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# The impact of large-scale employee share ownership plans on labour productivity: the case of Eircom

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Authors: Baublyte, L., Mullins, M. and Garvey, J.

## Synopsis

This paper presents a case study analysis of a large-scale employee share ownership plan (ESOP) in Eircom, Ireland's former national telecommunications operator. We identify changes in labour productivity during the 8 years before and after the establishment of the company's ESOP and use a framework based on Pierce et al. (1991, 2001) to explore the impact of the ESOP. The ESOP was found to play a key role in enabling firm-level reform through concession bargaining and changes in employee relations, and thereby indirectly affected labour productivity. However, despite the substantial shareholding and influence of the ESOP, we find that it failed to create a sense of psychological ownership among employees, and thereby further impact on productivity.

### Introduction and Background

Over the past two decades, there has been considerable growth in the number of employee share ownership (ESO) programmes established within the EU. The rationale underlying such schemes centres on promoting greater firm performance through creating a sense of ownership among employees. Existing research has therefore generally focused on examining the impact of ESO on labour and labour productivity. US research findings based on small privately held firms have found a consistent positive relationship between ESO and labour productivity, however, the extant literature has failed to establish a similar consistent relationship between ESO and the productivity of large publicly quoted firms. Employees in publicly quoted firms often receive only a limited shareholding, frequently less than 10% and as a result, ESO accounts for only a small proportion of total employee remuneration. Moreover, such ESO schemes generally involve little change in firm governance or management, and therefore fail to establish a greater sense of ownership among employees.

A unique development in Ireland has been the allocation of sizeable shareholdings to employees through the establishment of ESOPs as part of the privatisation of public enterprises since 1999. These ESOPs generally grant employees a 14.9% shareholding in return for a restructuring and rationalisation deal. The rationale underpinning their

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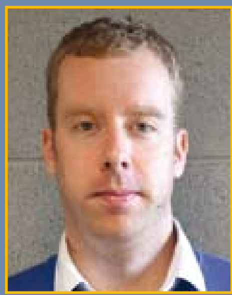

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establishment has been both pragmatic and ideological. Pragmatically, they have been used to neutralise union opposition to privatisation and ideologically, the government views them as a means of improving labour productivity by aligning worker goals with those of the firm.

## Issues and Questions Considered

The establishment of such substantial ESOPs in Irish public sector enterprises provides a unique opportunity to contribute to the literature on both ESO and public sector reform by investigating the role that employee financial participation can play in altering the impact of public sector reform on employee attitudes and firm productivity. Our paper adopts a case study approach, focusing on Ireland's former national telecommunications company, Eircom, where employees were granted a 14.9% stake in the firm as part of the privatisation process. This shareholding increased to 29.9% in 2001 when Eircom was taken over by a private equity group and increased further to 35% in 2006 when the company experienced another private equity takeover.

The establishment of a substantial ESO scheme as part of a reform programme can be expected to have a significant impact on labour productivity. Pierce et al. (1991, 2001) propose that this can occur through both the formal ownership rights that share ownership provides employees and their representatives with, and through psychologically experienced ownership and the resulting impact on employee attitudes and behaviour. The way in which employees view ESO is largely determined by the context in which it is introduced. Where it is introduced as part of concession bargaining or to provide employees with a form of financial benefit, the focus of employees and management is on the financial compensation they receive. On the other hand, where the aims of the ESO scheme are founded on a desire to create organisational advantages through employee participation in decision-making, a set of employee expectations based on information sharing and a shared burden can be expected.

## Methodology

Our analysis is based on the data sourced from Eircom annual reports, reports from the Eircom ESOP Trustee Ltd. and from a survey of 1000 Eircom employees (with 711 usable responses). We measure labour productivity using an index that relates changes in the quantity of output (measured as deflated turnover) to changes in the quantity of labour input (measured as physical man hours per annum). Changes in employee participation in firm decision-making were measured through the survey of Eircom employees. In the survey, employees indicated changes in their level of participation in decisions affecting nine items since the introduction of the ESOP. Information on employee financial returns from the ESOP was sourced from Eircom ESOP Trustee publications.

## Outcomes and Findings

From a policy perspective, the original objective in establishing the Eircom ESOP was both to incentivise and motivate employees through giving them a shareholding in their company leading to improved productivity and to transfer wealth to employees so as to reduce opposition to privatisation and firm restructuring. Of these two objectives, the latter has taken priority, with distributions totalling approximately €800 million made to employees between 2002 and 2010. The findings in our paper show that the structure of ESO schemes such as the Eircom ESOP faces limitations in promoting a culture of direct employee participation and enhanced employee behaviour. We find that although labour productivity growth was higher in the post-ESOP period, this cannot be attributed to the creation of a sense of psychological ownership among employees. Indeed, many employees reported a marked decrease in their level of participation in the firm decision-making, perhaps reflecting disappointed expectations. Instead, the improvement in labour productivity was driven by large reductions in staff and substantial changes to firm work practices.

The primary function of ESOPs established as part of the privatisation process in Ireland appears to be the transfer, over a defined period of time and in a tax efficient manner, a certain proportion of firm wealth to employees. If the objective of policymakers is to transfer wealth and a direct ownership stake in the firm to employees, it is necessary to question whether there is a more appropriate mechanism for achieving this (e.g. offering individual employees free or discounted shares). In the case of Eircom, the large stake in the firm transferred to the ESOP trust allowed the trust to become a key strategic decision-maker, particularly in relation to changes in firm ownership. Instead of using this position to promote the long-term future of the firm and its workforce, the trust acted as a wealth-maximising investor with a focus on increasing the financial gains for its participants beyond what was originally envisaged by policymakers. These are the issues that require serious consideration when establishing future ESO schemes as part of the restructuring and privatising of remaining state-owned enterprises.

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