

Responsibility and power of ownership

A report from LO's Ownership Power Project

Condensed version

Foreword

In 2005 and 2006 LO carried out a project together with national trade unions which dealt with issues of trade union ownership responsibility and how trade unions' power of share ownership should be used. The project is a follow-up of the work done for the LO Democracy Congress in 2000, which then resulted in investment regulations for LO and its affiliates. In 2004 the LO Congress further resolved that LO should take measures to stimulate a broad debate within the trade union movement concerning power over pension fund capital.

The overall purpose of the project was to create a more coordinated trade union, social and ethical profile as regards how the use of investment capital is viewed. The project was also aimed at increasing the competence of LO and its affiliates in the area. This report is a condensed version of the project group's report.

The project was led by LO's Third Vice President Leif Håkansson, LO economist Åsa-Pia Järliden Bergström was principal secretary.

The work of the project was carried out in a steering group, which included representatives from LO headquarters, with expertise in each respective field. The report has been discussed on several occasions in an inter-union group.

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1 Introduction

Issues of share ownership today occupy a prominent role both in Sweden and internationally. They mainly concern the requirements shareholders can and should impose on companies, but also the responsibility of shareholders and what type of ownership is best from the point of view of business. Several issues are gathered under the same roof, such as Corporate Social Responsibility (CSR), Socially Responsible Investment (SRI) and Corporate Governance. Under these headings lie questions such as the ethical basis of investment, corporate codes of conduct, remuneration to boards of directors, nominations and gender equality, as well as short-termism versus long-termism in investment contexts. As far as the trade unions are concerned, it is mainly a matter of what we can and should require in our capacity of capital owners. On the one hand we operate in this arena on the same terms as other investors, but on the other hand we believe that just we, in our capacity of capital owners, can have a positive impact on the market with respect to our primary goal – promoting the rights of workers. A coordinated view of ownership responsibility in the trade union movement may prove to be a very important policy instrument in the future, to promote members' interests in traditional trade union areas, but also as a trade union counterweight to capital in areas that are not traditionally those of trade unions.

A specification of the assets managed by the Swedish trade union movement together with the employers, our own trade union funds and our public pension funds (National Swedish Pension Funds) is presented below:

Portfolio structure for major fund managers, SEK millions, 2005

MANAGER	Sw. shares	For. shares	Interest-bearing	Other	Total
AP1	23 380	86 958	74 643	2 282	187 263
AP2	40 800	77 500	65 100	7 200	190 600
AP3	29 600	78 200	76 700	7 500	192 000
AP4	36 304	76 813	63 339	3 712	180 168
AP6 *	13 803		2 055		15 858
AP7	10 218	38 926	5 878	4 784	59 806
Folksam	25 498	27 859	98 988	6 547	158 892
<i>of which KPA AB</i>	<i>1 581</i>	<i>1 797</i>	<i>753</i>	<i>22</i>	<i>4 153</i>
<i>of which Folksam LO Fund</i>	<i>8 261</i>	<i>6 147</i>	<i>1 686</i>	<i>556</i>	<i>16 650</i>
AMF Pension	62 582	62 216	109 643	16 659	251 100
AFA	30 572	33 313	120 739	11 722	196 346
Alecta	68 739	81 687	219 078	26 841	396 345
KÅPAN	4 677	4 753	13 780	1 809	25 019
GRAND TOTAL	346 173	568 225	849 943	89 056	1 853 397

* No foreign holdings

It is in the interest of the members that LO and its affiliates are committed to promoting development towards a more responsible capital market. Partly so that in this way we can

create a more stable balance of power between labour and capital at a global level, but also through influencing companies and their managements in our own country.

2 A developed ethical policy

In response to the LO Democracy Congress in 2000, work was started on economic democracy and a broad discussion was initiated on employees' money in pension funds. Investment was brought up here as an important policy instrument for trade union and consumer power. At that time LO chose to differentiate between active ownership power and the power to impose restrictions. The historical background is that trade unions have always taken the line that the way to increased economic democracy is not necessarily via public ownership of the greater part of the economy. The trade union movement supports the idea of a mixed economy; that the economy is mainly privately owned but that the public sector is responsible for areas where fairness and accessibility are principal objectives. For us it is rather a matter of creating and maintaining a balance between the economic power that exists in a mainly privately owned economy and the democratic and trade union counterforces. There has always been faith in capitalism, even though it must be counterbalanced – this is included in the concept of a mixed economy combined with a strong trade union movement.

In the run up to the Democracy Congress it was stated that “*employee capital can be an important tool, not principally in an active ownership role, but through imposing restrictions on the use of the money in a way that can really have a long term impact on economic power that is mobile across borders*”. The conclusion was that one simple and effective requirement is that employees' money must not be used in companies and countries that obstruct unionisation and persecute trade union leaders. It was thought that imposing these demands - if this could be part of an international initiative – could have a real impact on the long term global balance of power between labour and capital. This reasoning led to a proposal for ethical rules for the investment of LO's own capital. Investment regulations were adopted by the Congress. These regulations are used today in fund management for LO and its affiliates (see appendix).

In 2005 LO carried out a follow-up survey of how these issues are dealt with by a number of investors. The eight core conventions that the ILO Governing Body has designated as core labour standards are included in most other fund managers' ethical policies. However, at present there are relatively large differences between how various fund managers have chosen to treat these issues.

The National Swedish Pension Funds' capital investment framework is regulated by law:

The National Pension Funds must manage pension capital so as to maximise the benefit to the insurance for income-related old-age pension. Allocation of assets must take place after analysis of the premium pension system commitments. The long term objective must be to maximise return in relation to investment risk. Management of funds must take place with good diversification of risk. The total risk level in the management of the assets must be low. Risk and return must be interpreted in terms of matured pensions. The low risk requirement, however, is not to apply to the management of the present

Seventh National Swedish Pension Fund's Premium Choice Fund (Premievalsfonden), into which premium pension funds are channelled for those who have actively selected this solution. Necessary liquidity must be maintained.

Management of the funds must not be influenced by prevailing government policies, either industrial or economic. Consideration must be given to the environment and ethics when investing, without compromising the overall goal of a high return.

In other respects all the buffer funds, together with the Seventh National Swedish Pension Fund, are free to draw up their own ethical rules for investments as well as their own ownership policies. With regard to the National Pension Funds' abilities to exert active corporate governance it can be mentioned in this context that holding large positions is partly restricted. This is because a fund may not have a holding in a Swedish or foreign company of more than 10 per cent of the votes. Moreover, only 5 per cent of the total fund assets may be invested in unlisted shares.

2.1 What significance does Corporate Social Responsibility have for the trade union movement?

In recent years the concept of "Corporate Social Responsibility" has established itself in the debate on multinational companies' obligations towards society and various stakeholder groups. However, it has no clear connection with the central role companies play for the trade union movement in their capacity of employers.

It is very common for representatives of companies, fund managers and other players to state that they have a policy for "CSR issues" or that they examine how companies live up to their "CSR policy". This is often non-transparent and impossible for outsiders to scrutinise. The lack of a definition is, on the one hand, convenient for companies, since it leaves them free to define CSR on the basis of their own interpretation of the expectations that customers, employees and others have. They can then link a voluntary code of conduct based on their view to the concept and report how they think they are following it – a type of "self regulation". The contents and definitions are then probably mainly based on what the media and customers regard as central questions as well as on a risk evaluation of the capacity of these groups to scrutinise the company.

