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## SOCIALISM AND PRIVATIZATION : THE ESOP COMBINATION

### 1. Introduction

Recent changes in Eastern Europe and the Soviet Union have taken place at a rate faster than anyone could really contemplate. These changes have marked the end of an era and the beginning of a new one. The end is marked by the extinction of the socialist system as a world order and the transformation of a bi-polar world to probably a uni-polar one, and the beginning is dubbed as the "Gorbachev era" when peoples' power has ushered in great changes from communism in Eastern Europe".<sup>1</sup> The changes have raised more questions than seem to have solved. One of the basic questions thus posed is : Can socialism no longer be held up as a competing model of development to that of the capitalist system? Pertinent to it is the question : what happens to the Third World countries<sup>2</sup> that have opted for the socialist model? The question, to be more specific, refers to : What is the future of socialism ?

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1. M. Rahman Khan, "Changes in the Soviet Union and Eastern Europe : Sources and nature", Paper presented at the *Seminar on Changes in Eastern Europe: Regional and Global Impact*, organised by the Bangladesh Institute of International and Strategic Studies (BISS Seminar), Dhaka, March 11, 1990, p. 1
  2. The concept of "Third world countries" needs to be redefined in the context of recent changes in the world order when the "second world" has practically ceased to exist as a system opposed to the "First World". However, the term is used in this paper in till-now generally held connotation.

Without going into ideological interpretation of changes in East-European and the Soviet Union, and theoretical debate as to superiority of any one of the conflicting world systems i.e. capitalism and socialism, it can be stated that traditional socialism has, unfortunately, failed to be a success and without a bit of exaggeration it can be said that the developing countries would think twice before looking at the centrally planned economy as the ideal development model. But does this mean the triumph of capitalism and of the western notion of democracy? Any affirmative answer to this question would surely be oversimplification of the issue in question. Marx's dictum that existing production relations become a fundamental obstacle to the development of productive forces, i.e. the prevailing economic system can stifle growth and necessitate revolutionary change has repeatedly asserted its truth and applicability in the history of societal development, and that socialism, the first stage of communism, is a higher form of socio-economic formation also corresponds to this development trend. It is now an established truth that no social order ever disappears before all the productive forces, for which there is room in it, have been developed, and new higher relations of production never appear before the material conditions of their existence have matured in womb of the old society. In Marx's own words : "The bourgeois relations of production are the last antagonistic form of the social process of production—antagonistic not in the sense of individual antagonism, but of one arising from conditions surrounding the life of individuals in society, at the same time the productive forces developing in the womb of bourgeois society create the material conditions for the solution of that antagonism. This social formation constitutes, therefore, the closing chapter of the prehistoric stage of human society."<sup>3</sup> In this context, recent changes in the socialist bloc, it is argued, are not so much systemic demerits and loopholes of socialism as much inability of the contemporary

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3. Karl Marx, *Critique of Political Economy* (1859), Chicago, Kerr, 1904, p. 13

common man to rise up to the level of common ownership of property, primarily of the means of production.

In Marx's own understanding, first stage of a communist society i.e. a socialist society could not claim to have wholly established equality among members of the society, which can only be attained at a higher stage of the communist society only, where the underlying principle of communism—"from each according to his capacity, to each according to his needs"—could be implemented. In that sense, socialism, although is more equitable than capitalism, cannot ensure full fairness and justice, because *the equal right* in the socialist society is still based on the same principle as bourgeois right, although principle and practice are no longer at daggers drawn. In spite of this advance, this *equal right* is still continually handicapped by bourgeois limitations. The right of the producers is proportionate to the amount of labour they contribute, the equality consists in the fact that everything is measured by an *equal measure, labour*.<sup>4</sup> For this more "equitable system" to be workable, the ideologues provided for abolition of private property of means of production. Though initially this accounted for accelerated economic growth, very soon, the failure of the governments in the respective countries to cope up with ever increasing consumer demands sowed seeds of frustration with the system itself. State ownership to means of production had resulted in passive attitude to production and "property of all" had virtually turned into "property of none" so far as personal initiative related to property was concerned.

