The European Commission,

Directorate-General for Justice and Consumers: JUST-CLEG@ec.europa.eu

Att.: Ms Saala Sastamoinen, acting Director-General: saala.SASTAMOINEN@ec.europa.eu

Ms Maija Laurila, Head of Unit for Company Law: Maija.Laurila@ec.europa.eu

Re. the European Commission's public consultation on sustainable corporate governance

Swedish Institutional Owners Association SIOA (Institutionella Ägares Förening, IÄF in Swedish), is an association with 16 of the largest institutional shareholders in Sweden[1]. The aim of the organization is to promote a sound development of the self-regulation in the Swedish stock market. IÄF includes among its members pension funds, insurance companies and fund managers representing approximately 20 percent of the Swedish stock market and with significant holdings in European companies. Some of us are investment managers and others are asset owners, but we would all describe ourselves as investors with a long term perspective.

The, SIOA requests its response to this consultation to be accepted in the form of this letter rather than through the web-based questionnaire. The reason is that we find it not feasible to express our opinion in a comprehensive way in the questionnaire due to its narrowly defined scope and biased design in favor of certain preconceived views of the underlying problems and their conceivable solutions.

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[1] AFA Försäkring, Alecta, AMF Folksam, Länsförsäkringar Fonder, Skandia, Didner & Gerge Fonder, Lannebo Fonder, Första AP-fonden, Andra AP-fonden, Tredje AP-fonden, Fjärde AP-fonden, Handelsbanken Fonder, Nordea Funds Ltd, SEB Fonder, Swedbank Robur Fonder

It is, for example, impossible for us to choose between believing on one hand: *"that corporate directors should balance the interests of all stakeholders […] and that this should be clarified in legislation as part of directors' duty of care"* and on the other hand that they should be *"focusing on the short-term financial interests of the shareholders"* (Question 8), since we strongly disagree with both these alternatives.

We want to underline, that the SIOA is a supporter of sustainability and of the mounting interest among many companies to take a broader responsibility for possible adverse effects on the surrounding society of their operations than what has been the case in the past. We also share the Commission's underlying objectives, fighting climate change and promoting human rights must certainly be top priorities for the European Union and each of its member states.

Certainly in many parts of Europe, it is today common practice among large companies to consider – in their own long-term interest – a wide range of sustainability aspects as an integral part of their business strategy, and many invest considerable amounts of time and money into the advancement of bold new projects aimed to alleviate their "footprint" on the physical environment as well as other aspects of the surrounding society. This is often done by demand from institutional owners. The attitude is also becoming the norm in smaller and medium sized companies in the business community. Among many start-ups sustainability is the very essence of their business model.

Although we believe that the bulk of societal measures to support and speed up this development is best undertaken at the national level, the SIOA also believes that well-targeted actions may also be warranted at the EU level, provided they are based on robust empirical evidence and respect the right to property according to the European Treaty as well as fundamental principles of the governance of companies and of the market economy. Unfortunately the initiative taken by the Commission regarding sustainable corporate governance does not fulfils these criteria's:

> ***First*** it would in our opinion be illegitimate according to the European Treaty to impose EU legislation on the basis of such inadequate empirical evidence as that which has been presented regarding the sustainable corporate governance aspects of the outlined intervention, generally referred to as the EY study. This study has been repudiated as totally unfit as evidence-basis for EU-level regulation by a wide range of highly distinguished commentators, a view that we entirely share as explained in our letter to the Commission of 30 September last year. In fact, in various discussion forums even representatives of the Commission have acknowledged the shortcomings of this study, referring instead to "other evidence" at the Commission's disposal (which, however, still remains to be publicly disclosed), and urging participants to supply any evidence available to them that might call the views expressed by the EY study and the Commission's ensuing Inception Impact Assessment in question.
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> In response to this request we would like to refer to a recent study at the Stockholm School of Economics (SSE),[2] a highly ranked academic institution in the field of Corporate Finance (attached to this letter). The study shows that (i) corporate short-termism is a much more complex and multi-faceted issue than what is asserted in the

[2] Carlsson-Wall, M., Eugster, F, Hjelström, T. and Nilsson, H.: *Corporpate Governance and short-termism: An in-depth analysis of Swedish data.* Stockholm School of Economics, 2021.

EY study, (ii) that pay-outs to the shareholders is at any rate no reliable indicator of short-sightedness in business management, and (iii) that very weak signs of financial short-termism could be observed among Swedish companies.

Second the purpose of capital markets is to re-allocate capital from companies that lack profitable investment alternatives to forward-looking companies with profitable projects. This is a profoundly central function in a dynamic and sustainable economy. Many small and medium sized companies are in need for capital to develop. As is often recognized these companies are crucial both for innovation and the creation of new jobs. Institutional owners provide capital to small and medium sized companies but that is to a large extent dependent on pay-outs from other investments to enable this. Institutional owners typically reinvest dividends and other pay-outs on a regular basis. Since these investors are integrating sustainability into their investment processes, in particular European investors, capital will be re-allocated and will support the transition into a sustainable European economy.

Third, changing fundamental principles of European companies acts in an attempt to improve corporate sustainability performance in various respects appears not only grossly excessive and out of proportion in view of the already on-going development, as outlined above, but also highly questionable from the point of view of the efficiency of the business sector and the functioning of the entire market economy. To transfer, as proposed, the power to define the purpose of the company from its owners to the board, require the board to do so by balancing a range of often mutually conflicting stakeholder interests against each other on an essentially equal footing, and hold the directors legally accountable to a number of different stakeholder groups, would amount to a fundamental change of paradigm for the governance of companies with far-reaching and negative consequences for the integrity of boards and hence the efficiency and competitiveness of the companies they manage.

Furthermore, in the recently improved Shareholder Rights Directive (SRD2) the basic idea was to counteract short-termism by giving shareholders greater opportunities and incentives to influence companies through active corporate governance. In the EY study, the underlying thought seems to be the opposite. Short-termism should be counteracted by reducing the owners' influence on the companies. As long-term and active institutional owners, the members of SIOA are convinced that it is better to give the owners greater opportunities to influence the companies in order to enhance the development of a more sustainable European economy.

Fourth, also from a democratic point of view it appears questionable to confer upon business leaders to be responsible for dealing with portions of the society’s sustainability issues. This is a viable strategy as long as the solution of such issues is consistent with the interests of the companies concerned which, as argued above, may lead quite far if seen in an overall, long-term “license to operate” perspective. However, beyond that democratically elected politicians, who may be held to account by the general public in open elections, must not hesitate to step in and use the society’s toolbox in terms of legally defined rules and restrictions, taxation, etc. to bring about the behavior of companies, necessary to fulfil urgent societal goals.

Against this background the SIOA calls upon the Commission to withdraw the present initiative, thoroughly reconsider the issues at hand, and then, if necessary, come back with a better proposal, duly underpinned by robust objective evidence. As part of such reconsideration, the underlying causes, prevalence and repercussions on sustainability behavior of short-termism in corporate management should be made subject to thorough scientific investigation, preferably distinguishing between different degrees of ownership concentration in the companies studied. In this context, re-iterating the SSE study on a pan-European scale would also be highly pertinent.

Stockholm, 5 February 2021

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