The lack of clarity is also at the same time a problem to companies, which the Confederation of Swedish Enterprise and its international federation have maintained, since they are accused and exposed in the media for non-compliance with the definitions of CSR put forward by individual organisations, consumer organisations or other groups.

CSR is not a concept that originates from the views and methods of the trade union movement. However, a large proportion of the trade union movement considers that the theory that companies not only have a responsibility to create a return and value for their shareholders, but are players that must also create value for stakeholders, is important to reconsider and apply to companies today. This was a predominant view of companies in the 1970s, for example. If the concept is to be meaningful for the trade union movement it must be explicitly specified and defined.

For the trade union movement it is a given to imbue the concept of CSR with the already strongly established charters, conventions and declarations that exist for nations and for companies, international and national. Apart from this, certain specific questions can be added, but only if they raise the standards that already exist. In that case this should be done through tripartite agreements or partner agreements in each national context.

The first step in defining the contents of CSR is to specify the view held by the trade union movement as to the role of companies. This lays the foundation for the terms of reference that can be applied later. A reasonable view is that companies have a given role in the economy as *producers* and that they have that role in order to create added value and profit. Through this, they are expected to create employment with good working conditions and to pay good wages and give employees pay rises. They must take care of production sustainably, socially, economically and environmentally and comply with laws and agreements. They are thereby taking their responsibility as producers.

Apart from the producer role, companies (and non-profit organisations) play a role in the labour market as *employers*. This role is entirely central to the trade union movement and it is in that role that trade union expectations of companies are most clearly expressed. For a company to be regarded as taking its responsibility it must be a good employer in accordance with the international standards agreed within the ILO and it must comply with laws and collective agreements. Companies that take a social responsibility become in this sense the same as employers that both comply with agreed standards, and promote good and well-functioning industrial relations.

A further role assigned to companies by those debating CSR is that companies have, or are expected to have, a responsibility for welfare services in the local communities or countries where they operate, for example to build schools in developing countries with deficient school systems and similar commitments. This is not a role that the trade union movement regards as reasonable to assign to companies. Welfare services and distribution policy are a function of the public sphere and must be determined in democratic order and financed with public funds. The role that companies can be expected to have in relation to fundamental welfare services is to pay the tax required by countries' legislation, so that countries receive the financing to build up their systems according to the mandate given to publicly elected representatives.

As far as LO is concerned, the concept of "Corporate Social Responsibility" is only possible to fulfil through companies complying fully with the obligations and expectations imposed on them in national laws and collective agreements, as well as in the two entirely central international instruments for multinational enterprises: The OECD Guidelines for Multinational Enterprises and the ILO Tripartite Declaration of Principles concerning Multinational Enterprises.

2.2 The environmental field – important for trade unions

Environmental issues are often linked to and integral to social issues and constitute part of "Corporate Social Responsibility". Companies with a more responsible view of their

role in environmental issues, that is to say that have a sustainability perspective on investments and production, usually also aspire to a sustainable personnel policy in the long-term. This implies a respect for employees' rights and a regard for labour as a resource to be maintained in accordance with a long-term strategy, in the same way as the environment.

The business world's work on environmental questions has in many cases changed from an unwilling acceptance of official requirements to a more proactive view in which environmental work is made into a profile issue and an important part of the company's branding. At the same time environmental work, above all in large and internationally active companies, has been broadened and integrated with a more clearly marked social responsibility in the context of "Corporate Social Responsibility". It has thereby become necessary for companies to develop instruments to introduce environmental considerations into investment plans, in current production and in various forms of control systems. Apart from companies' own needs to develop and evaluate environmental work, these instruments have assumed a growing significance for the assessments made of companies by external investors. They also have an increasing importance for official environmental controls.

As environmental problems become increasingly cross-border, environmental policy, as well as control and evaluation of corporate environmental work, is becoming more internationalised. The most important form of multilateral cooperation is the work of international environmental conventions, often in the context of the UN's work. Convention work got started on a broad front at the time of the UN's first environmental conference in Stockholm in 1972, but even in the fifties a couple of agreements had been signed, for example on oil discharges from ships.

The conventions that exist today cover areas such as climate and air pollution control, the law of the sea, biological diversity, chemical control, waste management and certain method issues for environmental work. The conventions are primarily directed at governments, to be incorporated into national legislation, which in turn regulates the practical work of companies. This means, at the same time, that contravention of the rules can lead to sanctions, which is not the case for contravention of the conventions themselves, where no real sanctions are possible. At present Sweden has ratified forty or so conventions, both global, such as the United Nations Framework Convention on Climate Change with the Kyoto Protocol, and regional, such as the Helsinki Convention on the Protection of the Baltic Sea.

Correspondingly, the EC Directives or Ordinances in the environmental field govern the environmental legislation within the European Union of the countries concerned. For example, EU 2007 is expected to have a coordinated Regulation in the field of chemicals, with great significance for management of industrial chemicals.

If companies are to attract investors for their environmental work it is not, however, sufficient for them to follow national regulations. Voluntary action is also required over

and above the legal requirements, together with a level of measures that drives development.

The most common example of an internationally accepted basis for assessment is environmental standardisation within the ISO 14000 series. Conformity with the ISO systems implies a commitment to follow certain principles and methods in one's environmental work as well as working for constant improvement. However, the companies themselves set the targets for the improvement in emissions or treatment of chemicals they are aiming for. The ISO system requirements are often integrated with other systems, above all the European EMAS, which also imposes specific requirements for public reporting of the results.

In order to be able to compare different companies' environmental and sustainability efforts, certain screening and benchmarking are also carried out, though to an increasing extent integrated with corresponding assessments in the social area. Among the leading companies in the field of sustainability indexes are Dow Jones and Morgan Stanley.

For the trade union movement, the fundamental requirement of a company's environmental work should of course be that it does not contravene national legislation in the countries in which the company operates. For operations in EU states this thereby includes many international conventions, EU rules etc, since they are integrated with the national regulatory framework. At the same time the requirement is of limited value. It is true that it can be followed up on a general level, but the risk of being convicted of environmental crime is in practice small, even in developed industrial countries.

One possibility of raising the level of ambition, above all for operations in East European countries and the third world, is to demand that companies follow a number of basic environmental conventions, for example in the areas of climate and chemicals. The problem here is, however, that the conventions are difficult to interpret for an individual company's operations and generally effective instruments for follow-up hardly exist. It is up to the investor, via screening companies or their own enquiries, to investigate compliance with the conventions.

It is also possible to choose companies that carry on proactive environmental work in some form by being part of the ISO system or Global Compact. This, however, restricts the circle of companies and the environmental management system ISO-14001, for example, only specifies that certain work is done, but says little about the level of this work.

2.3 Required return and ethical requirements

Even in the future, with a revised or supplemented view of ownership issues, it will be important to LO as a collective to maintain the importance of a good return as the overriding goal for investment policy. An investment policy with ethical overtones should be designed so as not to come into conflict with the required return.

In the short term there may of course be cases where there are investments that bring a higher rate of return but which do not comply with LO's ethical policy. However, there is no reason for ethical requirements on investments to also mean a lowering of the required return on a portfolio. If that were the case, the restrictions created via these requirements would not be sustainable in the long term for an investor. In plain language this would mean buying shares in companies with a poor long-term outlook. Such a strategy is of course not tenable.

