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## **1. Executive summary**

The main purpose of this project was to study the effects of worker participation on employment stability and the adoption of employment stabiliser mechanisms at the workplace level. The project provided evidence on the effect of employee representation on working time flexibility in private-sector European establishments. A 2002 European Union directive granted information, consultation and representation rights to employees on a range of key business, employment and work organization issues beyond a certain firm size. We exploit the quasi-experimental variation in employee representation introduced by the implementation of the Directive in four countries (Cyprus, Ireland, Poland and the UK) with no previous legislation on the subject. The main empirical analysis was based on repeated cross-section establishment-level data from the last three rounds of the European Company Survey. Difference-in-difference estimates suggested that the Directive had a positive and significant effect on both employee representation and the utilisation of flexible working-time arrangements for eligible establishments. The greater use of flexible working-time schemes was driven by establishments in which no local wage-negotiations take place and those with a high proportion of female workers. It has been shown that the utilisation of flexible working time schemes is positively associated with job preservation in certain contexts (Burda and Hunt 2011). The findings have important policy implications, highlighting one channel through which employee voice may favour less dramatic firm-level employment adjustments to negative shocks.

## **2. Project context, motivation and objectives**

European countries have recovered slowly from the Great Recession (2008-2009). In 2016, the eurozone's gross domestic product was slightly above its pre-crisis level but unemployment remained high (8.5%). The unemployment rate was still above the pre-crisis level (7.2%) and remains higher than in United States (4.9%).<sup>1</sup>

It is well-known that the crisis was accompanied by severe labour market conditions in many European countries. Between 2008 and 2013, the average unemployment rate in the EU28 rose by more than 56% (3.9 percentage points). In a market economy, such a change is the aggregate outcome of multiple decentralized firm-level decisions in response to shocks. Available survey evidence on firms' responses to the Great Recession has shown that employment reductions were relatively more frequent than other labour-cost cutting strategies (reduction in hours worked per employee, reduction in baseline and flexible wage components) among European

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<sup>1</sup> Figures refer to EU28 (Eurostat, 2017).

firms. According to Fabiani et al (2015), the reduction in permanent and temporary staff was the most important cost-cutting strategy for 40% of European firms.

Layoffs may be costly for both firms and workers and harmful for society as a whole. Employers may dislike high staff turnover rates as they are associated with recruitment and training costs. More stable employment relationships may provide stronger incentives for firms and employees to invest in firm-specific training (Jones et al, 2012) and increase productivity. Redundancies affect public finances by increasing unemployment benefit expenditure. Job displacement may also have negative effects on subsequent employees' earnings and health (Jacobson et al, 1993; Classen and Dunn, 2012).

The way in which firms cope with negative sectoral and macroeconomic shocks may be affected by their internal organization. Recent evidence shows that firms managed by their employees keep more stable levels of employment in response to demand shocks (Pencavel et al 2006, Burdín and Dean 2009). Employee involvement in firm decisions can provide incentive-compatible ways of internalising employee preferences for job security over income stability. A substantial literature also suggests that employee participation in decision-making may increase productivity (Addison, 2005; Fakhfakh, Pérotin and Robinson, 2011; Fakhfakh, Pérotin and Gago, 2012). It is thus possible that a degree of employee involvement in firm decisions results in more stable firm-level employment over the business cycle.

The project explored the relationships between employee participation in decisions, firm organization (working-time flexibility schemes) and employment stability. We defined participatory workplaces as establishments in which there is some formal mechanism that allows workers to have a voice in managerial decisions. This definition includes works councils, joint consultative committees, employee directors (on management and/or supervisory boards) and other "institutionalized bodies for representative communication" between a single employer and employees of a single establishment or enterprise (Rogers and Streeck 1995: p6; Ben-Ner and Jones 1995). This broad definition includes a range of arrangements. In the empirical analysis, we focus on the effect of shop-floor employee representation.

Freeman and Lazear (1995) point out that informational asymmetries between labour and management in conventional firms can produce inefficient social outcomes. Management may have incentives to misinform workers about the situation of the enterprise and to use this information strategically. This possibility in turn may generate distrust and make it difficult to establish credible commitments between the parties. Workers may not disclose productivity-enhancing initiatives for fear that the firm will use that information against them. For example, workers may fear that higher productivity will jeopardize their jobs. Works councils and other forms of worker participation may mitigate inefficiencies associated with asymmetric information and employer ex-post opportunism.

