



## **MSc in Business Administration**

# Investment stewardship of institutional investors in Iceland

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**Declaration of Research Work Integrity**

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## Abstract

A significant change in ownership of listed Icelandic companies has taken place over the past decade or so. The majority of the ownership is in the hands of institutional investors, such as pension funds. Icelandic institutional investors have generally not been active stewards of the companies they own. Investment stewardship is the process where investors try to influence the companies in which they are shareholders, to improve corporate governance of those companies and their performance.

The thesis aims to improve understanding of how Icelandic institutional investors interact with companies in which they are shareholders and use their ownership to influence those companies. The main findings are that investment stewardship by Icelandic institutional shareholders happens behind the scenes with meetings and communication between institutional investors and the listed companies they invest in. It does also happen with public dissent of shareholder proposals or by voting against management proposals at shareholder meetings of listed companies. These findings are in line with how investment stewardship is in neighbouring countries, with the exception that transparency is a more meaningful part of the stewardship in those countries than in Iceland.

**Keywords:** *Corporate governance, Investment stewardship, Iceland, institutional investor, pension fund.*

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## 1 Introduction

Corporate governance has been an important part of companies' reality since firms begun to raise capital or to expand their businesses. Individuals and institutions that lend or provide money do care how their funds are utilised, that is effective rather than being wasted for some personal benefit of the borrower (OECD, 2015). There are many different definitions of corporate governance, but essentially, it is about trust and honesty between parties (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 2000).

Following the financial crisis in 2008, awareness of the importance of corporate governance has been increasing while it was in hibernation when things were booming (A. Stachowicz-Stanusch, W. Amann, 2012). Moreover, historical trends show the same pattern, that is corporate governance is of high importance following a fraud or financial crisis, at other times the topic lies low. There is evidence that improved corporate governance does improve performance (Farber, 2005).

The financial crisis in Iceland had a significant impact on companies listed on the domestic exchange when the three commercial banks failed as they exceeded 80% of the market capitalisation within the Icelandic market (Óladóttir, Friðriksson, Magnússon, & Þráinsson, 2017). Since the financial crisis, when the domestic equity market was wiped out, listed companies have been in a gradual revival. Furthermore, the ownership structures of listed firms have dramatically changed since pre-crisis (Jóhannesson, 2017). Before the crisis, the ownership consisted of active investors, often leveraged, and other investors with less significant ownership. After the crisis, the ownership has become concentrated with institutional investors owning up to or even exceeding half of the companies' shares, and thereof the Icelandic pension funds are dominant, owning the bulk of that 50 % (Magnússon, 2016; Baldvinsson, Árnadóttir, & Guðmundsson, 2018).

The Icelandic pension funds have quite a high domestic exposure since they have been operating under capital controls since November 2008. At the year-end of 2008, foreign assets of the Icelandic pension funds peaked at 30%, but at the end of 2017, their foreign assets counted around 25% of total assets (Seðlabanki Íslands, 2018). Furthermore, the pension funds are quite big in comparison to GDP with funds exceeding 145% of GDP in 2016 (Seðlabanki Íslands, 2017), which is among the highest among OECD countries ("Pension funds' assets of GDP," 2018). With the lack of investment opportunities under the capital controls, they have become increasingly dominant in domestic capital markets (Baldvinsson, Árnadóttir, & Guðmundsson, 2018).

This shift in ownership is far from unique as the same thing has taken place for decades in the United States, and around the world. In the United States, it has been a gradual change where direct ownership by individuals has decreased significantly while being replaced by large funds. In fact, three large fund management companies control the largest share of the mutual and index fund market and thus, are significant shareholders in equity markets although each fund management company generally controls less than 10% of the listed companies. Hence, these firms are very influential through their ownership in many of the largest US companies (Fitcher, Heemskerk, & Garcia-Bernado, 2017).

This change in ownership does have implications, both negative and positive. A positive implication can be that less active funds, such as index funds, generally have more incentive to have a long-time horizon with their investments (Fink, Larry, 2017). However, investors with less significant ownership can be in control of a company as institutional investors tend to be less active in activism and engagement with companies (Schleifer & Vishny, 1986).

The research questions are as follows:

1. How do Icelandic investors conduct their investment stewardship towards listed companies where they are owners?
2. How do Icelandic investors set up their investment stewardess policies and how they compare?
3. How do some international investors conduct themselves in their investment stewardship?

The thesis is structured as follows; it begins by giving a review of the related literature before covering who the institutional investors in Iceland are, pension funds and fund management companies. The history of the capital markets with an emphasis on investment stewardship in Iceland is the next topic. Following the history, current shareholder policies of Icelandic institutional investors are explored along with the international context and coming regulatory changes from the European Union. The research methodology of the thesis is presented before the results of the research. Finally, the conclusions are reported, and discussion finalises the thesis.

## **2 Literature review - Investment stewardship of institutional investors**

There is a plethora of literature existing about corporate governance, and a lot of it supports the idea that good corporate governance will help firms perform better (Bhagat & Bolton, 2008). The focus of the literature review is to explore previous findings on why corporate governance is important as a basis for the importance of investment stewardships by institutional investors.

### **2.1 Why Corporate governance?**

The persons hired by the owners of companies to run the organisation are the executives or managers of the company. The executives are also fiduciaries, as they have a fiduciary duty to their principals who are the owners of the company (Carlson, 2009). There can be a conflict of interest for those two parties which makes it necessary for stakeholders to introduce certain corporate governance within the corporate structure. These conflicts of interest stem from two different reasons. The first one concerns the different goals agents, managers, and company owners have. The second concerns the imperfect information the owners have about the actions of the agents and the preferences of each other. This concept is known as the agency problem (Gilian & Starks, 2003).

Corporate governance is the relationship between the company's management, its board of directors, the owners and other stakeholders of the company. It provides the structure for the objectives of the company and how to reach those objectives and how performance is measured (OECD, 2015). From the perspective of the owner, corporate governance is the processes to monitor the company internally and the controls that are in place to ensure that management is running the company in the interests of the owners and other stakeholders (ICSA: The Governance Institute, 2017).

However, should corporate governance only consider the interests of other stakeholders rather than those that supply the finance for the company (Shleifer & Vishny, 1997)? It is a debate which has been ongoing since Berle (1931) and Dodd (1932). Even today this idea is still being discussed and debated. It is common to regard corporate governance as a setup to defend shareholders' interests against managers' interests. That view is regularly challenged in society and by scholars in business and economics. One scholar (Tirole, 2001) argues that in stakeholder society when firms solely focus on profit maximisation, they move some ramifications of their actions on to other stakeholders. It

is particularly true for employees, who are one of the main stakeholders, who will be affected during their work hours and for the off-work part of their lives, such as housing, spouse employment, schools and social relationships.

One way to look at corporate governance is the design of an organisation that urges management to take care of the welfare of all stakeholders. Comparably, Van Buren (1999) suggested that stakeholder voices should be a part of the corporate governance process. By considering all stakeholders, the organisation would have consented to all contractual relationships and take responsibility within its stakeholder network. Another way to look at corporate governance is as a way to maintain stakeholder relationships with all stakeholders, and it goes even further by claiming that legal protections should apply to other stakeholders than shareholders to ensure they are not short-changed (Marens & Wicks, 1999). Herciu and Serban (2016) have their take on company value, and they claim that companies can not only be valued purely on financial terms, whereas a more integrated approach is necessary to find a societal value. An integral part of the value measurement is looking at the value for all stakeholders, not only shareholders or employees.

The G20/OECD principles of corporate governance assume that corporate governance policies have a meaningful role in accomplishing the extensive economic purpose of investor trust, capital arrangement, and capital allocation. The assumption is that the nature of corporate governance does affect the cost of capital for companies. Also, it ensures those that provide the capital directly or indirectly will partake in the value creation on proper terms. If these assumptions hold, good quality of corporate governance is a meaningful part of reassuring shareholders and other stakeholders that their claims are secure. It leads to lower capital costs for companies and eases their access to the capital market (OECD, 2015).

Furthermore, the OECD principle for corporate governance states that a good governance framework should facilitate transparent and fair markets, which in turn would lead to an efficient allocation of assets. Importantly, there is no single method to ensure good governance. However, there are prevalent components that underline good governance (OECD, 2015). A study performed on Chinese data collected for the World Bank Group, on different governance structures of 1.268 firms, shows that there are quite strong signs of corporate governance associated with employee's interests and firm profitability (Zhong, Wang, & Yang, 2017).

A landmark paper from 2003 analysed the returns for a large set of companies based on 24 governance rules. The findings conclude that investors that invested in the companies that had the strongest shareholder rights and sold the ones with the weakest shareholder rights would have earned significantly more per year in the sample period or 8,5 % per year (Gompers, Ishii, & Metrick, 2003)

## **2.2 Investment stewardship**

As existing literature has shed light on the importance for good governance of companies, it is important to explore what investment stewardship is and to find out if institutional investors monitor their portfolio companies and whether they do engage the companies and finally, if what they do does affect the firm's performance.

Hirschman (1970) was one of the first to highlight the two choices available to investors that are unhappy with an investment. One is to engage management, talking to them directly, a choice that is known as 'the voice', while the second choice is to exit the investment by selling the shares referred to as 'exit' or 'voting with your feet'. As Hirschman claimed in 1970 there are two ways for an investor to influence a given firm in its portfolio, voice or exit. Some use the threat of an exit or selling, which mixes both methods as there is strong evidence that the threat of an exit by larger shareholders is as effective as a strong governance force on managers of publicly listed companies (Bharath, Jayaraman, & Nagar, 2013).

In its simplest terms, investment stewardship is when institutional investors monitor an investment within its portfolio and do something to help steer the said investment to, what it deems, a better way or performance (McCahery, Sautner, & Starks, 2016). The actions shareholders can take that count as 'the voice' are for example some of the following: Voting at general meetings, shareholder resolutions, communication with a company representative and shareholder litigation (Van der Elst & Aslan, 2009). Others believe the threat of an 'exit' is complementary to 'the voice' method of communicating dissatisfaction to firms (McCahery, Sautner, & Starks, 2016; Edmans, 2009).

The UK stewardship code does claim that stewardship is about promoting the long-term success of companies so that capital providers will also benefit from it. The UK stewardship code goes on to claim that effective stewardship can benefit corporations, investors, and the economy. Stewardship is not only about voting but also about monitoring and voicing opinions with companies on subjects such as strategy,

performance, risk, capital structure, and corporate governance, including culture and remuneration (Financial Reporting Council, 2012).

Countries do not require fund managers to vote in general meetings of a company they have invested in, but there are some notable exceptions. Israel requires fund managers, pension, and insurance, to vote if a resolution could harm the beneficial owner. Some countries also require voting when ownership in a company is quantitatively significant (OECD, 2011). The United Kingdom's authorities can force institutional investors to disclose their voting behaviour, but instead of relying on that they have in cooperation with the Financial Reporting Council created the UK stewardship code (OECD, 2011). The code implementation is a response to the financial crisis of 2008 where a report, put together by Sir David Walker for the United Kingdom government, showed that there were deficiencies in monitoring by institutional investors in the run-up to the crisis (Walker, 2009). Deficiencies in monitoring by institutional investors as shown in a study from 2008 which implied that institutional investors did not engage in any monitoring (Goergen, Renneboog, & Zhang, 2008).

McCharey et al. (2016) claim most of the investment stewardship performed by institutional investors happens behind the scenes, and thus the practices of the investors have not been fully documented. One of their main results is that in the past five years most investors they surveyed did engage management or the board without management intervention. They also found that investors with longer time horizons did engage their boards more intensely than short-term owners. These findings support views that short-term activist investors are not the primary conductors of investment stewardship (Bebchuk, Brav & Jiang, 2014).

There is a fundamental question in the literature on whether institutional investors have any reasons or incentives to influence companies. Some studies claim that institutional investors are not active in their stewardship, in their bid to improve their portfolio firm (Grossman and Hart, 1980; Schleifer & Vishny, 1986). Huddart argues that when there are many smaller shareholders and one large, the smaller ones tend to leave the monitoring to the larger one. Thus, the large one tends to set the course for the company with the other shareholders mostly staying on the sidelines (Huddart, 1993).

It is in line with a survey that showed that most asset owners and managers have five employees or less devoted to investment stewardship matters (Isaksson & Celik, 2013). Which supports Huddart and Goergen et al. (1993) claim that there has been minimal monitoring by institutional investors. The monitoring seems to be mostly

reactive and related to subject that investors do not have to commit a significant amount of time to analyse. Issues investors are most likely to disagree with about company proposals usually are remuneration, share incentive plans, and capital authorisation. Issues that are more complex get less attention from investors, so it is important to note that this only applies to proposed issues in general meetings but not to the informal communication where investors deal directly with management.

However, some funds are more active in their monitoring or activism, and there is evidence that implicitly suggests that sizeable independent pension funds and government pension funds, in particular, are active in corporate governance activism. Also, evidence suggests a positive relationship between an increase in public pension fund holdings and its return. The flip side is that pension funds connected to specific financial institutions or employers tend to be less active in their activism (Giannetti & Laeven, 2009).

Over the last decade's ownership of stock has changed drastically with individuals being large owners early in the development of capital markets in many jurisdictions. Now in most jurisdictions, securities are held by institutional investors on behalf of others. With this morphing of ownership from the beneficial owner to the institutional investor and the increased distance from the real owner to the intermediaries leaves the investors with a weaker ownership mandate (Wong, 2015).

This change has forced institutional investors to change their approach and monitor their portfolio companies. At the same time activism is increasing investors must be mindful of doing their business transparently. The OECD Principles of Corporate Governance notes that it is essential that corporate governance framework that institutional investors exercise their right as owners as they invest on behalf of their clients. It goes further and states that not using that right could result in a loss to the investor who should be made aware of the policy to be followed by the institutional investors and emphasising the importance of transparency (OECD, 2015).

In some cases, the funds are so large that they have a hard time not being active, they may be so large that they are unable to offload their stake in a listed company without affecting the stock price significantly. It follows that they have to be more active in corporate governance activism and take a very long-term view on their investments. When the ownership stake is so significant that it makes an investor more likely to monitor and engage with his investment (Schleifer & Vishny, 1986; Kahn & Winton, 1998).

Passive funds, such as index funds, are often not able to exit a position to voice their displeasure about the performance of a company's or its governance. This inability to exit positions may lead to the investor having a less powerful voice, but some say that this incentivises them to be active in their engagement of investments. However, does that mean that large owners such as passive investors are more willing to vote against the board of a specific company? According to Fichtner, Heemskerk, & Garcia-Bernardo that is not the case, as the largest passive investors in the world tend to vote with management. To some extent that may be because these investors tend to publish what their attitudes are towards issues and companies' management may incorporate that into their policies. The said companies may also engage with representatives from these investors who will convey that message directly to the company (Fichtner, Heemskerk, & Garcia-Bernardo, 2017).

One study found that increased monitoring by passive investors who were in contact with companies (voice) was found to lead to less support of management proposals. The study authors conclude that company management seemed to be confronted more often by passive funds, who are not able to sell when they hold a more substantial portion of the company. The larger holding of passive funds did not appear to shift the kind of amount of proposals management proposed, nor did the authors find evidence of proposals that were less owner friendly. They also show that passive investors tend to support proposals that are in support of governance-related proposals (Appel, Gormley, & Keim, 2016).