However, there is no reason to believe that companies that meet certain environmental requirements or requirements as to how employees are treated will report worse earnings than other companies in the long term. In the long term we therefore consider that the goals of good return and clear ethical requirements are fully compatible.

In the report "Etiska Fonder 2005" (Ethical Funds 2005) published by Folksam there is a general description of existing studies of the relation between social responsibility and financial performance. Its conclusion is that it is difficult to find any clear correlation. The report relates that there are studies supporting the idea that companies that take a major social responsibility are more profitable, as well as studies supporting the opposite. One decisive factor is the type of ethical fund studied.

The required return must always be weighed against the risks one wishes to take. Since the funds the trade unions have influence over are for the most part jointly managed pension funds and other insurance capital belonging to their members, the risk level must be kept low. As far as the trade unions and LO are concerned, a considerable part of the capital should be relatively easy to transform into strike funds. If this is to be possible there should be a high degree of liquidity in the portfolio and other risktaking should be restricted. Investment of capital must thus to a great extent be governed by the area of use to which it may be expected to be put and the risk level chosen on that basis.

A detailed definition of the investment alternatives allowed in a portfolio, for example in terms of ethical requirements, may also lead to a greater market risk. This is because fewer companies or countries would then be included in the selection available for diversifying the portfolio.

2.4 A developed ethical policy - summary

In future, LO should continue to select mainly general criteria for investment, applicable to the entire portfolio. The focus should continue to lie on requirements concerning employees and their rights. LO's view is, thus, that even future work should be directed towards general requirements for all its capital, and restrictions for all companies and fund managers, rather than specific requirements and separate funds. As far as possible the criteria should constitute international conventions supported by a large number of states and international regulations and standards that are already used by many companies.

Supplementing the criteria by an exclusion requirement for companies producing tobacco or tobacco products is not under consideration. An earlier motive for LO not to exclude

either tobacco, alcohol or arms production generally, is that this is not forbidden by Swedish law. It is clear that all of them are potentially harmful, each in their own way, but it is not primarily up to the trade unions to pursue these matters. In addition, LO organises members in the tobacco industry, which means that an excluding criterion in this area would be a difficult matter of principle for LO. As regards certain types of weapon, anti-personnel mines, there is a current UN Convention that concerns this area. It has been ratified by Sweden and we consider that LO's excluding criteria should include the requirement that companies do not produce landmines or cluster bombs.

The issue of investments in the pornographic industry is both easy and difficult. Of course LO and its affiliates must not invest in pure pornography production. Companies focussing on this are not, however, to any great extent listed on the stock exchange (with the exception of the "Private Media Group"). When investing in major media companies, however, there is an immediate risk of including companies that broadcast or possibly distribute pornography. LO and its affiliates could define how great a part of these companies may be involved with the pornography industry. The alternative for investments in this type of company is to form an opinion as to how this part of the company's operations is to be treated. As regards television channels, it would be important, for example, that this part is treated separately and not included in the ordinary programmes during "normal broadcasting hours", unless it is understood to be separate adult entertainment and nothing else. The requirement should be that the company has a clear policy for handling and following up this part of its operations.

As regards the CSR issues, LO's view is that the core regulations that constitute CSR are the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and the OECD Guidelines for Multinational Enterprises (see the discussion above). If these are complied with, and sound processes for their implementation are established, most of the companies' responsibilities are satisfactorily covered, in the opinion of LO.

However, LO does not put forward the entire ILO Tripartite Declaration as a negative criterion for investment activities. The reason is that it covers a large number of ILO Conventions apart from the eight core conventions that are part of other central instruments. As things are at present it will not be possible to ensure a reliable follow up of these as required in fund management, for example via a screening company. Applying the ILO Tripartite Declaration would mean that a very large number of companies would have to be excluded from the potential portfolio. Because of this it is not compatible with requirements for a good return and diversification of risk for pensioners.

On condition that a reliable follow up can be established for issues related to worker participation in the ILO Tripartite Declaration, LO wants to include such issues in a developed ethical policy for fund management. This means that the questions dealt with in paragraphs 55-57 of the ILO Tripartite Declaration concerning Multinational Enterprises should be included.

In order to give further support to activities that help the environment and prevent those that harm it, trade unions should also point out a number of environmental conventions or

ISO obligations as criteria for our own investment activities. These should be internationally viable and possible for rating companies, for example, to verify.

The required return should be the overriding goal of an investment policy. So an investment policy with ethical overtones should be designed in such a way as not to conflict with this requirement. We do not consider that there is anything to indicate that the ethical policy pursued by LO conflicts with the requirement for a good return.

As regards the risk level of investments, LO's view is that it should be kept low. However, we do not consider that there is any long-term conflict between fulfilling our general ethical criteria and the limited risk requirement.

2.5 The dilemma – requirements of countries or companies

It is the responsibility of the individual states to ensure compliance with ILO Conventions and other central instruments for securing ethical behaviour among companies, as we have pointed out earlier in this document. It may therefore be difficult to find avenues of action when an individual company violates an ILO Convention. The OECD Guidelines for Multinational Enterprises and the ILO Tripartite Declaration concerning Multinational Enterprises are, however, two instruments formulated with a focus on the company as actor, to try to overcome this problem.

A dilemma arises for example when a country has not ratified the ILO core conventions, but there has been investment in companies operating there. In that case, however, LO would expect the company to comply with the central ILO Conventions, or for that matter other instruments directed at states included in the ethical policy. This can be examined in a follow up process.

3 Share ownership policy and corporate governance issues

Most funds and managers make a distinction between ethical policy for funds management and policy for how they should conduct themselves as shareholders and what requirements they should make of the companies – *share ownership policy*. In the same way as most fund managers now have an ethical policy, most major owner institutions now have their own share ownership policies. As described above, LO has already been working on issues that concern ethical rules for investment of capital and decided on its own profile on the matter. However, LO has not had any distinct profile on share ownership policy issues. This may for instance concern such areas as rules for the work of the board of directors and evaluating this work, as well as drawing up remuneration systems and pension agreements for the board and executive management. This area has come to be known as *corporate governance*. This is primarily concerned with governance of companies “with a view to meeting the shareholders’ required return on invested capital and thus it contributes to economic growth and efficiency”.

All fund managers have different share ownership policies with diverse contents and varying emphasis for the different areas. Already now we have an ownership

policy/ethical policy based on the trade union core areas, but this can be developed and made clearer in certain areas. In addition, we should pursue this approach more clearly and more formally in external contexts.

3.1 The work of the Commission on Business Confidence

In 2002 the “Commission on Business Confidence” was instructed to investigate the impairment of public confidence in the Swedish business sector. The work of the Commission was completed at the end of 2004 and at that time it proposed a series of measures to enable the business sector to improve public confidence.

Part of this work consisted in proposing a "Code of Conduct" for corporate governance.¹ The Code supplements the Swedish Companies Act and other mandatory regulations and specifies a standard of good corporate governance over and above the minimum legal requirements. The Code is not a basis for legislation but is to control via *self regulation*.

