

# Chapter 9

## Workers' capital, corporate governance and social responsibility

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### 1. Introduction

A recent Towers Watson overview of pension fund assets worldwide shows that at the end of 2012 pension funds in the 13 major markets (of which the US is by far the greatest and covers more than half of the total volume) own almost USD 30 trillion in assets, which corresponds to more than € 25 trillion (Towers Watson 2013). This amount is almost 80 per cent of the GDP of these 13 countries, and in some countries pension funds own more than GDP (in the Netherlands 156 per cent of GDP). Almost half is invested in equities, which means that, taking the global market capitalization figure of the WFE at the end of 2012 of USD 54.6 trillion, that roughly a third of the stocks worldwide are owned by pension funds (World Federation of Exchanges 2013). Thus it is not exaggerated to say that workers have a large share in capital. But – dispersed and intermediated as it is via pension funds and their asset managers – they are still far from ‘ownership’ of this stock and from exerting influence.

In this chapter I sketch some trends in the direction of a more active ownership by pension funds and other large institutional investors as well as a broader focus than only on profits and shareholder value. These trends make me optimistic about the opportunities and chances for workers and their trade unions and pension fund trustees to increase their influence on corporate behaviour and social responsibility. In a presentation that I gave in the summer of 2011 for trade unionists in a Transatlantic Social Dialogue in Inzell, Germany I introduced ten-plus-one commandments, that in my view are still more than topical and will hopefully be followed up on both sides of the Atlantic.

## 2. Trends

In the attitude and behaviour of pension funds (and to a certain extent also of other institutional investors like mutual investment funds, sovereign wealth funds and insurance companies) I see two important trends.

The first is that they move from a traditionally very passive to a more active role vis-à-vis the portfolio companies and other asset classes in which they invest. With ‘active’ in this context I do not mean the short term oriented ‘activism’ that hedge funds have displayed in recent years. ‘Passivism’ with the double connotation of ‘more active but peaceful’ may be a better term for the way pension funds deal with their shareholders’ rights, taking into account the fact that for prudential reasons they possess widely diversified portfolios all over the world.<sup>1</sup> An exemption to this is the Norwegian Government Pension Fund Global (often in short called Norges) that invests in equities outside Norway and holds packages of around two per cent of some 60 big European listed companies (NBIM 2011). They target these companies for an active dialogue and their engagement in some cases leads to exclusions of investing in specific companies. Another example of a more active involvement in dialogue and shareholder meetings is how Dutch pension funds and a growing number of other institutional investors coordinate their policies for participation and voting at annual general meetings of shareholders (AGMs) of Dutch corporations through an association called Eumedion.<sup>2</sup> PGGM, the second largest Dutch fund, has announced that it will drastically reduce the number of its portfolio companies. Pension funds are also increasingly participating in collective redress legal actions against fraud, misinformation, mismanagement or other corporate failures, not least against the Wall Street banks that sold them the subprime and other risky securities with which the crisis started.

The second trend is that the originally predominantly Anglo-Saxon approach to corporate governance, embedded in for instance the ICGN (International Corporate Governance Network) and UK and other national codes, is gradually shifting to an approach that is focusing more on the substance and content of companies’ (long-term) strategies: long-

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1. ABP, the largest Dutch pension fund with assets of almost € 300 billion, owns shares in more than 4000 companies worldwide (ABP 2013).
  2. See <http://eumedion.nl/en>

term value instead of short-term share price (ICGN 2009). The original Anglo-Saxon approach based on the so-called 'principal – agent theory' did contribute a lot to improve transparency, disclosure and shareholder voting rights, issues that traditionally are considered to belong to good corporate governance (CG). Now it is extended to companies' ethical, environmental, and social behaviour, their so-called corporate social responsibility (CSR). Pension funds (sometimes triggered by public unrest over irresponsible practices) are defining their ESG (ethical/environmental, social and governance) policies, backed by international guidelines and standards like UNPRI<sup>3</sup> (United Nations Principles for Responsible Investment, the counterpart for investors of the UN Global Compact for the corporate sector) and the Global Reporting Initiative's GRI-G3 reporting standards.<sup>4</sup> There is also a rising movement to integrate financial and non-financial reporting in order to give investors and other stakeholders more in-depth information relevant for sustainable longer term value creation, instead of only quarterly financial figures.<sup>5</sup> The specific focus and methods of different pension funds and fund managers may differ and range from straightforward exclusion on ethical grounds (e.g. cluster bombs/weapons production, animal welfare, pollution) to intensive dialogue with management and (supervisory) boards of the companies. Topical issues at the moment, in which supervisory boards and independent directors have a major role to play, are the nomination and remuneration of top executives. These are issues in particular where in my view (as described in an article in *Transfer*) trade union trustees in pension funds and employee representatives in works councils and in company boards can work together and complement each other (Van den Burg 2011).

### **3. My ten commandments**

1. Let's first and foremost make a better use of the potential powers of workers' capital worldwide: coordination and cooperation within the EU (ETUC) and worldwide (Committee on Workers' Capital CWC and TUAC) should be reinforced. Individual pension funds only own very minor packages of stock per company (even Norges

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3. See <http://www.unpri.org>

4. See <http://www.globalreporting.org/Home>

5. International Integrated Reporting Council, <http://www.theiirc.org>

hardly reaches more than one or two per cent of shares per company); so only together can they make a fist with their total of one third of all equities worldwide!

