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SHARING SHARES WITH EMPLOYEES: TOOLS AND EMPIRICAL EVIDENCE FROM LITHUANIA

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ABSTRACT

This paper discloses the situation, specifics, tendencies, and limitations of employers' adjustment to employee financial participation (sharing shares) in companies in Lithuania. Three main tools are analyzed: the issuance of employee shares (known since 1990); a share granting (effective since 2018); and employee stock options. The empirical part of the paper is based on interviews conducted in 2019 and repeated in 2022–2023 with expert lawyers from Lithuanian law firms, alongside a survey of Lithuanian companies. The following aspects were analyzed: employers' knowledge of the possibilities of involving employees in company management (activities); instruments used by employers to implement employee financial participation; reasons that prevent successful employee involvement and barriers from the perspective of employees; tax-related issues; and measures that could facilitate greater employee involvement within the company. The research results show that there is a tendency that promotion via shares is becoming more

popular and that business culture is slowly evolving. Employee stock options are the most used instrument, surpassing the use of statutory tools to grant shares to employees.

KEYWORDS

Employee financial participation, share granting tools, employee stock option, employee shares.

INTRODUCTION

One way to harmonize the interests of employers and employees and to encourage employees to achieve the best business results is employees' financial participation in the company's activities. The importance, influence, and role of this phenomenon is growing. For example, The European Economic and Social Committee (hereinafter EESC) expressed the view that the combination of employee profit-sharing and share ownership should be the goal of future employee financial participation in the company's management.¹ It is clear that the institutions of the European Union (hereinafter EU) take a liberal approach from the point of view of employee financial participation, and encourage the use of measures to involve employees in the company's activities based on good national practices and research. The EESC has even called for the creation of a common European model for employee financial participation based on voluntary participation by employers and employees.²

Indirect employee participation (e.g., the obligation to establish works councils and the activities of trade unions) is well known in Lithuania. However, the manifestations of direct employee participation in the management of a company (including financial participation) are much more difficult to observe and assess than indirect participation, which is clearly established in laws and reflected in official state statistics. The Law on Companies of the Republic of Lithuania³ (hereinafter LoC) sufficiently clearly regulates two instruments of employee financial participation: employee shares (Art. 43); and granting of shares (hereinafter GoS) which came into force on 1 January 2018 (Art. 47¹). However, data on the use of these institutions are usually collected through voluntary company surveys, and the results obtained do not provide specific practical advice or suggestions on how to encourage the use of these tools or address other emerging issues. Thus, we do not have statistics on these instruments. Furthermore, it is not entirely clear what determines the lack of enthusiasm on the part of employers regarding the use of financial incentives, nor what determines the greater or lesser popularity of specific measures.

Although the financial participation of employees in the company's activities is not a new phenomenon, there are only fragments of scientific studies on this in Lithuania, and some of them are quite old.⁴ Here we could only distinguish the study conducted

¹ European Economic and Social Committee, "Opinion on Employee financial participation in Europe," *Official Journal of the European Union*, C 51/1 (2011): 5.

² Ibid., 5.

³ Law on Companies of the Republic of Lithuania, *State News* (2000, No. 64-1914).

⁴ Valdonė Darškuvienė, Stefan Hanish and Niels Mygind, "Financial Participation of Employees in Lithuania," Institute for Eastern European Studies, Free University of Berlin (2006); Valdonė Darškuvienė and Paulius Vazniokas, "Stock Ownership as a Form of Employee and Management Financial Participation: Factors of Development in Lithuania," *Organizacijų vadyba: sisteminiai tyrimai*, Vol. 38 (2006); Remigijus Civinskas and Jaroslav Dvorak, "New Social Cooperation Model in Service Oriented Economy: the Case of Employee Financial Participation in the Baltic States," *International Society for Manufacturing Service and Management Engineering*, Vol. 9, No. 3 (2017): 37–50.

by Remigijus Civinskas⁵ on the adaptation of employee representatives to the measures applied by companies to involve employees in management (activities). This study does not analyze the adaptation of employers to the aforementioned measures of involvement of employees.

The relevance of research in this area has been confirmed by studies conducted in other EU countries, such as Croatia,⁶ Poland,⁷ Ireland⁸, etc. There are also studies on the importance of employee financial participation at the institutional level and for private businesses.⁹ According to surveys, the majority of profit-sharing and employee share-sharing schemes are applied in Slovenia, Slovakia, Finland, France, Sweden, the United Kingdom, Estonia, Denmark and Lithuania.¹⁰ In other studies,¹¹ Lithuania is also presented as a country with sufficiently widespread application of employee financial participation measures (compared to other Member States). Nonetheless, the statistics are not staggering, which could be due to several factors, including: unclear legal regulation; skepticism of employers; administrative burden; poor knowledge of financial participation by employees and employers; lack of strong state traditions or clear political strategy; and current business culture, i.e., a reluctance to share ownership with employees or consider employees as partners.

To discern the attitudes of employers to the measures of employee financial participation and their application, we conducted an empirical study entitled "Adaptation of employers to direct participation of employees in the company's activities" in 2019. This research was carried out within the framework of the "Development of the International Network of Experts Related to Raising Awareness of Employee Participation in the Activities of Enterprises and Contribution to the Implementation of the EU Law and Policy in This Area" project conducted by the Lithuanian Confederation of Industrialists (hereinafter LCI), together with partners in the Viadrina European University, the Lithuanian Trade Union Alliance, the T&M Solutions Public Institution, and the Podkrepa Bulgarian Labor Confederation. This research was also partly funded by the European Commission. After 3 years had elapsed, we conducted repeated research in November 2022–April 2023 to obtain comparative results that allow us to better understand how the phenomenon of sharing shares with employees has improved over this period (including how it is understood) and where it currently stands in Lithuania.

The article presents the instruments of employee financial participation available in Lithuania and reveals the current situation, tendencies, and limitations of Lithuanian

⁵ Remigijus Civinskas, "Darbuotojų atstovų prisitaikymas būti pagalba įmonei konkurencinėje aplinkoje, kurioje informacijos vertė yra pagrindinis ekonominės sėkmės elementas," Tyrimo ataskaita (Adaptation of employee representatives to help a company in a competitive environment where the value of information is a key element of economic success, Research Report), (2018): 35.

⁶ Srecko Goic, "Employees' Attitudes Towards Employee Ownership and Financial Participation in Croatia: Experiences and Cases," *Journal of Business Ethics*, Vol. 21, No. 2 (January 1999).

⁷ Maciej Kozłowski, "Financial Participation Programs in Polish Public Companies," *Management*, Vol. 9, No. 4 (2014).

⁸ Jonathan Lavelle et al., "The Determinants of Financial Participation Schemes within Multinational Companies in Ireland," *The International Journal of Human Resource Management*, Vol. 23, No. 8 (2012).

⁹ Erik Poutsma, Joseph R. Blasi, and Douglas L. Kruse, "Employee Share Ownership and Profit Sharing in Different Institutional Contexts," *The International Journal of Human Resource Management*, Vol. 23, No. 8 (2012); Derek C. Jones et al., "Complementarities Between Employee Involvement and Financial Participation: Do Institutional Context, Differing Measures, and Empirical Methods Matter?" *ILR Review*, Vol. 70, No. 2 (2016).

¹⁰ Jens Lowitzsch and Iraj Hashi, "The Promotion of Employee Ownership and Participation," Inter-University Centre for European Commission's DG MARKT (2014): 30–32.

¹¹ Eurofound, *The Third European Company Survey – Workplace innovation in European Companies* (Luxembourg: Publications Office of the European Union, 2015), 98; Maria Caprile et al., *Measuring Varieties of Industrial Relations in Europe: A Quantitative Analysis* (Luxembourg: Publications Office of the European Union, December 2018), 26.

employers' adaptation to employee financial participation. Due to the aforementioned lack of statistics on usage of the available instruments, in this article we do not analyze in detail the legal peculiarities of the specific instruments (as we did more extensive research on this in our empirical study in 2019) but focus specifically on researching the practical use and distribution of the instruments by explaining how the phenomenon has developed in Lithuania from 2019 to 2023.

