

# Workers on boards: Thoughts from Europe

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Speaking shortly before her appointment in July last year, UK Prime Minister Theresa May stated *“If I’m Prime Minister, we’re going to... have not just consumers represented on company boards but employees as well”*. Re-stating her proposal at the Conservative Party Conference in October, Mrs. May took aim at existing corporate governance structures, stating that *“too often the scrutiny they provide is not good enough”*. More recent statements from the Prime Minister, and the government’s [green paper](#) on corporate governance reform published on 29 November 2016 (the *“Green Paper”*), make clear that the current government does not intend to mandate worker or trade union representation on company boards, or to require that works councils be established, in the UK. However, while the idea of voluntary board representation for workers, alongside a number of other models,<sup>1</sup> is being formally considered, in this memorandum we briefly survey the equivalent systems in France, Germany and the Netherlands, with additional insight from Belgium and Italy.

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<sup>1</sup> These include: (a) creating “stakeholder advisory panels” who could interact with company boards in a variety of ways, including by giving preliminary consideration to issues to be discussed at board meetings, or by attending board meetings themselves in an advisory capacity; (b) designating existing non-executive directors to represent particular stakeholder groups, such as employees, at board level, but who would nonetheless be restricted from prioritising the interests of different stakeholder groups where this was not in the best interests of the company as a whole; and (c) requiring companies to report on how often, and by which mechanism, company boards are giving consideration to different stakeholder interests. For more information, please see our memorandum [“The Government Consults on Corporate Governance Reform: What Next?”](#)



## I. The current UK landscape

Directors of companies with more than 250 employees are required to report annually on actions taken to introduce, maintain or develop arrangements aimed at providing employees with information on matters of concern to them and on regularly consulting employees so that their views can be taken into account in making decisions that are likely to affect their interests.<sup>2</sup> However, the substantive rights of UK employees to participate in or influence corporate decision-making are fairly limited in the UK as compared with our European neighbours, and fall short of co-determination at board or board committee level.

Company directors have a statutory duty to have regard to the interests of company employees when acting to promote the success of the company,<sup>3</sup> but such interests are considered alongside a number of other potentially conflicting interests and are secondary to the overriding requirement that a course of action must promote the success of the company for the benefit of its members as a whole.

Employees have the right to receive information and be consulted in certain particular circumstances, including in connection with the transfer of a business or a service provision change, where collective redundancies are proposed and before making certain pension changes.

Employees or their representatives are further entitled to receive information and copy documents during (but not to be consulted about) a public takeover.

Subject to certain minimum employee numbers, employees also have the right to initiate the negotiation of information and consultation or European works council agreements, in which there is flexibility for employees and employers to agree specific participation rights. However, to date there has been a relatively low take-up of this.<sup>4</sup>

Finally, although trade unions have played an important role in British industry since the 18<sup>th</sup> century, Government [statistics](#) show that trade union

membership, as a proportion of total employees, has been steadily declining since the late 1970s.

## II. The alternatives: worker representation models in Europe

Employee representation around Europe generally takes two distinct forms: the right to participate directly in board meetings and board decisions on the one hand (the “**Co-Decision Model**”), and the right on a collective basis through an elected works council to receive information and to be consulted on specified matters, on the other hand (the “**Works Council Model**”). Both of these forms may be present in the same country, and in the same company. We discuss the different features of these two models below.

### 1. Companies affected

*Co-Decision Model:* In many cases, the requirement for worker representation at board level is determined by the size of the company; in Germany, board representation is required where there are over 500 employees, whereas in France, the figure is 1,000. Often, in addition to the criterion of size, the right applies only to certain legal entities (for example, amongst other entities, the B.V. and N.V. in the Netherlands and *société anonyme* in France). Exceptions may exist for certain non-profit entities, and for religious communities and their educational and charitable institutions (Germany). France also has a separate right of board representation for employee-shareholders where in a listed company employees hold 3% or more of the share capital<sup>5</sup>.

*Works Council Model:* For works council representation, the determination is often based on the size of the company or individual site; in Belgium, employees at any business unit with 100 employees or more and, in Germany, employees working at any site with five or more employees, are entitled to have a works council. However, as in the UK and the Netherlands, this right may be latent, such that it only crystallises when an employee or a group of employees positively requests that a works council be established.

<sup>2</sup> Part 4 of Schedule 7 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, SI 2008/410.

<sup>3</sup> Companies Act 2006 s.172(1)(b).

<sup>4</sup> Only 112 UK-headquartered companies currently have an active European works council (Source: [European Works Council Database](#)).

<sup>5</sup> This right is not discussed in detail in this memorandum.

## 2. Number of worker representatives

*Co-Decision Model:* Board-level representatives may be prescribed as an absolute number, but are more usually determined as a proportion of the board as a whole. In Germany, worker representatives make up one-third of the supervisory board, rising to one-half for larger companies. In France, companies have more freedom to determine the number of employee representatives according to their by-laws, subject to certain *de minimis* requirements. Representatives will usually sit at the highest board level; in the Netherlands, this means that worker nominees make up one-third of the supervisory board in a two-tier board structure, or one-third of the non-executive seats in a single-tier board structure.