2. Stimulate individual pension participants (and trade union members) to lobby for responsible behaviour of their pension funds, and not less so of the banks, mutual funds and insurance companies that manage their pensions and savings. The UK ShareAction campaign<sup>6</sup> is a good example of how to mobilise and influence behaviour in the financial sector via campaigning on for instance ‘just pay’ and living wages.
3. Do not focus only on defensive action alert themes such as the WalMart or Sodexo campaigns of CTW and SEIU that of course are important and have proven and still will prove their effectiveness; pension funds’ mobilizing and voting strength should be capable of influencing also pro-actively the broader strategies and policies of companies worldwide with respect to remuneration and compensation, sustainability, supply chain responsibility, or lobbying and political party funding.
4. Strengthen the lobby of pension funds and other long-term oriented responsible investors on major regulatory issues like fighting tax evasion and adapting company and tax law, or reorienting prudential regulation and supervision, as well as accounting and auditing rules from their currently predominantly short-term focus into a direction that better supports and promotes long-term responsible investing.
5. Promote Public Private Partnerships of pension funds with regional and local authorities and governments to invest in the necessary public and social infrastructure (transport, housing, education and healthcare). A win-win situation may be created if governments provide the funds with a hedge against future inflation, which is of major importance for pension funds’ risk management to match their future liabilities. The EU 2020 Project Bond Initiative, recently set up by the European Commission and the European Investment bank to issue infrastructure bonds, is an example to be followed worldwide and at several levels (European Commission 2014).

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6. See: <http://shareaction.org>

6. Apply ESG policies and norms not only to the equities portfolio and the behaviour of portfolio companies, as is now almost exclusively the case, but also to the other asset categories in which pension funds invest. Real Estate for instance is an interesting asset class, in which financial revenues can be combined with major environmental results: CO<sub>2</sub> reduction, transfer to sustainable timber and other materials and energy saving and green buildings. In particular I would very much like to see critical and fundamental ESG attention to what is often entitled as 'Alternative or Innovative Assets'. This asset class in which pension funds increase their investments covers (among others) private equity (PE), hedge funds and other complex financial products that we got to know in recent years (derivatives, CDOs, etc.). In the PE and venture capital world ESG is gradually becoming an issue. The international organization of PE firms has formulated its own ESG guidelines, which some firms seem to take more seriously and build into a profitable strategy. A win-win situation can be achieved for instance with investing in sectors that defaulted due to preceding catastrophes.
7. Let's try to develop alternatives for and at least exert much more influence on the financial market service providers that make high profits with pension fund (and corporate) money: the vast number of advisors, law firms, audit firms, proxy voting firms, credit rating agencies and above all the bulge bracket of global investment banks that dominate the top of the market. Goldman Sachs, JP Morgan and the like, but also the Big Four audit firms, the rating agencies (Standard & Poor's and Moody's) and the proxy voting and advising agency ISS/Risk that serves both the investors and the portfolio companies, form global oligopolies that the biggest pension funds and listed companies can hardly avoid.
8. Pension funds should explicitly declare their interest in a drastic reform of the financial markets where systemic risks are reduced, where financial institutions are directed back to basics again, where long-term investing is stimulated and short term gains are discouraged through (among other things) a financial transactions tax (FTT), where the regulatory capture of governments and supervisors by Wall Street, London City and the other national financial centres will be broken by a strong international cooperation against moral hazard and too-big-to-fail arrogance and anti-trust measures against the dominant oligopolies. If this would sound too political, the

simple and a-political argument for pension fund trustees is that the funds' interest is to drastically reduce the huge fees they pay into the financial firms: calculated over the 40-50 years horizon of a future pension every one per cent fee means a 30 per cent reduction of the final pay out of pension benefits after retirement!

9. Trade unions and pension funds should increase their expertise and lobby activities regarding financial markets and banking regulation and forge alliances with other long-term investors, consumer groups and civil society to create some countervailing power to the hugely influential financial lobby in Washington, Brussels, London and elsewhere. Finance Watch in Brussels<sup>7</sup> is a major step in that direction; a similar initiative across the Atlantic is Better Markets.<sup>8</sup>
10. Do not expect everything solely from regulation and legislation. There is quite some activity going on in the financial and corporate sector in the field of self-regulation: codes of conduct, guidelines and charters, etc. Don't throw this all away as being not serious and not sufficiently binding. Serious voluntary commitment to internal standards is often a much more sustainable and reliable basis for intrinsic better behaviour than external norms and sanctions. It is worthwhile to explore the possibilities of self-regulation and to use the position that trade unions and workers inside companies possess, to exert influence on properly executed and monitored self-regulation.
11. My final – extra – eleventh commandment may perhaps sound strange for an ex- politician (who by the way never has stopped being a trade unionist). I added it during the Transatlantic Social Dialogue conference in Inzell, Germany, where I observed that some participants strongly pleaded for mobilizing and organizing activities, but focussed their campaigns predominantly on legislative demands and political lobbying. I have noticed that as well in Robert Reich's book on the Supercapitalism of our times. Although I share his brilliant analysis about the capture of Congress and the White House by Wall Street, I was surprised about one of his conclusions. He is quite outspoken in not believing in internal reform within the corporate sector towards real corporate social

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7. See [www.finance-watch.org](http://www.finance-watch.org)

8. See <http://www.bettermarkets.com>

responsibility. He puts all his stakes on reforming (or revolutionising?) the political democracy that – as he and others have rightly stated - has been overtaken so overwhelmingly by the corporate and financial sector. I would argue that trade unionists and workers through their positions inside these companies, in works councils, sometimes in (supervisory) boards, but also via shareholders' stewardship, dialogue and engagement of the pension funds in which boards of trustees they participate, have a major chance and challenge to exert considerable influence on changing corporate behaviour and strategies from within. My last recommendation thus would be to fight capitalism in its own quarters and ranks and not to rely exclusively on democracy and politicians!

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