Compliance with the Code through self regulation is to be guaranteed by means of companies reporting on their compliance with the Code and, in cases where they diverge from it, they must at the same time explain why (“comply or explain”). The Code applies from 1 January 2005 and subsequent developments will be supervised by the Swedish Corporate Governance Board. From 1 July 2005, under an agreement with the Swedish Association of Listed Companies, the Stockholm Stock Exchange will implement the Code for all companies on the exchange’s A list, as well as for companies on the O list with a market value in excess of SEK 3 billion – in other words the Code is to function as a listing requirement for companies. After evaluation and possible adjustments, the intention is to extend coverage of the Code to all listed companies. The idea is for developed corporate governance in these companies to serve as an example and model for other categories of companies as well.

LO’s view of the Code of Corporate Governance is by and large positive. The greatest doubt on the part of LO concerns the principle of self-regulation. There may be a point in holding those who now hold power fully responsible for companies’ compliance with the Code. However, in its statement of opinion on the report of the Commission on Business Confidence, LO wrote that “... developments must be monitored carefully and if self-regulation proves insufficient legislation must be introduced”.

3.2 Composition of the board - a matter of gender equality in company boards

Gender equality work and endeavours to treat women and men equally is a very important issue for LO. One of the goals of gender equality policy is equal distribution of power and influence between women and men. In view of this, the matter of equal gender distribution in senior management of companies will become central. It is also a question of utilising different competencies and thus raising the level of skills and improving companies' potential for growth and profitability.

¹ “Swedish Code for Corporate Governance” Swedish Government Official Reports, SOU 2004:130

The Swedish Code of Corporate Governance includes a rule stating that an equal gender distribution on the board is to be an aim. Like the other Code criteria, this is not a binding requirement, but if companies comply with the Code they should give an account of how they are fulfilling this criterion. Companies are also obliged to report female representation in company management and on company boards in their annual reports.

The Government previously set up the intermediate goal that the percentage of female board members in state-owned companies (or companies in which the state is a major shareholder) must be at least 40 per cent (2003). This goal has been met on average (the percentage is now an average of 42 per cent) but not by each individual state-owned company.

The trend in privately owned businesses is not advancing particularly rapidly. Efforts have been in progress for some time to get more women in leading positions, but in ten years this has only led to an increase from 2 to 8 per cent women on the boards of privately owned limited companies. In 2004 the percentage of women on the boards of listed companies was 14.6. This has raised the question of a quota system. Critics of a quota system believe, however, that this would be a disservice to women. One view is that at present there is not a sufficient number of female directors and leaders who are qualified to sit on company boards. As regards trade union representatives on company boards the choice may be restricted by the fact that the industry or company has a clear predominance of men or women.

3.2.1 LO's view

LO believes that the current Code of Corporate Governance should be used as an opening for gender equality work in this area. The Code of Corporate Governance states (Section 3.2.1): *“With the company’s operations, phase of development, and other conditions taken into consideration, the board is to have an appropriate composition, exhibiting diversity and breadth in the directors’ qualifications, experience and background. An equal gender distribution on the board is to be an aim.”* Moreover, the following is stipulated (under section 2.2.3) *“A report on how the nomination committee has conducted its work is to be posted on the company’s website.”*

LO believes it appropriate to link specific gender equality requirements at this stage to the work of recruitment to boards, in the same way as the active measures of the Equal Opportunities Act function. The objective should be to achieve equal gender distribution (40/60) and in each recruitment process this should be included in the requirement profiles for recruitment of new members. To make this clearer, the nomination committee should give a clear account of its efforts to achieve this objective in its recruitment. Hence it is not sufficient only to report the result - the route taken to achieve it must also be transparent.

Competence testing and evaluation of board members will be a very important element of this process, as in this way men and women can be evaluated on the same grounds.

This work should be subsequently evaluated. In that way it is to some extent possible to gain clearer insight as to whether the gender distribution on boards reflects deficient gender equality work or a deficiency in the recruitment base, i.e. whether there is an insufficient number of competent women from which to choose. It is also possible to develop the requirements of gender equality work as in the Equal Opportunities Act, and thereby impose specific reporting requirements for gender equality measures. Requirements can also be made more stringent by imposing conditional financial penalties for non-existent or deficient reporting.

If instead a picture emerges of deficient gender equality work in the recruiting processes, legislation for a quota system should be considered as a sure way of influencing this issue in the right direction.

3.2.2 The question of a quota system for trade union board representatives

The issue is somewhat more difficult when it comes to how legislation on a quota system should treat employee representatives on boards. Here the nomination process must be completely controlled by the employee side. If the employees are obliged to appoint one woman and one man to each post, the final decision as to who should be included on the company board will lie with the shareholders and the general meeting. This may weaken trade union positions in this context.

Consequently, LO considers that trade union board representatives should be covered by quota legislation. On the other hand, the trade union should be required to report a clear gender equality process in its nomination for these posts, i.e. that the appointments reflect the gender distribution of employees in the company.

The gender distribution where trade unions, centrally or via a national union, have board representation, illustrates that we ourselves have perhaps not gone the full distance as regards board composition.

Boards that manage "trade union capital", women and men 2006

	Board (excl. alternates and staff repr)				
	Men	Women	Total	% men	% women
AP1	4	5	9	44%	56%
AP2	5	4	9	56%	44%
AP3	5	4	9	56%	44%
AP4	5	4	9	56%	44%
AP6	3	2	5	60%	40%
AP7	5	4	9	56%	44%
Folksam Sak	7	5	12	58%	42%
Folksam Liv	6	5	11	55%	45%
Folksam Fond AB	4	4	8	50%	50%
KPA AB	5	1	6	83%	17%
Folksam LO Fondförsäkring AB	7	4	11	64%	36%
Folksam LO Fond AB	7	4	11	64%	36%
AMF Pension	8	2	10	80%	20%
AMF Pension Fondförvaltning AB	6	1	7	86%	14%
AFA Sjuk	8	1	9	89%	11%
AFA Trygg	7	2	9	78%	22%
AFA Liv	7	2	9	78%	22%
Alecta	10	2	12	83%	17%
FSO	6	0	6	100%	0%
TOTAL FOR ALL	115	56	171	67%	33%

Last updated on 24 May 2006

The table above shows the fund managers who mainly handle trade union insurance capital. The National Pension Funds manage the entire population's pension capital and just for that reason their board composition is of great importance. As described above, state-owned companies have a target of at least 40 per cent women and this target is met by all the National Pension Funds. Folksam has also achieved even gender distribution on its respective boards according to this measure.

The picture is somewhat different for the companies owned jointly with the trade unions. In Folksam LO Fondförsäkring 4 of the 11 board members are women, with the same distribution in Folksam LO Fond AB. Among the trade union representatives in each company there is only one woman representative. For AMF the gender distribution is very uneven, both in the parent company and the fund management company. Of those nominated by the trade unions in the parent company, however, there are 2 women and 3 men, which means that the responsibility for the uneven gender distribution rather lies with the employers. There are no women at the moment, however, on the board of the fund management company. AFA, Alecta and FSO also have a considerably lower percentage of women than men on their boards. However, in the case of AFA the trade unions (as for AMF's parent company) have by and large nominated two men and two women.

3.3 The requirement for a reasonable system of remuneration

Bonus schemes and incentive schemes are used in many contexts to give company management more interests in common with those of the company. For a long period it has been difficult to gain an overall view of the size and scope of these schemes. For employees, the most important view on remuneration to company management is that it must be reasonable and in relation to the work performed, regardless of the form it takes.