The state ownership of the means of production had resulted in a situation where the broad masses had no incentives to work. To quote an author on Eastern Europe : "...in fact, the long years of communist rule have bred cynicism, lethargy and unscrupulousness among the broad masses. They somehow tried to substantiate their

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4. Karl Marx, *Critique of the Gotha Programme* (1875), New York, IP, 1938, p. 30

meagre income through trading state properties in a black market or working in the "second economy" i.e. legalized private markets."<sup>5</sup>

If Marx was at all wrong in predicting the future trends of societal development, it was in his utopian (?) assessment of human relation to property in the XIXth century. This relation has undergone very little change over the last hundred years. However, even if socialist property relations are much ahead of time, the same is not true for other socialist values and guarantees. The scenario in Eastern Europe speaks not so much of the systemic crisis of socialism as it dictates the necessity to match "initiative in production" with socialist ideals. It is submitted in this article that it is possible, without reverting back to individual private ownership of means of production, to introduce initiative characteristic of a free-market economy, and thus overcome the difficulties of the centrally-planned economy. The measure referred to is what is now popularly known as the Employee Stock Ownership Programme—the ESOP technique. The purpose of this paper is to show how in the above mentioned background of world scenario it is possible to combine "justice and fairness" of socialism with "initiative and virtues" of capitalism. A fruitful combination of these two, it is believed, can well be prescribed as a development model for the developing countries confronted with the arduous task of deciding which way to go. In so doing, the obvious focus would be cast on East European countries on whose experience other countries, especially from the Third World are likely to draw extensively in search of a possible development model.

## 2. East European Choices :

In seeking remedial solutions in the future, several options and variables are open to transform East Europe's centrally planned economies. Three ways are often prescribed :<sup>6</sup>

5. M. Rahman Khan. op. cit. p. 6

6. Anisul Islam Mahmud, Statement of the Minister of Foreign Affairs at the BISS Seminar. p. 8

- a. The first is a capitalist variation that Eastern Europe must reject any lingering ideas about a third way—a sort of mixed market socialism based on public ownership or worker self-management and go straight for a western style market economy.
- b. The second is to follow the general direction taken by the USSR prior to June, 1989, namely that advanced capitalist societies have developed technical solutions to problems of production which can be integrated with minimum dislocation into the socialist variety. Some of these solutions are scientific in nature and therefore usable without change. Others are capitalist in nature which can be used for a limited time to boost production and accumulation and at some later date be re-socialized.
- c. The third option is to look at purely socialist traditions for an answer as capitalist forms will have consequences at variance with economic, political and social objectives of socialism and the re-emergence of class whether they are intended or not.

The basic foundations of the first two models are the same. In the above solutions, therefore, the choice is one between a market economy and a centrally planned one. But hardly can the market economy model provide solution to all ailing problems of a centrally planned economy since the free market brings with it the worst of capitalism like inflation, unemployment, cuts in social security etc. It is difficult to comprehend that people long used to a sort of care-free life would agree to surrender themselves to such grave uncertainties. Thus the only option left is in socialist traditions. But traditional socialism with state ownership on means of production has failed to be effective. On the contrary, "the state monopoly of the socialist countries over their wealth, rewards and punishments enabled the *nomenklatura*—the list of party-approved candidates to fill important party/government positions—to reward itself with a very comfortable life, unimaginable by the masses. In fact, this *nomenklatura*, otherwise called the *apparatchiks*, over time acquired

the characteristics of a hereditary caste and held the whole country virtually into their ownership.”<sup>7</sup>

Consequently, traditional approaches hardly provide us with solutions to above mentioned problems. New vision and approach is the call of the time. The way out, it is submitted, can be found in albeit discarding state ownership but yet not reverting to traditional private ownership—attainable by widening the ownership right in the society by a unique form of privatization known as the Employee Stock Ownership Programme—ESOP.

### 3.1. Privatization : Some Basic Issues

The connotation of privatization is far wider than transferring a public enterprise to the private sector and in fact, in several developing countries non-ownership options were of utmost relevance. “The concept is one of a continuum and rests essentially on the marketisation of the enterprise.”<sup>8</sup> In other words, the concept of privatization is that of a continuum ranging between full divestiture at one end and an operational change at the other. Many of the organisational and operational options explicitly contain elements of marketisation; hence conceptually they should be considered as facets of privatization, though of a second order and less spectacular than divestiture.<sup>9</sup>

The question of privatization is closely connected to the problem of role of the state in the economic life of the society and consequently, is associated with the notion of development planning. Any

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7. M. Rahman Khan. op. cit. p. 6

8. United Nations Development Programme, (Sponsored by), *Report of the Interregional Workshop on Privatisation*, Templeton College, Oxford, 1988, p. 13