In addition to methods specific to legal research (analysis of documents and information, comparative and analogy, systematic, historical, teleological and generalization), a quantitative research method was used: a survey of the Lithuanian companies (their managers and lawyers) that apply employee promotion measures, as well as associations of employers and employees and trade unions. Accordingly, a qualitative research method was also used which involved interviews with experts in the field of employee financial participation – mostly lawyers working in the largest Lithuanian law firms, lawyers in companies that apply measures of employee financial participation, etc. Our research and this article is predominantly based on qualitative research method (as opposed to only theoretical legal research) which is best suited to disclose the practical peculiarities of the development of the phenomenon in question.

In the second section, we present the employee share promotion (sharing) instruments available in Lithuania and their legal regulation while paying more attention to the analysis of the GoS. In the third section, we present data on the empirical research performed and its interpretation. Finally, the fourth section presents our findings and recommendations.

1. INSTRUMENTS OF EMPLOYEE FINANCIAL PARTICIPATION AVAILABLE IN LITHUANIA

Employee financial participation has been an idea since the early twentieth century, but it has been used more intensively and widely in the last 35-40 years.¹² It is a type of direct employee participation in the management of a company and can be understood as a way in which employees are involved in the company's decision-making. It is unquestionable that employee financial participation is closely linked to a company's financial performance and specific employee incentive schemes (by encouraging employees both individually and in groups). Employee financial participation is usually divided into profit-sharing and employee share ownership.¹³

Leaving aside profit-sharing, which is generally understood as a bonus where part of an employee's salary is directly linked to the company's profits, employee share ownership is characterized by an indirect link to the company's activities, i.e., not only can the owners of shares receive returns in the form of dividends, but they can also earn from growth in the value of the company's shares.¹⁴ The sharing of shares usually takes the form of an individual grant of shares to certain employees on favorable terms, such as being free of charge, partly charged or on par value of the shares.

Shares may be granted to employees by exercise of a share option. In Lithuania, the share option is not a directly regulated instrument, but is not prohibited; to give shares to an employee is a free-form transaction (agreement). The definition of a share

¹² Dermot McCarthy, "Employees Financial Participation": 508–509; in: Jens Hölscher, Horst Tomann, *Palgrave Dictionary of Emerging Markets and Transition Economics* (Palgrave Macmillan London, 2015).

¹³ Jens Lowitzsch et al., *Financial Participation for a New Social Europe, a Building Block Approach* (Rome and Berlin, 2008), 90.

¹⁴ Remigijus Civinskas and Jaroslav Dvorak, *supra* note 4, 41.

option is not explicitly provided within Lithuanian laws; it is only indirectly mentioned in the Law on State Social Insurance of the Republic of Lithuania (hereinafter LoSSI)¹⁵ and the Law on Personal Income Tax of the Republic of Lithuania (hereinafter LoPIT).¹⁶ Despite this lack of statutory definition, in 2023 the Supreme Court of Lithuania (hereinafter SCL) adopted a resolution where, for the first time, it more widely spoke about the nature and definition of share options as well as clearly distinguishing the former from preliminary agreements.¹⁷

In the sense of subjects that can be granted with the share option, the transaction is unrestricted, whereas the option can be granted to any type of employees by both the company (including the parent company and the subsidiary) as well as the shareholder. Any condition may be agreed upon, including deferral periods, objectives to be achieved, redemption arrangements, liability of the parties, etc., insofar as this is not contrary to the applicable laws. However, it has been observed that due to the lack of direct provisions regarding share options in Lithuanian legal acts, there was legal uncertainty (instability) regarding the mandatory feasibility of the share option as an instrument. This issue is partly solved by the abovementioned case practice of the SCL.

The company may issue ordinary shares with the special status of *employee shares* if this is provided for in the company's Articles of Association (Art. 43(1)). Unlike the share option or the GoS, the law does not provide the possibility to defer the acquisition of employee shares (to acquire the right to shares later). The law does not provide for a maximum number of employee shares to be issued. The decision to acquire employee shares is an employee right rather than obligation. Unlike in the case of the GoS, the right to acquire employee shares is not provided to the members of the company's management bodies. Thus, this institution is intended exclusively for employees, while separating it from management. There is also a mandatory restriction on disposing of shares within the term specified in the share subscription agreement, which must not be longer than 3 years from the date of the subscription, before which the owner of the employee shares may transfer the shares only to another employee of the company (Art. 43(3)). In addition, during this period employee shares also do not confer voting rights. Only at the end of the set restriction period do the shares become (i.e., convert to) ordinary registered shares. The law does not provide the possibility to acquire employee shares free of charge (granted) or partly charged, and the employee must pay for the subscribed shares before the restriction on the transfer of shares expires (Art. 43(4,5)).

The design of *granting of shares* (GoS) was based on the legislation of other EU Member States and sought to create a convenient and competitive instrument for employee promotion by shares by replacing the practically inapplicable employee share institution and introducing an alternative for share option. The possibility to grant shares to employees is provided in the legislation of the Czech Republic, Latvia, Germany, Poland, Hungary, France, the United Kingdom and Slovakia.¹⁸ It should be noted that

¹⁵ Law on State Social Insurance of the Republic of Lithuania, *Lietuvos aidas* (1991, No. I-1336), Art. 11(1), point 25.

¹⁶ Law on Personal Income Tax of the Republic of Lithuania, *State News* (2002, No. 73-3085), Art. 17(1), point 58.

¹⁷ *H. B. v A. K., J. K.*, Supreme Court of the Republic of Lithuania (2023, No. e3K-3-27-381/2023).

¹⁸ *German Stock Corporation Act (Aktiengesetz)* (1965, No. (BGBl. I p. 1089) FNA 4121-1), Art. 192(2)3; *Civil Code of Hungary*, Hungarian Gazette (2013, No. HUN-2013-L-96512), Art. 3:236; *Code de Commerce France* (1807, No. FRA-1807-L-73434), Art. L225-177, L225-197-5; *Commercial Code of Czech Republic* (1991, No 513/1991), Art. 158, 161a, 161e, 174, 178, 209a, 210; *Companies Act 2006 of United Kingdom* (2006, c. 46), Art. 1166; *Commercial Law of the Republic of Latvia*. (2000, 2069/2071), Art. 237, 240, 242, 254, 255.

compared to the legislation of different states, the GoS established in the LoC is more consolidated and should be more convenient to apply in practice.

This institution established new methods of granting of shares, i.e., free of charge or partly charged (Art. 47¹, par. 1, par. 5, point 3). In addition, the circle of subjects that can be granted with shares was expanded to be practically unlimited at the company level – i.e., shares may be granted also to the employees of the parent company or subsidiary, including the managing directors and members of the management/supervisory board of such companies. One restriction is that shares may be granted only to natural persons (Art. 47¹). Further, the shares may not be granted to a person who is a shareholder of the company, parent company or subsidiary and to whom the shares owned provide 1/20th or more of the total votes. The justification for this restriction is that it seeks to avoid conflicts of interest and possible abuses to prevent shareholders, including employees and/or members of the company's bodies, from taking unfair advantage of the GoS, and to enable employees and/or members of the management bodies who have already acquired shares to continue their promotion by shares.¹⁹ However, there are exceptions to this rule when shares are issued by a bank or brokerage firm.

The law does not determine the maximum part of the share capital which may consist of the shares to be granted, but such a proportion (threshold) may be established within the GoS rules (Art. 47¹(6)). Certain temporary restrictions on the rights conferred by the shares may also be provided (Art. 47¹(6), 15(1), points 2, 3, 6) – e.g., the GoS rules may provide that the shares will not confer the right to: receive the company's funds when the company's share capital is reduced in order to pay out the funds to the shareholders; receive shares free of charge when the share capital is increased from the company's funds; and/or receive a part of the assets of the company in the event of liquidation. In addition, the GoS rules may impose temporary restrictions (conditions) on the disposal of shares,²⁰ such as the prohibition on transferring the shares to a third party.