The Swedish Code of Corporate Governance stipulates the following (section 4.2.2):

“The board is to present a proposal for the company’s policy on remuneration and other terms of employment for senior management to the ordinary general meeting for its approval. The proposal is to be posted on the company’s website at the time notice of the general meeting of shareholders is given. The policy is to include:

- *the relative importance of fixed and variable components of the remuneration and the linkage between performance and remuneration;*
- *the principle terms of bonus and incentive schemes;*
- *the principle terms of non-monetary benefits, pension, notice of termination and severance pay; and*
- *the members of senior management covered by the terms.*

LO’s view of incentive schemes for employees and company management can be summarised as follows:

- Companies should as a general rule be restrictive with incentive schemes in addition to wages, salaries and pensions.
- The scheme must have a clear purpose which is in line with a long-term strategy for remuneration and which promotes the company’s long-term development.
- Remuneration must be linked to performance in the form of clear and measurable goals. These goals must be determined in advance.
- The performance goals must be set in relation to a reference portfolio, i.e. how the company performs in relation to competitors in the same industry.
- The costs of the remuneration schemes must be reasonable and there must be a remuneration ceiling.
- The time-frame of the scheme’s dividend distribution must stimulate a long-term perspective, for example by being based on an average outcome over a number of years.
- Remuneration must be reported clearly and fully in the company’s annual report.
- All the points above must be communicated to the shareholders and a resolution passed at the general meeting. The purpose should be clearly reported together with the design, goals and, not least, estimated cost of the incentive scheme.

LO does not consider it reasonable for boards to be included in incentive schemes. It is not compatible with the supervisory role of the board for its members to have an economic interest in the company. The members of the board should receive fixed remuneration clearly linked to the work contribution, for example in the form of the number of hours worked.

4 Industrial policy in the form of credit policy

The question of whether the Swedish trade union movement, as is the case with some of its sister organisations around the world, should contribute risk capital to small and medium sized companies, for example, is an issue that is still being discussed. Many people believe this would be in the nature of employment creation, thus benefiting trade union members. Thus it is a matter of supplying capital to areas where it is thought that the market has failed.

4.1 *Supply of capital – basic rationale*

In a closed economy, investments come from the saving that takes place within the country. In such a case the volume and structure of savings determines the volume and structure of investments. However, Sweden is a (small) economy which is open to the world through free capital flows, for example. The supply of capital to investments in Sweden is therefore not restricted to savings mobilised in the country, but is affected by the net flows coming from outside. In many individual years in the 1990s and early 2000s Sweden had considerable net inflows of capital in the form of direct investment from abroad.

The conditions for corporate financing are determined in the international capital market. The supply of capital in the market, or rather the required return, is governed by the risk-free real interest rate (nominal interest rate minus expected inflation). The higher the real interest rate, the higher the required return on production. This is because the alternative for an investor is to buy real interest bonds and thus utilise the real interest rate return. The cost of investment capital in Sweden in relation to other countries, and thus the level of capital supply to extend or maintain our production and infrastructure, is mainly governed by factors such as the exchange rate and inflation risk in the Swedish economy, together with how good conditions are judged to be for growth in the economy as a whole (market risk). Apart from this, individual companies' supply of capital is affected by the risk associated with an investment in the company in question (company-specific risk).

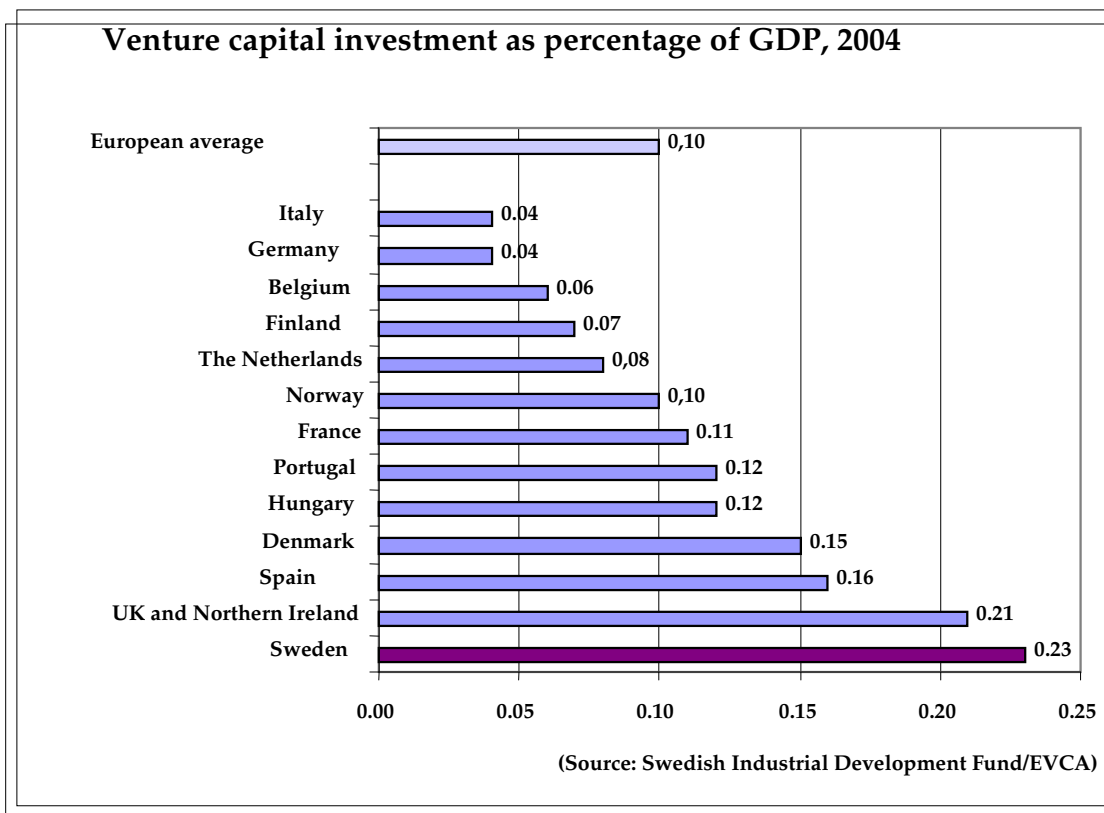
Estimating companies' future profits and consequently the return on investments, of course entails considerable uncertainty. The risk of a worse (or better) outcome must be included, as well as the risk of inflation being higher (or lower) together with any expected changes in the exchange rate.

A relatively new element is that companies' strategies on ethical issues are included in many fund managers' risk concepts. More and more market players believe that companies without ethical guidelines and strategies to handle that type of risk are not worth investing in. This means that more people believe that the existence and implementation of an ethical policy is a condition for a high long-term return and a low risk level in a portfolio. This can be linked both to the market risk concept and the company-specific risk concept – i.e. investments in a specific country that is not a democracy or in an industry characterised by major environmental risks, or in a specific company whose workers are not treated in accordance with international standards.

Moreover, other investors, in the same way as banks and credit institutions, must take the credit risk into consideration for certain types of investment. This means quite simply taking into account the repayment capacity when lending or the payment flows in a company. The key factor here is information. Perfect information results in a perfectly functioning market. However, we do not have a situation with perfect information about all conceivable investment projects. The consequence of this is that it is very difficult for banks to make risk assessments of different types of company projects and this in turn means that banks in general are very cautious. This would restrict the supply of capital severely, were it not for the fact that there are investors who are prepared to take a greater risk.