The central hypothesis we made is that the inefficiencies associated with the employment relationship that provide a rationale for worker participation become more salient during economic downturns, when firms need to reduce costs, and may result in an inefficiently high

level of layoffs. For instance, if managers do not have the obligation of informing employees and negotiating mass redundancy plans -as they would in participatory workplaces- employees' ideas regarding alternative cost-saving solutions that management fails to see are less likely to be considered and implemented. Secondly, mutually beneficial solutions may not be adopted. In a participatory firm, wage moderation might be agreed upon in exchange for job preservation and the promise that wage concessions in bad times will be compensated with higher wages in good times. However, such a promise may not be credible in the absence of employee information and participation, as managers cannot credibly commit not to distort information ex-post and renege on contracts (Dow 2003, p254). Finally, less conventional mechanisms that increase labour cost flexibility may be more complicated to implement in non-participatory workplaces, because they require considerable trust between management and employees. For these reasons, we hypothesized that worker participation through various forms of institutionalised involvement in decisions may be associated with effective employment-stabilising mechanisms at the firm or establishment level during recessions. More precisely, the project focused on analysing the effect of employee representation on the utilization of flexible working time arrangements, such as working time accounts (Burda and Hunt 2011).

The implementation of flexible working-time schemes may be vulnerable to incomplete contracting problem. While working-time on a fixed basis is easily contractible, working-time flexibility may not be. Two separate issues arise in this context. At the negotiation stage, it might be costly to write and agree on individual contracts specifying very detailed rules about how and when working time can be varied and rights over time credits/debits can be exercised by the parties. After the contract has been agreed upon, the specialized knowledge required to enforce highly idiosyncratic workplace-level contractual provisions may not be available to third parties. As a consequence, employers may behave in an opportunistic manner ex post and renege on their promise to compensate overtime with time-off. Employees may end up performing unpaid overtime hours, as the employer can always argue that employees' claims are not compatible with current company operational needs. In this context, employee representation may facilitate the introduction of flexible working-time arrangements by improving communication and information flows between the parties and protecting workers against the potential opportunistic manipulation of working time schedules. Employee representation provides an endogenous enforcement device for flexible working-time schemes, making more credible the employers' intertemporal commitment implicit in such schemes.

The European Union has long supported employee involvement in the form of information, consultation and/or negotiation, with in particular the Works Councils Directive of 1994 (94/45/EC) establishing transnational information and consultation rights for employees, recast in 2009 (Directive 2009/38/EC). In 1998 Directive 98/59/EC provided for consultation procedures in cases of collective redundancies in a large proportion of firms. More recently, Directive 2002/14/EU encouraging Member States to promote employee representation and information and consultation rights came into force in 2005. However, very little is known about the employment behaviour of participatory firms. Despite the fact that the legislation of many European countries provides for worker participation in enterprises above a certain size,

empirical studies have mainly focused on the German case and on union presence rather than actual union voice (Addison 2009). This may be due to the paucity, until recently, of firm-level data with consistent measures of employee participation across European countries and to the fact that identifying causal effects associated with worker participation is methodologically troublesome (Bloom and Van Reenen 2010).

The main objective of the project was to fill this gap by providing new evidence on the specific adjustment mechanisms employed in participatory workplaces (as compared with non-participatory ones) to cope with recessionary pressures. The project also contributed to an evaluation of the effects of the EU Directive on Information and Consultation of Employees.

### **3. Methodology and main results**

We examined whether European legal provisions establishing employee representation rights and requiring firms to inform and consult employees have resulted in increased employee representation, and whether this is associated with a greater use of flexitime and working-time accounts. We also explored the extent to which the changes observed are associated with differences in firms' employment responses and employee motivation problems, and whether effects vary with the level at which pay bargaining takes place and with workforce composition.

Identifying the causal effect of employee representation, and more generally, of work organization, is methodologically troublesome (DiNardo and Lee, 2004; Bloom and van Reenen, 2011). Ideally, one would require exogenous variations in the presence of employee representation at the workplace level. In the project, we exploited the quasi-experimental variation introduced by the implementation of the 2002 European Union (EU) Directive granting employees information and consultation rights beyond a certain firm size. The Directive 2002/14/EC on the Information and Consultation of Employees provides employees with minimum statutory rights to be informed and consulted by their employers on a range of key business, employment and work organization and restructuring issues (Directive 2002/14/EC; Hall, 2005). We focused on four countries (Cyprus, Ireland, Poland and the UK) in which the implementation ("transposition") of the Directive implied major changes in national legislation. The size-contingent nature of the Directive, which applies to establishments employing 50 employees or more, creates quasi-experimental conditions. This setting allowed us to use a difference-in-difference approach to compare the responses of eligible and non-eligible establishments. To conduct our empirical analysis, we relied on repeated-cross sectional establishment-level data from the European Company Survey (2004-2013). One major advantage of this survey is that it provides harmonized information on employee representation and working-time arrangements before and after the transposition of the Directive.