The right of initiative to prepare the GoS rules is granted to a wide range of subjects (Art. 47¹(4)): (1) shareholders of the company holding at least 1/20th of all votes; (2) a group of employees consisting of at least 1/3rd of all employees of the company; (3) the managing director and the management board; and (4) the supervisory board. From the date of receipt of the application and no later than within 6 months, a general meeting of the shareholders must adopt the final decision on the approval or non-approval of the rules of granting of shares with a qualified majority (not less than 2/3rds).

Finally, the tax aspects are closely linked to the successful implementation of employee financial participation and can sometimes even determine whether a particular employee incentive will be popular (applied in practice) or not. When an employee acquires shares, the obligations provided in Lithuanian laws on personal income, state social insurance and compulsory health insurance apply. According to the LoPIT, shares acquired by an employee free of charge are considered as income in kind,²¹ thus the obligation to pay personal income tax arises. The tax obligation does not arise from

¹⁹ Explanatory Letter of the Law on Companies of the Republic of Lithuania on change of Articles 2, 15, 20, 28, 32, 34, 37, 38, 45, 46, 47, 51, 52, 54, 57 and 59 as well as on supplementing with Articles 47-1 and 47-2, Register of Legal Acts, (2016, No. 12359(4)).

²⁰ By implementing the requirements of Article 4(d) of Directive (EU) 2017/1132 of the European Parliament and of the Council, Article 471(12) of the LoC provides an obligation to disclose such restrictions (conditions) on the disposal of the shares by submitting the GoS rules to the Register of Legal Entities within 10 working days from the date of their approval.

²¹ LoPIT, 16, Art. 2(15), 9.

the occurrence of the right to acquire shares (e.g., the signing of a share option agreement), but from the factual moment of acquisition of shares.²²

In July 2019, an additional personal income tax exemption was adopted, which provides that non-taxable income includes “employee benefits under an option from the employer or a person related to them received from the acquisition of shares free of charge or partly charged if the shares are acquired not earlier than 3 years after the grant of the option.”²³ This essentially means that if the share option stipulates that the employee will acquire the shares not earlier than after 3 years, they will not be obliged to pay personal income tax. This tax exemption applies to those share options that are granted as of 1 February 2020 or after that date (meaning that the first non-taxed shares likely emerged on 1 February 2023 at the earliest). This amendment has aligned the provisions of the LoPIT with the provisions of the LoSSI, which already provided that social insurance contributions are not calculated on shares received under options if the right to acquire the shares is granted to employees not earlier than after 3 years.²⁴

2. EMPIRICAL FINDINGS

2.1. Methodology

Quantitative research. An unrepresentative survey was developed for the empirical study conducted in August–September 2019. The survey was sent directly to approximately 20 companies (including public and private limited companies) and to confederations of employers and employees. The questionnaire was also distributed through the LCI among LCI members.

Unfortunately, the activity of the respondents was not high – out of 81 members of the LCI and companies that were asked to fill in the questionnaire, 12 responses (12%) were received. Some companies declined to participate on the grounds of confidentiality – they were reluctant to disclose their employee promotion practices – but most companies simply did not respond. As a result, the findings of the survey cannot be considered sufficient to draw specific conclusions and are presented in this article for information (illustrative) purposes only. The conclusions and recommendations are mainly based on the data obtained during the qualitative study (interviews with experts). However, such passivity on the part of respondents partially indicates a tendency that so far in Lithuania, employers, or at least members of the LCI, might not be sufficiently interested in the issues of employee financial participation. However, there may be other reasons as well (separate research was not conducted in this respect).

The questionnaire consisted of 12 questions with pre-prepared suggested answers and 4 open-ended questions. The survey questions were related to: employers’ knowledge of employee involvement opportunities; adequacy of information; the availability of information, including the channels through which the employers access such information; the application of appropriate incentives for employees in practice; regulatory clarity and acceptability; the reasons for not applying employee incentive measures, including an assessment of the position of the employees; and measures that could encourage greater use of incentives for employees.

²² Ibid., Art. 8(1).

²³ LoPIT, Art. 17(1), point 58.

²⁴ LoSSI, Art. 11(1), point 25.

According to the legal form of the companies, there were 6 public limited companies and 6 private limited companies. According to size, there was 1 company with 10–49 employees, 6 with 50–249 employees, and 5 with over 250 employees. In terms of annual revenue, 4 companies indicated that their annual revenue was EUR 2–10 million, 4 companies – EUR 10–50 million, and 4 companies – more than EUR 50 million. Based on the value of assets, 2 companies indicated that their value of assets was up to EUR 2 million, 2 companies – EUR 2–10 million, 1 company – EUR 10–43 million, and 7 companies – more than EUR 43 million.

Qualitative research. A total of 27 interviews were conducted with experts from the 13 largest Lithuanian law firms within the period of April–December 2019 and 3 years later, within the period of November 2022–April 2023. These interviews involved lawyers, other employees of the companies that apply employee promotion measures, and other persons who in practice faced employee financial participation. A total of 32 respondents were interviewed, including 1 representative of a trade union, 4 representatives of public limited companies (some were representatives of the commercial banks), and 27 experts from Lithuanian law firms. The data obtained during the interviews was the main source, revealing: (i) the practical subtleties of employee financial participation; (ii) the extent of the specific measures that are applied in practice; (iii) the reasons for not promoting (applying) incentives; as well as (iv) potential solutions.

2.2. Knowledge of Lithuanian employers about the possibilities of involving employees in the management of the company

The results of the survey showed that most respondents (representatives of companies) are aware of statutory and other opportunities for employees to participate in the company's activities (management), and even apply such measures in practice.

This may indicate that employers are aware of the possibilities for involving employees in management, but there are questions specifically about employee financial participation by sharing shares. In general, traditional measures of direct participation in a company's management, such as quality circles, discussions with employers and other similar means, are inherently simpler to apply in practice compared to share sharing/granting arrangements, which require additional knowledge and resources (and often the assistance of external consultants). Therefore, it is not surprising that such measures are less common in practice.

The results of the interviews may indicate another trend – that employers' knowledge and practices vary depending on the type and size of the company as well as the sector where the company operates. For example, in certain sectors, such as manufacturing, industry, and construction, employee financial participation is simply not as relevant (and in practice there is a lower number of cases evidencing the granting of shares in these sectors) as in the financial, fintech, technological services, or IT sector (e-commerce, gaming, etc.), which are characterized as having a long-term relationship with customers depending on the services provided. Most of the respondents indicated that share sharing practice (usually by share options) is a common thing within fast growing/young companies and in the start-up sector, including IT and technology firms. The practice of granting share options can be brought in either by venture capital firms or other investors, or simply due to the lack of monetary resources at the beginning of the lifecycle of the start-up. Accordingly, we conclude that for both employers and employees in "traditional" sectors, shares do not play such a significant role compared

to traditional bonuses and cash incentives. This is determined by (and connected to) the company's product, liquidity, and goals, as well as other factors such as risk (and sometimes fear) related with share sharing.

In addition, the interviews in 2019 showed that financial participation as an instrument was often implemented only for the key employees (managing director, members of the management board, key managers/employees) on whom a large part of the business's success depends. Interviewees pointed out that depending on the type of company the implementation of instrument differ, particularly because of the company's income, profit, number of employees, internal policies, etc. However, during the 2022–2023 interviews, some of the respondents (some were the same people as in 2019) stated that the share/option granting phenomenon had become more widespread and now these instruments are sometimes applied to larger groups of employees (not only the key employees or the management), or in rare cases even to all employees of the company. Other respondents mentioned that sharing shares with all employees within the company is the tendency toward which the whole phenomenon is moving. In addition, one of the key aspects that naturally facilitates the implementation of employee financial incentives in public companies is that the shares of these companies can be freely traded on the stock exchange, so the question of their value and liquidity does not arise. This gives employees a sense of security.