4.1.1 Risk capital/Venture capital

The term risk capital really refers to all investments in companies' equity. The risk refers to the fact that shareholders' risk is in fact greater than that taken by banks when they lend money or for example by suppliers when they act to get their share of the profit. In Swedish the term is used synonymously with the term venture capital to describe investments in unlisted companies' equity. The Swedish venture capital market (investments in unlisted shares) has developed at a rapid rate since the middle of the 1990s and the number of players is estimated to have doubled, while the capital managed has multiplied many times over. The Swedish venture capital market is estimated to be worth about SEK 220 billion (2003). Generally speaking there is no lack of venture capital in Sweden today. According to a report from the European Private Equity and Venture Capital Association, in 2004 Sweden was the country in Europe with the highest percentage of venture capital investment in relation to GDP.



4.1.2 Market imperfections?

Individual markets that do not function well may have major macro-economic consequences. If the credit market does not function perfectly, this means that certain unprofitable investments are made while some profitable projects are not undertaken. The supply of capital rests partly on assessments of risk, inflation and exchange rates. These factors can of course be wrongly assessed. When lenders make risk assessments that are wrong, the entire stability of the economy may be jeopardised, leaving typical effects such as property bubbles and bank crises in their wake.

Even if the Swedish capital market is entirely deregulated and an integrated part of the international market, it cannot be claimed that every single part is fully internationalised. There are probably substantial elements of inertia between the international capital market and the supply of venture capital to non-listed companies. A number of small companies and sole traders will thus not gain access to capital in the credit markets, among other things because a hallmark of such markets is that buyers and sellers have different information on the risk posed by the borrower. Lenders are reluctant to take risks and this will mean that some customers will not be granted any credit at all, even at a sky-high interest rate.

An example of how trade union organisations can contribute to a well-functioning credit market is when they are members of local credit guarantee associations (KGF). Through its local and regional knowledge of companies and people the trade union can have an information advantage that complements existing capital supply.

Local credit guarantee associations are found in an increasing number of places in Sweden and often have LO districts and national union branches as members. The association functions as a link between banks and small and medium sized companies and other actors involved in business development. KGF act as guarantors for parts of loans raised by companies from banks. Apart from financing help, KGF also arrange advisory services and exchange of experience.

We will come back to the fact that buyers and sellers have different information about the risk the lender constitutes. Information also has a price. The supply of information is worse and harder to appropriate for an investor when it comes to investments far from the stock exchange. This means in most cases that special competence and special resources are needed to review these investments and their potential.

It is important that the conditions for financing and credit are equal, regardless of where in the country a business operator is located. If this is not the case, it may lead to shortages of available capital for productive investments, which in the long run affects the country's growth. At present in Sweden we have a series of public sector actors whose task it is to solve that problem, for example by means of credit guarantees or other instruments. They then take over risk from the private sector and bear its cost.

4.1.3 State venture capital actors

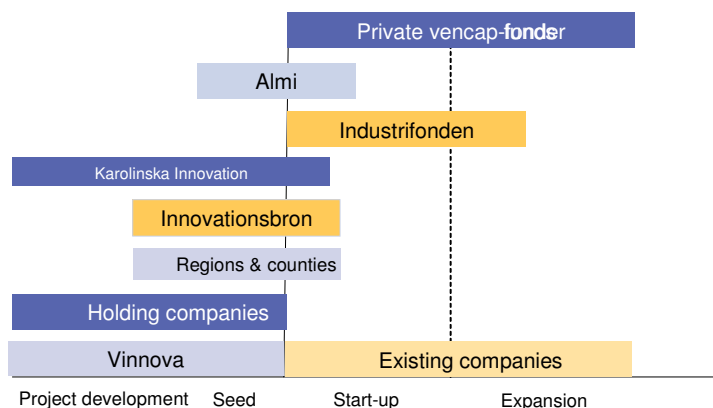
The state facilitates the supply of capital to small companies, for example via ALMI Företagspartner AB. ALMI is also represented in each county so as to be more closely informed about companies around the country. Their most important task is to supplement the financial infrastructure in areas where there are now deficiencies.

Moreover, NUTEK (the Swedish Agency for Economic and Regional Growth) has been responsible for *seed financing*. By this is meant financing of technical development projects at an early stage. This programme is to contribute both to the growth opportunities of small and medium size companies that run technical development projects and to supporting innovators and entrepreneurs who want to start new companies. These activities are now dealt with by the newly established group "Innovationsbron AB" and are mainly directed at linking institutes of higher education with the business sector, i.e. contributing to commercialisation of research results.

The government foundation Industrifonden has existed since 1979. The fund helps finance small and medium-sized companies. The fund also involves itself as an active minority shareholder, thus also contributing competence and long-term commitment.

The Swedish innovation system

Financers/providers



 Industrifonden

In Sweden we also have the substantial public pension capital held by the National Pension Funds. They invest in various forms of production with different time horizons. However, they are severely restricted as to the size of their Swedish shareholdings and the power of ownership they may exercise. This is governed by law. However, one of the funds, the Sixth AP Fund, has a clear emphasis on investment in private equity funds in the venture capital segment, with a Swedish or Nordic focus.

The National Pension Funds must, according to LO, provide the greatest possible benefit to the pension system. The political system has also set up restrictions as to how the funds' risks must be balanced and limited; they may not invest at too high a level of risk. Such an overall goal means that they cannot naturally fill a function involving lifting risk from private lenders, which investing fund assets in small and medium sized unlisted companies may mean. Investments with a narrow regional limitation and emphasis on specific companies have by definition a worse diversification of risk and thereby carry a higher risk. The National Pension Funds are directly deprived of the possibility of having industrial policy or other economic policy objectives.

As far as the trade unions are concerned, the most important thing to focus on in this context is the pension outcome. The size of the pension outcome is determined by the possibility of maintaining a long-term investment strategy and – as regards private fund managers – that the fees paid by pension savers are kept as low as possible.

4.1.4 Institutional and industrial ownership

Ownership can be roughly divided into different categories, where institutions, including the state, industrial owners and venture capitalists can be distinguished as the most important actors. The difference between industrial and institutional ownership can be

described as follows: an industrial owner's objective is to create value added while an institutional owner's objective is to meet its customers' demands for a return on their capital. If institutional ownership is of central importance for capital supply, industrial ownership is important for business development.

Swedish trade and industry typically has a high proportion of collective ownership, via extensive pension savings. As a percentage of the market value, institutional ownership (mainly consisting of public pension and savings capital) is about 20 per cent and foreign ownership accounts for about 33 per cent. Institutional owners and their role are often focused on. They are criticised for being far too short-sighted and not taking responsibility as owners, for "voting with their feet" if they are not satisfied with the growth in value and dividends. A more long-term view may possibly be desirable, but at the same time their role as asset managers does not allow them an active ownership responsibility. The question is whether ownership responsibility is compatible with their role as managers of pension funds, for example. Even if short-termism has increased through greater institutional ownership, there are fund managers who have a longer perspective, such as the National Pension Funds.

The National Pension Funds should themselves, in the framework of the present regulatory code, develop a clearer ownership role. Those who manage Swedes' pension savings should take more responsibility for ensuring companies' compliance with ethical rules and international codes of conduct. This may to a greater extent actively promote greater long-termism and will in turn benefit long-term growth in value in Swedish companies.