A good example can be found locally where Icelandic pension funds own around half of the market cap of listed companies in Iceland. In light of their size they are very much forced to monitor and engage with their portfolio companies in Iceland, a change from the years before the financial crisis when they were minority owners and not active in their monitoring (Baldvinsson, Árnadóttir, & Guðmundsson, 2018).

It is of interest that only government or public pension funds have positive effects on firm valuation or as can be seen in empirical evidence from the United States. In the same context, it appears that pension funds, such as CalPERS, are more active in their corporate governance stewardship than the non-public mutual funds (Davis and Kim, 2007). There are possible explanations related to public pension funds holding larger parts in listed companies, and they might be less influenced by management than non-public pension funds, for example, if they are a part of a financial institution (Brickley, Lease, & Smith, 1988). What is also of interest is the lack of systematic effects on firm value

linked with institutional ownership for other investors than pension funds (Karpoff, 2001; Gilian & Starks, 2003).

### **2.3 Measuring shareholder's engagement**

One way to measure shareholder monitoring and participation is to measure the voting turnout at shareholder meetings. Hewitt (2011), collected statistics on shareholder turnout in various OECD jurisdictions. His findings show a relatively large turnout at shareholder meetings. The United Kingdom (UK) and the United States (US) stand out with just under 70% and over 80% average voting turnout. These results for shareholder vote turnout are also in line with other studies (Van der Elst & Aslan, 2009). The voting turnout in the UK and the US is very high despite fairly disperse ownership. It is of interest that the high turnout in the UK and the US could be related to proxy voting, where service companies handle the bulk of voting for institutional investors (Isaksson & Celik, 2013, SEC, 2010).

The voting results for the rest of Europe follow those of UK and the US closely as average voting turnout has increased over the last years. In 2015 the turnout in Europe was 67,2% according to a 2015 report from Institutional Shareholder Services. It does, however, vary significantly between countries with Denmark having the lowest average turnout in 2015, 48,9%, and the highest in Luxembourg with 73,8% average turnout (Institutional Shareholder Services, 2015).

Another way to measure engagement and if companies actively do follow up on their monitoring is to look for issues where there is a disagreement or a dissent on issues in general meeting resolutions. Hewitt (2011), also inspected dissent about the turnout and found that it was reasonably low for the surveyed countries, ranging from 2%-6% of votes cast. It is possible that shareholders agree that management and, or board proposals to be in line with the interests they represent as can be seen in Figure 1 (Institutional Shareholder Services, 2015). However, it certainly does not quell questions on whether shareholders do monitor companies strictly.

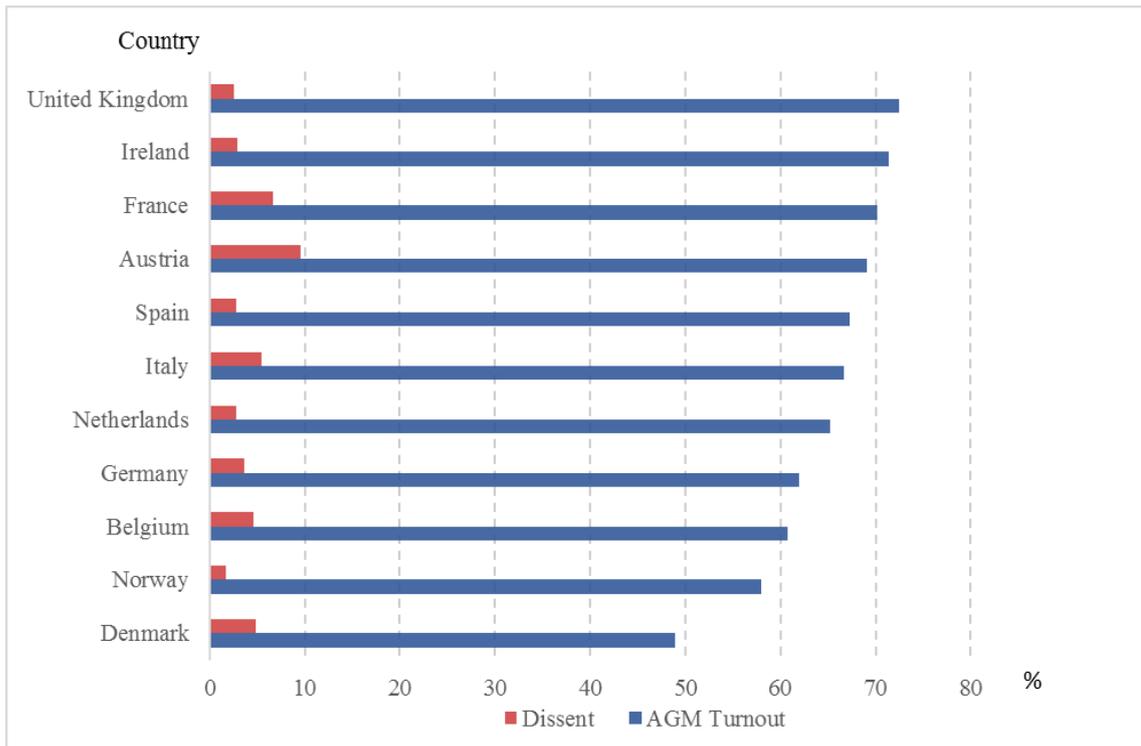


Figure 1. Shareholder turnout and average dissent, 2015. Adapted from *Institutional Shareholder Services, 2015*.

A good example of a controversial case is the Royal Bank of Scotland and Fortis buying ABN Amro in 2008. The takeover was subject to extensive debate, but only 5% of voting shareholders voted against the takeover. Sub-sequentially the acquisition was considered a failure and was among the factors that led to the failure of both banks and the government takeover of their respective banks (OECD, 2009).

Some issues are often disputed by shareholders, the most notable one being share plans and remuneration which both stand out in the amount of dissent they receive from shareholders as can be seen in Figure 2. Specifically, the figure shows, on average, the proportion of shareholders voting against these issues.

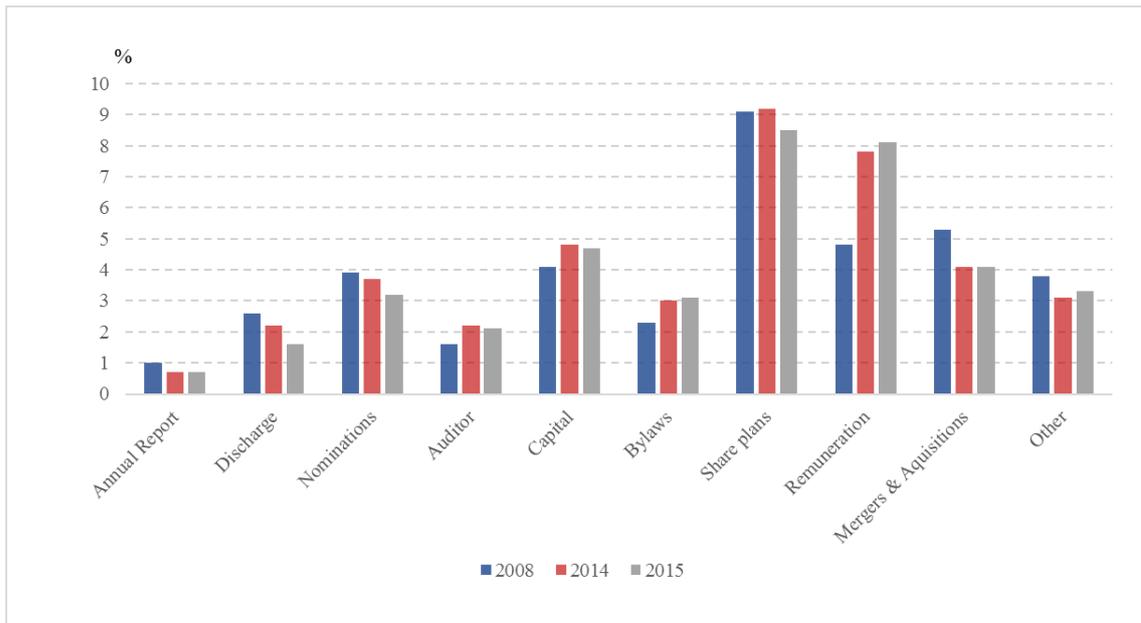


Figure 2. Average dissent in Europe, 2015. Adapted from Institutional Shareholder Services, 2015.

It can be claimed that the literature commonly agrees that corporate governance of firms is important for the performance of the company and sustainability in the long run. Corporate governance is important because the ownership of publicly listed companies has shifted from individuals towards institutions who invest on behalf of others, as fiduciaries. The beneficial owner is not the one controlling the investment and does not have his say in how the companies his money is invested and controlled. The general view today is that the institutional investors who are the owners on behalf of others should be active in their investment stewardship to safeguard and ensure the long-term success of the companies they invest in on behalf of others.

### 3 Institutional investors in Iceland

Broadly the Icelandic investment landscape can be divided into three parts, 1) institutional investors, 2) private individuals and 3) investment companies (Kristjánsdóttir, 2013). However, after the capital controls lifted in early 2017 foreign investment in Icelandic companies has also increased which can be the fourth participant in the capital markets in Iceland (Halldórsson, 2017). The foreign investors as active investors in Iceland are not a subject of this thesis and are not explicitly covered.

#### 3.1 Pension funds

The bulk of institutionally managed assets in Iceland are owned by pension funds. The Icelandic pension funds are by far the largest investors in Iceland with 3.890 billion Icelandic krónur (ISK) in assets at the end of 2017, thereof 40,5% or equal to 1.454 billion ISK invested in domestic securities and UCITS funds (Seðlabanki Íslands, 2018). The increase of total assets of pension funds can be seen in Figure 3, that despite a significant blowback in the crash of 2008 have recovered quite well. The three largest pension funds hold assets that amount to more than 1.780 billion ISK or about half the assets of the pension system (Fjármálaeftirlitið, 2017).

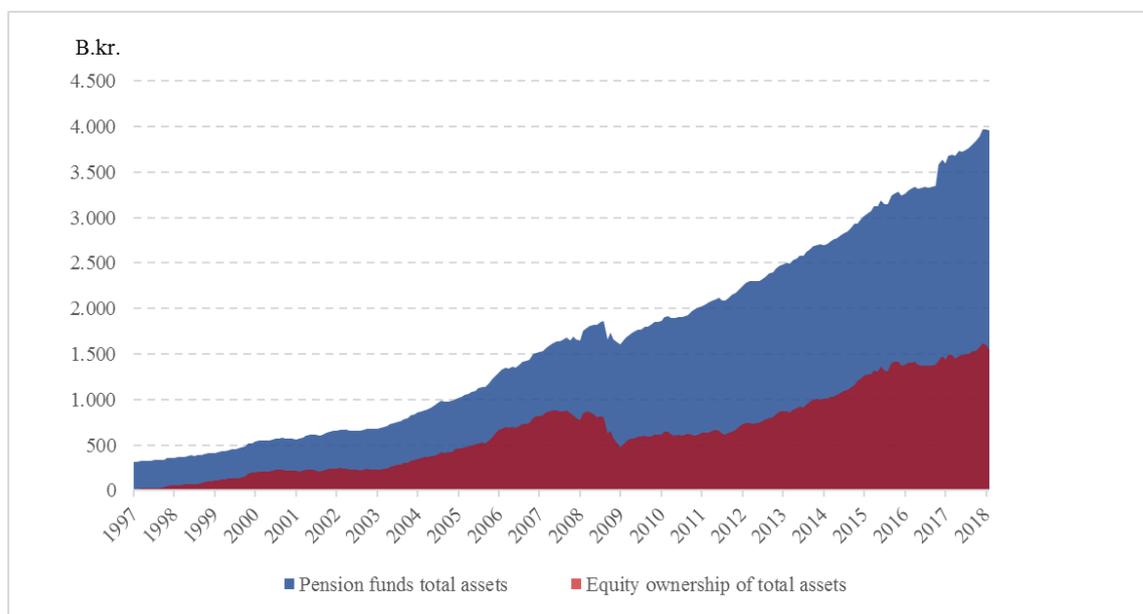


Figure 3. Total assets of pension funds and equity ownership thereof. Adapted from Seðlabanki Íslands 2018

The pension system in Iceland is split into the three-pillar system the World bank recommends. The first pillar is the public system with mandatory participation, the primary aim of the public system is to pay basic pension and work as ensure equal income

distribution through taxation in other terms social security. The second pillar is based on mandatory contributions for everyone to occupational pension funds for collective insurance. The system itself is private but under public supervision. The third pillar is based on private pension plans through the pension funds or other financial intermediaries (The World Bank, 2008; Guðmundsson, 2000).

Pension funds in Iceland are financial institution that cover Pillar 2 and 3 of the social security system in Iceland. Thus, the funds have collected and do invest significant amounts every year as well as paying pension. The current structure of pension funds was founded by law in 1997, or more specifically by Act No. 129/1997 on Mandatory Pension Insurance and on the activities of pension funds. The roots of the system can be traced back to 1969 when parties of the labour market made contributions to pension schemes mandatory as a part of the collective wage agreement in Iceland. The law passed in 1997 stems from an agreement from 1969 between the parties of the labour market, the federations of employees and employers (Guðmundsson, 2000).

In the first article of the law, all employees, as well as their employers, must pay a minimum fixed contribution to a pension fund and the pension funds shall collect premiums from all employees and give certain rights in return. The laws stipulate specific requirements the funds must fulfil (Helgadóttir, 2013; Guðmundsson, 2000). The requirements specify that the funds set up an investment policy, risk management and are prudent in their investments. There are also limits in the law about in what assets classes' pension funds can invest in as is stated in the act on Mandatory Pension Insurance and on the Activities of Pension Funds number 129 of 1997.

A recent report, made by the Institute of Economic Studies at the University of Iceland, about the impact and size of the Icelandic pension funds within the Icelandic economy highlights how large they are in comparison to the economy. It not only highlights how large they are currently but also shows how large they will be in the coming decades. If the funds grow at a similar speed as their required real return is, 3,5%, the funds' total assets will exceed 200% of GDP in 2046. Their assets counted 172% of GDP at the end of 2015. They could also end up owning over 40% of total funds in the Icelandic economy by 2060 if the share of foreign investment is not increased (Jóhannesson, 2017).

### 3.2 Fund management companies

There is another group of institutional investors in Iceland, investment and UCITS funds, who are managed by fund management companies on behalf of its investors. The Icelandic fund management companies operate under Act No. 128/2011 on Undertakings for Collective Investment in Transferable Securities (UCITS), Investment Funds and Professional Investment funds based on Directive 2007/16/EC and 2009/65/EC.

According to the Financial Supervisory Authority in Iceland, Fjármálaeftirlitið, there are ten fund management companies (Fjármálaeftirlitið, 2017) which held assets over 830 billion ISK at the end of 2017 (Seðlabanki Íslands, 2018). Figure 4 shows two explosive growth periods and a significant fall of assets under management following the crisis in 2008. It also shows how much these funds have invested into equity investments of total assets.