9. See : V.V. Ramanadham, “Basic Limits to Divestiture”, Paper submitted to the New York University Seminar on “Limits and Obstacles to Privatisation” in 1989-90. In: *IBT-13E Seminar Book, IDLI, Rome, 1990, p. 164A.*

development planning generally concentrates on any one of the following models.<sup>10</sup>

- a. The conservative view maintains that state intervention upsets the so-called "natural justice" of the existing social and distributive order. Hence, the state should not exceed the role of "Laissez-faire". This is the capitalist model.
- c. According to the second model the state may intervene to direct the development of the market along the lines dictated by pluralist decision making.
- c. The extreme leftist model reflects the third view which holds that fundamental and revolutionary changes are required to restructure social relations and rectify social injustices by replacing the market system with state planning. This is, in other words, the socialist model.

The advent of socialism in practice in the first quarter of this century was thought to be the logical consequence of the "inherent injustices" of the capitalist model of development. But now that socialism itself has been discredited not so much from outside as from within system, the obvious answer for relief and reconstruction has been growing interest toward privatization.

Privatization is a political process that operates in the field of economics, not the reverse.<sup>11</sup> The key questions that arise in any country's privatization program are political ones. The key decisions are also made on political grounds, and the problems that arise and the ways to solve them are also in the political arena.

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10. Mohammad Qasem Ahmed Al-Quaryoty, "Reconciling Development Planning with privatization: The case of Jordan". *Public Enterprise*, 1989, Vol. 9, No. 1, pp. 54-55-

See also: Wade D. Cook et al (ed). *Planning process in Developing Countries: Techniques and Achievements*. Amsterdam, 1982, pp. 15-46.

11. V.V. Ramanadham, "Policy, Economic, Political and Legal considerations for privatisation".—*IBT-13E Seminar Book*, IDDI, Rome, 1990, 2, *op. cit.*

Privatization is a means of achieving the national objective of efficiency in enterprise operations. It is not an end in itself. The essence of privatization is marketisation of enterprise operations.<sup>12</sup> It is not simply the sale of a public enterprise to private buyers. Although the concept of privatization is used by different people in different ways, a comprehensive definition would include all policies which aim at more dependence of the economy on the market system, and less involvement of the state, and where the performance of management is judged, rewarded or punished.<sup>13</sup>

Although some authors have described privatization as "the single most influential concept of the decade",<sup>14</sup> it is never a warmly-greeted program. On the contrary, any privatization scheme is, as a general rule, accompanied by special fears, specially by developing countries. Most countries approach privatization with apprehension and intense concern as to both political and the economic outcome. But developing countries have certain special fears. Many in those countries view privatization as a possible return to the bad old days. They fear, not without reason, neo-colonialism.

Now that privatization has made its way throughout the socialist bloc as well<sup>15</sup>, fears of privatization is sure to give birth to its opponents there too. Privatization inevitably has its opponents, all the more in the not-so-long-ago socialist countries with three quarter of a century's tradition of state ownership. These opponents represent distinct interest groups, which have, or perceive they have, more to lose to privatization than they have to gain from it. Main opponents to any privatization scheme in a developing

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12. Paul H. Elicker, *Some political aspects of privatisation*, Centre for Privatization, Washington D.C. 1988, p. 1.

13. Mohammad Qasem Ahmed Al-Quaryoty, *op. cit.* p. 55

14. Paul H. Elicker, *op. cit.* p. 1.

15. For statistics see : A. A. M. Baquer, "Privatisation of Enterprises", *The Dhaka University Studies*, part, C, Vol. 10 (1), 1989, p. 144

See also: *Sangbad*, March 7, 1990.



country and in states engaged in socialist "deconstruction" may be classed as follows :

The first is the bureaucracy itself. All state-owned enterprises have a sizable body of civil servants administering them. In many cases, there are a large number of people excess to the needs of the enterprise. In such cases, this bureaucracy is at risk in what many of the individuals see as a risk to their jobs. Under the present arrangement they have certain powers, they have certain prerequisites. They do not on the face of it see why they should put these at risk for an uncertain future.<sup>16</sup>

For much the same reasons, the military, especially when it has political power, is typically opposed. It is interesting to note that when the Pinochet regime in Chile first started its privatization programs in the 1970s it was estimated that 95% of the military politicians were opposed.<sup>17</sup>

Labour is traditionally opposed, particularly union officials. Their fears are somewhat different. One obvious consequence of privatization is cut in the labour force. They also fear a similar decline in union membership. For reasons of social responsibility, the government in many countries, even outside the socialist belt, has used state-owned enterprises as a disguised welfare system, where excessive employment masks what would otherwise be the true unemployment rate. Labour fears dismantling of this system.