Institutional ownership, Swedish and foreign, plays a role first and foremost in capital supply. Increasing foreign ownership in Swedish trade and industry, together with the fact that institutional ownership has increased, probably also affects the conditions for economic development. A direct effect of foreign ownership is that when a parent company is bought by a foreign owner the trade union representation on the parent company's board disappears, even if the subsidiary is still established in Sweden. This means that the trade union loses the possibility of participating in the important decisions that are made at central board level. In groups with at least 1,000 employees operating in at least two EU states, there must be a "European Works Council" for information and consultation with employees. This is, however, only a weak form of co-determination and cannot be compared with direct board representation.

Institutional foreign ownership operates in other respects mainly on the same principles as national institutional capital. Value growth is the crucial factor and they do not take active ownership responsibility in the companies.

One aspect that will have greater significance in attracting institutional capital in the long term is the ethics issue. There is increasing pressure on fund managers from their owners to take into account how companies live up to ethical principles. The question of codes of conduct will therefore become more important for institutions' analysis and evaluation of companies for investment decisions and thus for companies' capital supply.

Conclusions: Increased ownership responsibility and greater trade union influence on capital

Developed ethical rules

The initial goal of drawing up ethical investment rules is for LO and its affiliates to choose a particular investment policy via direct influence, thereby having an impact on companies. The next goal is to also influence other owners to pursue the same demands as LO.

The overall requirement of LO's own investment should be a sound long-term return with good diversification of risk and low total risk level. This requirement is also the most important in other contexts when discussing management of employee capital.

The ethical policy focusing on trade union rights which LO adopted in 2000 should still form the framework of the demands LO makes of companies and of other investors.

In this context, LO should urge all investors to report their ethical rules and give an account of how they are working to follow them up (see Share Ownership Policy below). The main thrust of LO's continued work will thus be towards general demands and restrictions for all companies and fund managers. LO should focus on the area of workers' rights.

In the light of this, the working group proposes that LO's own ethical guidelines be **supplemented** by:

- The UN Weapons Convention
- Exclusion of out and out pornographic industry
- Worker participation related parts of the ILO Tripartite Declaration of Principles concerning Multinational Enterprises, in accordance with its sections 55-57
- The UN Universal Declaration of Human Rights, and
- The UN International Covenant on Civil and Political rights (1966)
- The UN Convention on Economic, Social and Cultural Rights (1966)
- The UN Framework Convention on Climate Change including the Kyoto Protocol
- The Vienna Convention on the Protection of the Ozone Layer including the Montreal Protocol
- The Basel Convention on Transboundary Movement of Hazardous Waste
- The Stockholm Convention on Persistent Organic Pollutants

Even if a country has not ratified the ILO Core Conventions, LO would nevertheless expect that a company in which it has a holding would comply with the central ILO Conventions, or other instruments directed at states included in the ethical policy.

In the area of environmental conventions – which also are primarily directed at governments—experience of interpretation and control at company level is particularly

limited, and therefore it is a matter of general compliance with the intention of the conventions.

For example, to the extent media companies run operations that can be linked with pornography these should be carefully regulated.

LO does not consider that there is anything to indicate that the ethical policy pursued by LO conflicts with the requirement for a good return. The fact that these criteria are used to exclude companies rather implies that we vouch for a good long term return on the portfolio.

As regards the risk level of investments, LO's view is that it should be kept low. However, we do not consider that there is any long-term conflict between fulfilling our general ethical criteria and the limited risk requirement.

The work of an augmented ethical policy should mean that LO and its affiliates – apart from the requirements of their own investments – are imposing clearer demands on Swedish fund managers, above all on boards where they are now represented. This applies to AMF, Folksam, Folksam LO and AFA, as well as any other companies in which representatives of LO may be included.

At present the following statutory requirements apply to the National Pension Funds: “Management of the funds must not be influenced by prevailing government policies, either industrial or economic. *Consideration must be given to the environment and ethics when investing, without compromising the overall goal of a high return*”.

LO believes that the ownership policy of the National Pension Funds should be representative of how the Swedish population approaches these issues. At present each fund formulates its own view of ethics and corporate governance. In this light, LO considers that the Riksdag should determine a framework for the National Pension Funds' ethical guidelines and ownership policy. This does not mean that current legislation should be changed, only given a more specific content. This may function as very important standard-setting for other investors.

In their annual evaluations, the Government and Riksdag should demand detailed reports on the implementation of ethical and ownership policies in the National Pension Funds.

Good controls and follow-up systems for ethics and corporate governance

LO believes that the ethical policy in each fund management company over which LO exercises a direct influence should be monitored through an open and transparent, formalised follow-up procedure and a strategy established for how investments that conflict with the policy should be handled when discovered. In other companies, those who represent LO must make efforts to ensure an ambitious and transparent follow-up process of ethical policy.

Hence LO believes that ethical investment regulations are not complete without a formalised method for control and follow up. This method should also be reported openly so that third parties can examine its effectiveness and accuracy.

An important background is that governments have the principal responsibility for ensuring that all work carried out in a country respects basic workers' rights and the ILO core conventions. They are also responsible for ensuring that other international, universal instruments are respected, as well as ensuring compliance with national legislation. One ILO demand is that countries set up labour inspection systems to exercise this supervision. The demands in the LO investment regulations are, however, directed at companies, based on the conventions.

As regards examination and reporting on compliance with trade union freedoms and rights in countries and companies, LO's view is that the only really reliable sources are the ILO, the ICFTU and the International Trade Secretariats. LO should aim to influence the screening companies to use the ILO, ICFTU and the global union federations as well as TUAC/OECD as sources for increasing their knowledge of issues concerning workers' rights.

In its investment regulations LO should make efforts to draw attention to and promote global framework agreements as instruments of control and follow up, since they are a way of following up the OECD Guidelines for Multinational Enterprises.

LO should call for a clearer role for the ILO as monitor of international conventions that countries have ratified.

There is an LO Congress resolution from 2004 to take measures to ensure that internationally binding rules for the conduct of multinational enterprises are established. This would create neutrality of competition and the risk of dumping of working conditions would be reduced in the hunt for investments.

Exit or voice?

There are two main ways to react to a company's non-compliance with established ethical criteria: One is to shoulder the owner's responsibility and try to make the company change – VOICE. The other is to wind up the holding – EXIT. Both of these are used by the trade unions today. Not directly withdrawing from an investment, but rather conducting a dialogue is closest to the trade union's method of exerting influence in other contexts – i.e. negotiation and agreement, and if this is not possible, industrial action. In a follow-up process the steps to be taken before winding up a holding should be specified.

LO's view is that there should be a clear strategy for how fund managers should act when irregularities are discovered in companies. This does not necessarily mean immediate exclusion, but exclusion from the portfolio should, however, be a final alternative.

The international trade union movement can recommend winding up holdings in certain companies. How such demands should be handled should be part of the follow-up process for LO's ethical policy.

When a company behaves very badly, in the end it usually becomes known to the public via the media. This does not guarantee, however, that investors have taken measures against the company, for example in a dialogue or by winding up their holdings in that company, even if the company's ethical policy indicates such action. LO board representatives should actively urge openness in sanctions processes. Such actions should be coordinated within LO and its affiliates.

In the long term LO can, via international cooperation in the ICFTU and TUAC, contribute to creating a supplementary control system that focuses on trade union rights. Here there is also a formalised trade union network that makes joint action possible. LO should continue to support this work and contribute to its development.