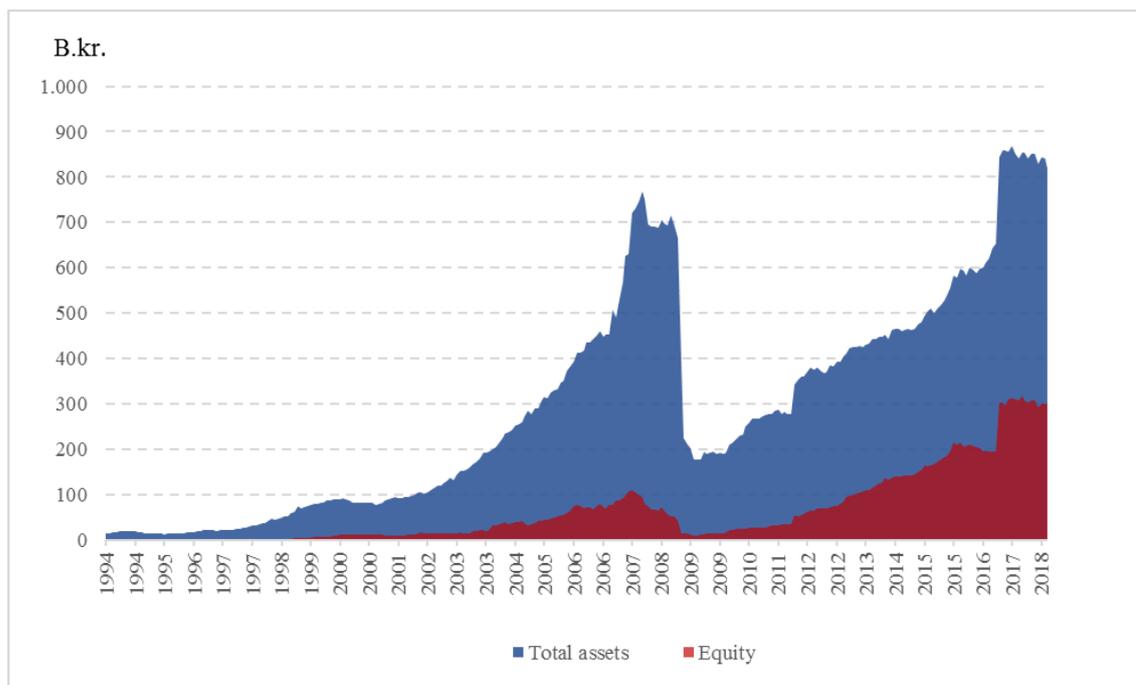


Figure 4. Total assets of UCITS and investment funds and equity ownership of total assets, adapted from Seðlabanki Íslands 2018.

There are a few fund management companies that control the bulk of the listed assets under management, Stefir hf., Íslandssjóðir hf. and Landsbréf hf. Each of these companies is owned fully by one of the three large commercial banks, Arion banki hf. owns Stefir, Íslandssjóðir owned by Íslandsbanki and Landsbréf hf. by Landsbankinn hf. Additionally, three companies have over 100 billion ISK under management, Kvika

hf., Gamma hf. and Íslensk verðbréf hf., all independent of the three large Icelandic commercial banks (Stefnir hf., 2018; Íslandssjóðir hf., 2018; Landsbréf hf., 2018).

## 4 Investment stewardship in Iceland

Investment stewardship in Iceland may not have a long story. However stewardship has evolved significantly over the last two decades. This chapter reviews historical context of investment stewardship, as well as some notable examples of stewardship, based on the public information available. The following examples are significant in some cases and probably speculation in others. Recent developments are covered along with comparisons of the policies of different institutional investors.

### 4.1 Historical evolution of investment stewardship in Iceland

Investment stewardship does not have a long history in Iceland in comparison to neighbouring countries, especially in light of the short history of public capital markets. Investment stewardship in Iceland is first mentioned in an article in a business magazine, *Frjáls Verslun*, in 1995 and was called, “To be or not to be” (Hauksson, 1995). In the article the managing director of *Lífeyrisjóður Verzlunarmanna* (*e. Pension Fund of Commerce*), Þorgeir Eyjólfsson, is interviewed along with managers of few investment funds. At the time the views of the pension fund differed from those of the investment funds. The pension fund had agreed on a policy on how it interacted with the investments it had made. The policy of the pension fund set up decision-making criteria for its actions based on every investment and the circumstances which meant that the fund had a board representation at public companies. It contradicted with what the investment funds stated as they neither participated in discussions with the companies nor did they have board representation.

At that time the Icelandic stock exchange had not been in operation for long either many active or listed companies. The stock exchange in Iceland was founded in 1985 and during the first years of operation there was only trade with debt instruments. It was not until 1990 that the first company listed shares on the exchange. Before that time there were some roadblocks which impeded the founding of a stock market. The banking system was almost entirely governmentally owned and relied extensively on knowing the right people, the tax system had incentives for a high debt load, and the Icelandic financial market was very isolated from international financial markets. Shareholder rights were not adequate as minority shareholder rights were sacrificed for primary owners and insiders. Furthermore, the operational environment was unfavourable in many aspects (Magnússon, 2007).

In the 1980's and 1990's, many of these hindrances were removed, and the general business environment made more feasible for all parties. Additionally, the banking system reformed with indexation of loans and the banks got more control over the interest rates they charged for loans. These changes along with the growth of the pension system increased demand for an active capital market and listed equity investments. When the wheels started moving in this direction, it happened very rapidly (Magnússon, 2007).

The first company to be listed on the exchange in Iceland (Verðbréfaþing) was Olúfélag Íslands, an oil retail company, in 1990. The first trade with the shares of the Olúfélag Íslands happened the year after. Shares of companies did exchange hands during that time but not through the exchange but intermediaries such as the banks. Regulatory burden along with taxation was most often mentioned as the reason for not listing companies (Magnússon, 2007).

The story of Icelandic capital markets is short, and the markets do not have the same history and experience like in neighbouring countries. However, the story has been eventful. From the infancy of the regulated capital markets when the first companies were listed to a long boom where the market grew at a breakneck pace from 2003 until 2007. After the growth period, it started going down before almost all listed shares were wiped out or around 95% of the index in 2008 when the Icelandic banks failed. Since then there has been considerable growth in the number of listed companies and the total market capital of those listed companies although it is far from the lofty heights in 2007 regarding market capitalisation or trading volume (Hreinsson, Benediktsdóttir, & Gunnarsson, 2010)

There was also some discussion and criticism on investors in the boom years between 2003 and 2008, but people did not take it very seriously at the time. One of the more notable criticisms from that time was by a politician, the leader of Samfylkingin, which at the time was the second largest political party in Iceland. Her criticism centred on the opinion that investors, especially pension funds, should invest their funds responsibly and set policies for their investments. The then chairman of the Lífeyrissjóður Verzlunarmanna, which was and is the second largest pension fund in Iceland, rejected those ideas as preposterous. His view was that firms that the fund invested in should only think about maximising profits and the pension fund should not be the nation's conscience. Additionally, he claimed that it did not matter where the yield comes from as long as the pension fund can meet its liabilities in the future ("Lífeyrissjóðir sýni félagslega ábyrgð," 2006).

Despite the words of the chairman of Lífeyrissjóður Verzlunarmanna in 2006, the fund did set a policy about investment stewardship in 2007. It was a very concise policy focused on the United Nations Principles for Responsible Investment, environmental factors, and social responsibility with an emphasis on human rights that the companies it invests in adhere to good corporate governance. The policy of the fund was to engage the companies when ownership was significant and importantly that staff and board members be responsible when discussing investment where there is the possibility of a conflict of interest (Lífeyrissjóður Verzlunarmanna, 2007; Logadóttir, 2007). Lífeyrissjóður Verzlunarmanna was not the only fund to incorporate policies regarding investment behaviour as Sameinaði Lífeyrissjóðurinn did also do so in 2007, but in both cases, the rules are centred on responsible investment and based on the UN Principles of responsible investments.

Following the crash of the Icelandic capital markets in 2008, there was a significant increase in criticism about the behaviour of investors in the Icelandic financial system. Following the discussion and criticism in Icelandic society at that time, the Icelandic Confederation of Labour (ASÍ) put forth demands that the pension funds would improve their conduct to increase credibility and trust in the funds. ASÍ does carry some weight with many of the funds as it does appoint half the board members for many of the pension funds. It published recommendations about the strategy and operations of the pension funds and put it very directly that the funds should establish ethics protocols concerning their investments and conduct of employees (ASÍ, 2009). The 2009 recommendations from ASÍ ended up forming the basis for a new pension policy by the organisation. One of the points, as mentioned before, related to the fact that the funds should establish ethic protocols for themselves and their investments. The funds should not stop at that point but also be responsible shareholders who are active in monitoring and engage in their investments. Additionally, the pension funds should have a clear policy on remuneration for the companies they invest in and that they should appoint representatives to the boards of companies they invest in (ASÍ, 2013).

According to an interviewee of Cardaklija (2015), one of the main reasons the pension funds started implementing stewardship policies can be related to an investigative report from the Icelandic Pensions Funds Association in 2012. In the report, the pension funds received considerable criticism for many aspects of the pension funds governance (Bragason, Eyjólfsson, & Frímansson, 2012).

## 4.2 Notable developments in investment stewardship in Iceland

In the last few years, some significant events have taken place that shines a light on how investment stewardship is conducted by institutional investors in Iceland over the last years. In the following chapters, there are brief points about each of the events, some of these events are then referred to later in the thesis. Each of these cases showcases a different kind of investor or investment stewardship by an institutional investor.

### 4.2.1 Gildi pension fund as an active investor

Gildi pension fund is the 3<sup>rd</sup> largest fund in Iceland with assets amounting to 517 billion ISK at the end of 2017 (Gildi lífeyrissjóður, 2018) or 20% of GDP. The pension fund has been very active in its stewardship of listed companies since it agreed on a stewardship policy. In 2015 the stewardship policy was updated where Gildi put more emphasis on mutual communication with boards, increased activity surrounding shareholder meetings. Moreover, the fund put norms on how it believes remuneration policies should be at companies it invests in (Pálsson, 2015).

The fund's stewardship policy explicitly states that Gildi is an active investor. The policy emphasises the role of the pension fund as an investor who promotes long-term thinking and sustainability along with responsible corporate governance. The policy covers many issues, e.g. how Gildi should conduct itself on shareholder meetings, how it puts proposals forwards, nominates board members, and the funds view on remuneration policies. The shareholder policy highlights the emphasis Gildi lays on remuneration with fairly detailed recommendations. (Gildi lífeyrissjóður, 2015).

The fund, according to the shareholder policy, does meet up with boards and CEO's and expresses its views on corporate governance and does engage companies about the issues it deems necessary. It does also promote board members to the boards of companies it is a shareholder in by choosing from potential candidates and by looking at board composition (Gildi lífeyrissjóður, 2015).

The fund has been active in its engagement which is seen in the dissent proposals Gildi has put forth on multiple occasions for different listed companies. Most of the dissent proposals the pension fund has put forth at shareholder meetings concerning remuneration policies, share buyback and nomination committees. An inspection of the proposals Gildi has put forth can be seen in Figure 5. The proposals are in total 31, but the fund introduced them on 25 different occasions. Further information about the fund's shareholder proposals is found in the content analysis research presented in this thesis.

The proposals put forth each year seem to show a particular theme by Gildi pension fund. In 2015 and 2016 buybacks and remuneration policies are high on the agendas. In 2018 nomination committees come in strong where Gildi did put forth proposals for five different companies, some of them as amendments on proposals put forth by Eaton Vance Management, a hedge fund management company that manages funds that have invested in multiple Icelandic companies, sometimes significantly as is covered in chapter 4.2.7.

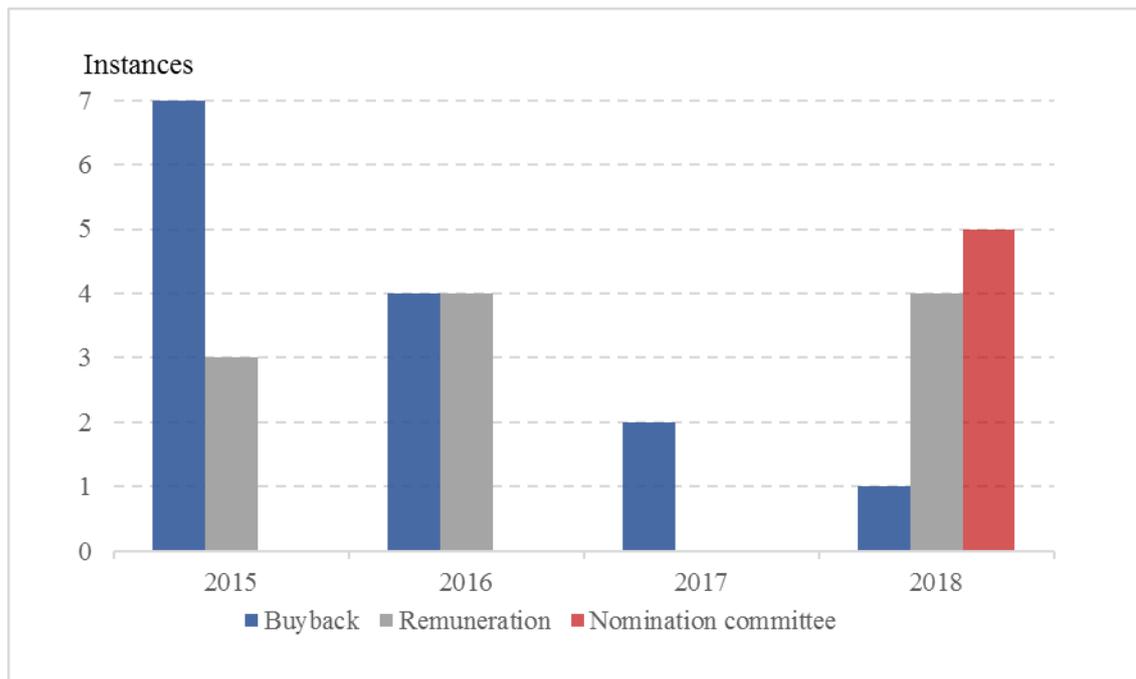


Figure 5. Amendment proposals by Gildi pension fund, adapted from Nasdaq OMX Nordic news website.

Gildi pension fund has also increased transparency about how it conducts its stewardship policy as it publishes yearly an overview of, e.g. the board members it votes for at each company's shareholder meet and for what proposal it votes for or against or when the fund abstains. Furthermore, it puts forth dissent concerning proposals at shareholder meetings. This transparency is a part of the evolution of the stewardship policy of the pension fund which was agreed to in 2013, and according to the fund, the size of the fund related to the market has a say in how the fund engages listed companies (Gildi lífeyrissjóður, n.d.).

#### 4.2.2 Pension fund board membership

In the year 2015, there was a commotion concerning one board member of the Lífeyrissjóður Verzlunarmanna. The board member who was a long-time board member of the pension fund was also investing considerable amounts in listed companies, in some cases the same companies as the pension fund. At the end of 2015, he was on the board

of three listed companies, Marel hf., Síminn hf. and N1 hf. as was highlighted by a report that inspected what other roles board members of pension funds had, such as board membership in listed companies (Talnakönnun hf., 2015).

