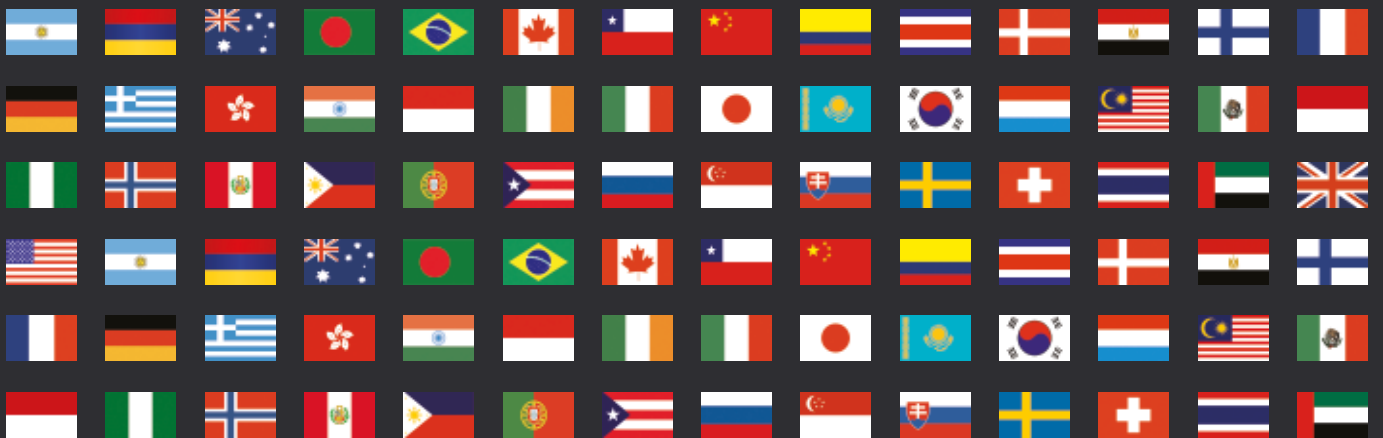


# Labour & Employment 2019

Contributing editors

Matthew Howse, Sabine Smith-Vidal, Walter Ahrens, K Lesli Ligorner and Mark E Zelek

*Morgan Lewis*



# Mandatory employee board representatives – fantasy or the future?

**Matthew Howse and Lee Harding**  
Morgan, Lewis & Bockius LLP

As the focus on workplace culture is intensifying around the globe, from the movement against sexual harassment in the workplace to pay equity, employees are increasingly finding their voice. Further, the growing trend in favour of the appointment of employee representatives on company boards may provide a further forum for employees to raise their concerns and share innovative ideas for progression. However, in an environment in which many employers are finding themselves under growing pressure from increased regulation and market pressures, are employee representatives on boards a meaningful force for good or a burdensome novelty?

## **The continental Europe paradigm**

The representation of employees on company boards is an important form of employee participation in many European countries. Employee representatives are generally directly elected by the workforce. The presence of employee representatives in the boardroom is an indirect form of employee participation. This structure differs from other types of indirect participation, such as works councils, in that this facilitates employee input into overall strategic decisions rather than focusing on day-to-day operational matters in the workplace. Nonetheless, there are often close links between employee representatives and other forms of employee representation, such as trade unions and works councils.

In a number of European countries, board-level employee representation is a long-standing feature of the industrial relations system. These countries include Austria, Denmark, Finland, Germany, Luxembourg, Norway and Sweden, where the concept of employee board representation is relatively uncontroversial. Germany has the most advanced system of mandatory employee board-level representation (referred to as 'co-determination'), having introduced the Co-Determination Act of 1976. This granted representation on what is known as a supervisory board to employees in companies with 500 or more employees. The proportion of employee representatives required varies from one-third to half of the supervisory board, depending on the overall number of employees in the company. The supervisory board is generally involved in appointing management board members, monitoring business operations, overseeing the activities of the management board and dealing with management board compensation.

While Germany is often regarded as the flagship example of employee board representation, there are numerous other examples of countries with varying levels of employee board representation. For example, employees in Danish companies with at least 50 employees are entitled to elect at least two representatives to the board of directors and up to one-third of the total number of members. In Sweden, employees in most companies with more than 25 employees have the right to appoint two board members, while in France, there is a less-developed right to co-determination, with between two and four representatives of a works council having the right to attend the meetings of the board of directors in a consultative capacity.