*Works Council Model:* The size of the works council depends on the size of the workforce to be represented. At the lower end, establishments of 5-20 employees in Germany will only have a single works council member. At the upper end, establishments of 7,000 or more employees in the Netherlands will have works councils comprising 25 representatives (unless the employer and the works council agree otherwise). In general, the works council is an employee-only body but, in France the chair of the works council is held by a representative of the employer. In Belgium, the works council is a mixed body, and the chair is held by a representative of the employer as in France.

## 3. Eligibility criteria

*Co-Decision Model:* In general, employee representatives at a board level must themselves be employees. In such cases, all employees are eligible to be elected, subject to certain criteria regarding length of service or age. For example, in Germany, employees who are over 18 with at least one year of service with the company are eligible to become representatives and, in France, only employees with two years of service or more are eligible for election. The Netherlands is an interesting exception, where worker nominees cannot themselves be employees of the company, and must fulfil certain minimum requirements of independence. In addition, in some jurisdictions (such as Germany) a certain proportion of employee representatives on the board must be trade union candidates.

*Works Council Model:* As for board representatives, works council representatives must be themselves

employees, and must generally meet certain *de minimis* requirements as to age and length of service (6 months in Germany; one year in the Netherlands). In France, any employees who have familial ties to the employer (for example, spouses or children) are ineligible for election to the works council. The final composition of the works council in Germany should include, to the extent possible, employees of the various units and employment categories represented in the establishment (with the exception of executive officers). In Belgium, there is additional separate representation on the works council for young workers (under 25) and for management employees if either group represents a sufficient proportion of the workforce.

## 4. Appointment of worker representatives

*Co-Decision Model:* The election of board-level representatives is often achieved via direct democracy, with all employees, regardless of seniority or length of service, being eligible to vote. However, larger German companies (those with over 8,000 employees) may use an electoral college-based system, whereby groups of employees elect a delegate, who then votes for the board representatives on their behalf. In France, companies can opt for different election models in their by-laws; the representative may be elected by the employees, or appointed by the works council (at entity or group level), or the trade unions. In some cases, the worker representative is subject to further approval by shareholders. In the Netherlands, works council nominees for the supervisory board must be nominated by the supervisory board (subject to certain limited grounds of refusal by the supervisory board) for formal appointment by the shareholders, who can block such nomination by a simple majority vote of the shareholders representing at least one-third of the issued share capital. Where there is a simple majority representing less than that one-third, a second meeting of shareholders may be convened in which a simple majority will suffice, failing which the nominee is appointed.

*Works Council Model:* Elections to the works council are usually carried out on the basis of lists of candidates submitted by trade unions and/or by the employees themselves (France, Germany, the Netherlands). Seats are then allocated on a proportional basis, depending on the popularity of the

different lists. All employees are eligible to vote, subject to length of service requirements in certain jurisdictions (6 months in the Netherlands; 3 months in France).

## 5. Powers and duties of worker representatives

*Co-Decision Model:* Where employee representation takes place at board level, the representatives or nominees generally have all of the same rights and responsibilities as other members of the relevant board, and are subject to the same fiduciary duties. Such duties, broadly, include a duty to act in the best interests of the company as a whole, meaning that worker representatives or nominees on boards, whilst they may at times advocate for the interests of worker stakeholders, cannot act to advance only those interests. It is not difficult to imagine situations where the company's interests conflict with the interests of its workers (or a certain subset thereof). Regardless of the legal position, many worker representatives see their role as to defend the interests of the employees, particularly in systems, like in France, where the board acts only as a collegiate body, taking collective decisions. In Germany, worker representatives have an additional right to elect the deputy chair of the board, but this is less valuable than the right of shareholder-designated directors, in the absence of a two thirds board majority, to elect the chair (a role that carries a casting vote in the event of a tie).

*Works Council Model:* Where employees have a right to representation at site level through works councils, this is often limited to a right to receive information and to be consulted on topics prescribed by law or agreed with the works council. In certain instances the prior consent of the works council may be required before the company take act on its proposals, but this is usually confined to "social" matters, such as regulations on overtime work (France), changes to the terms and conditions of employment (Netherlands) and the hiring, grading, transfer or relocation of employees (Germany). In Belgium, the works council has extremely limited decision-making powers (veto rights against the company's appointment of an auditor, establishment of the work regulations, *etc.*). Works council members often have protection against dismissal by the company; in Germany, extraordinary dismissal of a works council member requires the prior consent of the works council itself.

