to ramp up productivity, new research finds.

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ANN ARBOR — Broad-based employee stock ownership plans, if properly designed, are the best way to ramp up productivity, new research finds.

E. Han Kim, a finance professor with the University of Michigan's Ross School of Business, said the plans work best when the right incentives are in place.

Although firms with such plans, also known as ESOPs, claim they increase productivity by improving employee incentives, Kim's research finds that results vary by size of the plan as it relates to the total shares granted to employees and the number of employees.

Some ESOPs are implemented by firms with low cash reserves and limited access to external financing. These firms want to conserve cash by substituting wages with employee shares, leading to lower wages after the plans take effect. Other plans are meant to align managers and workers in an attempt to thwart hostile takeover bids, Kim said.

"These non-incentive motivated large ESOPs are unlikely to enhance productivity," Kim said. "And they do not improve wages or share price."

The research – based on an analysis of workplace level wage and employment data from the U.S. Census and on ESOPs at U.S. public firms from 1982 to 2001– also evaluated the outcomes for small plans at companies with fewer than 15,000 employees and those with staffs larger than that.

Small ESOPs comprising less than 5 percent of shares outstanding granted by firms with moderate employee size increase the economic pie, benefitting both employees and shareholders. On average, cash wages at these firms rose by 20 percent and share

be confounded by non-incentive motives.”

Small ESOPs at these firms are followed by significant increases in productivity. The productivity gains are shared by employees and shareholders according to their relative bargaining power. The average wages, level of employment and shareholder value increase.

When firms with smaller employee numbers adopt large ESOPs, the overall evidence is considerably weaker. Benefits to employees are largely limited to the value of ESOP shares granted, which because of sales restrictions are valued less by employees than the market.

For firms with numerous employees, the free-rider problem seems to be a dominant factor with the exception of larger ESOPs implemented by manufacturing firms, which are followed by higher productivity.

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