



report

IVL Swedish Environmental Research Institute

Ethical Aspects in Active Ownership

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Preface

In a customer survey carried out by Folksam, as many as 87 per cent of respondents said that it was important for them that we should allow environmental considerations and human rights to weigh heavily when deciding whether to invest in shares in big multinational companies.

In 2001, as the first asset manager in Sweden, Folksam introduced human rights and the environment as investment criteria for all our capital investments. Our policy was based on the UN's Universal Declaration of Human Rights and the ILO Convention on Fundamental Principles and Rights at Work.

Folksam's aim, by means of our investments, is to influence companies to work systematically towards better fundamental practices of employment law affecting their employees. The starting point for this work is the rules mentioned above, the UN Convention on the Rights of the Child, and the guidelines published by the OECD. We also assess a company's suppliers and sub-contractors based on these new criteria. The same applies in the area of the environment.

In 1995, Folksam was a signatory to the UNEP Statement of Environmental Commitment by the Insurance Industry. Folksam also operates a wide-ranging internal environmental programme. Several business divisions within the Folksam Group are environmentally certified to ISO 14001.

The importance of stakeholder issues for institutional investors has come increasingly into focus in recent years. Folksam has decided to concentrate on active share ownership for three principal reasons:

Firstly, our customers demand that their common interests in stakeholder issues be safeguarded so as to benefit their long-term returns; secondly, we are anxious to encourage a sound, long-term development of the venture capital market; and, thirdly, we want to influence the companies we invest in to respect the environment and human rights.

Folksam has also become a member of the United Nations' "Global Compact" initiative, and is backing the Swedish Government's "Swedish Partnership for Global Responsibility". The reason for this is that it is Folksam's vision to help bring about a long-term sustainable society, in which the individual feels secure. This accords well with the focus of Global Compact and is also in line with Folksam's environmental policies over the years.

Knowledge relating to corporate practices and governance based on a traditional Corporate Governance perspective is relatively extensive and well-recorded. The field of ethical corporate governance and of active ethical share ownership aiming to exert influence on companies is not so well documented, however. Folksam believes it is important to increase the knowledge of ethical share ownership through research.

Stockholm, 30 October 2003

Håkan Johansson

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Abstract

The overall objective of the study is to shed light on the subject of active ownership and the consequences of an increased ethical focus in the work of institutional investors.

The following questions are treated within the study;

- What do ethical aspects of ownership mean?
- To what extent, and in what way, are ethical aspects taken into account by institutional investors?
- What are the consequences of active ownership with ethical aspects taken into account?
- What effects would an increased ethical focus in the work with active ownership in Sweden have?
- What are the hindrances and possibilities for an increased ethical focus in active ownership in Sweden?

Generally, there are few indications that active ownership will become a powerful tool for driving the companies' ethical agenda. In order for this to change, the view of active ownership as solely a strategic tool must change and the activities of the investors must become more operative and proactive in their nature. Further, the Swedish institutions participating in this study, apart from Folksam, do not agree that institutional owners should be more active than they are today.

In Europe, active ownership is generally carried out through dialogue-based intervention. In the US, ethical aspects, or rather active ownership as a whole, is often a matter of confrontational propositions from owners on annual general meetings. The differences in how active ownership unfolds seem to stem largely from legislative differences and cultural differences, as active ownership is relatively homogenous within the studied countries.

Ethical aspects are often seen as operational rather than strategic, and are therefore disqualified from legitimate ownership influence. Shareholder value is of paramount importance, and ethical aspects are of concern only when this directly could affect shareholder value. Active ownership in Sweden concerning ethical aspects seems to be focussed on incidents rather than policy issues, and reactive in its nature rather than proactive.

The limited number of existing studies done on active ownership or on ethical screening of portfolios show little or no effect, positive or negative, on financial performance.

Legislation is not considered an obstacle to a more active ownership in Sweden, with the possible exception of the insider information that the dialogue-based intervention sometimes can lead to.

Sammanfattning

I studien beskrivs och analyseras aktivt ägarskap, med tyngdpunkt på etiska aspekter av begreppet.

Bland andra behandlas följande frågor i studien

- Vad innebär etiska aspekter av ägarskap?
- I vilken utsträckning, och på vilket sätt, beaktas etiska frågeställningar av institutionella investerare?
- Vilka är konsekvenserna av ett aktivt ägarskap där etiska aspekter tas med?
- Vilka effekter skulle ett ökat etiskt fokus i arbetet med ägarstyrning i Sverige innebära?
- Vilka hinder och möjligheter finns för att i högre grad ta med etiska frågor i ägarstyrningen i Sverige?

Det finns få tecken som tyder på att aktivt ägarskap inom den närmaste framtiden kommer att bli en stark drivkraft för de svenska företagens etik. För att det ska kunna ske måste synen på aktivt ägarskap som enbart ett strategiskt verktyg förändras. Investerarna måste också bli mer proaktiva i sina aktiviteter, och engagera sig även i frågor av mer operativ karaktär än vad som är fallet idag.

Synen på vad som är ”etik” i ägarstyrning varierar. Vissa aktörer inkluderar traditionella corporate governance-frågor, som bonussystem och styrelsesammansättning, medan andra gör en åtskillnad mellan dessa och miljö- och sociala frågor.

De svenska institutioner som deltog i studien, med ett undantag, tyckte inte att det finns skäl för svenska institutioner i allmänhet att vara mer aktiva som ägare än vad de är idag.

I Europa bygger ägarstyrningen i allmänhet på en dialog mellan ägare och företag. I USA är den aktiva påverkan från företagets ägare mer konfrontativ, och etiska frågor leder ofta till konflikter på företagets bolagsstämmor. Skillnaderna i hur ägarstyrningen tar sig uttryck mellan olika länder tycks grunda sig i skillnader i lagstiftning och företagskultur. Inom de enskilda länderna är olikheterna relativt små.

Etiska frågor ses av ägare ofta som operativa snarare än strategiska och är därför inte en fråga som tas upp i deras ägarstyrning. Avkastning på investerat kapital är det viktigaste intresset, och etiska frågor beaktas bara då de kan förväntas påverka detta. Ägarstyrningen i etiska frågor tycks i Sverige mer fokuserad på hantering av incidenter än på policyfrågor, och har reaktiv snarare än proaktiv karaktär.

Det begränsade antalet studier som gjorts av effekter av ägarstyrning eller etisk screening visar på liten eller ingen påverkan på avkastningen, vare sig positiv eller negativ.

Lagstiftning betraktas inte som ett hinder för ägarstyrning i Sverige. Möjligen kan dialoger mellan ägare och företag i vissa fall leda till insidersituationer.

Acknowledgements

We would like to thank the interviewed persons who have generously given of their time and experience to the project team. We are also grateful to Folksam and the Swedish Environmental Protection Agency who jointly financed the project and provided valuable input to our work.

Introduction

A popular opinion, often expressed in the business press during the last decade or so, is that there is a lack of powerful, old-style, capitalists with a strong and long term interest and involvement in the companies they own. Huge but anonymous institutions, like pension funds or insurance companies, will never be able to take the same responsibility as owners, it is argued. However, parallel to this rather pessimistic debate, there is an increasing awareness among individual shareholders, as well as institutional investors, of the importance of good corporate governance. During the last 35 years the role of the institutional owner, and the power of the institutions, has been discussed, albeit with shifting intensity and focus.

What role the financial markets have in influencing the actions and strategies of companies has been discussed widely in Sweden for fifteen years or more. Environmental and ethical funds of different kinds have slowly but surely grown in popularity on the market for financial products. During the last few years large institutions like the AP-funds and several life insurance companies have started basic screening of their entire portfolios as well. This has had repercussions in circles far outside the so-called SRI community. However, active ownership and how it is related to ethical issues has so far not received the same attention in Sweden as it has in other countries. Nor has the issue of active ownership been penetrated as thoroughly as, for example, the screening practices of fund managers have been. In this report, we try to describe the background and basic concepts of active ownership, what rationale lies behind active ownership, and we give an insight to what view a few of the major Swedish institutions have on the subject. Finally, we discuss the possibilities for, and hindrances to, active ownership in Sweden.

Objective of the Study

The overall objective of the study is to shed light on the subject of active ownership and the consequences of an increased ethical focus in the work of institutional investors. It is our hope that the study shall constitute an input to the discussion on how the role of an institutional investor may be developed further.

The following questions are treated within this study;

- What do ethical aspects of ownership mean?
- To what extent, and in what way, are ethical aspects taken into account by institutional investors?
- What are the consequences of active ownership with ethical aspects taken into account?
- What effects would an increased ethical focus in the work with active ownership in Sweden have?
- What are the hindrances and possibilities for an increased ethical focus in active ownership in Sweden?

Delimitation

The contents of this report shall be seen as examples of how active ownership may work, what issues are in focus and how the subject can be developed in the future. The study concerns ethical aspects of active ownership, and ethics and its implications have been in focus in as

much as has been possible. However, the literature in the field is by no means complete or exhaustive. Therefore, parallels have been drawn to adjacent areas.

We regard active ownership as one of three fields of activity that form the core of the wider term Socially Responsible Investments (SRI) or Ethical Investments (EI). The other two fields, which are not discussed in detail in this report, are Screening and Community Investment (figure 1). Screening refers to the evaluation of companies or shares for portfolio selection purposes. The theory of screening, different screening methodologies and their consequences have been thoroughly covered in several studies (Carlsson Reich et. al, 2001, Gottsman & Kessler 2000, Williams, 1999, MacKenzie 1998, Pava & Krausz, 1996)

Active Ownership – an Overview

What is Active Ownership?

We define active ownership as: “*activities performed by a shareholder of a company with the purpose of affecting the decision making bodies of, or decisions taken by, the company, using its power as a shareholder, without selling the shares*”.

Unlike conventional screened ethical investments, active ownership, in the sense we mean in this study, implies that the manager uses the ownership stakes to engage companies in dialogue and shareholder activism, rather than excluding such companies from its investments (McLaren, 2002). This contrasts to the use of ethical screens for portfolio selection, where an investor seeks to improve the performance of her investments, or influence the behaviour of companies for other reasons, through the inclusion or exclusion of shares in the portfolio. If a company acts in a way that violates the screening criteria, the shares are sold. This is sometimes referred to as “voting with your feet”. Although we recognise that this may very well be an action which an active owner could take at some point, in this report we focus on what an owner can do while still holding shares in a company.

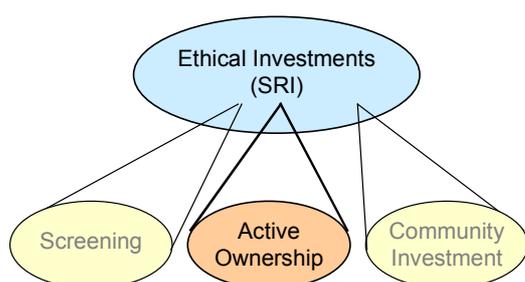


Figure 1. The concept of Socially Responsible Investments/Ethical Investments.