Quite surprisingly, one of the opponents of privatization in many countries outside the socialist belt is the private sector itself. Especially in countries with a wealthy private oligarchy, these individuals have privileged industrial, economic and social positions that, in their opinion, could only deteriorate with change.

While illustrations of determination of the government to privatize and steady, insistent pressure on the part of the policy-makers

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16. Cited in: A. A. M. Baquer, *op. cit.* p. 143.

17. Paul H. Elicker, *op. cit.* p. 4

may have positive effects in neutralizing the bureaucrats and military politicians, it is somewhat difficult to access the labour supported by the leftist political allies, and albeit, to a lesser degree, the existing private sector.

One of the most powerful ways, in our opinion, to neutralize and even make converts of their opposition is to bring them into the privatization program with more to gain than to lose. This may be achieved if it can be reasonably shown that the "inefficiency" of the state-owned enterprises may be totally overcome and "competition" infused to replace it without totally giving in to oligopoly capitalism and discarding socialist ideals. Such a powerful tool is provided by the already mentioned ESOP.

### **3.2 Privatization and the right to property :**

Since the time that written history of mankind can trace, property was recognised to be one of the fundamental and inalienable rights of an individual. The substance and content of this right though underwent subsequent changes with change in the socio-economic structure of the society, its total negation, was however, defined as a flagrant violation of basic human rights. Nevertheless, both the philosophies have been dominating human minds and affecting social revolutions ever since the birth of the Communist Manifesto in 1848. While one philosophy was founded on the empirical evaluations of human nature with its flaws and caprices, and was manifest in the works of classical economist Adam Smith, the other philosophy propounded by Karl Marx and F. Engels operated mainly on the notion of "ought to be" in human nature and abstraction of the concept of "natural justice". Consequently whereas the logical conclusion of the Adam Smith school was open competition and establishment of a free-market economy, the latter school advocated abolition of private property and establishment of a centrally-controlled economy. Although both the schools claimed, and continue to claim, to have accurately and properly

analysed and grasped the laws of human nature and societal development, the history has testified to the contrary. While disillusionment with capitalist ideology has compelled, ever since the 20s of this century, a considerable section of members of the community of states to bend toward and opt for socialism, the beginning of the "Gorbachev era" in much the same way has shown that the craving for total abolition and hence deprivation of an individual of his private property as a means of establishment of a fair and equitable society is still very much an utopian idea. Realisation of this reality, as it appears now, may be unpredictably painstaking for many states, especially in the developing world. It is very relevant for them to ask : which model of development to pursue ?

The situation is not that bleak as it might appear at first sight. It is now suggested that a fair and equitable model of development may be established by adoption of ESOP. This would also correspond to the objects of modern international law in the field of human rights. Article 17.1 of the Universal Declaration of Human Rights (1948) states : "Everyone has the right to own property alone as well as in association with other".<sup>18</sup>

It is now universally accepted that without property or the means to become an owner of modern forms of productive property, the person in today's high technology world remain permanently dependent on those who own and control society's productive enterprises. All other fundamental human rights remain vulnerable where the ownership and control of the means of production are not widely diffused throughout society. Just as deprivation of ownership rights constitute a breach of human rights, so also, concentration of ownership in the hands of a few cannot be upheld to be in tune with the notion of "natural justice". Moreover, inadequate participation in ownership brings problems of distribution. Hence, establishment of a realistic and fair system

18. United Nations, *Human Rights*, A compilation of international instruments. New York, 1988, p. 4.

necessitates a synthesis of ideas of Adam Smith and Karl Marx, and that is precisely what has been achieved in the Employee Stock Ownership Programme.