In principle, all respondents confirmed that stock options or other ways of sharing shares are a common practice in young, quickly growing companies and start-ups, and are quite widely used. Several reasons for this have been identified: (1) the desire to retain and motivate employees who create a lot of added value (important for the growth of the company); (2) lack of funds for employee salaries at early stages; (3) the goal of owners to sell the matured company and make a profit; and (4) the implementation of the share option plans is requested by investors.

In general, the answers received during the interviews show that the reasons for the application or non-application of share granting incentives for employees can be very different. These measures are applied mostly due to motivational (loyalty promotion) aspects, but the tax environment (benefits) also has a significant impact on this phenomenon. Tax-related benefits as the main reason to grant employees share options (motivational and financial incentive) were especially emphasized during the 2022–2023 interviews. This is closely related to 2019 amendments to the LoPIT, which likely had significant impact on encouraging the implementation of share sharing plans within Lithuanian companies. During the interviews, it was stated that it is simply beneficial for employers from the tax perspective to grant share options for employees based on the conditions stipulated within tax laws. Other stipulated reasons were: education of entrepreneurship and interest in the company's business policy; competition (application of share sharing in other companies); good examples and practices of other companies (including foreign practice); pressure from investors (especially relevant in the start-up sector); payment of additional remuneration (incentive measure); employee motivation policy of the company; instructions from the foreign parent company to implement an appropriate employee promotion policy²⁵ (instead of the traditional cash incentive); efficiency promotion, etc.

²⁵ This is typical for finance companies, banks, IT companies, and technology companies that provide services and concentrate on long-term relationships with their clients.

In general, employers are aware of the possibility(s) to provide employees with shares, although they often still need the assistance of legal advisors in the selection of a specific instrument, the preparation of contracts, etc. Accordingly, employees who are interested in contributing to this type of company (start-up) also tend to have knowledge of the opportunities to participate in the company's activities and earn income by acquiring shares. Therefore, they usually agree with the share options offered by employers or even themselves ask to settle on share-sharing arrangements.

Regarding the differences between the specific legal instruments implementing share-sharing, it appears that Lithuanian employers concentrate on the solutions that are the most financially attractive and can benefit from tax perspective. In general, most of the employers are aware of the traditional share transfer instruments, such as share purchase agreements and donation transactions, and are less aware of the particularities of share options (unless these companies are fast-growing start-ups in IT, technologies sector). Meanwhile, it would be difficult for employers to name the differences between the instruments of share sharing established in the LoC considering that the GoS only entered into force in early 2018. Therefore, employers tend to use the assistance of internal or external lawyers.

It is quite positive that Lithuanian employers perceive employee financial participation as a tool for employee promotion and often (especially in start-up companies' practice), depending on the company's goal, undertake to implement it. Meanwhile, the situation is completely different from the perspective of employees. Employees generally do not have the knowledge to distinguish between share sharing instruments unless they are C-level managers or other closely related corporate/legal workers. Therefore, they confuse different share sharing instruments and understand share sharing as a general tool. Other issues, such as employees' fear of asking for shares, the lack of awareness of the benefits of shares, and the intention to receive rewards/promotions here and now, should be mentioned. Without having the support of employees for share sharing (except in fast growing financial/fintech, e-commerce, gaming, technological, and IT sectors), this method of financial incentive (motivation) loses its essence. In addition, according to a trade union representative, it is too early to discuss broad employee financial participation at this market stage, as the current Lithuanian market is still at the level of defending workers' rights. This participant also added that from the point of view of employers, employees are not considered as equal partners who could be granted with shares.

The knowledge of Lithuanian employers highly depends on the extent to which the share sharing scheme can be successfully implemented in a particular company considering its type, size, and sector of activity, as well as applicable tax benefits (exemptions). Knowledge largely depends on the relevance to a particular company and the readiness of employees. Despite the aforementioned findings, we can state that employee financial participation is not a novelty for Lithuanian employers. However, open questions about implementation in practice remain.

2.3 Instruments of employees' financial participation applied by Lithuanian employers

Employee shares (Art. 43 of the LoC). The conducted interviews show that the institution of employee shares is not at all applicable in practice and is not recommended by Lithuanian legal advisors. This was acknowledged by all respondents and once again

confirmed during the interviews conducted in 2022–2023. Several reasons for this have been identified, all of which in principle relate to the regulations of the institution itself. As mentioned, employee shares may be granted only to employees, but not to members of the company's management bodies. Meanwhile, in principle, all respondents confirmed that promotion by shares is most effective when granted to the company's managing director, members of the management board, or other executives. This is a very important aspect of business culture, which also determines that in this case the employee share institution is obsolete and completely unusable in practice. In addition, other restrictions (as provided in Paragraph 2 above) reduce the attractiveness even more.

GoS (Art. 47¹ of the LoC). This instrument emerged in 2018, and only a few respondents during the 2019 interviews mentioned that they had faced this tool and advised clients on its application in practice (apart from the fact that during consultations with clients this tool is usually identified as a possible option to share shares). The reasons given by the respondents for not applying this instrument more broadly in practice were: overly detailed regulations (formalism); the need for additional analysis and evaluation of risks; complexity; uncertainty; and lack of market practice (unlike share options). This was partly confirmed during the 2022–2023 interviews, where additional reasons for the non-applicability of the mentioned institution were given by the majority of respondents: administrative burden (including the formation of a reserve from the profit, which is absent in a start-up company) and the complexity of the institution make it hard to implement for start-up companies; same goals can be achieved by share options. However, in 2019 one bank representative stated that the introduction of this measure has greatly facilitated the requirements²⁶ applicable for commercial banks in respect of promoting bank managers and granting them shares. Until then, various sophisticated share sharing mechanisms had to be developed. This was supported by some respondents during interviews conducted in 2022–2023, where it was confirmed that the GoS is usually considered amongst other incentives, and the interview participants consulted several public companies in respect of the implementation of the measure in practice. One respondent even suggested that the GoS is dominant against traditional share option agreements because using this measure makes it easier to create employee share option plans (*ESOPs*) and/or apply a share granting program for all employees of the company. It was also further substantiated that such agreements are easier to explain to local authorities (e.g., State Tax Inspectorate, hereinafter STI), which tend to challenge such transactions in respect of using tax benefits.

During interviews, several respondents confirmed that the GoS could be a very attractive tool for listed companies as the shares of such companies are traded on the stock exchange, their value can be easily determined, there are no liquidity problems, and such companies are usually large, highly staffed, and financially strong. Nevertheless, another part of the respondents emphasized that employee promotion as a phenomenon does not depend on capital adequacy (i.e., small capital is not a reason not to share shares), while this approach can be implemented simply for motivational reasons and should become the usual tool after reaching the appropriate level of business culture.

²⁶ Resolution of the Board of the Bank of Lithuania Regarding the approval of the description of the minimum remuneration policy requirements for employees of credit institutions and financial brokerage firms, Register of Legal Acts (2015, No. 2015-06993), para 18.

During the 2019 interviews, all respondents confirmed that cases where the proportion of the shares granted to employees exceeded 5% were very rare. However, for the employer to grant a larger proportion of the shares to employees, the managing director or other responsible persons, this institution became obsolete due to this restriction, so other incentives had to be chosen, such as share options. During the 2022–2023 interviews, most respondents said that the proportion of shares granted to employees usually does not exceed 15% when the shares are granted via the share option institution (see below).