However, it is important to note that in the literature, sometimes little or no distinction is made between screening and active ownership. Rather, screening is considered a tool for an active owner. Several fund managers that we have spoken to during the work with this study also hold this view (see Status in Sweden chapter).

In the literature, and indeed in this report, the terms *shareholder advocacy* and *shareholder activism* are sometimes used to describe phenomena that are closely related or identical to active ownership. If a distinction between the terms could be made at all, it is that *shareholder activism* often refers to activities where the shareholders are in conflict with the management of the company, whereas *active ownership* is a more neutral term.

What is ethics?

It is common to divide ethics into three dimensions: Financial, Environmental and Social Responsibility. In this sense, the term has great similarities to the concepts of Sustainability and Corporate Social Responsibility. This study focuses on the social and environmental dimensions of ethics.

However, it is our view that no absolute set of ‘good values’ is possible, or even desirable, to construct. We recognise the fact that over the last two and a half thousand years, there has been an ongoing debate whether ethical knowledge is at all possible. Some people have the conviction that the term “ethical” has no real meaning. Particularly when classical ethical issues, like moral, what is right and wrong, what is true etc., are discussed, this opinion is common. The argument is based on the judgement that each person has her own set of values, opinions and feelings, and that ethics thus is just a matter of individual opinion. If you embrace this concept of ethics, sometimes labelled “emotivism”, ethical knowledge is impossible and ethical inquiry is pointless (Mackenzie, 1998).

Even so, considering the intense discussions on the subject of business ethics that has taken place in many countries during the last few years, with the scandals surrounding Enron and Worldcom as prime international examples, there is no doubt that ethical issues are a real and true concern for shareholders of today. Without further definition, we will in this report use the word ethical in a very broad sense, roughly based on concepts such as the UN declarations on human and labour rights and sustainability.

Background

Monks (2001), outlines the development of the power of corporations and the role of their owners, from the 16th century until today. He argues that from the dawn of what is often called the first modern corporation, the East India Company in England, until the late twentieth century, the owners of ever-growing global corporations have lost their sense of involvement in the businesses they own. Although the owners of the East India Company, through the corporate form, had limited liability, they were involved. Should the ships that sailed to India have failed to accomplish their stated mission, the owners would have taken decisive action. This active ownership, Monks argues, has slowly but surely decreased over the four centuries that followed the birth of the East India Company. Since the beginning of the 20th century, the trend with more passive owners has accelerated. An important factor in this development is the emergence of the great institutional owners that now hold significant shares of the entire publicly traded companies of the world.

The history of active ownership and shareholder activism as defined in this study, dates back to the early 1970s’ when the phenomenon first occurred in the US. There exist very little literature on the situation in Europe during the 1970s and 1980s’. In the US, public interest resolutions originated in the social activism of the 1960s’ and drew their political and ideological strength

from the drive for increased public controls over the corporation that dominated the political agenda during much of the seventies. Their existence and legitimacy were thus closely linked to the relative decline of public support for business that began in the midsixties and continued for more than a decade. (Vogel, 1983). As is the case today, the most visible kind of activism was that of shareholder resolutions to the annual general meeting. During the mid seventies the US Securities and Exchange Commission (SEC) reformed some of the rules concerning active ownership, making it more difficult for boards of directors to ignore shareholder resolutions.

During the first years, the most common issue to be raised was that of corporate involvement in South Africa. Then followed activism on energy issues, particularly nuclear power, marketing of infant formulas in developing countries and in the early eighties environmental concerns began springing up as well. The ideological centre of gravity of shareholder activism was placed firmly to the left of centre, although the political spectrum began to broaden as early as 1975. Conservative groups then began pressuring boards on issues like the medias' alleged liberal bias and trade with communist countries. In a campaign that received a fair amount of attention in 1979, conservative individuals attempted to stop large corporations like Dow Chemicals and DuPont from giving contributions to universities that employed 'a vowed Communist, Marxist, Leninist or Maoist', or that prohibited members of the academic community from working with the Central Intelligence Agency (Vogel, 1983). One of these resolutions received as much as 15.7 percent of the shares voted, following a management decision to take no position on it.

After a downturn during the 1980s, largely due to changes in the political and economic systems, the interest for shareholder activism soared in 1992 when SEC began requiring data relating a corporation's returns and stock price performance to executive compensation (AIMR, 2003).

Why Focus on Institutional Investors?

There is no doubt that Swedish capital markets have a crucial role to play in enabling enterprise, innovation and growth. The so-called ethical funds, which have received much attention in the public debate, represent less than 6 % of the total fund assets under management in Sweden (Skillius, 2002). Although they can play an important role as symbols and forerunners in the SRI field, they will not be a significant financial power in the foreseeable future. Institutional investors however, which hold a very large part of the total assets under management in Sweden, are clearly key participants in the capital markets, and potentially very powerful ones as well. On a global scale, institutional investors are equally important. Pension funds have rapidly become one of the most important groups of owners in the world. In 1999, retirement funds held, on average, more than 15 % of the shares in 25 of the worlds largest corporations (Monks, 2001).

However, concerns that this strategic asset is not being used to its full potential are increasingly being raised. More often than not, institutional investors are described as being passive in their role as owners, "voting with their feet" rather than trying to actively convince the companies they own to change their strategies or behaviour. During the last few years, scandals like Enron and WorldCom, have put transparency, ethics and corporate governance issues on the front pages of the business papers of the world. In Sweden, lucrative retirement plans and incentive programs for top management of companies like Skandia and ABB, approved by the boards of directors, have left many shareholders wondering if the large institutions are not taking their responsibilities as owners.

Much has been written about the Annual General Meeting of a company, and in particular the non-attendance, or at least inaction, of institutional shareholders. This, it is argued, is a consequence of the fact that most institutional investors' prime responsibility is to achieve high short term investment return to their clients. In the case of pension funds or life insurances, the time horizon may be longer than for example someone investing in standard stock funds. However, considering the volatility of share prices, the returns sought by the fund manager's clients, most managers do not regard holdings to be 'permanent' or even 'very long term'. Instead, a relatively high proportion of the portfolio may have a quick turnover, a fact that does not encourage the owner to be actively involved in the company's business strategy.

Despite all this, the official policy of most of the large Swedish institutional investors is to be an active owner. Thus the question arises; why is that, and how will it be carried out in practice?

What are the Purposes of Active Ownership?

The motives behind shareholder activism during the 1970s' and 1980s' are in the literature described as being, for the most part, ideological or political. During the 1990s', however, there was a shift towards a more traditional financial approach towards active ownership and corporate governance. More and more frequently, active ownership was put forward as a way to increase the financial return for shareholders. This trend is analogue to the development of SRI and Corporate Social Responsibility in general. There are two radically different categories of objectives for SRI: Saving the World and Profit Maximising (Carlsson Reich et al, 2001).

With a Saving the World objective, the aim is to, directly or indirectly, change the way companies do business, with the overall goal to change our world to become a better place.

The Profit Maximising objective reflects the belief that the share of a company with a high ethical performance will do better on the share market than the shares of a company with a lower ethical performance. Someone with the Profit Maximising objective may or may not have a desire to save the world, but in this work we do not consider it to be the driving force behind the behaviour of the investor.

The public debate on SRI in Sweden, particularly regarding screening and portfolio selection, has mostly been held in the context of "saving the world". This debate has been strongly oriented towards the private investor segment, and the deregulation process in the Swedish pension system has especially encouraged financial institutions to heavily market their "ethical funds". Institutional investments and active ownership were, until only a few years ago, very seldom discussed at the same time as screening of funds, nor by the same people who talked about these funds. Instead, the more traditional business community has driven the debate on active ownership, introducing ethical aspects for solely financial reasons. Often used examples of such issues are staff incentive programs and board independence. Parallel to this, there has been a growing awareness in the Swedish SRI community and among Swedish NGOs, that the power of the institutional owners has been largely untapped so far. The increasing success of proxy voting campaigns in the US, and especially the activities in this field by large pension funds like CalPERS, are used as examples of how shareholder activism can be executed. Furthermore, since the development of SRI as a whole, in the US, has been a few years ahead of Europe, it does not seem unlikely that a similar increase in shareholder activism that has taken place in the US would occur in Sweden as well.

How does Active Ownership Work?

Active ownership can mean many different things. Depending on whom one asks, the opinions regarding how active ownership could and should be performed may vary. In this study, we differentiate between *voting* and *intervention*. Voting is executed at a company's annual general meeting, whereas intervention can be performed at any time. Owners are often represented by fund managers, and in this chapter we use these terms interchangeably.

Public companies have extensive obligations to provide information to share information with its shareholders, the owners of the company. The corporation must also provide information on all issues that may have an effect on its shareholder value to all stakeholders, including the financial markets, as well. One of the most central duties of a company is the annual general meeting (AGM). In fact, all public companies must, by law, hold an annual general meeting to which they invite all those who own shares in the company. At the AGM, companies usually ask shareholders to vote on several standard items that are always included in the agenda. Such an issue, which nearly always appear, is the ratification of the company's auditor. Another very important item is the election of the company's board of directors.

Other, less routine matters that may require the shareholders' votes are mergers and acquisitions and individual or shareholder group actions that qualify for the agenda of the AGM. This last category of items are the most interesting in the context of this study, since ethical issues connected to the company's activities often fall into that category. Matters that are brought before the AGM for voting are called resolutions. However, the vast majority of resolutions put to the shareholders do not typically relate directly to a company's current or future performance (notwithstanding the all-encompassing nature of resolutions to 'approve the Report and Accounts'). Instead, most items on the agenda of an AGM concern the governance of the company. Elections of non-executive directors are important, and the terms of share-option schemes have significant potential influence on management behaviour (UK Actuarial Profession, 2002). However, neither specifically addresses issues of strategy or operational management. Therefore, in order to be able to use voting at AGM's as a tool to influence corporate strategies and behaviour in operational issues, the likes of which ethical matters often are, a shareholder will often need to actively fight for the inclusion of such items in the agenda of the AGM.

Another problem related to active ownership and shareholder value, especially when ethical aspects are concerned, is related to public relations. Some investors may be worried that if they put pressure on a company in public regarding a routine or strategy that they believe is detrimental for the company's performance, it may create a public confrontation that itself may have serious adverse consequences for the business.