A developed share ownership policy

In the future LO should supplement its ethical policy with a corporate governance policy. This should focus on the areas in the Swedish Code of Corporate Governance which LO deems to be central for companies' fulfilment of their responsibility towards shareholders.

LO's share ownership policy should function as a guide to trade union people serving on boards or with shareholder influence.

We propose that LO selects the following areas:

- The responsibility of the board for ensuring that necessary ethical guidelines are established for the conduct of the company.
- The recruitment and composition of the board.
- Remuneration issues.
- Apart from the corporate governance matters included in the code, LO demands that a report is given on whether the eight ILO fundamental conventions on workers' rights and the OECD Guidelines for Multinational Enterprises are being followed.

Gender equality

LO believes that the current Code of Corporate Governance should be used as an opening for gender equality work in this area.

Recruitment to boards should be linked to specific gender equality work in this phase. The objective should be to achieve equal gender distribution (40/60) and in each recruitment process this should be included in the requirement profiles for recruitment of new members. To make this clearer, the nomination committee should give a clear account of its efforts to achieve this objective in its recruitment. Hence it is not sufficient to report the result - the route taken to achieve it must also be transparent.

Competence testing and evaluation of board members will be a very important element of this process, because then men and women can be evaluated on the same grounds. This work should be subsequently evaluated.

If instead a picture emerges of deficient gender equality work in recruiting processes, legislation for a quota system should be considered as a sure way of influencing this issue in the right direction.

The requirement for a reasonable system of remuneration

Bonus programmes and incentive programmes are used in many contexts to give company management more interests in common with those of the company. For a long period it has been difficult to gain an overall view of the size and scope of these programmes. For employees, the most important view on remuneration to company management is that it must be reasonable and in relation to performance, regardless of the form it takes.

LO's view of incentive schemes for employees and company management can be summarised as follows:

- Companies should as a general rule be restrictive with incentive schemes in addition to wages, salaries and pensions.
- The scheme must have a clear purpose which is in line with a long-term strategy for remuneration and which promotes the company's long-term development.
- Remuneration must be linked to performance in the form of clear and measurable goals. These goals must be determined in advance.
- The performance goals must be set in relation to a reference portfolio, i.e. how the company performs in relation to competitors in the same industry.
- The costs of the remuneration schemes must be reasonable and there must be a remuneration ceiling.
- The time-frame of the scheme's dividend distribution must stimulate a long-term perspective, for example by being based on an average outcome over a number of years.
- Remuneration must be reported clearly and fully in the company's annual report.
- All the points above must be communicated to the shareholders and a resolution passed at the general meeting. The purpose should be clearly reported together with the design, goals and, not least, estimated cost of the incentive scheme.

LO does not consider it reasonable for boards to be included in incentive schemes. It is not compatible with the supervisory role of the board for its members to have an economic interest in the company. The members of the board should receive fixed remuneration clearly linked to the work contribution, for example in the form of the number of hours worked.

Sound long term return at a low risk

Even in the future, with a revised or supplemented view of share ownership issues, it will be important to LO as a collective to maintain the importance of required return as the overriding goal for investment policy. Of course this will be done while considering the desired risk. In this area it is reasonable to have a low risk profile, because for the most part it concerns management of funds that may need to be used in future industrial disputes, in the case of the affiliates' own capital, and in a larger context, pension capital and other insurance capital belonging to the members. How capital is invested must then to a great extent be governed by the level of risk chosen.

Companies' strategies on ethical issues form part of many fund managers' risk concepts. More and more market players believe that companies without ethical guidelines and strategies to handle that type of risk are not worth investing in. This means that more people, including LO, believe that the existence and implementation of an ethical policy and a corporate governance policy are conditions for high long-term return and a low risk level in a portfolio.

In the short term there may of course be cases where there are investments that bring a higher rate of return, but which do not comply with LO's requirements. In the long term we consider that the goals of good return and clear ethical requirements, as well as demands for a clear corporate governance policy are fully compatible.

Industrial policy in the form of credit policy

The low risk requirement precludes LO or its affiliates from undertaking major roles in the venture capital market. Sweden has an extensive and by and large well-functioning venture capital market. Moreover, we have a number of state institutions that lift risk away from private actors. In cases where individual companies and people cannot gain access to capital on the credit markets, this is because the risk of the individual investment is too high, even for these venture capitalists.

One reason for difficulties in getting credit is that buyers and sellers have different information on the risk the lender constitutes. Information also has a price. The supply of information is considerably worse and harder to appropriate for an investor when it comes to investments far from the stock exchange.

To the extent the trade union has an information advantage in relation to the rest of the capital market, it may be possible to enter into this type of operation. The existence of such a situation or not can only be judged by the individual fund manager at the time. Today there are some LO districts that are involved in this through membership of local credit guarantee associations.

If the trade union is to have or advocate investments that involve greater risks and require more information processing, the capital should not be taken from funds that may later be needed for industrial action. Nor can we ask that investments earmarked for future pensions be used for this purpose.

To the extent that calculations show a surplus return in relation to targets set it is always possible, however, to use this money for other purposes, such as industrial policy or regional policy goals. There is also scope for creating special funds in which individual participants are able to choose one venture capital investment rather than another.

LO believes that it is important to discuss how short-termism in the business world can be balanced with initiatives for increased long-term development of Swedish trade and industry. However, it is not reasonable to demand a long-term perspective in all investments. If a long-term perspective is to be required for more types of investment, this should also be weighed against other demands, for example in terms of liquidity. When investments are made in the context of pension funds the time frame in which the money will be needed to pay pensioners should also be borne in mind. If pension capital is used to achieve a more long-term perspective, this should be done on the basis of the restrictions imposed by a desirable required return at a given risk level.

As far as the trade unions are concerned, the most important thing to focus on in this context is the pension outcome. For an individual this is largely determined by his or her own total working life, or that of others as regards the public system. The size of the pension outcome for funded pension plans is determined by the possibility of maintaining a long-term investment strategy and – as regards private fund managers – keeping fees paid by pension savers as low as possible.

APPENDIX 1

The LO investment regulations, adopted on 7 June 2004**1. A general requirement is that capital and investment is to be avoided in:**

- a) Operations that are in violation of Swedish or foreign legislation, i.e. the operation may not violate Swedish law in Sweden or to the extent it is applicable outside Sweden, and of course neither violate the laws of the country concerned when operations are run abroad. In that way operations are avoided that can be associated with violence, drugs, prostitution, child labour, irresponsible marketing, environmental pollution or other criminal activity.
- b) Operations conducted under unacceptable working conditions or which prevent trade union organisation (defined in accordance with the ILO core conventions and the OECD Guidelines for Multinational Enterprises)
- c) In 1998 the international community settled the grounds for the adoption of its Declaration on Fundamental Principles and Rights at Work and its follow-up. The Declaration has been ratified by all 175 member countries of the ILO (International Labour Organization) as well as by representatives for the countries' employers and employees.

The ILO core conventions are as follows:

- No. 87. Freedom of Association and Protection of the Right to Organise
- No. 98. Right to Organise and Collective Bargaining
- No. 29. Forced Labour
- No. 105. Abolition of Forced Labour
- No. 111. Discrimination (Employment and Occupation)
- No. 100. Equal Remuneration
- No. 138. Minimum Age
- No. 182. Worst Forms of Child Labour