## 6. Consequences of non-compliance

*Co-Decision Model:* Non-compliance with worker representation requirements usually gives rise to a risk of civil sanctions, including injunctions. Enforcement takes place through employee-led legal proceedings to seek an injunction (or similar ruling) requiring the company to comply. In France, such proceedings can be brought by any individual employee. In Germany and the Netherlands, however, legal challenges must be brought collectively through the works council, although in Germany the same role may also be fulfilled by a trade union, or by a group representing at least 10% of the total number of employees. Financial sanctions are not generally applied for non-compliance.

*Works Council Model:* Obstruction of the work of the works council (for example, by interfering in elections, trying to influence a member of the council, or failing to constitute the works council) may result in a fine or, in severe cases, criminal liability in Belgium, France and Germany. Works councils also usually have recourse to the courts to challenge decisions of the employer in particular circumstances. Works councils in the Netherlands, for example, can appeal on the basis that the employer could not reasonably have reached the decision had it weighed all the interests involved. The employer's failure to consult the works council prior to making its decision (or at all) raises an irrefutable presumption that this is the case. In Germany, the employer (and management) is exposed to a fine of up to €10,000 in case of dereliction of their duties, and in certain circumstances the works council may apply to court for an injunction. In France, works councils can obtain a suspension of the employer's decisions until the consultation procedure has been properly completed.

## III. The Issues: Perceptions, pitfalls and problems

In some jurisdictions, such as the Netherlands, local businesses are accustomed to the presence of workers or worker representatives on boards, as such countries have a long history of co-decision. Multinational companies operating in these jurisdictions may find themselves less comfortable with the requirements, and may seek to employ a number of strategies to try to avoid them, such as by using foreign entities. In the

Netherlands, multinationals may be able to “push down” the employee participation requirements to the level of a Dutch subsidiary (in which all Netherlands-based activities and employees are then centralised), provided the majority of employees of the group as a whole are situated outside of the Netherlands.

Criticisms levelled at employee representation in all forms include the added delay caused by the requirement for employee participation, particularly in jurisdictions (such as Germany) where such participation takes place at both site and board level. Critics also point out that worker participation does not necessarily strengthen corporate governance structures; the Volkswagen emissions scandal in 2015 was not averted by the worker representatives who made up half of the supervisory board. On the contrary, Volkswagen has a long history of corporate governance scandals, and its powerful works council was at the centre of the bribery and corruption scandal which rocked the company in 2005.

Depending on the strength of the participation right, employers sometimes feel that the rules tip the balance too far in favour of the employee, making it difficult or impossible for the board to implement strategic decisions. An example of this can be found in the troubles of KLM-Air France in early 2015, when the supervisory board of the Dutch entity (a first-tier subsidiary of the French parent company) apparently blocked the parent company’s intention to centralise cash management of the two carriers (by preventing a transfer of cash from the Dutch subsidiary to the French parent).

Interestingly, it is not only employers who may have issues with mandatory board representation. When proposals for employee representatives were raised in Italy in 2002, unions opposed the idea as it would mean direct involvement in company decisions, and therefore less freedom to oppose such decisions by collective action.

The Green Paper notes that employee representatives “can bring a new perspective to board discussions”<sup>6</sup>, and may help boards to focus on longer-term goals. However, it cites various challenges to the implementation of such procedures, including the difficulty of elections for large or multinational employers, and the risk that it may shift real decision-

making power away from the boardroom to less formal channels. Respondents to the consultation to date have, on the whole, raised concerns rather than expressed support for worker representation on boards (see box).

#### **UK businesses react to worker board representation proposals:**

- “We do not believe that encouraging or mandating employee representation on boards will, in isolation, create a strong system of corporate governance.” (John Lewis, UK department store)
- “We are fully supportive of the principle that the voices of employees should be adequately represented at a senior level, but ... we would be concerned with the appointment of employee Directors or any differentiation in the responsibilities of existing Directors.” (Fidelity International, investment manager)
- “Legislative intervention risks penalizing businesses that already have established structures for engaging their workforces.” (EEF – the UK Manufacturers’ Organization)
- “I have met ‘worker representatives’ who clearly have the aptitude as well as the experience to be fantastic board members... A worker representative on the Remuneration Committee would certainly be a big step forwards.” (Helena Morrissey, CEO of Newton Investment Management)

#### **IV. Conclusions**

Although the particular form and function of worker representatives differs among countries, there are some common threads. Representatives of employees at all levels are usually the employees themselves, who take on the task of representation in addition to their other duties. Worker representation rights are strongest in the matters that most closely concern employees, such as issues of redundancy, pay and

<sup>6</sup> Green Paper, paragraph 2.27.

overtime work. Where employee representatives are present at board level, they are generally expected to comply with the duties and obligations of all board members, and this can cause conflicts with the objective of representing and safeguarding workers' interests.

Although it now seems very unlikely in the short- to medium-term that UK companies will be *required* to appoint workers or their representatives to company boards, or to establish works councils, it seems probable that we will see some light-touch reform in this area under the Conservative government. Whatever the eventual measures adopted are, the Green Paper praises the flexibility of the UK's "comply or explain" approach to corporate governance and this principle may well be applied to any such measures.

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