Intervention, as opposed to voting, can be performed by an investor at any time, not just in connection with the AGM. Intervention can be almost anything that can be described as an attempt to get information from, or exert influence on, the company by one of its owner(s). Often, large owners have regular meetings with the company's board of directors. At such meetings, owners can engage in dialogue with the company over matters more closely connected to its operations and strategies. Many institutional investors state that intervention is a more effective and constructive way to act as an active owner. However, there are important limitations to what can be discussed at closed meetings between owners and a company. One of the most important is the insider dealing rules. These rules state that companies cannot share price-sensitive information with any one stakeholder before the entire market has access to the same information. Since meaningful intervention is very likely to involve, or even create,

information of such type, the insider rules may well put a constraint on intervention as a tool for owners.

Moreover, companies may very well be reluctant to reveal commercially sensitive information to a fund manager since he or she may have relations to the company's competitors. Further, it is of little interest for a fund manager to improve the performance of one company in the portfolio, if it is achieved at the expense of another company in the portfolio.

In general, financial institutions and fund managers have a greater influence over corporate behaviour and management in times of corporate crisis and need. In such times, institutions may use their power to negotiate changes in management and management succession. However, voting and intervention may differ somewhat in this respect. Since intervention in ethical issues is often aimed at avoiding crisis, for example emanating from bad strategies or reputational loss, it can take place in more 'ordinary' times than other forms of engagement. As a consequence, dialogue in ethical issues relies on high levels of trust between fund managers and corporate managers - rather than the threat of replacement (McLaren 2002).

Those who oppose intervention, or the whole concept of active ownership, argue that an owner, who in this context is often represented by a fund manager, has his expertise in portfolio selection, risk management and the relative valuations of different shares. That field of knowledge may not be particularly well suited for dealing with more hands-on business strategies and management of operational issues that demands business specific competence.

International Overview

Shareholder activism has long been on the agenda in the US, and also in the UK. Therefore, a description of the situation in these countries is important in order to see whether there are any structural differences between these countries and the Swedish case.

The US

In the US, the interest for shareholder activism soared in 1992 when the US Securities and Exchange Commission (SEC) began requiring data relating a corporation's returns and stock price performance to executive compensation. (AIMR, 2003)

Ever since the start of shareholder activism, an important, if not the most important, objective for many shareholders has been to strengthen the independence of the board of directors and make it more accountable to shareholders. This is, and has been, an important issue for SEC as well. Board independence definitely receives more attention in the US than in Sweden. This is not particularly surprising, considering that the board of directors in US companies often than has the company's CEO as its chairman. It is also common for other senior management, current or former, to be members of the board. This is very seldom the case in Sweden, and when it occurs it immediately draws criticism.

At least at first glance, shareholder activism in the US seems much more radical than it is in Sweden. Open conflicts between management of the company and shareholders are more common. An important characteristic of shareholder activism in the US is the kind of issues raised and voted on at the annual general meeting. Although a company can refuse to include an issue on the agenda of the AGM if it concerns 'ordinary business activities, SEC, who is the

regulating body of the AGM, has ever since the mid-1970s' frequently ruled against companies' efforts to exclude resolutions made by shareholders.

Each year, publicly held corporation must issue a proxy statement, calling upon their shareholders to vote on a variety of matters ranging from the approval of the Board of Directors, to executive compensation. In addition to the right to vote on these matters, shareholders also have the right to place their own proposals, or resolutions as they are also called, on the ballot, to be voted on by all shareholders at the company's annual general meeting. Every shareholder holding at least \$ 2000 worth of stock for at least a year, has the right to file a resolution. If the company does not get the approval from the SEC to exclude it, it must then be included in the agenda of the AGM as an item on the proxy ballot.

Typically between 200 and 300 social and environmental resolutions are filed every year (Socialfunds, 2003). Some never make it to a vote, either because they are withdrawn by the shareholder or successfully challenged at the SEC by the company. Withdrawals usually take place as a result of progress in dialogue with the company, if the shareholder no longer feels it is necessary for the AGM to vote on the resolution. Thus, a withdrawal can be a success for the shareholder, if it represents a positive settlement of an issue or at least an understanding between the company management and the shareholders.

Environmental or social resolutions rarely receive more than a few percent of the votes. Still, the proxy voting systems is considered to be a powerful tool to put pressure on management. The resolution must receive 3 percent of the votes the first year in order to be allowed to be resubmitted the following year, 6 percent the second year and 10 percent every year after that. Resolutions that receive enough support to come back year after year are a message to management that the issue will not go away easily.

It is common for shareholder activists to organise themselves under different umbrella organisations. Some of these, e.g the Shareholder Action Network and the Interfaith Center on Corporate Responsibility (ICCR), are permanent organisations specialising in proxy voting campaigns and other shareholder services. Other groups are organised around specific issues or companies. There are several public databases of shareholder resolutions accessible on the Internet, providing information to investors as well as facilitating the communication with the company on the issue of the resolution. One of the most extensive databases is provided SRI WorldGroup in collaboration with the IRRC (Domini, 2003).

The regulations for the AGM, and the rules regarding what issues are beyond the scope of shareholder control, stipulates that the AGM should not discuss or decide in issues related to day-to-day activities of the company. However, in the US the issues included in the proxy statement (the official document stating what will be voted on at the AGM) have a much more operative character than what is usually the case in Sweden. Over the last 30 years, issues like in what markets a company should be active, policies on overseas manufacturing, resource use, environmental risk management and product safety have frequently occurred in the proxy statements of US firms. The shareholder initiatives cover many of the same topics social investors look for in screening their portfolios.

Shareholder Activism - Examples from the US

The shareholder activism in the US often consists of shareholder proposals at the AGM's. Often, it is difficult to directly assess whether the shareholder proposals are a driving force when companies change their policies or actions, as the companies rarely give credit to

shareholder proposals, and as the proposals rarely or never obtain enough mandate to carry through changes directly. Typically, a shareholder proposal may reach as much as 10 or even 15% of the votes, which is enough to keep the question on the agenda. When changes take place the company usually states business reasons rather than a long-running shareholder proposal as the driving force (Mathiasen, IRRC).

The example most frequently used as a success story for shareholder activism is the case of South Africa during the five years before Mandela was released from prison in 1990, during which the demand for a boycott of South Africa was rising. During this period, the amount of shareholder proposals, and the support for them, rose sharply. In the 1985 proxy season, shareholders proposed 38 resolutions on the South Africa issue. Eighteen of those were withdrawn when companies complied. The number of South Africa-related proposals that came to votes in 1986 increased to 61—more than half of the social policy resolutions considered by shareholders. In 1987, altogether, 156 South Africa resolutions were filed for the spring proxy season, more than the number of social policy resolutions on all issues that had come to votes the previous year. Of those, proponents withdrew 45 that asked for disinvestment as companies agreed to leave South Africa. Sixty-three other proposals on withdrawal came to votes, picking up an average of 12.2 percent support. Although there are other reasons, the shareholder activism on this issue could well be a contributing factor for US companies to leave South Africa (Mathiasen, IRRC).

The situation with shareholder resolutions on tobacco issues has been different; institutional investors that were comfortable asking a company to get out of South Africa have been much less willing to ask companies to take action that would clearly hurt their core business, and votes have been on the low side. Success stories include in 1991, for example, church shareholders tackled the question of tobacco ads on billboards and were able to withdraw a resolution to 3M when the company said it would stop all such advertising. In 1992, church shareholders withdrew a resolution asking Philip Morris to place warning labels on cigarette packages in countries that did not require them. The company agreed to follow suit, fulfilling the request of a second-year resolution that had got 6.7 percent support the year before. The sponsors hailed the action as a major victory, but the company, in a policy statement, said merely that it had decided to take the action because “the relatively small number of packages involved has become an issue out of proportion to its importance.” (Mathiasen, IRRC)

In 1989, longtime shareholder activists such as the Interfaith Center on Corporate Responsibility and the controllers of the New York City and the California public employees’ retirement systems (CalPERS) joined forces with environmental groups and socially responsible investment advisers to form CERES, the Coalition for Environmentally Responsible Economies. The CERES principles emphasise the need for standardised annual reports to stakeholders on corporations’ treatment of the environment. CERES representatives entered into a dialogue with scores of companies shortly after the announcement of the principles, and filed their first shareholder proposals in 1990. While only five of nearly two dozen resolutions proposed that year came to votes, support levels averaged 12.5 percent, the highest of any first-year shareholder initiative in the 20-year history of proxy voting on social issues. (Mathiasen, IRRC)

As a more recent example, a coalition of institutional investors has filed a global warming shareholder resolution at the five largest carbon dioxide emitters in the US electric power industry, called the “filthy five”. The Connecticut Retirement Plans and Trust Funds (CRPTF) led the initiative, with co-ordinating support from the Coalition for Environmentally Responsible Economies (CERES) and the Interfaith Center on Corporate Responsibility

(ICCR). The resolution asks the companies to report on the business risk of their greenhouse gas emissions and on the potential economic benefit of curtailing those emissions. The motif for the action is, according to the State of Connecticut Treasurer, that “investors need the full picture to assess companies’ long-term investment value: air pollutant emissions are some of the most measurable, relevant, and significant indicators of risk for this particular industry, and it’s our responsibility to ask what the companies’ plans are to address that risk”. (Baue, Socialfunds a)

Another example is ExxonMobil, which this year receives 23 shareholder resolutions on issues ranging from climate change to corporate governance. It is the refusal of the company to address climate change and renewable energy whatsoever that makes investors wonder whether the lack of climate change and alternative energy strategies is in the best long-term interest of ExxonMobil, as they thereby ignore a major risk. (Baue, Socialfunds b)

Water supply is a growing concern, and is going to be one of the most important environmental and social issues of the 21st century. Therefore, investors in PepsiCo, a company that uses large amounts of water, have filed a resolution asking the company to disclose its “current policies and procedures for mitigating the impact of operations on local communities in areas of water scarcity”. (Baue, Socialfunds c)

The UK

The prospects for shareholder activism in the UK are favourable, compared to the US. Legislation gives much more room for co-operative intervention rather than forcing institutional investors to use confrontational voting. Further, ownership is more concentrated in the UK – among the twenty largest institutional investors, no more than ten usually own over fifty percent of the stock of most traded companies. (Monks, 2001)

One reason for this climate (although the history of the differences probably is much longer) could be the Myners’ Review of Institutional Investment in the UK, which was commissioned by the Chancellor of the Exchequer in the 2000 Budget, to investigate whether there were factors distorting institutional investment in the UK, resulting in inefficiency and inflexibility in capital markets. The review found that, although institutional investors are engaging with companies in which they invest, there was currently a lack of active intervention in such companies even when there were a reasonable expectation that this would enhance the value of investments. Specifically, the report found that fund managers argued that there was no need for them to engage in such intervention, either because it was no part of their role or because there was no need for them to adopt such a strategy. The review gained a lot of attention and has had an important role in the development of shareholder activism in the UK.