The discussion surrounded the board member potential conflict of interest where he had shares in the same companies as the fund. His role as chairman, vice chairman and board member during his tenure allowed him broad access to information not available to the general public, although not necessarily inside information. His interests were not necessarily the same as those of the pension fund which is a long-term investor.

Two vocal critics of his tenure in the board of the pension fund talked about it being unsuitable while he was also on the board of listed companies. The then leader of VR, one of the biggest labour union in Iceland that appoints members to the board of the pension fund said it was unacceptable that a board member should also be a board member of companies listed on the exchange. The leader of VR claimed that she had requested that he would leave the board (Júlíusson, 2015).

A reporter at Kjarninn, an online news media outlet, criticised similar arrangements within the pension funds, explicitly highlighting the importance of transparency in light of potential conflicts of interest. The big question for him related to trading, who was going to make a trade before the other, based on what information. The critic goes on to highlight the critical task the pension funds face, concerning how to limit conflicts of interest with the interests of fund members, the beneficial owner, in mind (Halldórsson, 2015). The said board member ended his tenure on the board of Lífeyrissjóður Verzlunarmanna early in 2016 after nine years on the board (Viðskiptablaðið, 2016).

The current shareholder policies of pension funds that are presented in chapter 4.3 that those shareholders policies, which take a stance regarding board membership of their board members and employees of the institutional investor and do not permit them to sit on boards of listed companies. A few pension funds and none of the fund management companies do disclose a stance concerning this topic. In the case of the fund management companies, other rules or laws may prohibit them from sitting on the board of publicly listed companies.

#### **4.2.3 Stefnir fund management company and proxy voting rules**

Stefnir is a fund management company, the largest one in Iceland with 347 billion ISK under management at the end of 2017. Stefnir published its stewardship policy and

proxy voting rules in 2013. Both the stewardship policy and the CEO of the company have stated that the company is an active shareholder (Halldórsson, 2015b).

Since 2015 the company has published its voting behaviour on the company's website. It includes information such as how Stefmir voted at a given shareholder meeting and whether the vote was for, against or abstain. Additional information highlights who put the given proposal to the shareholder meeting, each company's board or a specific shareholder with dissent.

The CEO of Stefmir has publicly stated that the company engages with listed companies and is active in its investment stewardship. The engagement is twofold, Stefmir meets with the management of the company to discuss how management communication with the board of the company is supporting and restraining management. Additionally, Stefmir communicates with the boards ahead of shareholder meetings to ask about board functions (Halldórsson, 2015b). There is at least one indication of Stefmir's influence on the prospects of a company it is a shareholder in. It is related to the case of VÍS (an insurance company in Iceland), which is covered more closely the next sub-chapter. In that case, Stefmir may have been a part of a larger consortium gaining control in the insurance company, VÍS, or willing to support the measures the consortium planned on taking.

Stefmir is the fund management company in Iceland that has been, at least publicly, most active in its stewardship of listed companies. The company only became active in its shareholder engagement several years after the crash of the Icelandic economy in 2008, early in comparison to most institutional investors in Iceland.

#### **4.2.4 Vátryggingafélag Íslands hf.**

During a particular period recently, there was a protracted conflict over the control of VÍS, the largest insurance company in Iceland. The fighting may have started when some investors saw an opportunity to improve the operations of the company which seemed to be run less efficiently than the two other insurance companies listed on the exchange. According to newspaper reports, the group of investors were looking for changes in the operation and policies of the insurance company. There seemed to be a particular clash between the emphasis of the private investors and those board members whom the pension funds had supported to the board of VÍS. The fact that 15 people have sat on the board of the company from the start of 2015 until the end of the year 2017 indicates some conflicts among shareholders, with four different persons taking on the role as chairman of the board during that period (Ægisson, 2017).

Following the annual shareholder meeting in March of 2017 suggestions of significant conflict could be seen when the board convened for the first time determine the roles of board members. A new chairman was voted, a significant shareholder and the previous chairman seemed less pleased with being a board member and resigned citing different views on corporate governance.

The resignation and governance at VÍS gained significant media attention. A few reports mention that the pension funds, who owned at least a third of the insurance company, were less than pleased with how matters were progressing and there was a mention of the possibility of asking for a new shareholder meeting to vote for a new board. There was hesitation concerning that though as some pension funds believed that further conflict would lead to lower share price (Stefánsson & Þórisson, 2017).

A pension fund voiced their displeasure by reducing their stake in VÍS significantly. Representatives of at least one fund confirmed that they had sold part of their shareholding in VÍS and that the sales were related to the resignation of the aforementioned board member. The stakes sold were significant, Gildi sold a 4,4% ownership stake in the insurance company. The chairman of the board of Lífeyrissjóður Verzlunarmanna, on the other hand, voiced the threat of selling a stake in the insurance company after the resignation of the board member, whom the pension fund had supported (“Selja hlutabréf í VÍS,” 2017). Shortly after that Lífeyrissjóður Verzlunarmanna, allegedly, declined an offer for half its stake in the insurance company (Ægisson, 2017b).

This example from VÍS shows how conflict can emerge between the different parties of shareholders, i.e. private investors and institutional investors that may have different perspectives regarding time horizons of their investment. It is also one of the few examples of using the threat of exit, voice, in Iceland, in such a public way (Ægisson, 2017c).

#### **4.2.5 Debate on dividends, empirical evidence in 2016**

A debate took place in February of 2016 when Félag Íslenskra Bifreiðaeigenda, an association of car owners in Iceland, scolded the insurance company VÍS, for its dividend proposal. The insurance company meant to pay out 5 billion Icelandic kronas (ISK) which was more than double the profit of the company for the preceding year. Not only was the dividend proposal high in the mind of the association but the insurance company had a few months prior sent a letter to many of its clients where it stated that it did need to increase premiums on automobile insurance (FÍB, 2016). The debate that the

car owner's association started affected all three of the large insurance companies in Iceland, especially the two that planned to pay dividends that exceeded their profits (Júlíusson, 2016).

The debate had seemingly some adverse effects on the reputation of the insurance companies, which resulted in some clients moving to other insurance companies. A smaller insurance company, Vörður tryggingar hf., did receive a significant number of new clients during that period which can be traced to these events ("Mjög mikil hreyfing á tryggingamarkaði," 2016).

In the end, two of the insurance companies lowered their dividends as a reaction to the debate and criticism they received. VÍS and Sjóvá-Almennar did lower their proposed dividends to match the profits of the preceding year, from 8,1 billion ISK to 2,7 billion ISK (Júlíusson, 2016).

A case of activism outside the boardroom and shareholder meetings. Where public pressure, lobbying by a special interests group and the insurance companies' reputation was dented by how the insurance companies reacted to the criticism. It is more than possible that some shareholders may have contacted the companies and having their say concerning the proposed dividends but no mention of that can be found in the media.

#### **4.2.6 HB Grandi and corporate governance**

HB Grandi is one of the largest seafood companies in Iceland with a turnover of over 200 million Euros (HB Grandi hf., 2017). The company is also one of the largest single owner of fishing quota in Icelandic jurisdiction with over 10% share of the quota (Kvótinn, 2017). Before the annual general meeting of HB Grandi in 2015 Gildi pension fund did nominate and support a board member to sit on the board of HB Grandi, without success. The fund did also put forth a proposal concerning the remuneration policy of HB Grandi, where the fund wanted the company to seek the agreement of a shareholders meeting for stock options, pre-emptive rights or share related remuneration. The chairman of Gildi pension fund was surprised that the proposal for the remuneration policy was not approved as it had been agreed upon by most listed companies (Jónsson, 2015).

The chairman of HB Grandi was not pleased with the board member proposal or the changes to the remuneration policy and voiced his opinions vocally at the annual general meeting of Gildi pension fund a few days later. He also laid down a proposal for the pension fund, that it would not interfere with the operations of companies that it has shares in and claimed he would put forth a similar proposal for the general meeting of SA, the Confederation of Icelandic Enterprise. The chairman also voiced his displeasure

with how Lífeyrissjóður Verzlunarmanna conducted itself at the annual general meeting of HB Grandi (Gildi lífeyrissjóður, 2015).

The story does not end there because the pension funds continued to put pressure on the board of HB Grandi at the next AGM in 2016 where seven people did make themselves available for five seats on the board of HB Grandi. To increase the odds of changes in the board one of the pension funds asked for cumulative voting, which would increase the chances of their board member being voted (“Framboð til stjórnar HB Granda hf.,” 29. March 2016). Gildi pension fund also put forth two requests for changes in the company bylaws, thereof one related to remuneration, the same one as the year before (“Dagskrá og tillögur fyrir aðalfund,” 2016).

The changes in the bylaws were agreed upon by the shareholders of HB Grandi. Five of the seven board members withdrew their nominations, resulting in a failed board election and a demand for another shareholder meeting to take place (“Yfirlýsing stjórnar HB Granda hf.,” 2016). The meeting took place a few weeks later where a board member, nominated by the Lífeyrissjóður Verzlunarmanna, was elected along with every four of the previous board members (“Niðurstaða framhaldsaðalfundar,” 2016)

Following the annual general meeting of HB Grandi in 2016 the chairman of the board of HB Grandi did a centrefold interview with Morgunblaðið, an Icelandic daily newspaper. In the interview, he went over his views on how pension funds should not interfere with the companies they are shareholders in and how the pension system should be set up. He also claimed that the pension funds worked together to ensure their people joined the boards of listed companies (Stefánsson, 2016).

In the interview he stated:

*“The main thing is that pension funds must invest. They should think about the benefit of investors, and it is not their role to interfere with the listed companies they invest in. If they are dissatisfied, they should simply sell their shares in them.” (Stefánsson, 2016)*

Based on this case which is public to some extent it can be inferred that the chairman of HB Grandi was all but happy with the policy and execution by Gildi and did have concerns surrounding the engagement and appointment to the board of directors of the company.

This story highlights the difference of opinion whether institutional investors such as pension funds should be passive or active investors. Before the crash of the Icelandic

economy in 2008, they tended to be very passive but in light of their relative size compared to the economy and as shareholders of listed companies they were forced to change their stance and become active investors.

#### **4.2.7 Eaton Vance Management and other foreign investors**

In the last few years, foreign investors have been increasing their exposure to Icelandic equities with a hedge fund management company by the name of Eaton Vance Management being the most prominent one. According to Morgunblaðið, Eaton Vance sent a letter in March 2018 to all Icelandic companies it has a stake in, where it outlined the benefits of setting up nomination committees (Morgunblaðið, 2018). It is of interest that not all the companies Eaton Vance Management was found to be a shareholder in published the letter or have a nomination committee on their agenda, in some cases, this has been a discussion at shareholder meetings. Nonetheless, Eaton Vance has six instances of shareholder proposals related to nomination committees in the year 2018 as can be seen in chapter 7.2.

According to interviewee seven, the engagement of foreign investors is not isolated to Eaton Vance Management. Some of the other foreign investors in listed Icelandic companies have claimed that they are not active in their engagement, but for simple issues, the investors might be in contact with the companies. For the more complex issues, they would exit their investment, walk.

### **4.3 Institutional investor stewardship policies**

The pension funds who had set up some policies before the financial crash of 2008 in Iceland did mostly have a relatively simple one, but the bulk of the funds set up their policies after the crash and to some extent based on what ASÍ did promote. Lífeyrissjóður Verzlunarmanna did agree on a policy in 2007 as has previously been mentioned (Lífeyrissjóður Verzlunarmanna, 2007).

Most of them the stewardship policies agreed by institutional investors in the last few years consider the recommendations from the policy paper published by ASÍ (ASÍ, 2013). Each of the stewardship policies does have their flair and emphasis, e.g. Gildi pension fund seems to put some emphasis on remuneration policies. The fund also seems to treat its stewardship as an integral part of the investment process and is very active in comparison to many other Icelandic institutional investors (Gildi, 2015).

The number of investment policies published by institutional investors varies between investors. The policies by pension funds seem to signal more engagement while the fund management companies set up the policies more as proxy voting policies.

Ten Icelandic pension funds were found to have published their stewardship policies on their website. Also, three of the investment management companies published proxy voting policy; those three are affiliated and owned by the three large commercial banks in Iceland. The institutional investors found to have public policies can be found in Table 1 and Table 2. The shareholder policies were inspected for specific elements to check if they did mention those aspects or take a specific stance concerning that element. The elements are the following:

- Active shareholders; whether the institutional investor does consider itself being an active investor.
- Voting at shareholder meetings; whether the institutional investors do cast a vote for or against proposals at shareholder meetings
- Nomination of board members; whether the institutional investor nominates specific board members to the board of listed companies
- Remuneration policies; whether the institutional investor has a policy concerning remuneration policies of listed companies.
- Transparency; whether the institutional investor does publish publicly or give people access to information about voting at shareholder meetings.
- Company engagement; whether the institutional investor does communicate with listed companies to get across messages, whether it concerns some aspect of corporate governance or related to the operations of the said publicly listed company.

The fields of Table 1 and Table 2 are compiled with the following:

- Yes, the institutional investor does have information in its stewardship policy concerning the elements.
- No, the institutional investor does not have information in its stewardship policy concerning the elements.
- Case by Case, meaning that the institutional investors go over each instance and make a decision about potential action, such as voting.
- N/A it is unclear by the policy whether the fund does so or not

The pension funds are not the only investors who set policies concerning their conduct. Probably the first fund management company to do so was Stefnir hf., a wholly owned subsidiary of Arion banki hf., which agreed on a proxy voting policy in 2013. The company subsequently updated that policy in 2015 and from that time on the company has published how it has utilised its voting rights concerning their investments. The CEO of Stefnir claimed that the increased transparency is to increase the trust in how the company performs its duties on behalf of its beneficial owners (Stefnir hf., 2015).

The ten pension funds that have published their shareholder policies are the following:

- Lífeyrissjóður starfsmanna ríkisins, the Pension Fund for State Employees; LSR.
- Lífeyrissjóður Verzlunarmanna, the Pension fund of Commerce; LV.
- Gildi lífeyrissjóður, Gildi pension fund; Gildi.
- Birta lífeyrissjóður, Birta pension fund; Birta.
- Stapi lífeyrissjóðu, Stapi pension fund; Stapi:
- Frjálsi lífeyrissjóðurinn, Frjálsi pension fund; FL.
- Almenni lífeyrissjóðurinn, Almenni pension fund; AL.
- Söfnunarsjóður lífeyrisréttinda, the General Pension fund; SL.
- Festa lífeyrissjóður, Festa pension fund; Festa.
- Lífsverk lífeyrissjóður, Lífsverk pension fund; LVERK.