According to the respondents (both 2019 and 2022–2023), another problem that may prevent employers from choosing the GoS in practice is its formal requirements. It is necessary to prepare the GoS rules (describing the methods, sources, recipients of shares, etc.), approve them at the general meeting of the shareholders, form a reserve from the profit and only then take practical steps to grant shares. This might seem burdensome to employers and especially start-ups (as described above). Additionally, this institution may not be relevant for all employers (e.g., in cases when pursuing to promote only individually without seeking publicity). Still further, the adoption of the rules on granting shares and the promotion of a large proportion of employees may also, within the scope of such rules, bring forward persons who the employer does not necessarily seek to promote. Thus, the institution is not flexible from this point of view. In addition, the abovementioned feature – that this institution is most relevant in companies with many employees – has been confirmed, as the GoS rules are essentially intended for long-term, not one-time use, and are specifically dedicated to the promotion of a large circle of persons. For employers this may seem to be a process that requires a lot of administrative resources, so it is not surprising that depending on the company's goals, size, and liquidity, share options are often chosen as a relatively simpler and more individual alternative. It should also be noted that the GoS can be combined with share options by approving the GoS rules and concluding individual options with employees (by setting acquisition conditions, deadlines for taking advantage of tax benefits, etc.). This was confirmed during interviews in 2022–2023, but only very few respondents confirmed the applicability of such a model in practice.

Share option agreements/options (not established directly within the laws). According to all respondents, this instrument is the most attractive and commonly used to provide shares to employees. Nevertheless, no specific answers were received from one of the open-ended questions of the online survey about the number of companies in Lithuania that exercise share options (quantitative survey of 2019). This is because there are no public statistics about the usage of share options in practice, nor are there statutory registration obligations. The results of the survey also partly indicate that companies are reluctant to disclose or make public their employee promotion policies (possibly due to competition and confidentiality reasons).

However, the share option as an instrument also has shortcomings, chief among is legal uncertainty. Most interviewees confirmed that this problem exists, but they added that they have never faced a situation where the employee would not be able to exercise the option, or the contract would be in dispute. Additionally, in 2019 most Lithuanian experts hinted that, even though such share option agreements usually include an arbitration clause, the issue could one day become the subject of a dispute in a court, and then the court would essentially resolve the issue by a providing formal official position and offering a clarification of the situation. The expressed doubt was

partly solved on 8 March 2023 when the SCL adopted a resolution²⁷ in a case where the court spoke more widely about the nature and definition of share options and clearly distinguished the former from the preliminary agreement. The SCL explained that share option is not a preliminary agreement, and the claimant is eligible to request the fulfilment of share option in kind. In this way, the Court set a precedent for future disputes potentially arising from share option agreements. In short, the Court reiterated that the holder of the share option has the right but not the obligation to enter into a transaction with a certain financial asset (e.g., company shares) at a predetermined price, and the grantor of the option (e.g. company, shareholder, etc.) must execute the transaction if the option holder calls the option subject to the terms of the contract.

The share option is widely used and recommended by lawyers, and the problem of feasibility can also be addressed in several ways. First, the share option may stipulate that it is an irrevocable offer or provide other means of collateral. Second, the accounting of the company's share may be delegated from the managing director to a financial brokerage firm that would ensure the transfer of shares to the employee in the event of the exercise of the right to the shares. According to several respondents, these measures would likely reduce the risk of the option not being exercised. In addition, some experts mentioned that such a promotion is based on a trust, so it is unlikely that dispute would arise.

The opinions of the experts interviewed in 2019 on possible ways to solve the abovementioned uncertainty issue of the exercise of the share option can be split into two camps. The first group was not inclined to agree with the suggestion of establishing a share option institution in the law (e.g., adding a separate regulation like one of the preliminary contracts in the Civil Code). These respondents mentioned that the business culture (of employee promotion) in Lithuania is still at an early stage and should not be overburdened, so the current unchained regulation perfectly meets the needs of the market. Some respondents even emphasized that state interference in business relations should be kept at a minimum, stating that the regulation usually lags behind the actual business relationship and has to periodically adapt to the market, so additional rules in this case would only complicate open business relations. Other respondents indicated that the current regulatory situation is mature and acceptable, thus no additional measures are needed. This was also confirmed by some of the respondents during the 2022–2023 interviews, who added that current agreements and share sharing plans offered in the market are well developed. There was also a call for the broader and more liberal interpretation of the law in the courts, instead of the introduction of strict regulation.

The second group was inclined to agree that the establishment of a share option institution in law (to ensure its enforceability and clarity) is a good idea. During interviews conducted in 2022–2023, more than half of the respondents also agreed to this idea. It is considered that such regulation should not be very detailed and complicated. Thus, a description of the basic transaction would suffice to make it easier to prove the authenticity of the transaction and the will of the parties in court. This would help to take a united stand in the event of a dispute and in exercising the share option, including using tax benefits against the STI (the STI tends to follow its own explanations which are not always consistent and may change). Respondents argued that such regulation would certainly introduce more clarity and transparency (including for

²⁷ Supreme Court of the Republic of Lithuania, *supra* note 17.

employees) as there is currently no clear definition of an option or share option, but these transactions/instruments are mentioned in the laws²⁸ and broadly implemented in practice. However, it must be highlighted that one of the major reasons for granting share options in practice outlined by the respondents remains tax benefits (see Paragraph 3.5 for more details).

Thus, it can be argued that a share option is an attractive and fairly frequently chosen (as well as recommended by legal advisors) tool for Lithuanian employers to implement employee share incentives. Although there are some legal risks associated with the exercise of the option itself, they are usually controlled through flexible and creative means, such as anticipating and describing all possible unwanted scenarios in the agreements themselves. Doing this avoids potential future conflicts between interested parties. The fact that businesses tend to rely more on the principle of freedom of contract rather than statutory institutions (and their formal requirements) established in the laws when promoting employees may indicate a certain maturity and independence of the business culture. The interviews of 2022–2023 showed that expert lawyers who have assisted clients with the implementation of sharing shares over several years (since 2019) have developed fairly advanced and at the same time mature agreements and share sharing plans/programs for use within the Lithuanian market.

In most of the Lithuanian law firms that participated in the interviews in 2019, the need for advice related to share options over the last few years has increased several fold (including assistance with the implementation of the specific instrument). The following reasons for this were: development of business culture; competition between companies; foreign companies' examples; the aim of motivating employees (rewarding them); and increasing loyalty. The increasing need for share sharing consultations (compared to 3–4 years ago) was also confirmed during most interviews in 2022–2023 (even in the more traditional, e.g., industrial/manufacturing sectors). This was mostly due to the new tax benefits applicable for share options.²⁹ Several years ago (before the amendments to the LoPIT), it was simply too costly for companies to incentivize employees by granting them share options (the potential benefits usually did not outweigh the expenses).

Alternative employee incentive measures (derivatives from the other instruments). During the interviews in 2022–2023, it was clarified with the respondents that there are other alternative/hybrid employee share sharing models available in the market. Examples of similar models to ESOPs were provided, where a special purpose vehicle (SPV) as a limited liability company (LLC) or other form of entity is established, the employees become shareholders of the SPV, while the SPV becomes the main shareholder of the company with which the employees have contracts. The structure is nonetheless still implemented by using share options as the main instruments. In this way, according to the respondents, the risks related to voting and potential disturbances in the management of the company are eliminated.

Despite the above, according to the 2019 survey, in Lithuania bonuses were the dominant means of employee promotion,³⁰ often emphasizing that bonuses can easily (without high administrative costs) achieve similar or even identical results to promotion by shares. Granting cash bonuses does not need specific complicated adminis-

²⁸ E. g., the LoSSI, the LoPIT and others (see Paragraph 2 of this paper).

²⁹ LoPIT, Art. 17(1), point 58.

³⁰ However, the online survey showed no positive answers regarding information on how many companies in Lithuania apply the profit-sharing institution.

trative actions like the adoption of GoS rules, a share granting plan or the creation of share option agreements as they are usually tied to the performance of the employee. According to the respondents, the application of cash bonuses also depends on the employees' perception of incentives, income, and the desire to have liquid assets here and now. During 2022–2023 interviews, most respondents confirmed that simple cash bonuses can in most cases achieve similar or even better results compared to sharing shares with employees, even though share sharing goals are different, i.e., involving long-term motivational results and stronger connection to the company. This is because in some cases employees may not understand how to sell or otherwise realize the shares, and in view of other emerging issues, particularly the issue of tax questions, such incentives become less attractive to them.