This situation has led to a shareholder activism that differs substantially from the US case. The most important actors are managers of pension funds who, with a substantial long-term index tracking holding, have a good base for long-term involvement.

Hermes

Hermes is one of the largest fund managers in Britain. As at 31 December 2002 Hermes had approximately £37 billion under management and managed assets of four of the seven largest UK pension funds. Hermes’ official view on corporate governance is that “responsible pension fund investment requires investors to behave like owners rather than gamblers”. This, according

to Hermes, is particularly important when funds are managed on a passive or index-tracking basis, as is the case with the majority of funds managed by Hermes.

Hermes has over 40 people working with stewardship and corporate governance: a mixture of analysts/managers, fund managers, engagement specialists and investor liaison people. Hermes submits votes on behalf of its clients at some 1200 annual and extraordinary meetings a year. However, Hermes differentiates its programmes from those of the “raider activist” by adopting a relational approach on behalf of all shareholders and is particularly critical of activist programmes involving greenmail or micro-management of companies. Hermes’ programmes have generally been conducted in private and have not therefore been widely published.

In addition to its stated in-house commitment to corporate governance, Hermes participates in a number of fora dedicated to the topic. These have proven to be a source of potential allies when action is needed in relation to an individual company. In one of these fora, the Corporate Governance Forum (CGF), best practices on social, ethical and environmental matters and executive pay have recently been developed. Hermes also has international contact with e.g. CalPERS, where they generally vote in accordance with CalPERS governance policy in the US, and CalPERS votes in accordance with the Hermes policy in the UK. Hermes also has close co-operation with pension funds in Scandinavia.

One of Hermes’ investment principles is that a company should be able to demonstrate its competitive advantage, both at corporate and at business unit level, and that it in so doing it should demonstrate ethical behaviour. They have 10 investment principles, two of which are social, ethical and environmental in nature:

- Companies should manage effectively relationships with their employees, suppliers and customers and with others who have a legitimate interest in the company’s activities. Companies should behave ethically and have regard for the environment and society as a whole.
- Companies should support voluntary and statutory measures that minimise the externalisation of costs to the detriment of society at large.

Hermes states that it is not their role to act as moral philosophers, still less to micromanage companies’ responses to ethical issues, any more than they would wish to micromanage their commercial operations.

Thus, Hermes is an active owner, and its role as a passive fund manager allows a long-term involvement. They do have explicit investment principles concerning social, ethical and environmental principles. This stems from the fact that their ultimate beneficiaries includes the greater part of the adult population who depend on private pensions and life insurances, and therefore an externalisation of costs from managed companies would still end up being paid by the fund beneficiaries. Therefore, even the social, ethical and environmental policies stem from a will to maximise long-term shareholder value, not only through stock prices but through minimising external effects as well.

(Hermes, 2003)

Morley

Morley holdings amount to some 2.7% of all UK quoted companies, as well as significant holdings in companies operating in Europe, the US and Asia. Morley say that they incorporate

environmental, social and ethical issues into their investment decision process in order to protect and maximise returns for their clients,. As an example of their impact, over 40 FTSE companies have responded to Morley’s voting policy with a commitment to begin environmental reporting.

Morley is active not only in board election and shareholder proposals, but have a wider engagement also on specific issues:

- Morley has, together with several other institutional investors, signed up to the Carbon Disclosure Project. This project aims to collect data on the climate change strategies of the Fortune 500. This initiative makes possible a powerful joint action by large investors to raise the climate change issue to the boards of the Fortune 500. This engagement is extended by Morley to individual meetings with high climate change impact companies, such as ExxonMobil.
- Morley believes it is necessary for companies to understand what sustainability means to their organisation and to their sector. Therefore, Morley has developed “Sustainability Blueprints” for key industry sectors. The Blueprints outline the key sustainability issues facing the sector, both in terms of risks and opportunities.
- In 2001 Morley joined forces with a number of financial institutions to launch “Business involvement in Myanmar (Burma) – a statement from institutional investors”. The group suggests that companies operating in unstable political climates can be exposed to negative press and publicity campaigns, safety risks, and corruption.
- Morley claims that its involvement in the Balford Beatty involvement in Ilisu dam in Turkey featured significantly in the company decision process to withdraw.
- Another joint project, the International Cocoa Initiative, where Morley participated, contributed to a hopeful resolution to tackle enforced labour in the production of chocolate.

(Morley, 2003)

Henderson

Henderson Global Investors is a large provider of socially responsible investment (SRI). Part of Australian financial services group, AMP, Henderson has been managing funds with social, environmental or ethical perspective since 1977. Henderson now has over £1.2 billion of SRI assets under management in 17 different funds for a range of individual investors, local authorities, companies and charities.

For Henderson, SRI research and engagement activities operate on a spectrum stretching from desk-based analysis through to research meetings with company management and active intervention in companies with inadequate corporate responsibility performance. Henderson state that the use an active dialogue with both company management and key stakeholders to influence company policies and performance.

Conclusive Comments on the UK

Both Morley and Henderson use examples of a very active engagement in specific issues that may be judged as micro-management or operational issues (although of ethical character). Examples are the Ilisu Dam in Turkey, and labour conditions in chocolate manufacturing. These companies also engage in the production of, and signed up to, institutional investor collaboration statements on e.g. climate change and global health, and have shown proactive

engagement in ethical issues. However, this study has not allowed us to penetrate all information on the UK market and its players, so the reader should be aware that the picture is not complete and all aspects have not been covered.

Rest of Europe

For the rest of Europe, there does not seem to be either any shareholder activism of note or at least no literature describing this activism. One source claims that as large blocks of shares are held by families or single institutions which have exercised their ownership responsibilities and been treated by boards in a way which was more in their particular interests than of all the shareholders, there has been no “open” shareholder activism. So far, relational shareholder activism seems less straightforward in e.g. France and Germany than in the UK, where the rules for e.g. board selection gives more room for such measures. (Watson, 2002)

Status in Sweden – five cases

About the Case Studies

Five institutional investors were interviewed: AMF, Folksam, Nordea, Robur and SEB. They all have their head offices in Stockholm. The institutions differ significantly in size and character. AMF has recently changed from being a pension fund with clients that had no choice of fund manager, to becoming a fund manager who is subject to competition on the open market. Nordea, Robur and SEB are all banks with a large number of bank offices spread across Sweden, whereas Folksam is an insurance company with very few offices outside Stockholm.

Even though the institutions represent different types of management and have slightly different client categories, we do not claim to have captured a statistically representative sample of the Swedish institutions, nor was that the aim. The interviews should be taken for what they are; five important voices and examples from the Swedish financial community, but not interpreted as more than that.

No single definition of ethics or ethical issues was imposed on the interviewed persons. Instead they were left to interpret the term as they wished. However, all institutions in the study mentioned environmental and social issues as part of the ethical scope of their organisations, as well as more traditional business ethics like accounting practices, corruption and compensation programmes.

The interviews lasted for 1-1,5 hours. All institutions received the same questions, sent to them in advance to allow for preparations and thought. However, during each interview discussions arose that sometimes led to other questions being raised. Different amounts of time were devoted to each question depending on how the interview proceeded.

Apart from the interviews, we have also collected information from official documents provided to us by the institutions. This material includes ownership policies, marketing material and web pages.

AMF

Facts about the Company

Company: AMF

Principal client categories: Individuals in private sector employment

Assets under management: 180 BSEK

Share of holdings actively managed: 100 %

Internal management or management under direct control: 100 %

Estimated number of holdings: 150 companies

Estimated annual turnover in portfolio: not available

Direct investments: Marginal

Date of Interview: 2003-04-03

Company representative: Tor Marthin

Position: Vice Managing Director, Chief Financial Officer

General on Active Ownership

It is AMF's policy to be an active owner in its Swedish holdings. The sole formal reason for this is to increase shareholder value, but Mr Marthin adds that "common sense" and "general decency" in reality also act as guidelines in all of AMF's activities. This, according to Mr Marthin, is particularly important in ethical issues. Furthermore, AMF's ownership policy states that "AMF should act in a manner that creates trust with the public and business".

Mr Marthin points out that it is important to distinguish between the different roles that exist in the relationship owner-company, and what mandate each actor has. AMF believes that by far the most important responsibility of an owner is to elect the board of directors and to hold them accountable for the finances and accounts of the firm. The board of directors, for their part, should concentrate on the long-term management of the company and they also appoint the CEO. Furthermore, the board decides in matters not addressed in the day-to-day management of the firm, but leaves all the daily operations to the CEO to manage. Many ethical issues, as they are defined in this project, according to Mr Marthin, falls under the responsibility of the CEO. Thus they should not, under normal circumstances, be discussed by the board, and consequently not by the owners either.

Activities of Institutional Investors. Mr Marthin believes institutional investors do a lot that never comes to the attention of the public. This is one of the reasons why media often gives the (incorrect) description of institutions as being passive and irresponsible owners. Mr Marthin carries no view on whether institutions in general would benefit from being more active than they are today. The most important work of AMF in their role as an owner is carried out in advance of the AGM. AMF has no written guidelines on how to vote in certain types of issues, and Mr Marthin does not believe that such guidelines would serve any purpose.

Company response. According to Mr Marthin, companies are generally very attentive and eager to hear the views of the owners. Whether this leads to a different behaviour is more uncertain, however.

Legislation. Mr Marthin does not believe that Sweden and the Swedish financial markets would benefit from a legislation more similar to the one found in the US. He points out, however, that it is his impression that much of the debate on active ownership in connection with ethics originates from the US, and that the legislation may contribute to that fact.

Practical Work with Active Ownership

The policy of AMF is to engage in direct contact with the companies, rather than using the option of selling the shares or use its voting power.

To AMF, “Active ownership” means three things:

1. Influencing the decision making bodies of a company
2. Screening and analysis of holdings and potential holdings
3. Entrepreneurship, where the owner actively engages in the activities of the company.

AMF actively pursues the first and second items on this list, but has no intention to become an entrepreneur. This is also reflected in the portfolio composition. AMF has only marginal direct investment, and deliberately avoids becoming a major owner in any company, since such a position would force them into longer commitments and more direct involvement in the daily operations of the company. At present, AMF does not hold more than 5-6 % of the votes in any company.

Ethical Aspects in Active Ownership and Consequences of Active Ownership

It is rare that AMF takes environmental or social issues into account in their role as an owner, and AMF has no publicly available policy on ethical issues in general. There is, however, an internal document describing how ethical issues should be addressed by AMF staff, including fund managers and analysts.

Even though it is uncommon that AMF takes action in ethical issues, as an owner, Mr Marthin mentions three factors that can trigger such actions:

1. Staff reactions.
2. Media, for example covering an incident related to a company in the portfolio.
3. Financial analysis of individual companies.