*Table 1. Pension fund shareholder policies.*

| <b>FUND</b>                    | <b>LSR</b>   | <b>LV</b> | <b>Gildi</b> | <b>Birta</b> | <b>Stapi</b> | <b>FL</b> | <b>AL</b>    | <b>SL</b> | <b>Festa</b> | <b>LVerk</b> |
|--------------------------------|--------------|-----------|--------------|--------------|--------------|-----------|--------------|-----------|--------------|--------------|
| Active shareholder             | Yes          | Yes       | Yes          | Yes          | Yes          | N/A       | Yes          | Yes       | Yes          | N/A          |
| Voting at shareholder meetings | Case by case | Yes       | Case by case | Case by case | Yes          | Yes       | Yes          | Yes       | Yes          | Yes          |
| Nomination of board members    | Yes          | Yes       | Yes          | Yes          | Yes          | No        | Yes          | Yes       | Yes          | Yes          |
| Remuneration policies          | Yes          | Yes       | Yes          | Yes          | Yes          | Yes       | Yes          | Yes       | Yes          | Yes          |
| Company engagement             | Case by case | Yes       | Case by case | Maybe        | Yes          | Yes       | Case by case | Yes       | N/a          | No           |
| Transparency                   | Yes          | Yes       | Yes          | Yes          | Yes          | N/A       | No           | No        | No           | No           |

*Table 2. Fund management company shareholder policies.*

| <b>Company</b>                 | <b>Stefnir</b> | <b>Íslandssjóðir</b> | <b>Landsbréf</b> |
|--------------------------------|----------------|----------------------|------------------|
| Active shareholder             | Yes            | N/A                  | N/A              |
| Voting at shareholder meetings | Yes            | Yes                  | Yes              |
| Nomination of board members    | No             | No                   | No               |
| Remuneration policies          | Yes            | Yes                  | Yes              |
| Company engagement             | Yes            | No                   | No               |
| Transparency                   | Yes            | Request              | No               |

The pension funds generally are active shareholders who vote at general meetings. The larger pension funds tend to nominate independent members to the boards of companies when they deem it to be necessary. The smaller pension fund tends to support board nominations but generally, lack the voting numbers to support nominations on their own. In many of the shareholder policies of the smaller pension funds, there is a mention of potentially working together on a board nomination. Fund management companies on behalf of the funds under management tend not to nominate on their own but may, similarly to the smaller pension funds take part in board nomination in association with other investors or simple vote. Most of the institutional investors tend to engage listed companies concerning issues they deem necessary.

A few institutional investors have increased their transparency and started publishing their voting behaviour publicly at shareholder meetings. Stefnir fund management and Gildi pension fund have done so for a few years. Lífeyrissjóður Verzlunarmanna has transparency in its stewardship policy which they will publish voting behaviour for the year before following its annual general meeting. As of April 22nd, 2018 the fund has not published the voting behaviour for 2017, the year before, on its web page as the policy states.

These cases covered in the previous chapters and the shareholder policies of institutional investors give some understanding and information about investment stewardship in Iceland. How it has developed historically and some of the primary drivers for change in the last ten years. How the investors were trying to rebuild trust and react to a changed world where they are now the majority owner of most or all listed companies in Iceland.

There has been discussion and critique surrounding the behaviour of institutional investors, particularly pension funds, in recent year. The CEO of NASDAQ OMX Iceland, Páll Harðarson, believes the pension funds should be much more transparent,

explicitly surrounding their stewardship. It is important considering how much they own of the listed Icelandic companies and because the beneficial owner is the Icelandic public. Such a large investor as the pension funds cannot sit by on the sidelines and watch; they should similarly wield their power as other investors and thus protect their interests and those of the fund members (Jónsson, 2017).

There are others who believe that the boards of listed companies should be populated by private investors who have invested their own money in the company. That company strategy should be formed by private investors and not by the independent board members at listed companies. An article in *Fréttablaðið*, a daily newspaper in Iceland, inspected the board members of listed Icelandic companies and found that most of them were independent with little or no ownership stake in the companies. Sixteen of the eighty board members in the listed companies own at least 1% in the company they are board members in, where forty-five of the eighty board members own nothing in the companies. It is crucial to note that whether board members own a share of a company or not they are obliged by Icelandic law to bear in mind the common interests of the company and not particular shareholders (Jónsson, 2018).

## 5 Investment stewardship outside of Iceland

Icelandic capital markets developed late in comparison to neighbouring countries who have a longer tradition and history of capital markets. The same goes for investment stewardship. Although it has evolved rapidly in Iceland over the last few years, it is healthy to learn from our neighbours who have a more extended experience regarding investment stewardship. Some have put into force stewardship codes that guides investors. Some stewardship codes are explored along with some institutional investor stewardship activities of notable investors for further insight. Importantly for investment stewardship, the European Parliament has made amendments to the Shareholders Rights Directive to increase long-term shareholder engagement, which is covered in this chapter as it will impact how institutional investors conduct their investment stewardship.

### 5.1 Shareholder Rights Directive amendment

In May 2017, the European Parliament agreed to amendments to Directive 2007/36/EC, the Shareholders Rights Directive, to encourage long-term shareholder engagement. The rationale for the changes can be traced back to the financial crisis where shareholders supported managers' short-term risk-taking. The changes to the directive are meant to remedy that and lead to more sustainable companies. The directive will put in force measures that apply to the following ("Shareholders' rights in EU companies: Council formal adoption," 2017; Directive 2007/36/EC, 2017):

- Remuneration of directors, where remuneration policies should work towards the long-term interests and sustainability of the company.
- Companies should be able to identify its shareholders from any intermediary that potentially could have the information.
- Intermediaries shall have to assist shareholders so that they can exercise their right to vote.
- Institutional investors and asset manager shall be more transparent in their shareholder engagement. They should publish their policy of engagement or explain why they are not doing so. The policy should describe how shareholder engagement integrates with their investment strategy and how engagement execution. The policies should also contain information about how to handle potential or actual conflicts of interest.

- All significant transaction with related parties should be put to the vote at the administrative or supervisory board. All material transactions with related parties should be announced with the information needed to assess the integrity of the transaction.

The directive could have a significant effect on stewardship by institutional investors when it comes into effect in the member states by the 10<sup>th</sup> of June 2019 (Directive 2007/36/EC, 2017). Currently, the act is under scrutiny by the European Free Trade Association, but it is deemed highly likely that it will also be implemented in Iceland as the Shareholders Rights Directive is already in effect in Iceland (“Directive (EU) 2017/828 - EFTA,” 2017).

## 5.2 Stewardship codes

Some notable markets have adopted codes of conduct about investment stewardship by institutional investors. Eight out of fifty countries have implemented a stewardship code, most being voluntary but two which are implemented under a “comply or explain” basis as was explored by the OECD (OECD, 2017). The most notable ones are the UK stewardship code (Financial Reporting Council, 2012), and another one is the Dutch stewardship code (“Institutional investors establish the first edition of a Dutch Stewardship Code,” 2017). The UK stewardship code originated after a recommendation in the so-called Walker report and was published by the Financial Reporting Council in 2010 and revised in 2012 (Financial Reporting Council, 2012). In principle, the code is set up to increase the long-term success of companies so that the beneficial owners of the capital prosper. Effective investment stewardship benefits companies, investors and the economy. The code emphasises that the stewardship is not only voting but also monitoring and communicating with companies on strategy, performance, risk and corporate governance to name some issues. One of the purposes of the code is to improve the dialogue between companies and institutional investors. Which in turn is believed to reduce the risks of really bad outcomes (Financial Reporting Council, 2012).

The code itself is set up as seven principles that asset managers should look to when constructing their investment stewardship. The seven principles are set for institutional investors to protect and increase the value for the ultimate owner of assets and are as follows:

1. Publicly disclose their policy on how they will discharge their stewardship responsibilities.

2. Have a robust policy on managing conflicts of interest about stewardship which should be publicly disclosed.
3. Monitor their investee companies.
4. Establish clear guidelines on when and how they will escalate their stewardship activities.
5. Be willing to act collectively with other investors where appropriate.
6. Have a clear policy on voting and disclosure of voting activity.
7. Report periodically on their stewardship and voting activities.

It is important that the UK stewardship code will be revised in 2018 which may be related to the changes to the Shareholders Rights Directive (Financial Reporting Council, 2012).

A new version of a Dutch stewardship code was published by EUMEDION, a non-profit representative of institutional investors in the field of corporate governance, in 2017. To a large extent, it is a response to the Europeans Commission's drive to emphasise sustainability ("Institutional investors establish the first edition of a Dutch Stewardship Code," 2017). Similar to the UK stewardship code, it is based on principles for the institutional investors to adhere to, but the principles go further than the UK code.

The code highlights long-term value creation at investees companies. It also requires asset managers to monitor its investments and engage with the companies. It goes on to make the investor do escalate issues that are not resolved in a dialogue. The code puts some duties to the asset manager to better the conduct of investors and to increase the impact of the stewardship. Finally, the code requires public disclosure of voting policy and how they voted, down to individual voting item ("Institutional investors establish the first edition of a Dutch Stewardship Code," 2017).

### **5.3 Institutional investor stewardship**

Institutional investors conduct their stewardship activities in a very different manner, but the profile of stewardship has increased significantly over the last years with huge asset management companies like Blackrock and Vanguard embracing stewardship publicly ("ESG," 2018).

Blackrock, the largest asset management company in the world, publishes its primary goals which are to protect and increase the value of clients' assets by engaging with companies. It also encourages businesses to stick to sustainable practices that support a company in the long term. The company does vote every year at more than 15.000 shareholder meetings, on over 130.000 proposals. The company states that it

generally does engage companies to allow management time to address the said issues. Should the company not address the issues Blackrock claims it will vote against management. Blackrock does also claim to have Environmental, Social and Governance (ESG) issues as an integral part of its investment stewardship activities (“Investment Stewardship | BlackRock,” n.d.).

For the last few years, Blackrock has published the engagement priorities for each year by issuing a letter from the CEO where the main factors of corporate governance are highlighted (Fink, Larry, 2017). The information is provided for the portfolio companies along with the beneficial owners of the investments. However, the asset manager also publishes engagement and voting reports for each fund which owns a stake in each company. At times the company does publish notes related to high profile proposals at shareholder meetings (“Guidelines, reports and position papers,” 2018).

Nordea asset management is the largest asset manager in the Nordics managing assets over USD 360 billion (Schwartzkopff, 2017). Nordea has been active since 2014 in its engagement, mainly in its primary markets but also internationally. Nordea has claimed that it uses its engagement with companies to improve governance systems, ESG performance and reporting. The main reasons for their level of engagement are related because the company believes this will deliver better long-term progress of companies beneficial to all stakeholders (“Summary,” n.d.). To focus the engagement the fund has ESG themes which it works with, the main themes currently relate to climate change, water, human rights and corruption (“Thematic and focus area engagement,” n.d.).

One of the cornerstones of Nordea’s engagement can be traced to its transparency as the company publishes all its voting behaviour with information on whether it is with or against management’s suggestions. Nordea does utilise OECD’s corporate governance principles when working with companies. Most importantly Nordea looks at corporate governance as indispensable part of being an owner, and as such it seeks to make a difference.

## **5.4 Summary**

Although some jurisdictions have implemented codes of conduct relating to investment stewardship, it is not deemed as going far enough by European politicians who have gone further and agreed to amendments to directives that make such codes almost mandatory for most European countries. Up until 2019, many institutional

investors will be making changes to their investment framework to incorporate stewardship into the framework.

Many large institutions have worked with investment stewardship in mind for some time and will probably continue to deepen their work. What the Icelandic companies might learn from their foreign counterparts does involve transparency. Transparency in how the investors vote, how the voting is prepared and conducted and finally by publishing each year's focus or engagement priorities. The UK stewardship code does give a solid ground to work with for most Icelandic institutional investors, but because of the small size of Icelandic society, conflicts of interests should receive a comprehensive review in each stewardship policy.

## **6 Research methodology and empirical evidence**

The data collection for the research is divided into two main qualitative categories: 1) interviews and 2) content analysis. Interviews are the primary research tool as they are an excellent way to highlight individual perceptions and gain a good overview of the market. The content analysis is meant to improve the understanding of the behaviour of institutional investors, how they work and how their methods have developed (Bell, 2014).

The interview part of the analysis is centred on interviews with institutional investors and boards members of companies to get information about the informal part of institutional investor behaviour, ‘the voice’. The content analysis part is based on data collection on how and when institutional investors have utilised proposals at shareholders’ meetings, according to publicly available data. It should be taken into account that the interview analysis is the main method used in this thesis while the content analysis is to support and show how institutional investors have evolved their stewardship in Iceland over time.

### **6.1 Qualitative research - Interviews**

There are mainly three methods used for interviews, structured, unstructured and semi-structured interviews. For this thesis, semi-structured interviews were deemed the most appropriate considering their flexibility. The interviewer had a specific and open-ended question to get as much free flow of information from the interviewee. Semi-structured interviews are useful when exploring a subject with some structure which allows for more straightforward analysis of the interview results than open interviews (Bourgeault, Dingwall, & Vries, 2010).

#### **6.1.1 Sample**

For the interviews to be insightful, it was considered essential to get the opinions of both institutional investors and listed companies. The persons contacted to gain insight into the behaviour of institutional investors were some CEO’s of pension funds and fund management companies. Hence, board members, generally the chairman of the board, and CEO, of listed companies were also interviewed to have both sides of the story. The sample, in the end, is based on the number of interviews conducted. In total 24 requests were sent out with eight that ended up answering and speaking to the author of the study. The number of representatives interviewed on behalf of institutional investors is four

while representatives of listed companies were 4. The representatives of institutional investors were in all instances CEO's of those entities and altogether they control significant assets on the Icelandic market. On the listed companies' side, two chairmen of the board were interviewed, along with a CEO and a board member. The interviews were conducted in November 2017, February 2018 and April 2018. For the anonymity of those individuals, no further information about their profile is given.

Institutional investors without a public stewardship policy were not a part of the sample. Additionally, the author is an employee of Fjármálaeftirlitið, the Financial Supervisory Authority, Iceland, as such those institutional investors whom the author does have a current working relationship with were not interviewed for this study. The institutions excluded from the sample is one of the three large insurance companies, one mid-size pension fund and two small pension funds. It does not cause a bias in the research as these companies are not deemed significant in their stewardship or size. It must also be noted that the author has not used any information which he has gained through his employer. The author has by signing his employment contract with Fjármálaeftirlitið pledged of confidentiality, about any knowledge gained during his employment in accordance with article 13 of act number 87 from 1998 on Official Supervision of Financial Activities.

### **6.1.2 Interview methods**

All interview candidates were invited to participate with an introductory email, or another digital means of contact, with a summary of the aim of the thesis along with a request for an interview. There were two different invitation templates, one for representatives of institutional investors and another for listed companies. Samples of both invites can be found in Appendix A – interview invites

The interviews all began with a brief introduction of the analysis and the subject of the interview. Additional questions were asked in all interviews to clarify some specifics that came up during the interview. The interviews were conducted in person, to gain better rapport between the interviewer and interviewee, except one which was conducted over the telephone (DiCicco-Bloom & Crabtree, 2006). The interviews were 20 to 40 minutes long without a pause and were recorded to ensure that there was no misunderstanding or misinterpretation.

The semi-structured interviews were the most appropriate considering their flexibility and their ability to get the interviewee to reveal as much information as possible. The interviewer did utilise a list of questions and keywords to ensure that

specific information was brought forward during those interviews. The list varies between the two different groups of investors and is in Appendix B – Interview . The questions are replicated in some extent from a survey used in a study published by McChaery et al. (2016b). The study was used to survey institutional investors to improve the understanding of their role in corporate governance of portfolio firms. The questions used were to gain a better understanding of corporate governance, shareholder engagement and shareholder voice such as the threat of an exit (McCahery, Starks, & Sautner, 2016b).