#### 4. Employee Stock Ownership Programme ( ESOP ) :

It is commonplace that ownership is largely determined by who has access to capital credit. Just as society can structure its laws and institutions to concentrate ownership, society can reform its laws and institutions to decentralize ownership. Similarly future corporate credit can be used to build more ownership into the same tiny group of present shareholders, Or it can be used to create new owners with a new social contract based on private property for workers in the bargain. "The Employee Stock Ownership Programme ( ESOP ) is one such powerful ownership-expanding technique which provides widespread access to capital credit to each employee in a company on a systematic basis".<sup>19</sup>

Regardless of how we define privatization the predominant method today is to seek out existing savers, either domestic or foreign, who can purchase state-owned enterprises. Considering that most people live from hand to mouth and have very little savings to invest, particularly in high risk, heavily subsidized state-owned enterprises, the concept of depending on existing savings pools automatically relegates most of the future ownership of these divested enterprises to only those with sufficient savings, i. e. those who already own and control most of today's private sector enterprises.

Furthermore, the very people, who most need to be motivated to make these divested enterprises operate profitably—the employees—are viewed as outside contractors. In general, participation by workers, labour unions and citizens generally in the restructuring process and in the intended benefits, is at best an afterthought.

19. Equity Expansion International Inc : What is an ESOP ?-*IBT-13E Seminar Book*, IDLI, Rome, 1990, p. 500.

Consequently, in many countries where privatization has been launched, there is often tremendous resistance from unions, workers and consumer groups who have learned that privatization may mean that they have to give up something, with little or nothing in exchange.

Attempts have been made in the past to mitigate these complaints in one of two ways :

- i. where the workers are thrown a few ownership crumbs to reduce their political resistance to privatization or to drive a wedge between workers and their labour unions, or
- ii. through public offerings where the majority of ownership and control will flow to wealthy domestic and foreign investors. Both the methods may be epitomized as "part of the zero-sum approach to privatization, where the past controls the future and where one can gain only at someone else's loss."<sup>20</sup>

The recent experiences in socio-economic development of different countries explicitly exhibit and which we have already mentioned in the paper, that privatization in the traditional way, for different reasons than with socialism, also won't work. As one of the leading exponents of ESOP concludes : "the greatest obstacle to privatization is that privatization experts have been locked into the past savings paradigm"<sup>21</sup> An alternative paradigm that would make privatization practical involves synergy-creating new capital ownership opportunities for non-owners, without taking away existing wealth from present owners. And in most cases, this means maximizing participatory ownership opportunities for workers and citizens generally.

ESOP "enables uncapitalized employees to buy employer's stock, and to pay for it out of the yield of the assets represented by that

20. Norman G. Kurland & Dawn M. Kurland, *Beyond privatization: An Egyptian model for democratizing capital credit for workers*, New York, 1989, p. 1.

21. *ibid.*

stock, without impairing the employees' job earnings or their virtually non-existent savings."<sup>22</sup> The company's reward from an ESOP—in addition to a motivated workforce of workers/owners—is the low cost financing of its own capital needs.

The ESOP does not seek to tax the already rich. Broadening the base of private property via ESOP does not involve the expropriation of anyone's property. The whole aim of an ESOP-type financing technique is to strengthen rather than erode the rights of private property ownership. It is quite aptly remarked that "an ESOP is the only tool in the world of investment finance that can create new owners and generate new sources of capital credit for corporate growth or transfers of ownership."<sup>23</sup>

#### 4.1. ESOP : The Modus Operandi

The ultimate object of the ESOP technique may be stated to implement a more just global economy, in conformity with the concepts of "natural justice" and "democracy." Such an economy is comprehended to be based on four main tenets :<sup>24</sup>

- a. Restore open markets for determining just prices, just wages and just profits. This would inevitably lead to decentralization of economic choice and power to each person.
- b. Restore personal rights of property in means of production. Its consequence is access to profits and control secures personal choice and self-determination. Thus it is an ultimate democratic check on centralized government power.
- c. Limit government power in economy to settling goals for private sector growth and equal ownership opportunities. This in its turn frees public sector to promote justice for all, to prevent mono-

22. Rania Fahmy, ESOPs : "Why Employee-owners are winners", *Business Monthly*, July, 1989, p. 24.

23. *ibid.*

24. Norman G. Kurland & Dawn M. Kurland, *op. cit.* p. 2

polies to protect property, to enforce contracts, and to lift barriers to equal opportunity.

- d. Promote widespread citizen participation in capital ownership, through the democratization of capital credit. It results in promoting rising property incomes and economic participation to every citizen, by diffusing future ownership opportunities while safeguarding property rights of present owners. It further builds a broader constituency for restoring personal access to property and open market policies.