At present staff reactions and incidents reported in the media are the most important of these factors. In this sense the actions taken by AMF are often reactive rather than pro-active. Mr Marthin cannot recall any case where ethical aspects have been considered as having such a significant impact on the financial performance of a company in the portfolio so the analyst has recommended AMF to take action in their role as an owner.

AMF has developed routines for how to handle incidents related to their holdings. The most important is to get an independent view on what has actually happened. In many cases things are not as simple as they seem, so AMF always seeks to get information from several media sources, researchers or companies. The next step is to take direct contact with the company in question and hear their version of the story. In most cases this leads to a fruitful discussion on how the issue can be resolved.

Folksam

Facts about the Company

Company: Folksam Asset Management, a division of Folksam Mutual General Insurance

Main client categories: Major popular movements and members of these.

Assets under management: 105 BSEK (August 2003)

Share of holdings actively managed: 100 %

Internal management or management under direct control: 100 %

Estimated number of holdings: 1500

Estimated annual turnover in portfolio: not available

Direct investments: Marginal

Date of Interview: 2003-02-20

Company representative: Håkan Johansson

Position: Manager Folksam Asset Management

General on Active Ownership

It is Folksam's view that practising active ownership is both a right and a responsibility of a shareholder. The main objective of Folksam's activities is always to increase the return on investments. However, Folksam also hopes that the company's commitment will have a positive influence on society at large. And if, which is the conviction of Mr Johansson, investing in companies which take a broader range of stakeholders into consideration in their business will provide a better long term return on investments, these two objectives are not contradictory. Further, Mr Johansson believes that the importance of active ownership is increasing in the financial markets, both as a tool for investors and as a competitive advantage.

Activities of Institutional Investors. Folksam has previously, as many other institutional investors, been relatively passive as an owner. Issues that called for action were related to board composition, mergers and acquisitions and, in more recent years, executive compensation. However, over the last few years, the company has gradually changed its policy, and is making increasing efforts to pursue the role of an active owner. It is the view of Folksam that there is a trend of institutions in Sweden becoming more active. However, in general Swedish institutions are still too passive as owners. This is true for traditional corporate governance matters, but even more so for issues related to environmental and social aspects of business. An important reason is the short-term investment horizon of most institutions. However, even investment companies which in some cases have holding dating back to the founding of the company, show a surprising lack of interest in acting in ethical issues, according to Mr Johansson. Furthermore, practising active ownership is resource consuming and demands different skills and competence than a more passive owner needs.

Company Response. In general, Mr Johansson has the impression companies welcome owners that take an interest and express an opinion on issues important to them. Swedish companies are also well aware of many of the potential ethical problems associated with their operations, and welcome a discussion about them. It remains to be seen, however, how companies react if institutions attempt to significantly increase their influence over the companies in which they hold shares.

Legislation. Mr Johansson does not see that legislation constrains Folksam's possibility to act as an owner. However, there can be situations where an owner engaging in direct dialogue becomes an insider. This is one of the reasons why transparency is crucial, both from companies and owners. Mr Johansson recognises that this can create problems for analysts, whose whole job is to seek out information and act on it before the rest of the market.

Practical Work with Active Ownership

Folksam adopted a new ownership policy in January 2003. It is the intention that the ownership policy should be revised once a year, and the company is currently developing new routines for implementation of the policy.

Folksam states in its ownership policy to "actively influence companies through investments where it is considered to be feasible and successful". The OECD-guidelines on corporate governance apply to all of Folksam's holdings, both Swedish and foreign. Furthermore, more detailed guidelines are applied to Swedish holdings i.e. companies that are traded the Stockholm Stock Exchange. Folksam's intention is to practice its role as an owner at annual general meetings, through direct contacts with corporate management and boards, through participating in nominating committees and through co-operation with other owners. So far, the policy only covers holdings traded on the Stockholm Stock Exchange.

Due to shortage of resources, Folksam cannot attend all annual general meetings of the companies in which they are owners, nor can Folksam be active in all those companies. Consequently, Folksam seeks to act in issues they consider particularly important, and where the potential for success is believed to be the greatest. The experience of Folksam is that the annual general meeting is not the most effective way to influence a company. In fact, Folksam has never participated in rejecting a proposal from a sitting board of directors. Instead, engaging in direct dialogue with the company has proven to give better results, regardless if the issue at hand is very controversial or if Folksam merely seeks information from the management or board of directors of a company. The confrontational approach taken by many shareholder groups, particularly in the US, would not be effective in Sweden. Transparency and trust must form the foundation in the interaction between owners and companies.

Folksam only occasionally co-operates in ethical issues with other Swedish institutions. It is Mr Johansson's view that that institutions should express opinions on issues of principal and strategic character to a greater extent than what is the case today. Today institutions often only act on very specific incidents, and in a reactive manner. Folksam continually seeks possibilities to co-operate with international institutions, both through networks and by one-to-one partnerships. So far, however, this has not led to any co-actions in specific ownership issues.

Ethical Aspects in Active Ownership and Consequences of Active Ownership

The vision of Folksam is "to offer a broad majority of people a better and more secure life". In accordance with this vision and as a large stockholder the company views it as a natural action to be engaged in active ownership, including having opinions and acting in ethical issues. As mentioned earlier, Folksam also carries the conviction that companies that are ethically sound and has a broad stakeholder perspective will give better return on investment.

According to Mr Johansson, it is essential to counteract a situation where ownership diverges too much from the management of companies. This is particularly true in ethical issues. Mr Johansson considers an integration of Folksam's activities as an owner, e.g. at annual general meetings, and the day-to-day portfolio management is essential. This is due to the fact that many ethical issues never reaches the annual general meeting or even the top management of the companies. It is the analysts who study individual companies who are most often in contact with the companies. Consequently, the single most important task in Folksam's current work in developing its ownership practices is to make the individual portfolio managers and analysts aware of the ownership policy's full extent and meaning, including the ethical aspects. Furthermore, Folksam uses ethical screening for all portfolio selection, and ideally this should form an integral part of the work with ownership as well.

Nordea funds

Facts about the Company

Date: 2003-04-16

Company: Nordea Investment Funds Sweden

Name: Thomas Ehlin

Position: Senior Vice President, Corporate Governance

Main client categories: Retail and some institutional

Assets under management: Approximately 30 billion SEK (invested in Swedish equities)

Share of holdings actively managed: 100 %

Internal management or management under direct control: 100 %

Estimated number of holdings: Approximately 100

Estimated annual turnover in portfolio: Not available

Direct investments: Insignificant

All facts and views in the text refer to the activities of Nordea investment fund companies with domicile in Sweden or Luxembourg, managed by Nordea Investment Management. However, for the sake of readability, we also use "Nordea funds" in the text, but the reader should be aware that this does not mean the entire Nordea group.

Nordea Investment Funds Sweden has some 30 BSEK in management, all of which are actively managed according to the guidelines below. The ownership activities are carried out in close co-operation with the asset managers.

The time perspective on possessions is long term, defined as more than three years. The time perspective does not affect the view on active ownership.

Nordea Investment Funds has recently started ethical screening, performed by an external consultant. This is done for a limited number of funds, aimed primarily at the institutional market.

General on Active Ownership

Nordea funds take an active role as an owner in order to maximise shareholder value. Presently, Nordea does not have any asset management, and does not manage any fund, with any other goal than maximising shareholder value.

Nordea funds' definition of shareholder issues are those that are subject to decision at the AGM (or EGM). Nordea funds' representatives do not directly sit on company boards. Nordea manages open investment funds, and must thus be able to adjust its holdings on short notice. Therefore, it cannot form a long-term physical presence in a company.

Activities of Institutional owners. Mr Ehlin considers institutional investors in Sweden very active: those who criticise institutions for being too passive disregard the type of ownership, i.e. no direct board involvement, which limits the commitment to the type of issues described above. Mr Ehlin considers Swedish institutional investors as more active than their counterparts in for example UK and USA, with regards to their role in nomination committees. It is difficult to say whether Swedish institutional investors should be even more active or not when viewed from the inside: how much can be done is a question of resources rather than intention.

Company Response. Swedish companies generally welcome active ownership. Nordea funds' view is that its opinions and actions should not come as a surprise for the companies, which is one of the reasons why the active ownership policy exists.

Legislation. The protection for minority shareholders is well developed in Sweden, which gives good opportunities for institutional investors to act as active owners. For example, all shareholders, regardless of size, can raise issues for inclusion on the agenda of the AGM.

Practical work with Active Ownership

Nordea funds have a written policy on active ownership. This document will soon be subject to revision, but only in detail: those involved find it a well-functioning active document, and the policy as such will not be changed, apart from an addition on auditing policy. Today, Nordea funds take an active role as an owner where they have a "substantial ownership" of a company. This happens for example when either:

1. Nordea is one of the major owners of a company (normally among top 10 owners)
2. Nordea's investment in the company is substantial

Sometimes this leads to engagement in relatively small companies, where the shareholder value for the total asset management is limited.

The priority issues for Nordea funds are:

- board election
- capital structure (new issue of shares, repurchase of shares)
- incentive structures for employees
- structural questions (company purchases, mergers)

Board election is considered as the most important ownership tool. Also, Swedish legislation concerning incentive programs demands 90% majority for many decisions, which puts minority holders in an important position (i.e. with a holding of 10% you can practically have the

decisive voting power), which gives this question an important status for institutional investors in Sweden.

Nordea funds act as an active owner almost exclusively in Swedish companies, plus in a limited number of non-Swedish companies.

Nordea funds do work actively at AGMs, and in the policy on ownership they have publicly available guidelines (although relatively broad) on how they will act on different issues. Nordea participates on some 50-70 AGMs per annum, and in some 15 board nomination committees. The nomination committees are seen as one of the most important tools of shareholder influence.

Nordea funds are also in direct contact with the company through the board of directors, or occasionally with the CEO through asset managers. Mr Ehlin considers that Nordea funds have little involvement in the operation of the companies, neither directly nor indirectly, as this is not the role of the owner.

Mr Ehlin considers that Nordea funds manage to do what they sets out to do in terms of active ownership, and that the company has enough knowledge to do it. Nordea funds often work in concord with other institutional investors, even though no formal working groups exist. Most often the active ownership policies of the institutional investors are close enough to allow co-operation: as an example, eight institutional investors jointly developed the guidelines concerning information to shareholders about incentive programs in stock market companies.

Ethical aspects in Active Ownership and Consequences of Active Ownership

Nordea funds include environmental, and thereby also ethical, aspects in their active ownership process in order to analyse a company's long-term performance. This is done in order to maximise shareholder value. In reality, Nordea funds have never had to act on any of these issues, positively or negatively.

As for the actual effect of active ownership on shareholder value it is very difficult to prove any connection. It is rather a conviction that it must have a positive impact. There are examples of individual transactions that have led to a better shareholder value, but a quantitative analysis of the entire area has not been done.