### **6.1.3 Limitations**

One of the main limitations of the interviews may be that those willing to do the interview may be the ones who are more interested in the subject, which may lead to some bias and considered as an empirical restriction of the analysis. The interviewees did represent pension funds and fund management companies on one side, and representatives of listed companies did have diverse backgrounds and represent companies in a variety of industries.

## **6.2 Qualitative research - content analysis**

For a better understanding of how institutional investors have conducted their stewardship and how it has evolved over the last 15 years, it was deemed necessary to examine how shareholder dissent has been in Iceland. The news system of the NASDAQ OMX exchange is a source that provides data on a lengthy period despite company bankruptcies and incomplete documentation. Thus, it also means that not many companies have been listed on the exchange for the whole period.

To be able to evaluate institutional investor engagement, shareholder proposals over the last 15 years were gathered through the news system of the NASDAQ OMX Iceland exchange. The news system contains information released by listed companies such as earnings, annual results, and insider trading to name some but most importantly, in this context, it does contain information about shareholder meetings. The information about shareholder meetings in the news system does contain a notice about meetings, the agenda of the meeting, the proposals for those meetings and finally the results of the meetings (“Company News - Nasdaq,” n.d.).

### **6.2.1 Empirical data and sample size**

The development of the Icelandic market before and after the financial crash of in 2008 is examined to get a time-series with a realistic outcome of the analysis as possible.

The period from 2003 until 2018 was chosen as it represents a good business cycle of both booms and recessions, and should give a good overview of how shareholder proposals have evolved in Iceland through different states of the economy.

Some companies may have fuller notes from shareholder meetings on their web pages but because of the extended sampling period and the fact that many companies are no longer operational as well as changes that have been made to security laws in Iceland it is not deemed feasible to use other sources than the news site of the exchange.

The number of registered shareholder proposals found in the news system was fifty-one that took place on 43 occasions. The year of 2018 has the highest number of dissent proposals or 19, still only four months down.

### **6.2.2 Methodology**

This study is based on analysis of shareholder's proposals retrieved from market notices and provided by the NASDAQ OMX Iceland exchange. The objective is to collect data about each shareholder proposal. It is performed by registering a keyword for each proposal that explains the said subject. The keywords and more detailed explanations of them can be found later in this chapter.

The sample was collected by going over each year at a time by using the news system of the exchange and searching manually for market notices that had proposals from shareholders for January 1<sup>st</sup> of 2003 until April 15<sup>th</sup> of 2018. Each sample found was then registered to a master document with the relevant details.

The shareholder notices that contained proposals are gathered into a master document where the following four categories classify the data, 1) the promoter of the proposal, 2) what year the proposal is put forward, 3) what company the proposal concerns and, 4) the subject of the proposal. Additionally, a source for each proposal is market with a direct website link to the relevant market notice in the news system of the NASDAQ OMX exchange.

The data gathered from the news system of the NASDAQ OMX Iceland exchange is about specific companies and shareholder proposals. To organise the market notices from the news system, they are sorted into a table by the company, who is putting forth the proposal and when it is available, the year of the shareholder meeting and concerning what issue the proposal is about. The proposals are classified by keywords which cover the issue proposed by the shareholder. Following are the classification keywords:

- *Remuneration* covers proposals which affect the remuneration policy of the company, the remuneration proposals related to remuneration policies and other remuneration-related issues.
- *Board remuneration* covers proposals related to board remuneration.
- *Buybacks* concerns company buybacks and the issues connected to the company bylaws surrounding buybacks.
- *Bylaws* cover other bylaws issues shareholders are concerned about than those covered here.
- *Shareholder return* relates to when shareholders are influencing, e.g. dividends, share buyback and other means of returning capital to owners.
- *Nomination committee* is when shareholders ask that a nomination committee is set up or amendment to the policy of the committee and other related topics.
- *Auditor change* covers issues where shareholders may have put forth proposals related to the potential change of auditor or other company auditor related issues.
- *Shareholder meeting* is when shareholders request a shareholder meeting related to some issues concerning the company.
- *Revaluation of asset purchase* is when shareholders ask for a revaluation related to an asset or capital purchase by the company.
- *Takeover* is when a shareholder asks for a meeting to discuss issues related to a takeover or takeover offer.
- *Voting* is when shareholders ask for cumulative voting or when shareholders ask that issues are put up for voting during and at shareholder meetings.

The content of the data file is analysed in a few ways but mostly based on the frequency occurrence. The following shows the exact analysis:

1. By the number of proposals per year to look for a trend.
2. For each company that gets a proposal to see if some companies get a higher number of proposals than others.
3. By classified keywords to see what issues get the most attention of investors.
4. If a particular promoter or type of promoter of a proposal is more active than others.

### **6.2.3 Limitations**

There are limitations in the setup of the research of the content analysis. The main one is the fact that not all cases of shareholder dissent are reported by listed companies into the news system of the exchange. A few cases are on the home pages of some companies, some reports of dissent could be found on the pages of newspapers while other lay buried in the memories of those who attended the meeting. The extended period for which the news system was inspected does make it harder to look up potential announcement outside of the news system, which is the main reasons for why the news system was the method of choice.

Considering the large number of announcements inspected and read there is the possibility that an announcement was inadvertently missed by the author especially how in light of the few instances of dissent found. It is estimated that the announcements looked through exceeded 50.000 but the ones inspected more closely were over 2.000 which were opened and read through along with attachments when applicable.

It is also important to note that not all shareholder dissent happens in public market. A significant amount of it happens in media and social media, and it does have effects on how companies operate as can be seen with the insurance companies and their dividend payments in 2016 which is covered in more detail in chapter 4.2.5.

## 7 Results

The findings of the research are split into two segments for each part of the qualitative research. The first part concerns the interviews conducted with institutional investors and representatives of listed companies. The second part is related to the content analysis of shareholder dissent reported in the news system of the NASDAQ OMX Iceland exchange. The findings highlight some aspects of corporate stewardship in Iceland over the last years and how it has developed.

### 7.1 Qualitative research –Interviews

The interviews did give a similar view of the communication between both parties. Since the number of institutional investors increased, the investors have become more proactive in their relationship with the companies, initiating contact and engaging with them to ensure that they are not working against the principal shareholder's policies. The results of the interviews can be found in the following chapters to draw out the main conclusions derived from the interviews.

#### 7.1.1 Shareholder policies

The institutional investors in Iceland begun working on their shareholder policies in earnest a few years after the fall of the Icelandic banking system. Many funds did have some semblance of shareholder policies in their investment policies as one board member of a pension fund goes over.

*“... we did not have an independent shareholder policy but some provisions in the investment policy, and then we made such an investment plan, and a part of it was the shareholder policy. The actual shareholder policy was very limited and based primarily on whether we were going to be active shareholders or not. (Cardaklija, 2015)”*

Gildi pension fund and Stefnir published their initial policies in 2013 with many institutional investors following suit. As one of the interviewees claimed:

*“A few years ago, the pension fund began with their shareholder policies. The company [that interviewee is on the board of] has always emphasised good corporate governance, so this is in*

*no way a burden. We [the board] have covered the shareholder policies, and often received a presentation from the institutional investor about their shareholder policy.” (Interviewee 8)*

As covered earlier the shareholder policies came about after the financial crisis. The policies were encouraged by ASÍ and as a reaction to the findings of a committee established on the request of the pension funds that went over the period leading up to the financial crisis. One interviewee claimed that the policies were set up because of issues related to how investors conducted themselves concerning VÍS, the insurance company, as is covered in chapter 4.2.4.

*“What happened after the VÍS case is that investors started defining how they should conduct their communication with company boards (Interviewee 3).”*

Some institutional investors claim that the above is in line with general changes in corporate governance and because of a significant shift in ownership of listed companies from individuals to institutional investors.

*“Shares are increasingly less in direct-ownership, and mostly managed by agents, pension funds, insurance companies and other funds [such as UCITS] ... We are also participating in this wave where the weight of ESG matters is increasing where investors tend to start with G [governance](interviewee 1)”*

These developments have led to changes in the corporate governance of institutional investors, those who act as agents on behalf of others. The institutional investors investing on behalf of others must protect their reputation and gain trust, or as one interviewee claims, they had to rebuild trust and find a way to do so.

*“The funds had decreased and needed to rebuild from scratch again, scratch –trust in the funds and financial system was at rock bottom. How were we going to rebuild the trust in the market again?” ...”Whether people approach this with a sincere will to better improve or whether men are just ticking in a box. Others look at this not only for the professional investor but also for the market as a whole and its goodwill. People understand that it is imperative that the market will flourish in the long run. Especially after so much shock like the one*

*we encountered. It is a great effort to restore trust; it is not a simple matter” (Interviewee 1).*

### **7.1.2 Communication between institutional investors and listed companies**

Communication between the investors and the listed companies they are shareholders in can be tricky. Sometimes it has gone wrong and been on the covers of papers, but mostly it does go unnoticed and is done professionally for the benefit of the companies in mind. That is in line with institutional stewardship literature outside of Iceland where it happens significantly behind closed doors rather than in the public eye (McCahery, Starks, & Sautner, 2016a). The same seems to be the experience in Iceland.

*“Generally board membership, changes in the articles of association and such beforehand.” and “In fact note settled in communication with other shareholders but rather with the chairman of the board ... generally, the chairman of the board knows what is underway.” (Interviewee 5)*

The consensus of the interviews was that the communication between the boards of listed companies and the institutional investors happens through the chairman of the boards, sometimes the vice chairman and the CEO.

*“Today it is very clear that the communication is with the CEO and chairman of the board. The pension funds are also working as such. We have found a basis for cooperation which is good. It means that every single member of the board, even though he is in support of someone, works with the interests of the company as a guiding principle. That is what I am experiencing today.”*  
(Interviewee 2)

The institutional investors seem to be working professionally with the listed companies and communicating with them. The communications are generally in meetings that take place in advance of the annual general meeting of the company. One interviewee mentioned that the meetings are generally about the governance of the firms rather than operational issues.

*“Companies do want to speak to the largest shareholders running up to the Annual General Meeting. Usually, this is not about*

*operations, which is covered in public meetings with market participants following the publishing of results. However, at these meetings, there is more discussion about governance, numerous issues relating to the work of the board, knowledge, even strategic focus in the coming years and if the board is equipped to drive them through. Board communication with the CEO, whether the board receives adequate information from the company and many such matters.” and “there may also be questions concerning the self-evaluation of the board or, which is best, the results of the self-evaluation. Was there some knowledge or skill lacking from the board and so on” (Interviewee 1)*

Some institutional investors may have started these meetings between the listed companies and institutional investors in Iceland, but currently, many of the listed companies do this annually.

*“... The companies have begun to contact the largest shareholders in advance. In general, not a discussion about company operations but shareholders matters such as governance.”*  
*(Interviewee 4)*

The discussion does not always go without some problems or confrontations between shareholders. One very public battle of control played out in public concerning VÍS, which was portrayed in chapter 4.2.4. That case may have been one of the reasons some institutional investors started to evaluate how they communicate with listed companies, “...started defining how they should conduct their communication with company boards” (Interviewee 3). The same interviewee went on and highlighted that it is important that when there has been a vote for a board that there is not continuous communication with the board about decisions, strategy or operations.

*“But, in some cases, people are trying to influence the regime in the middle of the term. The board is elected to make decisions. Shareholders may, however, elect a shareholders' meeting on issues such as submitted proposals or dividend payment proposals.”*  
*(Interviewee 3)*

Currently, both investors and companies agreed that the contact between the companies and investors is professional and has improved over the last few years. Although, some claim that the communication has been peculiar at times it is no longer the case.

*“I think we are going down the right path and these matters are finding some kind of balance. Shareholder policies are forming, and people are figuring out how to implement the shareholder engagement.” (Interviewee 3)*

### **7.1.3 Board member appointments**

Over the years in Iceland, one of the most controversial issues concerning institutional investors' corporate governance has been related to the appointment of board members of listed companies. Preceding the crisis, the pension funds that actively nominated people to the boards of listed companies did so with the knowledge that those board members were their representatives on that board. This practice did continue after the crash of 2008 or as one interviewee put it:

*“...these investors appointed members of the board that were very clearly represented by the relevant institutional investor concerned with the relevant owner. The owner was requesting information and kept his relationship with the company through his representative.” (Interviewee 2)*

There was a heated debate related to this when one board member of Lífeyrissjóður Verzlunarmanna was also on the board of more than one listed company, which has the potential for a conflict of interest as is covered in chapter 4.2.2. One pension fund was explicitly mentioned about appointments to the boards of listed companies.

*“It is quite known that LIVE has applied its shareholder policy differently than others. Just with its board members. At least they have changed it, so you do not sit on the board of directors [of the pension fund] and board of directors on his behalf”. (Interviewee 4)*

There are different opinions on how the pension fund should act when appointing or when not appointing board members to companies in its portfolio. One interviewee

was very clear that they should follow up on their investment in an active way, and looked at it as the part of the duty

*"Is it not irresponsible by such a large investor to not being active - not just part of being on the board of the pension fund to take responsibility and be ready to follow the investments after investment decisions by the board?" (Interviewee 6)*

The majority of institutional investors had another take on the matter and believed that it had potential for conflicts of interests and potentially detrimental for the reputation. Currently, institutional investors take a stand when voting for boards of listed companies, as well as other issues, according to their shareholder policies. Not many investors do appoint board members as only the largest can do so on its own so they would have to cooperate. Quite often communication between the chairman of the board leads to the appointment of board members as this interviewee gives an overview of.

*"Normally there is a communication with the chairman of the board leading up to the general meetings, and he knows if there are potential changes on the board and if a candidate is coming forward. Often he [the chairman] has an idea about the skills that would be helpful for the board so he may ask if there is a candidate."*  
(Interviewee 7)

This interviewee gives the impression that board candidates are arranged before it is made public which is in line with reality as it is common that it is not necessary to vote for the boards at shareholder meetings.

In many shareholder meetings in March and April of the current year, 2018, two investors have put in dissent proposals where they ask that the companies set up nomination committees. These two were a foreign investor, Eaton Vance management company, and Gildi pension fund. There has been some ongoing discussion about the nomination committees, but one interviewee said,

*"I am in favour of the nomination committees, but we are yet to find the form that best fits here in Iceland with the special circumstances where a few parties are so large they can always squeeze in a board member."* (Interviewee 5)

The establishment and development of nomination committees in Iceland is a development that will be interesting to watch in the coming years.

#### **7.1.4 Exit or threat of an exit**

In the literature it is common to talk about voice and voting with feet, selling a stake. When looking for examples of both within the Icelandic market the case of VÍS in chapter 4.2.4 comes up. In that case, one pension fund threatens publicly to sell its 10% stake in the company, thus communicating the threat of sell to the board. Another pension fund simply sold a large chunk of its stake and did not communicate about it publicly. However, it was asked about it afterwards in the news, where it cited governance issues as a reason to sell. Interviewees claimed they continuously revaluated their holdings in listed companies and they would merely sell rather than communicate the threat of a sell to the market.

*“No, we would never threaten to sell, simply sell our stake...however, we would not threaten a sale.” (Interviewee 5)*

Furthermore,

*“We have not criticised companies publicly, that is not how we do things. We would rather sell our stake which is better for our principals [clients]. We would have communicated with the company our worries about the company.” (Interviewee 1)*

Another interviewee claimed that his entity would, during a regular meeting with a company's chairman, cover the actions it could resort to, without it making a threat of selling. The interviewees did generally not know of examples of a threat of a sale or had used that as a tool to force a change within a listed company.

