inducement to implement schemes. It is however considered that the tax exemptions to French companies under the Ordinance of 17 August 1967[148] go too far, being a burden which has to be met by the rest of the community.[149] The United States Internal Revenue Code of 1952 in the writer's opinion, provides us with a better example of how to balance the interest of encouraging companies to have profit-sharing schemes while on the other hand not unduly favouring those companies at the expense of the general taxpayer. Thus under the Code the employer's contributions to an approved profit-sharing plan are deductible as a business expense, up to 15 per cent of the annual compensation of the participants.[150]

h. Worker information and involvement

Perhaps one of the most socially significant aspects of the French reform is the emphasis placed on stimulating the worker's personal interest and involvement with the progress of his firm. This goal is sought to be achieved by the detailed legislative requirements as to the dissemination at regular intervals of information on the firm and its profit-sharing programme to the workers. American experience also supports the view that effective communication to employees is the life-blood of any profit-sharing scheme and that most of the benefits which can be derived from a scheme may be lost if workers are not fully informed as to how their efforts will contribute to the final result.

There are profound social implications in ensuring that workers are fully informed about the firm and their role in it; they are thereby

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147 The West German figure of 624DM per annum (about $NZ163.00) is probably a useful starting point in determining a suitable maximum level of tax exemption.

148 See note 50. Under Art. 8 of the Ordinance the whole amount distributed to the employee's special participation reserve in each year is deductible from that year's taxable profit.

149 For Lasserre's strong criticism of the Ordinance on this ground see note 89 and text.

150 The tax advantages of the Code are described at note 135 and text.

treated as thinking and creative human beings rather than "wage-pursuing automata". As we saw in the previous section the pay packet theory is only part of the story of worker motivation. Job satisfaction and a sense of achievement may be just as important in realising better industrial relations and improved production and efficiency.

It is therefore recommended that a requirement for any profit-sharing agreement should be that it contains detailed provisions to ensure that workers are regularly informed as to the functioning of the scheme and the progress of their company. The information should endeavour to show each worker why his efforts are important and how they may influence the overall results achieved by the company. In this way the stage may be set for encouraging employees better to utilise their individual skills and resources and thereby derive greater satisfaction and sense of achievement from their work.

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