Nordea funds do not have any specific ethical or environmental issue they consider more important than any other issue.

Robur

Facts about the Company

Company: Robur

Principal client categories: Retail (majority) and institutional.

Assets under management: Approximately 230 billion SEK.

Share of holdings actively managed: 100 %.

Internal management or management under direct control: 100 %.

Estimated number of holdings: Close to 150 companies in Sweden + a very large number of companies outside of Sweden.

Estimated annual turnover in portfolio: Not available.

Direct investments: 0 %.

Date of Interview: 2003-02-18

Company representatives: Marianne Nilsson

Position: Deputy Head of Equities

General on Active Ownership

It is Robur's policy to be an active owner, with the principal objective to increase shareholder value and return on investments. Furthermore, Robur is convinced that, as one of the largest institutional investors in Scandinavia, they have the duty and responsibility to act as an active owner.

According to Ms Nilsson, shareholder activism has gained more attention among institutional investors as the positive effects of good corporate governance on returns have become known. The complexity of corporations and the financial market of today also call for a counterpart in the form of an active owner.

Activities of Institutional Investors. An open dialogue between management and the owners is not a new phenomenon in Sweden. However, talks may have become more in depth and frequent in recent times. In many cases more is done than said, i.e. a lot of activities take place without the general public knowing about it. As conflicts between owners and management rarely are resolved in the public arena, the Swedish climate for ownership issues may be perceived as less spectacular compared to that in other countries, particularly the US. Owners would rather come to a mutual understanding or an acceptable compromise with a company's board than confront them in public.

Company Response. In Robur's experience, corporate management and boards of directors more often than not welcome active owners. In general, owners who choose to take action are well responded to and supported. Furthermore, it is Robur's impression that CEOs and CFOs are often well-informed on ethical issues. A financial analyst may very well be contacted directly by the CEO or head of investor relations on questions related to corporate governance and active ownership. However, when questions related to the ethical performance of companies are debated by shareholders in the media, it can have a counterproductive effect on the company's willingness to listen to the views of the owners.

Practical Work with Active Ownership

Robur has a newly revised ownership policy that primarily applies to companies on the Swedish stock market. As for foreign companies, it is decided on a case to case basis whether Robur should take on the role of an active owner. If this is the case, it is the intention that the ownership policy shall apply to those companies as well.

Central questions in Robur's work with ownership are:

- Composition of the board of directors
- Corporate structure (mergers and acquisitions)

- Executive compensation
- Information and transparency
- Accounting

A well-composed board of directors is a prerequisite for a well-functioning and managed company. Therefore, participating in nominating committees is a central activity for Robur.

In general, Robur attends the AGMs of the companies of which they are among the 10-15 largest owners. Some 80-90 AGMs are attended annually.

However, preparing and attending the AGM is but one part of active ownership. Contacts with management and the board of directors of a company are regarded as equally important. Consequently, contacts are taken on a regular basis. It does happen that these talks result in insider situations developing, although it is not common.

The communication between the owner and the company works in both directions. In many cases the owner may act as a sounding board for a company in a stressful situation, rather than reacting with immediate divestment as a response to incidents that may influence a company's share price negatively. The general procedure when such incidents occur is to send a letter to the management of the company of concern, in order to get an explanation and a confirmation of the facts.

In the discussions between Robur and the management of the company, focus lies on the problem, the responsibility of the company and the needed actions to solve the problem. Environmental analysts, heads of department and management may all be engaged in the process, depending on the complexity and size of the issue. Divestment is seen as a last way out, if discussions are proven to be fruitless.

Ms Nilsson stresses that Robur should not be seen as a kind of "Superboard" with the ultimate responsibility for a company. That responsibility always lies with the board of directors and the management of the company. Thus the importance of composing an adequate selection of board members.

Robur does a majority of its communications through the bank offices of Föreningsbanken. Only little communication is conducted through the media, and Robur does never intentionally expose specific companies in which they hold shares in the media. In this regard Robur differs from institutions like Folksam and Banco. These have few local offices and are therefore more dependent on the media to get their message across, according to Ms Nilsson.

Robur welcomes co-operation between institutions, although Robur itself is not part of any network of lasting character with this objective. Instead, they co-operate with other institutions if they share the same views, and if working together increases the chances of success, on a case by case basis.

Ethical Aspects in Active Ownership and Consequences of Active Ownership

Ms Nilsson is convinced that as a large institutional investor, Robur has the opportunity to influence the way companies act and do business. The process of incorporating specific environmental and social issues on the agenda of active ownership and corporate governance has only begun. It is important to have a holistic view on ownership, however. Fund managers or analysts best handle some issues, whereas other questions should be discussed at the level of the board of directors or at the AGM. The ownership structure is also of importance, it

obviously makes a difference whether the holdings of a company make up 1% or 10% of the total votes.

The trend within the field is clear. Robur allocates more resources and attention to ownership and corporate governance issues now than ever before. Recently, the organisational structure of Robur was changed with the intention of reinforcing the implementation of the ownership policy and making it easier to put specific environmental and ethical issues on the agenda. All matters related to ownership are now handled by one holding company.

SEB

Facts about the Company

Company: SEB Fonder

Principal client categories: Institutions, life insurance companies and private investors

Assets under management: SEK 487 billion (December 2002)

Share of holdings actively managed: 100 %

Internal management or management under direct control: 98 %

Estimated number of holdings: SEB manages 198 funds and 399 institutional mandates. Of these, some 50 % are stock funds, each with approximately 50 shares (December 2002)

Estimated annual turnover in portfolio: Not available

Direct investments: Marginal

Date of Interview: 2003-04-16

Company representative: Cecilia Lager

Position: President SEB Fonder

General on Active Ownership

SEB uses active ownership for Swedish companies exclusively. They have advisors for Japan, Asia, and Latin America, and for the rest in-house management. They manage some 125 BSEK within funds, and 500 BSEK in asset management.

SEB has a policy to be an active owner, with the purpose of increasing value for the shareholders. The most important mean of influence is the nomination and influence of board members and board composition. Indirectly, this gives the possibility to influence the boards election of CEO, and thus the CEOs choice of top management. It is also important to influence the work of the board and the transparency in the board work. SEB is represented at some 70 annual general meetings every year.

SEB definitely has a major influence on the companies they decide to be active owners in. The effort put in by SEB also depends on the estimated potential for success. This is of course dependant on how large share of the company they own, and the size of the investment.

Activities of Institutional owners. Ms Lager does not see that the institutional owners in Sweden are passive. Especially during the last three years, a notable increase in institutional shareholder activism has taken place – a historical comparison would show many differences to the situation today. The institutional owners are not active in the same way as, say, a large private owner, for structural reasons. An institutional owner aims at maximising shareholder

value and must be able to change companies in the portfolio on short notice. Therefore, a “deep” engagement with direct institutional representation in boards etc. is not possible.

Today, institutional owners are beginning to diversify their funds and asset management from other institutional owners with respect to shareholder activism policies. Ms Lager sees one potential danger in this trend, as it may lead to “jumpy” working conditions for the boards of the companies as the institutional owners change their portfolios composition. Therefore, it is important that institutional owners do not directly control the business activities in the companies.

That negotiations and contacts happen behind closed doors is not necessarily a negative thing – this improves the chances for a frictionless solution. It is however important that facts are accounted for afterwards: that the owner has contacted the board on a certain issue and what the outcome was.

Company Response. The companies are generally positive to institutional shareholder activism. However, the activism must be long-term oriented, even though institutional owners do change the composition of their portfolios. The institutional owners must also to a large degree represent the “collective” institutional ownership in Sweden, even though no such formal group exists. Otherwise, no continuity could be achieved in the institutional shareholder activism.

Legislation Fund companies may own up to 5% of companies according to Swedish law. This law is however practically bypassed through institutional investors owning several fund companies: SEB owns three separate fund companies mainly for this reason. Ms Lager perceives she has insufficient knowledge of the legislative framework in other countries to be able to say whether or not these would be beneficial to the Swedish situation.

Practical work with Active Ownership

The main tool for shareholder activism is the AGM: SEB yearly visit some 70 AGMs. SEB tries to solve issues and conflicts well before the AGM in order to increase the impact – it is not a matter of confrontational politics.

The second main tool for activism is the participation in nomination committees for the company board, through which SEB may influence the composition of the board and also nominate individuals they believe would be suitable. In the board nomination committees, it is always a matter of unanimously supporting the entire board and not a matter of supporting individual candidates.

The SEB policy for shareholder activism in asset management gives the guidelines for how SEB acts. As this policy is relatively general, there will often be room for interpretation depending on the specific case.

SEB does not normally involve in active ownership of foreign companies, as their relative shares of company holding are usually small. In these instances SEB votes with its feet, i.e. sell when important issues are discovered.

SEB uses a reference group of 6 persons to gain adequate knowledge of the companies they are active within. These persons all have extensive background as CEOs and board members in

large companies in diverse sectors, so that they may not only provide knowledge but also improve communications between SEB and the companies.

Ms Lager believes Swedish companies are sensitive to shareholder demands. When asked whether the same confrontational policy that large institutional owners in the US seem to adopt would be viable in Sweden, Ms Lager says that that could happen, but it is long journey before we get there. If an operational issue would occur to which SEB would not consent, they would sell their stock if it was a small holding, or talk to the board if it was a large holding. If this dialogue would not entail any acceptable action from the board, a formal letter would be written and distributed to media, and in the worst case lead to a confrontational voting on the AGM. This has never happened, at least for ethical issues, as far as Ms Lager could recall.

Ethical aspects in Active Ownership and Consequences of Active Ownership

SEB includes ethical and environmental aspects in their shareholder activism process in order to maximise shareholder value. They demand an integrated environmental and ethical report from their companies, but otherwise depend on external analysts.

The written policy that exists on ethical issues is SEB's ownership policy. There is no specific ethical or environmental issue that is more important than any other for SEB in their shareholder activism.

According to Ms Lager, capital does not save the world. Active ownership has not affected the legislation on ethical issues in Sweden, but active ownership does contribute to the abiding of the legislation. Shareholder activism aims to maximise shareholder value, and therefore maximises ethical performance as well as long as ethical performance affects shareholder value. There are institutional owners whose policy is that the equivalence Swedish legislation should be followed independent of where the company is active. This is not a policy adhered to by SEB.

Ms Lager does conceive that SEB's shareholder activism has an effect on the shareholder value, even though it is difficult to show in figures. One example that could be used is the price negotiations in take-overs, in which the activism can have a discernible, direct effect. However, Ms Lager claims that there are no studies whatsoever that show that ethical and economic performance are positively correlated. There are also no studies that show the same for active ownership and economic performance. Still, the bottom line is a conviction that active ownership does have a positive effect on shareholder value, and that ethical performance can effect economic performance.