Our results suggest that the Directive had a positive and significant effect on both the presence of employee representation and the utilisation of flexible working-time arrangements in eligible establishments. More precisely, the proportion of establishments with employee representation among those establishments affected by the Directive increased by 7 percentage points

compared to the control group over the reform period. Furthermore, the utilisation of working-time accounts in the establishments affected by the Directive (the treatment establishments) increased by 5 percentage points compared to control establishments in the same period. In relation to the pre-reform situation, the magnitude of these effects is sizeable, representing increases of 33% and 21% respectively. We also find a significant reduction in the incidence of staff motivation problems as perceived by managers. Interestingly, the effect of employee representation on flexible working-time schemes is driven by establishments where no local wage bargaining takes place and those with a high proportion of female workers. Employee representation appears to play an important role in aggregating and communicating preferences for temporal flexibility, which are often thought to be stronger in the case of female employees (Goldin, 2014). The validity of our identification strategy is robust to a series of placebo tests in which we arbitrarily manipulate the size threshold, the pre-policy and post-policy periods, and the countries affected by the Directive. The results are not confounded with compositional changes of treatment and control groups over time. We also show that our findings do not reflect long-run differential trends in the utilisation of flexible working-time arrangements between affected and unaffected firms. Our results are consistent with the idea that employee voice may foster flexibility along other margins of adjustment (hours) than employment in second-best scenarios in which incomplete contracting problems are pervasive (see for instance, Freeman and Medoff, 1984; Hogan, 2001; Jacobsen and Skillman, 2004; Addison, 2015) and allow for more efficient contracting.

The project adds to the literature on shop-floor employee representation and works councils. Previous research has mainly focused on the German case, exploring the effects of representation on productivity, investment, employment, and wages. Our paper relates to the literature on the economic effects of unionization (DiNardo and Lee, 2004), including a relatively smaller literature on the effects of employee representation on nonwage aspects of work (Buchmueller, DiNardo, and Valletta, 2004). Evidence about the relationship between employee representation and working-time flexibility is scant and mostly based on case studies (Berg et al, 2014; Herzog-Stein and Zapf, 2014). Due to the lack of exogenous variation in employee representation structures, the proper identification of causal effects has been a major concern about these studies.

The project also contributes to the literature on working-time flexibility. While previous research has mainly focused on technology as a key driver of flexible working time utilisation, we highlight the role played by an important labour market institution--employee representation--in mitigating the kind of commitment problems that may undermine the implementation of such practices.

A paper presenting this analysis has been published as an IZA Working Paper and is currently under review with the *European Economic Review*.

#### 4. UK specific analysis

Another part of the proposed analyses focuses solely on the UK, where the Workplace Employment Relations Survey (WERS) provides more detailed data and can be matched with confidential data on employment levels and other variables. This analysis, which also looks at employment effects, is still in progress. The conditions in which the merged dataset can be accessed are quite cumbersome and considerably more complex than we anticipated. We expect this part of the analysis to be completed in the coming months.

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## **4. Impact and dissemination activities**

### **4.1 Impact**

The knowledge generated by the project gives policymakers in national governments and the European Commission an empirical base for understanding the effects of recent EU Directives on employee information and consultation. The fact that employee representation has a positive effect on working time flexibility may have important economic and social implications in areas of crucial policy relevance (employment adjustment to shocks, firm productivity and work-life balance). Our findings suggest that well-designed public policies encouraging firms to adopt participatory schemes involving employee representation could reduce many social costs associated with the pressing problems of high unemployment and job displacements, having important implications for Europe's competitiveness and social cohesion.

### **4.2. Dissemination**

We have presented the results of this research to international scientific audiences, to policy stakeholders and social partners and to the general public in a number of forums.