Thus, employee share instruments face significant competition arising from employee bonuses (monetary incentives). Nonetheless, Lithuanian employers tend to show an increased interest in modern and unconventional ways to increase the loyalty of employees and often opt for share sharing to do so. The results of these interviews show that share sharing is a growing phenomenon but is still developing.

2.4. Reasons preventing the successful implementation of employee financial participation

Financial promotion of employees by shares (e.g., share options) is not a primary measure taken by Lithuanian employers to encourage or involve employees in the management of a company. During the interviews with legal experts, the legal uncertainty of specific instruments³¹ for employee promotion was not identified as a relevant reason for not implementing employee financial participation. Nonetheless, unclear regulation surrounding methods to easily involve employees in the company's activities is the most relevant reason why employers often refuse to apply the promotion of employees by shares in general. The survey showed that the legal framework is more vague than clear and raises several questions in practice, including tax related questions. Based on the results of the interviews conducted in 2019–2020, we can argue that the successful application of share sharing instruments strongly depends on the attractiveness of the tax environment. This was fully confirmed by the results of the 2022–2023 interviews, which showed that existing tax benefits are the main reason to incentivize employees by sharing shares with them.

As regards the (in)sufficiency of information, Lithuanian legal experts have no problems accessing information or implementing these processes. The results of the survey also presuppose that the existing legal and regulatory framework seems sufficient and accessible for Lithuanian employers.

Returning to the reasons that may prevent the successful application (implementation) of employee participation (involvement) in the company's activities, it should be noted that there were no answers related to employers' bad experiences of employee involvement in the company's activities. However, during the interviews conducted in 2019–2020, more than half of all respondents indicated that, in their opinion, employers (especially in the case of highly consolidated, family, or multi-person businesses) still fear that sharing shares with employees will pose a real threat to the company's operations, or such operations may be disrupted in the future. Interviewees confirmed

³¹ As mentioned above, the legal uncertainty of the share option agreement implementation was solved to a certain extent by the resolution of the SCL on 8 March 2023.

that such a fear factor exists due to unpleasant business experiences in the past when companies went bankrupt or were disrupted when certain individuals acquired a stake in them (and then blocked key business decisions). However, the 2022–2023 interviews showed that the fear of potential disruption within the company when sharing shares with employees was no longer a stigma. We conclude that this shows how much the market has matured since 2019. Reasons such as not considering the employee as an equal business partner (distrust of the employee) and lack of capital were also mentioned during the 2019–2020 interviews, but during the 2022–2023 interviews the lack of capital justification was no longer expressed.

Employers (during the survey conducted in 2019) were also asked about the reasons that make Lithuanian employees less willing to participate in share sharing programs/schemes.³² Here again the tax issue was highlighted. However, most respondents indicated that employees lack education, do not perceive and value shares as fully-fledged incentives (especially when compared to bonuses), and usually lack information about such opportunities (initiatives). Interviewees also confirmed that for the motivational system (share sharing) to work effectively, employees must also be aware of the long-term and other benefits granted by shares (including the feeling of a business owner). This was confirmed during later interviews in 2022–2023. Unfortunately, in principle all respondents believe that most employees (depending on the sector³³) still lack education and awareness of the benefits of shares. In addition, Lithuanian employees often desire to receive liquid benefits immediately (e.g., bonuses in cash). During the 2019–2020 interviews, the respondents expressed the view that the granting of shares imposes more obligations to employees (they might have to pay the part of the nominal price of the shares, tax liabilities arise) than benefits (difficult to assess the value and liquidity of the shares – e.g., in LLC – company may go bankrupt, it is unclear whether dividends will be paid, it may be difficult to find a buyer for the shares, etc.). Thus, from one point of view, we can argue that it might simply be inconvenient for employees to acquire shares. Another inconvenience for employees can be high deferral (retention) terms (e.g., in case of a share option, the usual deferral period is 3 years), where immediate benefit is usually desired. Similar findings were obtained during the 2022–2023 interviews, which showed that incentive selection (e.g., share option vs bonuses) highly depends on the specific situation but is usually strongly influenced by: (i) seeking to connect the employee with the company (motivational grounds); and (ii) the existence of tax benefits (which simply determines the selection of the less costly instrument in order to incentivize employees). It was also noted that employees strongly appreciate such aspects as simplicity and periodic involvement in the organization (active interest and engagement).

During the 2019–2020 interviews, some respondents of public limited companies revealed that when employee promotion by shares was applied in their companies, the employees tended to sell shares immediately after acquiring them – in other words, turning them into liquid cash. The respondents of 2022–2023 confirmed that usually the period for which the employee holds the shares is short due to the following circumstances: (i) after obtainment of the shares under share options, employees usually sell them (cash out); or (ii) after the company which shares they hold (or are eligible

³² The results of this survey cannot show the exact real problems that employees face, as the survey aimed at employers and their representatives. To achieve accurate results, it is necessary to conduct a separate study by interviewing target groups of employees.

³³ E.g., the situation is different in the technology and IT sectors.

to acquire according to the share option) is bought by an investor or third party, they are mandated (according to the share option agreement) to call the share options and sell out the shares immediately. Thus, employees who acquire a small proportion of the company's shares as an incentive do not feel like owners of the company and do not show an interest in holding the shares for a longer period, or else by contractual conditions are mandated to exit as soon as they obtain the actual shares. Some of the respondents emphasized the proportion of the shares granted as a significant factor for properly involving the employee (e.g., managing director) and making them interested in the company's activities, essentially by turning them into a partner. Only a tangible part of the company's stock (e.g., 10–30% of the company's share capital) which guarantees a high return can properly motivate an employee and allow them to feel like an owner. Accordingly, the restriction of granting more than 5% of company shares established within Article 47¹ of the LoC could be treated as one of the reasons for the unsuccessful implementation of the GoS. Nonetheless, the interviews conducted in 2022–2023 showed that the idea of a tangible part of the company's stock does not play too significant a role, as in practice a smaller part of shares granted to managers and/or other key employees (or even all employees) can also make a productive impact.

The representatives of the employers stated in the survey of 2019 that the involvement of employees in the management of the company was in principle applied only by the initiative of the employer or by consensus. Meanwhile, no responses were received indicating that such measures were initiated by the employees. The same was confirmed during the interviews of 2022–2023. Thus, the introduction of employee financial participation measures mostly depends on the will of the employer – even though, e.g., the GoS also provides a statutory right of initiative for employees. A lack of employee initiative may also be due to factors such as fear, lack of information, or future tax issues.

The online survey showed that simpler regulation could encourage the more active financial involvement of employees. This suggests that employers would like to have a sufficiently clear and adaptable legal framework, as the exercise of options/share sharing schemes often requires consultation with external lawyers. Survey respondents also indicated the importance of appropriate education.

Meanwhile, all interviewees in 2019–2020 noted that employee financial participation and promotion through shares is a cultural phenomenon that is currently at a relatively early stage in Lithuania. Respondents stated that the (non)implementation of these instruments depends precisely on the will of the employers, and not on the presence of specific legal measures/instruments. According to the respondents, active sharing of good practices (examples) of the application of share sharing schemes alongside the education and training of employers and employees through events, conferences, would make the phenomenon of the financial participation of employees more visible, public, and acceptable from the business perspective. Several years later, the results of the 2022–2023 interviews showed that the phenomenon had become more mature (regarding the legal and tax framework, including the practice available in the market), and therefore Lithuanian employers are more advanced now in terms of incentivizing employees by sharing shares with them. The availability of tax benefits in the market (exemptions from personal tax income and social insurance payments if the share option is held for at least 3 years) was mentioned as the major reason for increasing the

applicability of share sharing schemes in Lithuania (despite the instruments which are clearly established within the laws).