Apart from this, ethical and environmental performance does have an impact outside ownership, e.g. in asset management: bad performance may lead to a no-buy decision or a sell decision. Thus, many ethical questions are managed by asset managers rather than through shareholder activism.

Owners and media often go hand in hand when it comes to pressure on boards and companies.

Summary of the Case Studies

General on Active Ownership

All interviewed institutions have a policy to be active owners. They also all declared that the objective of their activities is to increase the return on investment. Only one of the interviewed institutions, Folksam, said that an parallel objective is to affect and improve society at large, for a greater number of stakeholders than just their own clients.

All institutions mainly limit their activities as owners to the holdings traded on the Swedish stock exchange. They also all focus their attention to companies and issues where the likelihood of success is thought to be the greatest. This estimated success-rate is closely coupled to what share of the votes is held by the institutions.

Only one institution, Folksam, carries the view that Swedish institutions are too passive. The other four institutions believe the criticism raised against institutional investors to a large extent stems from media's lack of knowledge about what the institutions actually do as owners.

All institutions in the study have experienced mainly positive response from the companies where they have taken action in their role as owners.

Practical Work with Active Ownership

All interviewed institutions attend a large number of AGMs every year.

Board election and participation in nomination committees are considered to be very important by all institutions in the study. However, all institutional investors also mention that direct and more informal contacts with the company and with the board of directors can often be an equally, or even more, fruitful and effective way to communicate their views.

All institutions stated that dialogue, transparency and trust are the most important components in the interactions between the owners and the company. No interviewee believed that a more confrontational approach would be beneficial. Only Folksam declared that they use the media as an integrated part of their ownership strategy, although SEB recognises that media and owners sometimes go hand in hand in putting pressure on companies in certain questions.

The only legislative concern seems to be that insider situations can sometimes occur. Apart from that, no institution believes that legislation restricts their ability to act in a way that they would have liked.

Ethical Aspects in Active Ownership

All institutions except AMF explicitly mention ethics in their ownership policy. However, what is included in the term "ethics" is not very clear, and it varies between institutions.

No institution had participated in rejecting a proposal from a board of directors on ethical grounds. Nor did any institution give examples of how environmental or social issues had been taken into the process of active ownership as defined in this project. Several institutions stressed that such issues are often too operational to be discussed at board-level. Instead, ethical aspects are managed in the daily fund management and share analysis. Several institutions also

mentioned that they consider screening and portfolio selection as a part of their ownership activities.

All institutions declare that they have routines for handling incidents occurring in companies in which they have holdings.

Robur, SEB and Folksam stated that they see a clear trend of increasing activism from owners. This trend is also true for ethical issues, with the reservations mentioned above. These three institutions also expressed the strongest conviction that institutional investors can influence the companies in ethical issues. Folksam and Robur went as far as saying they have a duty to be active in such issues.

No institution has done any quantitative consequence analysis of their ownership activities, nor does any institution in the study have knowledge of any studies showing a positive correlation between active ownership and return on investment.

The overall findings from the interviews are summarised in table 1

Table 1. Summarised findings from the interviews

	AMF	Folksam	Nordea	Robur	SEB
Active owner?	Yes	Yes	Yes	Yes	Yes
Rationale for active ownership	Shareholder value	Shareholder value, parallel objective responsibility	Shareholder value	Shareholder value	Shareholder value
Are institutions too passive?	No	Yes	No	No	No
Company response	Positive, but will to change not great	Positive	Positive	Positive	Positive
Restricted by legislation	No	No	No	No	No
US approach applicable in Sweden?	No	No	No	No	Not at present, maybe in the future
Ethics included in publicly available ownership policy?	No	Yes	Yes	Yes	Yes
Special focus on certain ethical issues?	No	Climate change	No	No	No
Consequence analysis of ownership activities performed?	No	No	No	No	No

Consequences of Active Ownership

Active owners motivate their actions through a belief that what they do has a positive impact on shareholder value, although most agree that any firm proof of this is difficult to obtain. In this section a presentation is made of some scientific views on the consequences of active ownership.

There are few, if any, studies that unmistakably point out shareholder activism as positive for shareholder value. Actually, there are very few studies that find any strong connection, positive or negative, between shareholder activism and shareholder value. Apparently, there seems to be a difference in results between management studies and financial studies, depending on the scope of the studies made. There is little written about ethical shareholder activism and performance, but some on shareholder value and Corporate Social Responsibility, CSR. These studies usually show a weak relationship between CSR performance and financial performance. As CSR can be seen as the logical effect of ethical shareholder activism (i.e. companies taking an ethical responsibility for their activities), it is interesting to see that there seems to be relatively weak correlation between CSR and shareholder value as well.

Active ownership and performance

Korac-Kakabadse et al (2001) finds that there is no conclusive evidence of contribution of corporate governance on financial performance. Further, large scale surveys of UK and US corporations suggest that institutional investors consider financial performance and growth potential as key investment criteria, while corporate governance was ranked towards the bottom of the list (Pic, 1997). Several large-scale, long-term empirical studies find no clear evidence of a substantive relationship between board composition and financial performance (Dalton et al, 1998, and Dalton and Daily, 1999), and other studies come to basically the same conclusion (Zahra and Pearce, 1989, and Maassen, 1999). Shareholder activism can be divided into non-confrontational, long-term strategies (such as negotiated settlements or board election) and confrontational strategies (such as where the owners vote against the company board at AGM's). Research suggests that non-confrontational shareholder activism has a positive impact on stock return in the short-term, but that the long-term effects are negligible, and that there is no evidence that confrontational activism has any effect on returns or performance (Karpoff et al, 1996, Wahal, 1996, Del Guercio and Hawkins, 1999).

In a study on the active ownership performed by CalPERS, the California Public Employees' Retirement System, it shows that shareholder value benefits from active ownership when targeting events were successful (Smith, 1996). CalPERS exercise activism on the bottom ¼ performers in the portfolio where they have a chance of doing an impact (i.e. where CalPERS also is a major owner). On a net, it was estimated that the value increase from active ownership over the studied period was 19 million USD, while the costs were 3,5 million USD. However, the performance of the companies intervened in was not unambiguous: there was a significant positive stock price reaction for successful targeting events and a significant negative reaction for unsuccessful events.

Romano, 2001, tries to unfold the reasons behind that financial analysts normally find little or negative impact on financial performance from shareholder activism. There are several possible reasons:

1. What firms are targeted? Targets of shareholder activism are normally poor performers. Targets have high institutional and low insider shareholding.
2. Shareholder proposals usually have no significant effect on company performance, while private negotiations over proposals in advance of the shareholders' meeting usually has at least short-term impact, positive or negative. Therefore, studies based on shareholder proposals as indicators of activism naturally show low impact.
3. Financial analysts have not been able to identify a positive impact of activism because a lot of the activism is misdirected: it does further shareholder value.

Romano also finds that it is not possible to document positive stock price effects from shareholder proposals on board composition. Overall, there seems to be very little evidence of the impact of shareholder activism on company performance. On the other hand there are objections that it would be impossible to prove a positive effect on stock prices from shareholder activism even if it does occur – fundamentally, shareholder activism seems more rooted in beliefs than in undisputable facts.

CSR and performance

There are two alternative views of the impact of socially responsible decisions in companies (McWilliams, 1997):

1. Socially responsible behaviour has a negative impact on financial performance, representing a redistribution of wealth from the firms' shareholders to its other stakeholders.
2. Socially responsible behaviour enhances financial performance and creates benefits for other stakeholders.

McWilliams has a belief that there is a trade-off between CSR and financial return, and therefore adheres to the first view. She does however not find any conclusive evidence for either view when analysing studies that originally come to the conclusion that the second view must be correct. The studies criticised by McWilliams are Wright et al 1995, Meznar, Nigh and Kwok 1994, Clinebell and Clinebell 1994, Davidson and Worrel 1992, Worrel, Davidson and Sharma 1991, Davidson and Worrell 1988. McWilliams' main critique is that these studies use an "event window" that is too long, so that confounding effects have time to take place, thereby making it difficult to derive cause and effect. McWilliams' conclusion is that it is hard to isolate effects of any single decision, especially if many financially relevant effects happen within a short period of time.

Diltz (1995) has examined 28 stock portfolios in order to determine whether ethical screening has an impact on portfolio performance. The analysis shows little impact, and to the extent that any impacts could be observed, they were both positive and negative, depending on what criteria were used in the portfolio screening.

Harrison and Freeman (1999) find that empirical research in the area of social responsibility and company performance is in an early stage. However, Johnson and Greening (1999) test an integrated model of the effects of institutional investors and various governance devices on corporate social performance. They find that organisations with higher equity ownership by pension funds and organisations with higher levels of outside director representation tend to have higher corporate social performance on a number of dimensions. In this study, organisations that perform well on the "people" dimension of social performance (relations with

employees, women and minorities, and communities) tend to have higher financial performance as well. This conclusion is contrary to Diltz's finding that companies that provide family-oriented benefits are penalised in their financial performance (Diltz, 1995). Molley et al (2002) in turn find that environmental performance measures have no significant impact or even a negative impact on financial performance, as measured by returns. Kurtz (2000) concludes that, as social screenings simply seem to have no effect on financial performance, there is no controversy in screening a portfolio, as it then would be both consistent with ethical values and offer a competitive return on investment.

As a conclusion, it seems that the relation between ethical performance and financial performance is weak, and in the rare cases that any correlation can be seen, it can be both positive and negative. Thus, ethical performance does not seem to be of importance for financial performance.

Discussion

As this study has shown, active ownership can come in many forms and with many different purposes. Very roughly, one can distinguish between two types of active ownership: either the shareholders force the management to act by using some sort of direct or indirect threat, or the engagement takes on a form built more on dialogue and mutual trust than threat. It is clear that the first type of engagement is much more common in the US than it is in Sweden.

How, and to what extent shareholders are active in is to a large extent defined by in which institutional setting they are operating, what kind of shareholder they are, but also what ambition and policy they have. The setting and the character of the investor also govern what kinds of issues are defined as 'ethical'. Some investors make no difference between traditional corporate governance issues like board independence and executive compensation, and SRI-type issues like environment or labour rights. One danger of this could be that staff hired to work with, say, environmental issues in connection to active ownership, are suddenly expected to have opinions on all matters ranging from mergers and acquisitions to child labour. This, however, is a matter for each institution to avoid. We have no strong opinion on whether the lack of separation between issues of different kinds is correct or not, but are content to note that this is the case.