The functioning of the ESOP technique may be viewed as corresponding to the following stages :

*Stage one*, when the stock corporation forms ESOP. Initially, the Board approves ESOP, appoints ESOP trustees and then approves purchase by ESOP of seller's shares;

*Stage two*, when the existing stock is purchased with loan to ESOP. Primarily the Banks or other financial institutions loan money to ESOP at reduced interest rates. Correspondingly, the Trust signs note to the concerned Bank, and the corporation guarantees to make contribution to ESOP to repay loans. ESOP pays seller for shares and the seller on its part transfers shares to ESOP. Shares are pledged as collateral or held in suspense account. Thereupon, ESOP accounts are set up for each employee. This form of credit purchase requires no cash or guarantee by employees. The seller also avoids capital gains taxes by buying new shares in another company.

*Stage three*, whereupon the company pays out profits for repaying buy-out loans, bonuses and dividends as new employee benefits. The company makes annual contribution and dividends to ESOP for loan repayment which is tax deductible. The ESOP pays annual principal and interest due on loan. Shares are then released for annual allocations. Released shares are allocated and held in ESOP accounts of participants, which is also non-taxable. This stage also

encompasses distribution of monthly and annual cash bonuses and dividends, if available.

*Stage four*, which involves distribution of vested shares upon retirement or termination i.e. distribution of cash and ESOP shares and sale of distributed shares at appraised fair market value.

The main difference between a leveraged ESOP and conventional debt financing, as evident from its *modus operandi* is that, in the latter only interest payments are deductible for income tax purposes, while amounts used to repay loan principal are not. The employers contributions to an ESOP, however, are fully deductible. They are considered to be employer contributions to an employee benefit plan, including those applied by the trust to repay loan principal.<sup>25</sup>

The ESOP participants, however, earn their right of ownership in the company through the ESOP's requirement that employees work for the company for a prescribed period of time before the stock in their ESOP accounts become vested. Employee share-ownership increases with the length of service and career advancement. Allocations of shares are made annually and the employee's share is called his "vested interest". The provisions which determine his vested interest are called the "vesting schedule".

If an employee terminates employment for any reason other than retirement, death or disability, his vested interest under the ESOP will be determined by referring to the vesting schedule. He, or his beneficiary, is eligible to receive a liquidation of his vested benefit, the payment of which may be in a lump-sum or in installments over a period of upto five years.

#### 4.2. Advantages of the ESOP:

The rapid expansion of participatory ownership is partly explained by the fact that is an economic system in which all the

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25, Rania Fahmy, *op. cit.* p. 24.



parties involved stand to gain something : the ESOP presents a win-win situation. In a nutshell, the advantages for various quarters may be presented as follows :

**a. For the employees :**

- i) Elevates the dignity and status of every worker to that of an owner,
- ii) diversifies worker's income beyond wages alone to include profit-sharing bonuses, share accumulations and dividend income,
- iii) provides workers as a group with access to productive credit for up to 100% of the shares of their company, secured and payable out of future profits,
- iv) creates greater harmony and cooperation between management and non-management employees.

**b. For the company:**

- i) Increases employee loyalty to the company,
- ii) motivates workers to help expand profits to pay for their shares and receive dividend payouts,
- iii) unites the interest of workers with that of other investors, foreign as well as domestic,
- iv) reduces the likelihood of strikes and labour problems.

**c. For the present owners :**

- i) Provides new partners who will contribute not only capital but also efforts,
- ii) gives the possibility of releasing a part of their capital for investing in new projects,
- iii) assures receiving a fair, objectively determined price for the shares sold,
- iv) leaves control of the enterprise in friendly hands.

**d. For the lender :**

- i) Higher labour motivation and more harmonious labour-management relations enhance the security of debt-repayment,
- ii) repayment of credit through the lender's participation in the borrower's profits not only agrees with Islamic principles which forbid interest, but offers the lender in an inflationary environment a way to conserve the real value of his capital and receive a fair return for his administrative expenses and risk.

**e. For the Government :**

- i) Reduced political pressures for subsidies, public sector payrolls and fiscal deficits,
- ii) a way to divest itself of inappropriate economic activities without the political liabilities associated with conventional forms of privatization,
- iii) increased private sector productivity and a broader base of taxation from rising incomes among workers,
- iv) a broader political constituency against redistributive taxation and over-regulation of business,
- v) enhanced economic democracy, which is the foundation for social and political democracy.