The results of the survey conducted in 2019 also show that the main reasons for non-implementation of employee share promotion instruments were: emerging additional derivative (tax) questions; lack of information or uncertainty; unclear results of application of the specific measure; and level of education. Accordingly, in addition to the aforementioned reasons of fear and reluctance to include employees in the company's management, the results of the interviews show that, in most cases, employers do not take action to promote employees through shares because it may be inconvenient for them (e.g., too costly and hard to administer), or they simply do not aim to do so because a similar result in terms of motivation and loyalty can be achieved by implementing simpler tools (e.g., bonuses or the sharing of other benefits). Promoting employees by shares can be inconvenient for employers due to its high administrative burden, associated costs, lengthy, intimidating processes, and the need for prior communication (especially if the incentive is applied for all employees), and many corporate decisions must be adopted or changes to the shareholders' agreement (if any) need to be introduced. In summary, the following reasons can be identified as to why employee financial participation is not popular in Lithuania: (1) a lack of traditions – some of the respondents mentioned that it is simply unacceptable to promote employees with shares in Lithuania (there is no culture of promotion), and the available examples are determined by the promotion policies applied/mandated by foreign capital companies; (2) a lack of education; (3) a lack of clear initiatives or communication on employee financial participation; (4) not particularly attractive regulation due to administrative burdens (since the majority of employers currently select free-form share option agreements); (5) potential hidden (pre-programmed) shareholder disputes in the future (in the case of a private company, it is difficult to recover transferred shares or to sell the company, unless buyback of shares mechanisms are established); and (6) not treating the employee as a business partner, etc. Another reason mentioned by the interview respondents was the underdevelopment of share classes in Lithuania. Up until recent changes in the LoC which established a more liberal approach to shares classes, it was not possible to grant employees shares that would not grant certain rights or would be different from ordinary shares. From 1 May 2023, the company could issue not only preferred shares, which would be with or without voting rights and/or with cumulative or non-cumulative dividends, but also other preferred shares, where the property and non-property rights granted by them would be determined in the company's articles of association.³⁴

2.5. Trends and limitations of Lithuanian employees' financial participation

The research results show that the phenomenon of employees' financial participation is becoming more and more popular in Lithuania. Interviewees confirmed that they provide much more advice on employee incentives compared to 5 or 10 years ago, while during the later interviews of 2022–2023 most of the respondents confirmed that the amount of advice and consultations they provided (alongside the employer's general level of interest expressed in sharing shares with employees) increased even further. This shows that Lithuanian business culture is developing, where the interests

³⁴ LoC, Art. 42(2).

of employers and employees are more often considered and coordinated (harmonized). Start-ups should be distinguished, where sharing shares with employees is a normal and frequently used practice. This is typically due to several reasons: the business model (the goal of selling a “grown” company); a lack of working capital; and seeking to maintain the loyalty of employees (especially in the IT sector). This was confirmed during the interviews of 2022–2023, where each respondent named start-up companies (usually acting under the LLC legal form) as those most actively using share options in their business practice. The IT, finance (and Fintech), technology, e-commerce (and trade), and energy sectors were mentioned as particularly active when it comes to using share options. The results of the survey and interviews from 2019–2020 showed that share sharing was more common in listed companies. This was due to several reasons: company size, sector, stock liquidity and publicity, financial stability, better communication, etc. However, almost all interviewees in 2022–2023 confirmed that in their practice it is actually LLCs which dominate in share sharing practice. This finding is supplemented by the fact that despite public listed companies applying share sharing schemes (or being obliged to do it, e.g., in the credit and finance sector), the number of public companies is approximately 400 times lower than the number of LLCs. It should be also mentioned that a significant part of those start-ups is of Lithuanian origin (and not beholden to foreign investors). However, as for foreign start-ups in Lithuania, the influence coming from foreign investors and/or general group policy towards sharing shares with employees was a major deciding factor regarding its implementation.

In Lithuania, small and medium-sized private limited companies are typically facing the greatest challenges in implementing employee promotion, especially if they are traditional companies operating in the manufacturing and industrial sectors. Several reasons can be distinguished: a lack of tradition (mentality) and education (especially for lower-ranking employees); poor communication; the legal regulation of private companies; and the domination of traditional bonus incentives. Notably, the successful implementation of employee financial participation also highly depends on the sector in which the company operates. As previously mentioned, this is particularly true in sectors such as IT, technology, finance, and e-commerce, where employees can create long-term added value, have a completely different view, and where we could even state that there is a positive perception of securities as incentive tools. Thus, mutual understanding emerges from both the employer and employee perspective.

Accordingly, considering all aspects of share sharing (administrative burden, employee perception, communication, taxes, etc.) and the fact that the traditional profit-sharing mechanism is likely to achieve the same (or even higher) increase in employee motivation, the employer might tend to decide to promote employees in the traditional monetary way. This is not considered to be abnormal practice in Lithuania (nor in abroad), as every employee incentive scheme has to meet the expectations and needs of a particular business. To successfully implement employee promotion through shares, the employee should be involved in the company’s activities step by step, and later even in management processes. By doing this, the employee should feel a more significant part of the company on which the successful operation of the company depends, and only then, to further bind the employee to the company, should shares be shared with them so that the employee would understand their value.

The results of the interviews of 2019–2020 show that the promotion of employees through shares is most effective when a significant part of the company’s shares is shared with the employee. This allows the employee to truly feel like an owner and to

receive tangible benefit. This is especially relevant when shares are shared with managing employees (executives). The results of the interviews showed that employees who receive a small proportion of the shares do not feel like owners of the company and equate the shares to traditional monetary incentives (only in different form). However, the interviews conducted in 2022–2023 show slightly different results. Most of the respondents stated that the notion of receiving a tangible part of the company's stock does not play that significant a role, as in practice a smaller part of shares granted to managers and/or other key employees (or even all employees) of the company can also make a productive impact. These results allow us to conclude that the phenomenon of share sharing in Lithuania has matured even further.

As regards the limitations of employee financial participation in the company's management, the results of the survey and interviews show that uncertainties in the regulation and the unattractiveness of the tax environment are the essential factors for the successful and wider implementation of incentive instruments. Nevertheless, according to the interviewees, the wider implementation of these specific measures also strongly depends on the business culture, existing examples in the local market and abroad, and competition between companies. Thus, the specific legal instruments established in laws can help to make this phenomenon more popular due to its simpler and easier implementation in practice, but in no way can they force businesses to mass-implement employee share promotions if they are not necessary for them. Attractive legal instruments and a favorable tax environment may indeed lead to the increased application of employee financial participation (tax benefits were mentioned as the main reason for implementing share sharing during the 2022–2023 interviews), but many interviewees indicated that the use of specific instruments should not be encouraged on a mandatory basis. Most respondents from 2022–2023 were of the position that it would be useful to have a share option clearly established within the laws (e.g., the Civil Code of Lithuania). The overall results show that businesses and the culture of employee promotion develop best unhindered, while legal instruments (laws) gradually adapt to actual practice.

The authors of this article believe that share sharing with employees should be a more effective and productive form of promotion, especially from a long-term perspective. This form of promotion is more binding, promotes loyalty, and should bring greater benefits to both the employee and the employer when it is in line with the strategy and objectives of the company.

By acquiring shares, employees also inevitably acquire certain shareholder rights (depending on the proportion of shares held and the terms of the contract), such as the right to a company's information, the right to a dividend, etc.³⁵ Naturally, no controlling shareholder will want to share a controlling stake or a larger proportion of shares than is necessary to encourage (promote) the employee. If the employer's decision is to share only a small proportion of shares with employees, the employees will not be able to make any significant impact in corporate decision-making. The laws of Lithuania provide a threshold of 1/10th of a company's authorized capital (voting rights) for a shareholder to be able to apply for the investigation of a legal person.³⁶ The implementation of other non-property rights of a shareholder in practice also heavily depends on the proportion of shares held. Thus, if an employee is given a minimum number of shares,

³⁵ As provided in paragraph 3.4 above, this might change shortly due to the amendments to the LoC in respect of preferred shares.

³⁶ *Civil Code of the Republic of Lithuania*, State News (2000, No. 74-2262), Art. 2.125(1)(1).

their ability to influence the company's management and strategic decision-making will be very limited. Based on the opinion of the authors of this research, the recent amendments to the regulation on preferred shares (and its regime of classes) might introduce significant change for the employee share sharing phenomenon soon.

