

**Legal and Economic Aspects of Corporate Governance  
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**Board efficiency with special emphasis on  
employee participation: the German experience**

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# Agenda

## **I. General Expectations for Board Efficiency**

## **II. Employee Participation in the German Two-Tier Board System**

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## **III. International Examples of Employee Participation in Boards**

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## I. General Expectations for Board Efficiency

- Composition
  - Appropriate size
  - Relevant qualification & expertise
  - Sufficient independence (formal and 'in mind')
  - Sufficient time availability
- Committees to achieve intensive work:
  - Audit
  - Risk Management
  - Compensation
  - Nomination
- Self-evaluation of board efficiency on a regular basis

## II. Employee Participation in the German Two-Tier Board System

### 1) Structure of the German Two-Tier Board System

#### Management Board

- Manages the business
- Elected (and dismissed) by the Supervisory Board (with 75% majority)
- Reports to the Supervisory Board and the General Meeting

#### Supervisory Board

- Controls & Advises the Management Board
- Elected by the Shareholder Meeting
- Nominates Management Board Members
- Reports to the General Meeting

#### Co-Determination Act of 1976

- Mandatory for all companies with more than 2,000 employees
- Employee Participation depending on the number of total employees (table below)
- Equal rights & duties
- Exception: Vote of the Chairman (always a shareholder representative) has two votes in case of split votes

#### Supervisory Board Composition

Total Employees	2,000 to 10,000	10,001 to 20,000	>20,000
$\Sigma$ Seats	12	16	20
50% Labour Rep.	6	8	10
Employee Rep.	4	6	7
Union Rep.	2	2	3

## II. Employee Participation in the German Two-Tier Board System

### 2) The Impact on Board Efficiency: Advantages & Disadvantages

#### Advantages

- Useful input from the 'shop floor'
- 'Early warning system' for social conflicts, thereby reducing the probability of strikes.
- Usually better cooperation in case of necessary reconstruction.
- Strong influence against hostile takeovers.

#### Disadvantages

- Size of the supervisory board (max. 20 for large companies) not efficient.
- Employee representatives have often predominant focus on employee matters.
- Hinders full discussion of sensitive issues that relate to employee interests: certain issues are therefore difficult to discuss with the whole supervisory board.
- Labour representatives can not be considered independent.
- The legal requirement that employee representatives should come from German workplaces does not reflect the international picture as most German companies have more than 50% international business.

### III. International Examples of Employee Participation in Boards (1)

- Denmark (Privately- and state-owned companies):
  - In companies with at least 35 employees over the last 3 years, it is up to the employees to vote for or against representation on the board of directors.
  - The employees must elect half the number of directors elected by the shareholders (at least two).
  - No special seats for union representatives or management employees.
- France (Privately-owned companies only):
  - French legislation leaves shareholders complete freedom to choose between the monistic system or the dualistic system.
  - Shareholders can choose whether they want participation of employees in the board of directors.
  - The number of board members elected by the employees should not make up more than one third of the other members of the board of directors (i.e. max 25% of total board).
  - In addition, one or several representatives of 'share-scheme employees' can be admitted to the board of directors by an extraordinary general meeting (before the ordinary GM) if they hold at least 3% of the registered capital.

### III. International Examples of Employee Participation in Boards (2)

- Norway:
  - 30 to 50 employees: employees are entitled to a single director (on request of employees).
  - 51 to 199 employees: employees are entitled to one third of the seats (on request of employees).
  - More than 200 employees:
    - Employees can choose between a system with or without a corporate assembly.
    - A corporate assembly has normally 12 members (with two-thirds elected by the shareholders and one third elected by and from the employees) as well as a board (with one third employee representatives) elected by the corporate assembly.
    - In case of a vote against this system, the employees are entitled to an additional board member on top of the one third they already have, plus two additional observers.
    - In practice, only around one fifth of companies with more than 200 employees have a corporate assembly.
- Sweden:
  - Companies are free to choose the size of the board of directors (7 members are common).
  - Only the Trade Unions, through the collective bargaining agreement, have the right to decide if they want to appoint employee representatives to the board or not.
  - The employees of a company with at least 25 employees shall be entitled to 2 and in companies with at least 1,000 employees to 3 employee representatives. The number of employee representatives must not exceed the total number of other board representatives.

### III. International Examples of Employee Participation in Boards (3)

- Croatia:
  - One member of the supervisory board/board of directors has to be an employee representative elected by the works council.
  
- Netherlands:
  - Works councils of larger companies – defined as those with issued capital of more than €16 million, at least 100 employees and a works council (obligatory for companies with more than 50 employees) – can opt for representation of employees at supervisory board level (two-tier system).
  - The works council has special nominating rights for one third of the seats on the supervisory board but members of the works council cannot be on the supervisory board.
  - Since July 2010, the works council has the right for its views on certain issues to be heard at the shareholders' general meeting of a public company.
  
- Countries without employee participation:
  - United Kingdom and Ireland
  - United States



## IV. A Proposal for Sensible Employee Participation in Europe: a Combination of the SE Structure and the Austrian Approach

### Societas Europaea (SE)

- Board size not to exceed 12 members.
- Employee representation must reflect the European employee situation.
- The possible decrease in supervisory board seats from 20 to 12 and the European employee representation led to comparatively high acceptance of the SE in Germany (with well-known examples: Allianz SE, BASF SE, E.ON SE, Fresenius SE).

### Austria

- Statutory provision restricts the number of employee representatives to one-third as the company's work council can delegate one member to the supervisory board for every two shareholder representatives.
- Employee board members must be active workers in the company (no special seat for union representatives or management employees).
- They receive no extra compensation for their board work.