However, there are conflicting arguments regarding the impact of board-level employee representation. The proponents of board-level employee representation emphasise the productive effects of consensus and cooperation, with improved cooperation and communication between management and employees, which helps facilitate a corporate culture based on trust and a shared understanding of the needs of the company as a whole. Likewise, the earlier access to information afforded to employee representatives facilitates meaningful input from employees, with employee board representatives able to bring substantial industrial experience to the boardroom. Decisions influenced by employees are more likely to be in the long-term interest of the company, avoiding overly risky projects, maximisation of short-term profits and aggressive expansion by mergers and acquisitions. In turn, an engaged workforce is more likely to be productive, with a positive employee attendance and retention rate. This is often argued to be the case in Germany, which has a higher employment rate than, for example, the United States (which of course does not operate a co-determination model).

However, the employee representative model has come under criticism from many commentators, who argue that no real influence is exercised by employee representatives. This is because employee representatives are always in the minority on the board, even in countries such as Germany where there is a strong emphasis on employee participation. Similarly, it is argued that following the introduction of the 1976 law in Germany, many companies responded by downgrading the role of the supervisory board, reducing meeting frequency and shortening the length of meetings to minimise the impact of employee representatives on board decisions. It has also been suggested that the duty of confidentiality covering representatives, and the fact that they generally have liabilities in line with other board members, may be factors in dissuading employee representatives from undertaking the role in the first place or voicing opinions contrary to the majority. Employee representatives may also come under pressure from trade unions that object to the role of employee representatives as diluting the need for trade union membership. Even if employee representatives were to exercise significant influence, there are concerns that this could result in a preference for structurally conservative corporate strategies, ultimately leading to technological immobility, excessive emphasis on personnel and overly consensus-orientated management, which negatively affects economic efficiency, flexibility and adaptability.

## **The Anglo-Saxon approach**

Both the United Kingdom and United States are a long way from the co-determination system of countries such as Germany, Denmark and Sweden. Nonetheless, it appears that there is growing enthusiasm for greater employee representation at board level in both the United Kingdom and the United States. In the United States, Senator Elizabeth Warren controversially called for large US corporations with more than US\$1 billion in revenue to permit employees

to elect 40 per cent of their boards of directors, while in the United Kingdom, Prime Minister Theresa May has called for greater representation of workers and consumers on corporate boards. While wholesale reform of corporate governance to introduce mandatory employee representation in line with the German model has yet to be implemented in the United Kingdom, there has been some movement towards greater employee representation in recent years. For example, the UK Corporate Governance Code (from 1 January 2019) requires premium listed companies to use, on a 'comply or explain' basis, one or a combination of the following employee engagement mechanisms: a director appointed from the workforce; a formal employee advisory panel; or a designated non-executive director. However, this requirement only applies to a smaller category of companies that are premium listed and subject to the highest level of regulation in the United Kingdom.

While Theresa May and the Conservative Party in the United Kingdom appear to have stepped away from any concrete proposals to introduce mandatory employee board representation for a wider class of companies, in an uncertain political landscape there is still potential for further development in this area. At the end of 2018, the leader of the main opposition Labour Party, Jeremy Corbyn, revealed plans to implement mandatory employee representation if his party is elected to government. Under the proposals, companies with a workforce of 250 or more would be required to reserve at least one-third of board positions for employee representatives.

### Perspectives from the rest of the world

Employee board representation remains a primarily European phenomenon. There is generally no system of mandatory employee board-level representation in the Middle East or Asia. Likewise, Australia, similar to the United Kingdom and the United States, has no current system of employee board-level representation, although there have been calls by some, such as the Australian Council of Trade Unions, for its introduction. The closest existing concept to co-determination under the European model is Australia's industry superannuation funds, where employee representatives sit on not-for-profit industry fund trustee boards with employers. This has been praised as an example of employee interests at board level heightening institutional performance.

### Conclusion

While there are evidently strong arguments in favour of a co-operative system of co-determination in line with the European example, it is also clear that the appointment of employees to company boards is not a silver bullet for workplace issues. There is no conclusive evidence that employee representatives improve the performance of companies for the better or worse. What is clear is that there is growing interest, in both the United Kingdom and the United States, in the idea of strengthening employees' voices in the workplace, whether this relates to strategic business decisions or speaking up about inappropriate sexual conduct following the #MeToo movement. However, it remains to be seen whether implementation of mandatory employee board representation is a meaningful, effective and sustainable way of achieving greater openness and accountability to employees.

# Morgan Lewis

---

## Matthew Howse

matthew.howse@morganlewis.com

## Lee Harding

lee.harding@morganlewis.com

---

Condor House  
5-10 St Paul's Churchyard  
London EC4M 8AL  
United Kingdom  
Tel: +44 20 3201 5000  
Fax: +44 20 3201 5001  
www.morganlewis.com