ESOP, for all its considerable advantages, nonetheless, is not a work place miracle. Increased productivity, improved profits and highly energized employees do not just happen upon an ESOP's announcement. This is only a beginning. An ESOP cannot be a real payoff unless there is effective employee participation in the functioning of their company.

**4.3. ESOP : The Reality**

From its very inception in the early 50s by the American lawyer and economist Louis Kelso, ESOP has travelled a long way. It can now be said that ESOP has rapidly come of age, at least in

the USA. Ten million US workers, about one fourth of all corporate employees, are enrolled in an ESOP, up from 3 million only a decade ago. More than 9,800 companies in the US offer such programmes, including 1,500 in which employees own the majority of the stock<sup>26</sup>. Success stories of several companies that have adopted ESOP tempted viewers to dub the program as the "American legend"<sup>27</sup>. In fact, experience shows that over a ten year period, ESOP companies grew 40-46 percent faster with their ESOP than they would without them.<sup>28</sup>

A number of other countries are also taking steps to implement ESOPs. In 1989, the United Kingdom passed laws similar to US laws to encourage the formation of ESOPs. Several outstanding demonstrations of ESOPs involve employee buyouts of formerly state-owned enterprises, including National Freight Lines and Peoples' Provincial Bus Company. In May, 1989, Egypt launched the first ESOP in the developing world with the formation of Alexandria Tyre Company, a 150 million joint venture with the Pirelli Tyre Company of Italy and some other investors.<sup>29</sup>

Acceptance of ESOP is now being increasingly prescribed as a precondition for economic aid, especially by the US. In fact, a White House Task Force Report to President Reagan in 1987 recommended promotion of ESOP initiatives in US economic assistance efforts in Central America and the Carribean<sup>30</sup>. At present, at least one country in Central America—Costa Rica—is engaged in framing and adopting coherent and comprehensive legislation consistent with concepts of economic justice and democracy underlying the ESOP technique and based on principles derived from the experiences of thousands of companies which have imple-

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26. *Time*, February 6, 1989, p. 50

27. See : *Business Week*, November 12, 1984, p. 136.

28. Rania Fahmy, *op. cit.* p. 25

29. "Equity Expansion International Inc: What is an ESOP"? *op. cit.* p. 500

30. *ibid.*

mented ESOPs from the first one in 1956<sup>31</sup>. Expected success of ESOPs in Egypt and Costa Rica is sure to multiply instances of ESOP adoption by developing countries in their pursuit of democratization of the economy.

### 5. Conclusion :

The "ghosts" of not only Laissez-faire economies but also of centrally planned economies have been haunting the minds of politicians and social scientists alike for quite some time. The recent momentum for privatization is part of the pendulum's swing away from socialism—which has proven to be unworkable—to something new. This "something new", however, cannot merely be a return to private sector "wage system" solutions with little or no safeguards against exploitation of workers and special privileges for the few. It cannot ask the workers to make concessions and sacrifices, and to make more efficiently, but for some one else's profits.

It has also been repeatedly emphasised that privatization in the traditional way, for different reasons than with socialism, does not yield positive results.

The possible wayout, as has been shown in this paper, might be a combination of initiative and efficiency of participatory ownership with equitable distribution of wealth—the purpose best served by ESOP which guarantees one of the basic human rights i.e the right to property without succumbing to the "excesses" of traditional capitalist ownership.

Unfortunately, human being is still miles away from that ideal state when he would be free from all lusts for private property and ownership. Sense of private ownership continues to dominate an individual and alienates him from the sense of "common ownership" and "belongingness". The human civilization is yet to reach that high level of awareness and maturity which was the dream of

31. See Explanatory Guide to Draft 1, Costa Rica, ESOP Law Project developed by Equity Expansion International Inc. July 17, 1989, p. 1.

Karl Marx. Till then, ESOP may be the only possible way to achieve both economic efficiency and economic justice.

Good practice follows sound ideas, and successful privatizations will involve a delicate balancing of principles of efficiency with maximizing ownership opportunities for today's disenfranchised workers and citizens. The process will necessarily evolve gradually, as policy-makers, corporate executives, labour leaders and institutional leaders lift their minds above the zero-sum paradigm to a more synergistic framework designed to make every citizen an owner. This framework may suitably be provided by ESOP which may well be dubbed as the "capitalist form of socialism",<sup>32</sup> undoubtedly with more proximity to socialism than to capitalism.

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32. *The Economist*, July 22, 1989.