There was a consensus among the interviewees, representatives of institutional investors and listed companies, that the communication between them has become increasingly professional over the last few years. The shareholder policies are also better defined, and both parties have used the experience gained to find out how to implement the policies to benefit the listed companies. The communication with the listed companies goes through the chairman of the board and sometimes the CEO and not through board members that the institutional investor may have appointed to the board. All according to the rules that each company has set out in its rules, not decided by the preferences of the institutional investor.

## 7.2 Qualitative research –content analysis

When looking at the announcements Icelandic listed companies have published in the news system of the NASDAQ OMX Iceland exchange, some interesting information can be found. The main result is how dissent seems to have been almost non-existent in the years before the financial crisis in 2008. Most of the dissent found while going through company announcements are in the years after 2008 with notable peaks in 2015, 2016 and 2018.

*Table 3. The number of dissent proposals per year.*

|                   | 2003 | 2009 | 2010 | 2013 | 2015 | 2016 | 2017 | 2018 | Total |
|-------------------|------|------|------|------|------|------|------|------|-------|
| Dissent instances | 3    | 2    | 1    | 1    | 10   | 6    | 2    | 18   | 43    |
| Dissent proposals | 3    | 2    | 1    | 1    | 14   | 9    | 2    | 19   | 51    |

Table 3 shows the number of dissent proposals found for each year. The first line shows the number of instances where a company receives one or more proposals from a shareholder, irrelevant on the number of proposals included. The second line singles out each proposal and as such there were fifty-one independent proposals found in forty-three instances. The highest year is 2018 with 18 instances and 19 proposals. It is important to note that Table 3 excludes the years from 2004 until 2008 as there were no dissent issues found in the news system of the stock exchange. That there was no public dissent by institutional investors in the years running up to the crash of the three large commercial banks is a fascinating finding by itself. It is an issue that was raised in the report of the Rannsóknarnefnd Alþingis about the fall of the Icelandic commercial bank's failure. In the report, it was criticised that the pension funds did not influence the companies in their portfolio to improve their corporate governance, where investment dissent is one of the ways to do so (Hreinsson, Benediktsdóttir, & Gunnarsson, 2010)

It is a signal that capital markets in Iceland are evolving with investors such as Gildi pension fund paving the way. It seems more likely that institutional investors, and others, to challenge companies and company boards publicly, which is a significant change from the years before the crash of the Icelandic banks in 2008. It is in line with findings from a 2012 paper (A. Stachowicz-Stanusch, W. Amann, 2012) where the authors claim that corporate governance is in hibernation during the boom years but awakes again following crisis or recession.

### 7.2.1 Investors with dissent

The investors with dissent are not many, but one was particularly prominent in their dissent. Gildi pension fund has since updating its stewardship policy in January 2015 been very active in its dissent. As can be seen in Table 4 Gildi is by far the most active investor with dissent followed by a recent entrant to Icelandic capital market, Eaton Vance Management. It is going to be interesting to follow Eaton Vance and if the management company will continue to be active in its dissent towards listed companies in Iceland and if it will cover other issues besides nomination committees.

*Table 4. Investors with dissent proposals*

| <b>Company</b>         | <b>Number of dissent proposals</b> |
|------------------------|------------------------------------|
| Gildi                  | 25                                 |
| Eaton Vance Management | 6                                  |
| Unknown                | 5                                  |
| VR                     | 1                                  |
| Vilhjálmur Bjarnason   | 1                                  |
| Sundagarðar hf.        | 1                                  |
| Íscap ehf.             | 1                                  |
| EFÍA                   | 1                                  |
| Brú lifeyrissjóður     | 1                                  |
| Afl Fjárfestingafélag  | 1                                  |
| <b>Total</b>           | <b>43</b>                          |

### 7.2.2 Dissent issues

A few issues appear to stand out when examining the dissents of investors, as can be seen in Table 5, such as remunerations and company buyback allowances. In both these cases, Gildi is the most active investors in bringing forth proposals as is detailed in chapter 4.2.1. The third most frequent issue concerns nomination committees where Eaton Vance Management and Gildi pension fund have been very active in 2018. Their dissent may very much shape the board's compositions of listed Icelandic companies in the coming years.

*Table 5. Number of dissents proposals by issue*

| <b>Issue</b>                    | <b>Number of issues</b> |
|---------------------------------|-------------------------|
| Remuneration                    | 18                      |
| Buyback                         | 14                      |
| Nomination committee            | 9                       |
| Takeover                        | 2                       |
| Voting                          | 2                       |
| Auditor change                  | 1                       |
| Board remuneration              | 1                       |
| Bylaws change                   | 1                       |
| Re-evaluation of asset purchase | 1                       |
| Return to shareholders          | 1                       |
| Shareholder meeting             | 1                       |
| <b>Total</b>                    | <b>51</b>               |

The issues most commonly under dispute at shareholder meetings are related to remuneration, an issue most people can relate to, which is not uncommon to cause controversy and lead to an uproar. A recent issue in Icelandic society surrounds the remuneration of the CEO of N1 hf., a publicly listed oil retail and service company (Halldórsson, 2018). The remuneration leads to a public uproar, primarily by labour unions, along with media attention surrounding and two dissent proposals on remuneration policy.

Buyback issues are the second most commonly disputed issue. Unlike remuneration, buyback authorisations in company bylaws is an issue less talked about and receives far less coverage. The execution of the buyback has been the most relevant aspect of the dissent proposals, Gildi pension fund has been the only one to present dissent proposals related to buybacks.

### **7.2.3 Dissent proposals by companies**

When looking at companies on the receiving end of dissent proposals, the number of proposals are quite moderate and even between firms, although Sjóvá-Almennar and HB Grandi have the most proposals directed at them. Those companies have received seven and six proposals while the next three companies have four proposals as can be seen in Table 6. For both Sjóvá-Almennar and HB Grandi, a number of the dissent proposals are concerning the same issues year after year.

*Table 6. Number of dissent issues by company*

| <b>Company</b>                       | <b>Proposal</b> |
|--------------------------------------|-----------------|
| <b>Sjóvá-Almennar tryggingar hf.</b> | 7               |
| <b>HB Grandi hf.</b>                 | 6               |
| <b>N1 hf.</b>                        | 4               |
| <b>Reitir fasteignafélag hf.</b>     | 4               |
| <b>Vátryggingafélag Íslands hf.</b>  | 4               |
| <b>Eimskipafélag Íslands hf.</b>     | 3               |
| <b>Marel hf.</b>                     | 3               |
| <b>Reginn hf.</b>                    | 3               |
| <b>Síminn hf.</b>                    | 3               |
| <b>Alfesca hf.</b>                   | 2               |
| <b>Eik fasteignafélag hf.</b>        | 2               |
| <b>Hagar hf.</b>                     | 2               |
| <b>Fjarskipti hf.</b>                | 1               |
| <b>Hraðfrystihús Þórshafnar hf.</b>  | 1               |
| <b>Icelandair hf.</b>                | 1               |
| <b>líf hf.</b>                       | 1               |
| <b>Pharmaco hf.</b>                  | 1               |
| <b>Skeljungur hf.</b>                | 1               |
| <b>Tryggingamiðstöðin hf.</b>        | 1               |
| <b>Össur hf.</b>                     | 1               |
| <b>Total</b>                         | <b>51</b>       |

Shareholder dissent in Iceland may not have a long history, but Gildi pension fund and Stefnir asset management company active a few years ago and have led the way for other investors. Gildi has increased the profile of dissent shareholder proposals while Stefnir increased transparency of their actions by publishing how it votes. The issues most discussed are remuneration, buyback and the current hot topic of nomination committees. Further development is expected in the coming years by institutional investors who may have a harder time free riding on the back of Gildi and Stefnir stewardship work going forward.

Shareholder policies of institutional investors in Iceland are currently common. The policies along with better understanding of their role in investment stewardship have lead to much-improved communication between institutional investors and listed companies and increased professionalism. Investors seem abler and willing to speak their mind about issues that concern the companies they are investors in, whether it is publicly or in private talks with those companies.

## 8 Discussion

This thesis gives an overview of how shareholder engagement is conducted in Iceland, an area where there has been very limited research. It is an area of interest to many as the institutional investors in Iceland are exceptionally large.

Recently a member of the Parliament of Iceland asked the Minister of Finance and Economic affairs about the stewardship policy of the Pension Fund for State Employees, highlighting issues related to remuneration. It is one of the facts that highlight how significant the issue is currently in Iceland (Sæmundsson, 2018). The primary result is that shareholder engagement mostly happens behind closed doors, just like outside of Iceland (McCharey et al., 2016), in meetings between institutional investors and the listed companies, but has increasingly moved to the public eye with increasing shareholder dissent. For most institutional investors it is important that they realise the importance of not doing nothing, at the least supporting the decision not to be active.

### 8.1 Investment stewardship

- 1. How do Icelandic investors conduct their investment stewardship towards listed companies where they are owners?*

Investment stewardship is the communication between the institutional investors and the listed companies. The communication happens primarily with the board of directors of the listed companies, with letters sent out to the listed companies and meetings where the listed companies meet with the most significant investors. The discussion in these meetings concerns the shareholder policies of the investor and the investor's emphasis for the current year. The discussion goes on about issues such as the corporate governance of the company, board composition and dynamics. The discussion also concerns what proposals the company board is considering for the annual general meeting along with long-term strategic issues. Day-to-day operational issues or how the annual results for the prior year are usually not discussed, precisely because of potential insider information. An element that is commonly lacking for many of the policies relates to transparency.

Gildi pension fund is the institutional investor who has been most active in shareholder engagement for its portfolio. The pension fund has put forth proposals to shareholder meetings, more than half of the proposals found in the content analysis results

presented in chapter 7.2. The main issues Gildi has promoted are remuneration, share buyback and nomination committees. It is more than possible that some other investors have come to rely on Gildi with their dissent and trust that the pension fund does keep up its work, essentially piggybacking on Gildi's activism. If that is the case, it is in line with findings from Huddart (1993) who found that when there are many small shareholders and few large the small ones tend to leave monitoring to the larger one. That is not saying that other investors are not active in their engagement, but their activism is not as significant, such as Gildi with public dissent proposals. According to Davis and Kim (2007) pension funds who are independent of financial institutions, such as Gildi, tend to be more active in their investment stewardship than mutual funds are non-public. Brickley et al. (1988) support that view and explain it by the fact that the independent pension fund might be less influenced by management. Stefnir asset management company does in itself counter this by being active in its engagement despite being a part of a larger financial institution.

By publishing shareholder policies and corporate governance preferences, it is possible that the companies take the recommendations of their largest owners into account and internalise them. Which means that by merely talking about and publishing their views on corporate governance, it may lead to the companies in their portfolio taking those views into account and may how affect they conduct themselves which is in line with findings from Fitcher et al. in 2017.

Voting is one of the essential tools the investor has at its disposal, where they can vote with, against or abstain from voting on specific issues. It is hard to find reliable numbers in Iceland about voting behaviour at shareholder meetings of listed companies. The companies usually only publish what measures were adopted, and in some cases, there may be mentions of dissent proposals, but it is even rarer to find actual voting numbers for specific issues. Although sometimes voting numbers for board members can be found. It is a field where further research could be helpful in Iceland, i.e. how investors vote, with or against management and on what issues. The issues that received the most dissent shareholder proposals are the same ones in Iceland as the ones covered in the Institutional Shareholder Services report (2015) and can be explored in Figure 2.

## **8.2 Shareholder policies**

- 2. How do Icelandic investors set up their investment stewardess policies and how they compare?*

A key component of investment stewardship by institutional investor is the framework surrounding it, the shareholder policy. A few institutional investors adopted shareholder policies and investment stewardship pre-crash based on the United Nations PRI. However, following the financial crisis of 2008, Icelandic institutional investors are increasingly aware of the importance of setting policies and implementing investment stewardship. Hence, policies have become fuller and rigorous. The policies became more public in 2013 with most of the current institutional investors publishing their policies between 2013 and 2015. The institutional investors in Iceland have become such a large part of the market that they, as their foreign counterparts (Schleifer & Vishny, 1986; Kahn & Winton, 1998), that they can not easily offload their stake in listed companies and as such are forced to be active investors.

The shareholder policies of Icelandic investors are similar in setup and content; there is some difference between the policies of pension funds and fund management companies though. The latter have set up proxy voting policies, which may be related to potential conflicts of interest by the fund management companies as the three that have public shareholder policies are owned by large commercial banks. All the shareholder policies promote that companies should have the long-term interests of the company in mind, in remuneration, company strategy and other issues. Larger investors often support a board member to the board of companies. Usually, the nomination is based on the composition of the board and what skill or knowledge is believed to be lacking. There are examples of this in cooperation with the chairman of the board as explained by more than one interviewee. It is in line with findings from Bebchuk et al. who claim that investors with longer-term horizons engage boards more intensely.

### **8.3 International investment stewardship**

#### *3. How do some international investors conduct themselves in their investment stewardship?*

In most aspects, the investment stewardship of Icelandic institutional investors is like that of their neighbours. There is one fundamental difference though as the foreign counterparts generally utilise proxy voting services to perform voting and proposing shareholder proposals for them. It is common that the proxy voting services also advise them on corporate governance issues concerning the portfolio companies. An essential

aspect in the international context is the foreign investors emphasising transparency. The UK stewardship code and the changes in the Shareholder Rights Directive ensure increased transparency. The UK stewardship code calls for public disclosure on how the investors will conduct their stewardship responsibilities. Additionally, the code calls for public disclosure on how the investor casts their votes.

Only a few of the Icelandic institutional investors publish their voting behaviour at shareholder meetings. Stefnir is the investor which pioneered that kind of transparency in Iceland, with information on votes on specific issues, board members and the company has listed down dissent brought at shareholder meetings by other investors. Gildi followed up with similar transparency about its voting from 2016, and the LSR started publishing its voting on board members from 2017. According to the shareholder policy of Lífeyrissjóður Verzlunarmanna, which was agreed on in December 2017, voting behaviour is published. The remaining institutional investors do not publish their voting behaviour publicly. There are instances of smaller pension funds who are active in investment stewardship although they are not transparent about their activism (Hallgrímsson, 2016). To some, the transparency may not be the most important issue but the activism, it might also be a stepping stone in the development of the investors' investment stewardship.

When the Shareholder Rights Directive amendments are implemented into Icelandic law in the coming years, assuming that it will, there will be additional requirements for institutional investors and publicly listed companies. Some relate to more transparency by the investors while others are to ease voting for shareholders. Hence, it will continue the development of many investor's stewardship policies and engagement with investors, primarily related to transparency.

#### **8.4 Board member appointments**

Most shareholder policies published by Icelandic institutional investors claim that the said investors will support or promote board members to company boards, some shareholder policies do not take a stance on whether they will promote a specific board member or not. In every policy that covers board member appointments, the policy takes into account the composition of the board and the relevant skills that are lacking. According to some of the interviews issues such as board, member composition is one of the themes in the meetings between the listed companies and the owners of the companies. In some cases, the chairman of the board knows that there will be a vacant seat during the

next board member election and may sometimes ask for a recommendation from the institutional investor. Some of the investors have lists of potential candidates as they have asked interested parties to put in applications and can then select people from those lists.