#### ***2.1 Participation in scientific conferences and seminars***

Preliminary results from the project were presented in the following conferences and seminars:

- First World Conference in Comparative Economics (Roma Tre University, 25-27 June 2015)
- Research Seminar at the Copenhagen Business School (30 October 2015)
- Research seminar at DEPS, University of Siena (30 March 2016).
- 20th Annual Conference of the Society for Institutional & Organizational Economics (15-17 June 2016, Paris).
- 18th Conference of the International Association for the Economics of Participation (IAFEP). (7-9 July 2016, Copenhagen).
- Annual Conference Royal Economic Society (10-12 April 2017; University of Bristol UK).

Related papers were presented in the following conferences and seminars:

- Conference of the Franco-Swedish Program for Philosophy and Economics, Uppsala (Sweden) 8-10 June 2015.
- Research seminar, Institute for Futures Studies, Stockholm, 9 December 2015 (Virginie Pérotin , “Are more democratic firms more productive?”).
- Research seminar, Institute for Futures Studies, Stockholm, 23 November 2016 (Virginie Pérotin, “The effect of employee empowerment on job satisfaction”).

### **2.3 Research workshops and panel sessions organized by the project**

- Panel session on “*Employee voice and firm behaviour*”, organized as part of the 14th Conference of the European Association for Comparative Economic Studies (EACES). (8-9 September 2017, Regensburg). Participants: Aleksandra Gregorič (Copenhagen Business School), Gabriel Burdin (Leeds University Business School & IZA), Virginie Pérotin (Leeds University Business School) and Filippo Belloc (University “G. d’Annunzio” Pescara).
- Leeds international research workshop on “*Economics and management of workplace democracy, employee participation, and emerging organisational models*” (4 May 2017). The list of papers/participants is available in the project website: <http://wpart-project.eu/workshop/>

### **2.4 Policy-oriented workshops**

- Keynote presentations at the annual Irish ProShare Association (IPSA) Conference in Dublin (October 2016): “The resilience of employee-owned firms. Statistical evidence and implications for turbulent times” (Virginie Pérotin) and “Tackling Inequality through Employee Ownership: prospects and challenges” (Gabriel Burdín) . <http://www.ipsa.ie/wp-content/uploads/2016/10/Dr-Gabriel-Burdin.pdf>
- Invited presentation at the International Labour Office & International Cooperative Alliance Research Conference on cooperatives and the world of work, Antalya (Turkey), November 2015.
- Participation in the Corporate Governance Reform Workshop at London School of Economics (6-7 February 2017). Presentation at the panel session on “Participation, Performance and Works Councils”

### **2.5 Outreach activities**

A major outreach activity, the Leeds Festival of Economics, Democracy and the Workplace, was organized as a project closing event. The festival brought together leading international researchers, practitioners and the policy-making community with the general public interested in workplace democracy and emerging organizational models. Some of the speakers included Profs Pencavel (Stanford University) and Samuel Bowles (Santa Fe Institute), and representatives of trade unions and employers organizations. The format facilitated interactions between

researchers, the policy community and the public as well as better networking among researchers, practitioners and the policy-making community. Apart from the support provided by the Marie Skłodowska-Curie actions, the Festival was sponsored by the Society for the Advancement of Management Studies, the Royal Economic Society, Leeds University Business School's Engagement Support Fund, and the European Association for Comparative Economic Studies. The event was part of the Leeds University Business School's Ideas in Practice Seminars series.

Some 70 delegates from the UK, Europe (Belgium, Cyprus, Denmark, France, Germany, Ireland, Italy, and Spain) and the US participated in the event. The Festival's programme is available here: <http://wpart-project.eu/2017/04/28/may-5-final-programme-leeds-festival-of-economics-democracy-the-workplace-still-time-to-register/>

## **2.6 Publications**

- Burdín, Gabriel & Pérotin, Virginie, 2016. "Employee Representation and Flexible Working Time," IZA Discussion Papers 10437, Institute for the Study of Labor (IZA) [currently under review with *European Economic Review*].

## **2.7 Research blog and social media**

- 9 posts on topics related to the main theme of the proposal were published in the project's blog: <http://wpart-project.eu/category/blog/>
- Project's Twitter account: [@WpartProjectEU](https://twitter.com/WpartProjectEU)
- Website: <http://wpart-project.eu/>

### **Related documents and publications**

- Leeds Festival of Economics, Democracy and the Workplace (4-5 May 2017). Flickr album: <https://www.flickr.com/photos/66003587@N06/albums/72157680380122684>
- Employee representation in Europe by country, sector and establishment size (collection of digital maps).
- Leeds Festival of Economics, Democracy and the Workplace (4-5 May 2017). Audio files.

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