It is our view that a direct dialogue between institutions and company boards seems to have more relevance to company behaviour and performance than voting does. This was indicated in the interviews, and the same conclusion has been expressed by actors in other European countries (e.g. Actuarial Profession, 2001). There is a clear difference in the way ownership is executed in Sweden compared to what seems to be the case in the US in particular. In Sweden, the institutions seem to prefer to work closely together with the board and management of the companies in which they own shares, giving their opinions at informal 'one-to-one meetings', rather than criticising the boards in public, e.g. at the AGM. It is very rare that controversial environmental or social issues are decided by voting at AGM's in Sweden. This contrasts to the US, where shareholder campaigns regularly result in open conflicts at the AGM.

Further, from an ethical point of view it is equally, or even more, important that an institution has analysts who can ask well informed and relevant questions about the ethical performance of the companies in the investment universe, in her or his regular work with portfolio selection. Several of the interviewed institutions expressed that the more an issue relates to the day-to-day operative management and strategies of a company, the further away from the board and AGM

it gets. As a consequence, such issues are not addressed by the institution in their role as an owner, but rather in their role as possible investor and then their analysts handle them.

The companies in the US, UK, and Sweden, which we have studied, may not be perfect representatives of owners in general in these countries. However, the tendency that the differences in active ownership lie rather in what market the companies operate than between companies in the same market is relatively clear. US activism is more confrontational than is the case in Europe. Swedish activism is relatively low-key and reactive, while UK activism seems more proactive. According to the interviewed persons, none of these specific profiles would work very well in any other market. Therefore it seems natural to suspect that market structure has an important role in deciding how active ownership is carried out.

There is no legislative aspect that hinders Swedish shareholder to act in the same way as the British or the American institutions. A structural difference may be that Swedish institutional owners have less influence on companies, as they are smaller owners than their British and U.S. counterparts. According to the Swedish case studies, a lot of the activism in the UK and in the U.S. would be considered involvement in operative matters or micro-management in Sweden, something which is considered to be outside the mandate for active ownership.

According to the British fund manager Hermes, one of the critical factors of long-term active ownership is passive fund management of index tracking funds. Index tracking often means long-term commitment to certain shares, which gives less room for quick exits, and consequently higher incentive for active ownership as a mean of improving the return on investment. The Swedish institutional owners in this study all have a very large share of active management of the shares traded on the Swedish stock exchange. These are also the holdings that are subject to the institutions' activities as owners. This may be one of the reasons why the Swedish institutions in this study seem more reactive and passive than, for example, the large pension funds on the UK and the U.S..

However, active shareholders in the U.S and in the UK do not act alone, but often network with other institutional owners when creating policy documents and campaigns. Maybe Swedish institutional owners could become more active in these networks? At least one of the British pension funds explicitly states that in order to maximise shareholder value, they have to work for internalisation of ethical effects, as their shareholders are representative of the society as a whole. If this is an important driving force, maybe the largest potential increase in active ownership in Sweden lies with the pension funds?

We note that all institutional actors we have interviewed, and indeed an overwhelming majority of the ones described in the literature, subscribe to the view that active ownership maximises shareholder value. This may come across as somewhat puzzling given that we have found no quantitative studies that prove a positive correlation between return on investment and active ownership.

The UK institutions seem to believe that being proactive in the ethical field as an owner maximises shareholder value in the long run, while this conviction does not seem to have reached Sweden. Here, the belief seems to be that ethical issues do not influence stock value, at least not enough to motivate proactive behaviour their ownership activities.

With all this in mind, we believe that the recommendation expressed by Myners, 2001, is very relevant for Swedish institutions: "Managers should have an explicit strategy, elucidating the circumstances in which they will intervene in a company; the approach they will use in doing

so; and how they measure the effectiveness of this strategy”. Today, there is room for improvement in all these areas.

None of the institutions we spoke to state that they use active ownership as a way to gain market shares directly. One institution even expressed a fear of a situation where investors compete in being the most active. Thus there still seems to be a lack of direct demand for active ownership from the clients of the institutions. Rather, the average client seems to want maximum return on investment, and does not care how it is achieved.

Conclusions

In order to follow the objective of the study, the questions from the first chapter of the report will be treated below.

What do ethical aspects of ownership mean?

In the US, ethical aspects, or rather active ownership as a whole, is often a matter of confrontational propositions from owners on annual general meetings. In Europe, active ownership is generally carried out through dialogue-based intervention. In the UK, active owners take a proactive, operative role in forming policy documents and guidance in specific issues, while in the rest of Europe active ownership usually limits itself to board elections. The differences in how active ownership unfolds stem largely from legislative differences and cultural differences, as active ownership is relatively homogenous in the studied countries.

To what extent, and in what way, are ethical aspects taken into account by institutional investors?

Active ownership in Sweden concerning ethical aspects seems to be focussed on incidents rather than policy issues, and reactive in its nature rather than proactive. Shareholder value is of paramount importance, and ethical aspects are of concern only when this directly could affect shareholder value. There are few tendencies to a broadened perspective. Ethical aspects are often seen as operational rather than strategic, and therefore disqualified from legitimate ownership influence.

What are the consequences of active ownership with ethical aspects taken into account?

There are few, if any, quantitative studies on ethical aspects of active ownership. The studies done on active ownership or on ethical screening of portfolios show little or no effect, positive or negative, on financial performance. It is considered difficult, if not impossible, to prove any effects, even though the relationship seems to be weak. It is even more difficult to say anything about the effects on corporate ethical performance emanating from ethical active ownership.

What effects would an increased ethical focus in the work with active ownership in Sweden have?

Following the above question, it is not possible to answer what effect increased ethical active ownership would have in Sweden. To be pessimistic, one could say it would have little or no effect on financial and ethical performance alike.

What are the hindrances and possibilities for an increased ethical focus in active ownership in Sweden?

The Swedish institutional owners participating in this study, apart from Folksam, do not agree that institutional owners should be more active than they are today. Ethical aspects do not seem to be suited for bringing up in the same form as e.g. board composition.

The American system is not desirable to implement in Sweden, as such a confrontational system would be a step backwards from the dialogue-based intervention used today.

Legislation is not considered an obstacle to a more active ownership in Sweden, with the possible exception of the insider information that the dialogue-based intervention sometimes can lead to.

Generally, there are few indications that active ownership will become a powerful tool for driving the companies' ethical agenda. In order for this to change, the view of active ownership as solely a strategic tool must change and the activities of the investors must become more operative and proactive in their nature. If ethical active ownership will become more important in Sweden in the future, it will still be very hard, if not impossible, to discern any quantitative facts on its effect.

Further Research

During the process of this project a number of questions have arisen that remain unanswered:

- In what way could Swedish institutions take part in the shareholder networks developing in the U.S. and the UK? Many of the views expressed in the ownership policies of, for example, UK investors, are shared by the Swedish institutions. An increased co-operation with foreign investors could be a way to extend the active ownership to holdings outside of Sweden.
- How could the integration of the ownership activities and the daily fund management and company analysis at the institutions be enhanced and developed? Several of the institutions in this study states that this integration is a priority issue for them, but how it is to be achieved is still unclear.
- All the Swedish institutions in this study declared that their ownership activities are limited to issues like board composition and company structure. This differs from the situation in the U.S. and in the UK. How can issues of more operational character be included in the ownership activities of the Swedish institutions?
- How can the effects of active ownership be measured?
- How should the process of active ownership be organised, and what should it involve, in order to have credibility for both corporations and other stakeholders?
- Do the clients of the institutions, i.e. the individual fund savers, have the same views on what active ownership should mean? If no, how do they differ?
- Is ethics in connection with active ownership a strong sales argument for the financial institutions?

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Appendix A

Questions at interviews (Swedish only)

Om företaget

Huvudsaklig kundgrupp:

Förvalt kapital:

Huvudsaklig inriktning på placeringarna:

Andel av portföljen som förvaltas aktivt:

Andel av förvaltning som sker internt eller under direkt kontroll av företaget:

Ungefärligt antal företag i portföljen:

Ungefärlig årlig omsättning av innehaven i portföljen:

Andel onoterade företag i portföljen:

Allmänna frågor om aktivt ägarskap

1. Har ni som policy att agera aktivt i er roll som ägare?
2. Av vilka skäl?
3. Vilka frågor anser ni är viktigast för er att påverka i er roll som ägare?
4. Anser ni att ni har stort inflytande på hur företagen agerar i de frågor som är viktiga för er?
5. Bedömer ni att det vore önskvärt att institutionella ägare i Sverige agerar mer aktivt?
6. Varför/varför inte?
7. Om ja, på vilket sätt bör ett mer aktivt ägarskap i första hand ske?
8. Anser ni att företagen välkomnar ett aktivt ägarskap från er sida?
9. Anser ni att ni har tillräcklig kunskap om vilka konsekvenser ert agerande som ägare har?
10. Om inte, vad saknas?
11. Upplever ni att lagstiftning eller andra regelverk gör att ni tvingas vara mindre aktiva i er roll som ägare än vad ni skulle vilja vara?
12. Om ja, på vilket sätt?
13. Finns det exempel på lagstiftning/rutiner/traditioner i andra länder ni anser vore önskvärt att överföra till Sverige?
14. Av vilka skäl?

Det praktiska arbetet med aktivt ägarskap

15. Agerar ni på bolagsstämmor, t ex genom röstning?
16. Har ni skrivna riktlinjer för hur ni skall rösta i olika frågor?
17. Är dessa offentliga?
18. Hur ofta och på vilket sätt är ni i direkt kontakt med företagen?
19. Har ni olika ägarpolicy för svenska respektive utländska företag?
20. Samverkar ni ofta med andra institutionella ägare?
21. Sker detta offentligt?
22. Med vilka andra ägare samverkar ni oftast?

Etiska aspekter – miljö- och sociala frågor – i arbetet med ägarstyrning

23. Tar ni med miljö- och sociala frågor i ägarstyrningsprocessen?
 24. Om ja, på vilket sätt?
 25. Om nej, varför inte?
 26. Hanterar ni andra typer av etiska frågor i ägarstyrningen (t ex incitamentsystem, affärsetik, arbetsrätt)?
 27. Bedömer ni att aktivt ägarskap kan spela en stor roll för hur företagen agerar i miljö- och sociala frågor?
 28. Finns det i ägarstyrningspolicyn beskrivet hur miljö- och sociala frågor skall hanteras?
 29. Vilka skäl anser ni kan finnas att beakta miljö- och sociala frågor i ägarstyrning?
 30. Vilka konsekvenser bedömer ni att ett aktivt ägarskap i miljö- och sociala frågor får/skulle kunna få för de företag i vilka ni är ägare?
 31. Hur bedömer ni att avkastningen påverkas av att ni utövar aktivt ägarskap i miljö- och sociala frågor?
 32. Har ni genomfört några specifika analyser av de två ovanstående frågorna?
 33. Vilken fråga inom miljö- och det sociala området är högst prioriterad för er?
 34. Av vilket skäl?
- Övrigt ni skulle vilja tillägga i ämnet?