There are also instances of resistance to institutional ownership engagement, where the reigning board and owner is not content with the “meddling” from the pension funds. One such case was at HB Grandi, which is covered in more detail in chapter 4.2.6, where the chairman of the board was not at all happy with the support of the pension fund for a board member. The then chairman showed up at the annual general meeting of at least one pension fund and appeared in an interview a centrefold with a local newspaper voicing his displeasure. The views of the chairman are not in line with those of Hirschman (1970), who gave the option of engaging or selling, while the chairman insisted that selling be the correct way for the pension funds. Generally, the board member appointments seem to be done in cooperation and harmony with the companies.

## **8.5 What does the future hold?**

It is hard to predict what the future holds in store, but based on current trends, incoming regulation and sentiment it is likely that investment stewardship is here to stay. The trend in Iceland has been towards increased activism by investors along with more transparency, with herd behaviour of investors, following each other footstep. Also, the amendments to the Shareholders Rights Directive are the fundamental driver of the coming changes in shareholder policies as has been mentioned before. It is meant to increase transparency and trust in how institutional investors conduct their stewardship. Public sentiment and pressure are also an increasingly important factor where two recently elected leaders of two large labour unions might have some impact on the policies of pension funds connected to their unions.

Icelandic capital market participants might feel well to follow their Dutch counterparts in developing an investment stewardship code for the Icelandic market which could serve as a minimum standard for investors to work by and to accelerate development of investment stewardship in Iceland. Although there could be some guidelines or code, it is essential that each investor adapt the code to its operational model and use it as a guide to develop its approach as there is not one right way to steward ones’ investments.

## 9 Limitations and future research

The research in the thesis is twofold, interviews and content analysis of shareholder dissent in the news system of the NASDAQ OMX Iceland exchange. The interviewees who accepted the invitation to speak with the author may have interest in the shareholder policies and investment stewardship and thus represent a bias for the study. It is considered necessary that the individuals interviewed represented both institutional investors and listed companies and had a varied background and experience. Thus, the author believes the potential impact of the bias is not significant.

In the content analysis of shareholder dissent in the exchange news system, the author did his best to find and cover all announcements of potential dissent recorded in the news system. The sheer amount of company announcements over the period does create the possibility that some are overlooked but to counter that some years were checked a second time to lower the possibility of a missed company announcement.

The fact that most dissent is settled between companies and shareholder before the shareholder meetings, according to one interviewee, does mean that not all dissent appears to the public. However, the author believes that the level of dissent found with the content analysis gives an excellent indication of the dissent work performed by investors.

Voting behaviour or shareholder turnout at shareholder meetings are not commonly available in Iceland which makes it hard to measure dissent of shareholders in the form of voting against management proposals, according to Fichtner et al. large shareholders tend to vote with management. The meeting minutes spell out whether proposals were agreed upon or not, and shareholder meetings the author has attended seldom call for a vote except by raising hands. Sometimes companies do vote for board members and divulge full voting numbers in those cases. It is something that can be improved in Iceland, by implementing Article 14 of the European Shareholders Rights Directive from 2007 to improve transparency surrounding the results of voting at shareholder meetings. The directive calls for companies to publish voting results on its internet site no later than 15 days after the general meeting with the number of votes and details of the voting results.

However, according to Icelandic law, it is only compulsive to register the results of the voting in the meeting minutes, not the voting tally (Company Law, 1995). Lack of information on voting results made it harder to collect further data on shareholders

proposals and dissent. Future research can be conducted by gaining more insight into voting dissent of shareholders in Iceland now that more institutional investors are publishing their voting results. Preferably the results of the general meeting should include this information for further academic work and to give shareholders more information about how shareholders regard specific proposals.

## 10 Conclusion

Iceland is one of the countries where ownership of listed companies has significantly shifted from individuals to institutional investors; this development has been quicker in Iceland than in most countries although general adoption is yet to come. This development has left institutional investors as the most significant shareholders in most listed companies, and as such with significant control of many companies. The institutions have not been very active in investment stewardship of their assets which may have been changing over the last years. These changes in ownership along with pressure from ASÍ governing body, general sentiment and the review panel of the pension funds work before the financial crisis in 2008 to name some have led to some change. The most significant change is that many institutional investors have adopted shareholder policies on how they conduct themselves in their stewardship, in some cases stopped being passive investors and become active. Others have gone further and published information on their investment stewardship, explicitly voting and by promoting dissent shareholder proposals to shareholder meetings of companies.

The primary driver for investment stewardship is for the long-term success of investments and improved corporate governance of the companies the investor has a stake in. The improved corporate governance is the crucial factor in safeguarding the investment for the investor, referring to the agency problem. Research has also shown that improved corporate governance leads to improved performance of companies. When the institutional investors are the most significant investors in a listed company, there is the risk that a smaller, very active, a shareholder may gain control of the company and may have different priorities than the institution. It may lead to the institutional investor having to react, but many have chosen to be active rather than reactive. Other vital issues interviewees mentioned on why they conducted investment stewardship related to responsibility towards the beneficial owners of the funds held by the institutional investor. Some mentioned that the investment stewardship was a journey in safeguarding all stakeholder's interests related to the investments. The journey usually starts in Governance before moving to other areas of ESG.

The qualitative research carried out for this thesis was meant to give insight into the conduct of institutional investors about investment stewardship, which the author believes it has. The interviews and the content analysis both show that investment stewardship of the institutional investors begun in earnest in the years following the

financial crisis of 2008. There was a significant milestone when Gildi pension fund published the second version of its shareholder policy, in January 2015, which it followed upon by promoting dissent shareholder proposals at multiple shareholder meetings. Another milestone was when Stefmir asset management company begun, in 2014, disclosing its voting behaviour at shareholder meetings. These changes are in line what has been going on outside of Iceland over the same timeframe, where institutional investor engagement and disclosure of stewardship activity has increased significantly.

Three main issues are most relevant ones for investors in their stewardship, remuneration and remuneration policies, share buyback and most recently nomination committees.

It is clear to the author that there are substantial changes to the Icelandic capital market about the investment stewardship of institutional investors. It is also essential that each investor shape his or her policy concerning investor engagement, independent of other investors, as there is not one right approach. The goal of improved corporate governance and performance with the portfolio companies of the institutional investors can be gained with different methods and approaches. Investors should keep that in mind and craft their path in their investment stewardship.

Although Gildi increased shareholder dissent by pushing for changes at companies with shareholder proposals the most significant part of the investment stewardship happens behind closed doors. The investment stewardship happens with communication between the companies and largest shareholders where the shareholders discuss their preferences about the corporate governance, how active the board is and long-term strategic issues. About these meetings, which generally happen before the annual general meetings of companies, details are hammered out about who will be on the board of the said company, and changes to company bylaws are discussed. The three most substantial pension funds may be large enough to place a board member at the most listed company in Iceland, but most institutional investors are not that large which leads to cooperation on investment stewardship when they do want to have a significant influence on the corporate governance of a company.

There have naturally been some missteps while investors and companies have been learning the ropes no how to conduct investment stewardship. The consensus of the interviewees was that the institutional investors and companies were crafting a path that is mutually beneficial and that the stewardship process has become more professional over time. One of the necessary steps was to formulate shareholder policies to frame how

the investment stewardship is conducted. The institutional investor has been picking up knowledge from foreign counterparts, and one foreign hedge fund company has entered the Icelandic investment landscape by promoting nomination committees to its portfolio companies with shareholder proposals. Work relating to other aspects of the ESG spectrum is increasing. There are factors such as changes in the law governing pension funds and the founding of IcelandSIF (Iceland Sustainable Investment Forum). Incoming regulatory changes and general social development make it very likely that investment stewardship is here to stay as a part of the investment strategy of institutional investors.

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## Appendix A – interview invites

### Invites for representatives of institutional investors:

Bjarni Magnússon

Meistararitgerð Viðskiptafærði

Háskólinn í Reykjavík

Sími 663-0435 / tölvupóstur bjarnim09@ru.is

Reykjavík, [Dagsetning]

[Nafn]

Efni: Samskipti stofnanafjárfesta við skráð félög

Ég heiti Bjarni Magnússon og er að taka viðtöl vegna MS ritgerðar minnar í viðskiptafræði við Háskólann í Reykjavík. Ritgerðin fjallar um það hvernig stofnanafjárfestar haga samskiptum gagnvart skráðum félögum á Íslandi. Sérstaklega er litið til hluthafastefna stofnanafjárfesta og hvernig þeim er beitt.

Mig langar til þess að ræða um hluthafastefnu þíns sem fagfjárfestis; hver sú stefna sé, hvernig henni er beitt og til hvaða þátta er horft við beitingu hennar. Enn fremur hvernig samskipti við skráð félög fari fram og hvernig haldið er utan um þau.

Viðtalið, sem ekki mun taka lengri tíma en klukkustund, er á því formi sem er nefnt er opið viðtal (e. unstructured interview). Það þýðir að viðtalið þróast líkt og samtal en þó hef ég viðtalsramma (þætti) sem þyrfti að fjalla um í viðtalinu.

Vegna úrvinnslu ritgerðarinnar óska ég eftir því að fá að taka viðtalið upp til úrvinnslu fyrir mig. Fullum trúnaði er að heitið. Upptökunum er fargað þegar verkefninu er lokið. Ég gef ekki upp hverjir mínir viðmælendur eru.

Hluthafar hafa nokkrar leiðir til að segja sitt um starfsemi félaga og eru tvær leiðir algengastar til að tjá óánægju sína. Annars vegar er sú leið að segja hug sinn við stjórnendur eða hluthafa og svo hin leiðin að selja hlut sinn í viðkomandi félagi. Mig langar að ræða hvernig þú sem stofnanafjárfestir hagar samskiptum þínum við skráð félög.

Því óska ég eftir því að fá að ræða við þig um þessi mál eftir þínum hentugleik.

Með von um jákvæð viðbrögð,

Bjarni Magnússon

**Invite for representatives of listed companies.**

Bjarni Magnússon

Meistararitgerð Viðskiptafærði

Háskólinn í Reykjavík

Sími 663-0435 / tölvupóstur bjarnim09@ru.is

Reykjavík, [dagsetning]

[nafn]

Efni: Samskipti stofnanafjárfesta við skráð félög

Ég heiti Bjarni Magnússon og er að taka viðtöl vegna MS ritgerðar minnar í viðskiptafræði við Háskólann í Reykjavík. Ritgerðin fjallar um það hvernig stofnanafjárfestar haga samskiptum gagnvart skráðum félögum á Íslandi. Sérstaklega er litið til hluthafastefna stofnanafjárfesta og hvernig þeim er beitt.

Flestir íslenskir stofnannafjárfestar hafa sett sér svokallaðar hluthafastefnur þar sem þeir fjalla um samskipti sín við skráð félög, hvernig þeim er háttað og hvaða viðmið fjárfestirinn hafi vegna samskipta sinna. Hluthafar hafa nokkrar leiðir til að segja sitt um starfsemi félaga og eru tvær leiðir algengastar til að tjá óánægju sína. Annars vegar er sú leið að segja hug sinn við stjórnendur og reyna hafa áhrif á stjórnun félags og svo hin leiðin að selja hlut sinn í viðkomandi félagi. Mig langar að ræða hvernig þú sem fjárfestir og stjórnarmaður hefur upplifað samskipti við stofnanna fjárfesta.

Viðtalið, sem ekki mun taka lengri tíma en klukkustund, er á því formi sem er nefnt er opið viðtal (e. unstructured interview). Það þýðir að viðtalið þróast líkt og samtal en þó hef ég viðtalsramma (þætti) sem þyrfti að fjalla um í viðtalinu.

Vegna úrvinnslu ritgerðarinnar óska ég eftir því að fá að taka viðtalið upp til úrvinnslu fyrir mig. Fullum trúnaði er að heitið. Upptökunum er fargað þegar verkefninu er lokið. Ég gef ekki upp hverjir mínir viðmælendur eru.

Því óska ég eftir því að fá að ræða við þig um þessi mál eftir þínum hentugleik.

Með von um jákvæð viðbrögð,

Bjarni Magnússon

## Appendix B – Interview guidelines

*Interview guidelines for representatives of institutional investors.*

- Á þitt félag í samskiptum við stjórn og stjórnendur skráðra félaga sem það á í.
  - Hvernig fara þau samskipti fram
- Umræður við stjórn án aðkomu stjórnenda
- Er haldið utan um samskipti við skráð félög – hvað er skráð ( samskipti – atkvæði – haft skoðun og kosið um stjórnarskipan)
  - Að þau hafi farið fram
  - Í hvaða formi þau hafi verið
  - Hvað hafi verið rætt
- Hefur selt bréf í skráðu félagi vegna óánægju?
  - Eða hótað sölu – hvort það virkar?
- Leggja til ákveðna aðgerð við stjórnendur eða stjórn skráðs félags
- Gagnrýna stjórn og stjórnendur á ársfundi eða opinberlega
- Vekja umfjöllun um atkvæði á móti stjórnendum
- Málsókn gagnvart félagi eða stjórnendum þess
- Aldrei átt í samskiptum við skráð félag í eignasafni
- Þegar verið er að undirbúa aðgerðir vegna óánægju með árangur og stjórnun skráðs félags, til hvaða þátta er horft, eru einhver innri viðmið um hvernig samskiptum skuli háttað, hvernig tillögur skulu lagðar fram á fundum (aðalfundum).
- Er horft til atriða eins og möguleikans á að selja fjárfestingu (flot, e. Liquidity) – hlutfallsleg fjárfesting í skráðu félagi (eignarhluti í eigin safni sem og sem hlutfall af útgefanda).
- Hótun um að selja – hvernig er tekin ákvörðun um það? Hangir það saman með ákvörðun um samskipti við hluthafa
- Annað sem skiptir máli að komi fram varðandi samskipti við stofnanna fjárfesta

*Interview guidelines for representatives of listed companies.*

- Er skipan þín í stjórn fyrir atbeina fagfjárfesta líkt og lífeyrisjóða?
  - Eftir skipan þína, hafa verið samskipti við viðkomandi aðila? Regluleg?
- Hefur þú átt í samskiptum við stofnannafjárfesta vegna þess félags sem þú starfar hjá/fyrir
  - Hver hóf þau samskipti
  - Voru þau samskipti í samræmi við hluthafastefnu viðkomandi fjárfestis?
  - Voru þau samskipti fagleg og til þess gerð að auka veg félagsins?
  - Fjallað þú um fundi með fagfjárfestum – hvernig þeir eru og hvernig upplifun þín af þeim er.
- Hefur stofnanna fjárfestir hótad sölu á hlutum sínum í félagi til að knýja fram breytingar? Eða selt bréf í félaginu
- Voru lagðar til ákveðnar aðgerðir af hendi fagfjárfestunum
- Hvernig er brugðist við samskiptum fagfjárfesta við félagið?
- Finnst þér hlutir sem megi fara betur hjá íslenskum stofnanna fjárfestum?
- Annað sem þú vilt ræða um samskipti þín við stofnannafjárfesta?