The interviews of 2022–2023 show that the usual proportion of the share pool granted to a group of employees is between 5% and 15%. The interviews also show that share options are not necessarily granted only to management or key employees but can be granted for other (or even all) employees of the company according to the general incentive scheme. The findings show that there is a tendency to grant shares to a wider spectrum of employees (to motivate them under the general company incentive policy in a manner like traditional monetary bonuses). The interviews also show that shares are usually granted or promised to be granted in the future on the following conditions: (i) ordinary shares are granted; (ii) the shares are granted free of charge or at a nominal price; and (iii) they come without voting rights. When comparing the two share sharing instruments established in the laws of Lithuania (employee shares and GoS), it is very clear that the GoS is more flexible and attractive to both employers and employees (see Paragraph 2 for more information). The results of the interviews show that shares with the status of employee shares are not used in practice at all due to their statutory limitations – other institutions are simply more advanced and easier to apply.

In addition to the main differences listed above, the advantages of the GoS are its more detailed regulation, which provides clarity on processes, and its more user-friendly nature. It clearly defines the methods of GoS, the content of the GoS rules, the holders of the rights of initiative and other procedures. It is possible to combine the GoS with share options, where the company would undertake to grant the shares free of charge after a certain period. The authors believe that the only disadvantage of this institution is the restriction on granting shares to a person to whom the owned shares would give 1/20th or more of all votes in the authorized capital. Thus, as was provided in Paragraph 3.3, because of this restriction, in certain cases employer must opt for other incentives, such as the share option.

Based on these findings, the most attractive share sharing incentive in Lithuania is the share option. This instrument is attractive due to its free form, the possibility to individually agree on specific terms with the concerned employee, and the absence of strict requirements. This allows the parties to agree on the same or even better terms and conditions than those provided within GoS. Nevertheless, in practice, uncertainty in the implementation of these transactions could arise, as the performance of such a contract largely depends on the will of the parties. For example, if the shareholders of the company would change in the future, they could hypothetically refuse to increase the share capital and grant employees shares under the share option agreement. However, there is already new court practice formed by the SCL which would be of help in case of potential future disputes.

The use of a particular employee financial participation scheme depends on many factors, such as the age, size, capital, technology and operating sector of the company, its shareholder structure, location, state traditions, the influence of trade unions or works councils, etc.³⁷ Opportunities for employees to participate in the management of

³⁷ Jonathan Lavelle et al., "The Determinants of Financial Participation Schemes within Multinational Companies in Ireland," *The International Journal of Human Resource Management*, Vol. 23, No. 8 (2012): 1591.

the company also strongly depend on national factors, such as: state incentive policy, initiatives, laws, tax environment and benefits (exemptions), traditions, history, etc. We can state that although the financial participation of employees as a phenomenon in Lithuania began from the time of privatization (and the restoration of independence), so far, we do not have strong traditions. However, we can also state that the market for sharing shares with employees is certainly growing more mature. A larger change cannot yet be observed because employees are simply not seen as partners with whom business could be developed, and shares are often given solely for motivational purposes. Although the GoS seems to have made the regulation more flexible and liberal, it did not have a significant impact on the market overall (the share option remains dominant here). We would say that employee financial participation in the company's activities in Lithuania is improving (especially in start-ups and in the IT, technology and finance sectors), but it is still quite uncertain and underdeveloped, although we have tools to promote employees (profit sharing, employee shares, GoS, share options). Despite introduction of the GoS, the strongest impact has been made by the availability of tax benefits. State initiatives or public policies to encourage businesses to use such tools could improve the situation, but the perception and mentality of employers themselves is also very important for the use of such incentive measures. Additionally, employees often perceive financial participation in the management of a company only as an additional short-term reward. Thus, a certain level of apathy is inherent for all three interest groups (employer, employee, and state).

The authors of this article believe that profit-sharing and employee share ownership can be effectively coordinated with each other, which would further involve employees in the company's activities, giving them more responsibility and further increasing their loyalty. Education and the sharing of good practices would play a key role here. One of the measures to encourage greater financial participation could be public initiatives of the state, e.g., the implementation of the promotion of employees with shares in state-owned public companies, and later sharing such practices in public. In addition, the successful implementation of the respective instrument is heavily dependent on the following factors: (i) the tax environment and its benefits; (ii) the separation of clear legal instruments for employee promotion by shares in the laws (by removing institutions which are not used in practice such as the employee shares institution and the establishment of a share option in the laws to ensure its enforceability); and (iii) the improvement of share classes.

CONCLUSIONS

This empirical study demonstrates that the need for consultations for the implementation of employee financial participation in the company's activities (to share shares) in Lithuania has increased over the last 10 years. Nevertheless, the survey results may show the tendency that, so far, employers in Lithuania might not be sufficiently interested in the issues of employee financial participation, except for in fast-growing sectors. Of course, there may be other reasons as well. In addition, traditional bonuses (profit-sharing) are applied much more often in practice to achieve the same result of employee motivation.

The most common reasons given by respondents for businesses not applying employee financial participation were: unclear (complicated) legal regulation; high administrative burden; additional and derivative implementation questions; not considering

the employee as an equal partner; inflexible share regulation; tax environment; and the development of business culture. In addition, one of the obstacles mentioned by the respondents was the lack of education of employees and their desire to obtain liquid benefit immediately (in cash). The main reasons for the implementation of employee promotion by shares in some Lithuanian companies are: the promotion of motivation and loyalty; competition between local companies or the influence of good practice examples; the pursuit of greater company efficiency; and the desire to take advantage of tax benefits (exemptions).

We can distinguish a tendency that in Lithuania the implementation of employee promotion in practice differs depending on the type, size, and sector of the company, as well as employers' attitudes and knowledge. The most common cases of financial incentives (share sharing) can be seen in the finance, energy, e-commerce, IT, and other technology sectors. Start-ups and other fast-growing LLCs were named as the major implementors of employee promotion by shares. It is also noteworthy that, as a means of motivation, shares are usually given to managing employees (executives) in a company or to a small, substantial group of key employees. However, these recent research results show the tendency to grant shares to a wider spectrum of employees.

Measures to encourage the more effective application of employee financial participation in the activities of Lithuanian companies could include the improvement of legal regulation and the provision of greater clarity to facilitate the implementation of employee financial participation measures as much as possible. This is partly solved by share option agreements, but this measure has an element of legal uncertainty. However, employee promotion by shares is likely a phenomenon of the business culture, and its implementation may not depend on the existence of attractive legal instruments.

The measures for the promotion of employees by shares established in Lithuanian laws (employee shares and GoS) are sufficiently formal, overlapping (largely repeating each other's content) and, compared to share options, cannot boast of such a wide application. The employee shares institution is generally not applied in practice by Lithuanian employers. Therefore, we recommend that it be rejected by amending the law and leaving only one statutory measure for the promotion of employees by shares – the GoS. However, this institution also needs to be improved by softening the restriction on the proportion of shares which might be granted to employees in the company from 5% to 10%, or even abolishing this restriction altogether. If the employer needs such a restriction, it could be provided in the GoS rules.

These research findings show that the personal income tax benefit (exemption) which came into force in 2020 played a significant role in the implementation of share sharing with employees while also increasing its attractiveness. This tax benefit provides that non-taxable income will include the benefit received by the employee from the acquisition of the shares free of charge or at a reduced price under the share options if the shares are acquired not earlier than 3 years after the granting of the right to the share option. This amendment harmonized the taxation of share options by personal income tax and state social insurance tax. However, the Lithuanian tax environment can be improved even further. Currently, the shares acquired by employees are taxed twice: when the shares are acquired, and when the shares are sold at a higher price. It is proposed to change the moment of taxation of the shares provided in the laws by establishing that the tax liability related to the payment of personal income tax arises only when the shares are sold or otherwise realized by waiving the moment of taxation when the shares are actually acquired.

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