



# Sustainable Capital Markets Union Manifesto

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A photograph taken from a low angle under a bridge, looking out over a body of water towards a city skyline. The water is dark and reflects the sky and buildings. The bridge's structure is visible in the foreground, and the city buildings are in the background. The text is overlaid on the left side of the image.

**Aviva will focus on maximising our positive impact in transforming capital markets so that we help to create an integrated, sustainable single market in capital in the EU. We will continue to encourage and support European and global companies that we invest in to integrate sustainability into their long term strategy and reporting. This will enable our analysts and fund managers to integrate these issues into their investment decisions and help to protect the long-term value of our clients' investments.**



# We will be regarded as good ancestors

Aviva has a proud history of over 300 years. In the EU, we operate in the UK, Ireland, France, Italy, Spain, Poland and Lithuania. To say that radical change has taken place in these countries and across Europe during our lifetime would be saying the obvious. The world is unrecognisable.

But some things do not change: the need for a company like us, as an insurer and investor, to have thoughtful strategic planning; to adapt to changing circumstances; to think in the long term; and to analyse carefully the opportunities and risks ahead, so we look after our customers and their families for the long term.

The recent financial and economic crisis put all that at risk. The flaws in the system were exposed. Immediate action was needed. But now that the fire has been tackled, we need to take a breath and look at the longer term measures required to rebuild our model in a sustainable way. We need to tackle unsustainable economic activity motivated by the assumption of unlimited natural resources and driven by short-termism.

My vision is that, as business leaders, we will be regarded as good ancestors by future generations. The same, of course, applies to our politicians.

## I believe in:

- the power of the market to catalyse innovation and entrepreneurialism to meet our growing demand for goods and services within the EU and across the world;
- the role of governments to correct market failure;
- the call for a capital markets union to develop - across the EU - a more robust and balanced system to pump money around our economy, from a variety of sources, to help, notably, our SMEs.

This is why a capital markets union needs to help take forward the Europe 2020 agenda, because public policy-makers, at a national, European and global level, need to move capital markets onto a more sustainable basis.

Aviva, as a British, European and global company, has an undeniable long term interest in this work: the underlying issues are material to the long term success of many of the companies and economies in which we invest. Reforms will benefit the long term investment returns of our clients and shareholders, and their families.

I believe this paper's key contribution is the series of ambitious and systemic, yet practical and proportionate, measures for a sustainable capital markets union under the four pillars of better information; long term success; capital for sustainable growth; and increasing responsible ownership. More fluidity in European capital markets across Member States is fundamental, but not enough in itself.

Aviva will focus on maximising our positive impact in transforming capital markets so that we help to create an integrated, sustainable single market in capital in the EU. We will continue to encourage and support European and global companies that we invest in to integrate sustainability into their long term strategy and reporting. This will enable our analysts and fund managers to integrate these issues into their investment decisions and help to protect the long-term value of our clients' investments.

So I welcome President Juncker's push for a capital markets union under Lord Hill, as well as Vice President Timmermans' sustainable development responsibility. And I welcome the previous President's push on a long term vision under the EU2020 agenda.

In simple terms, politicians and businessmen have a moral and economic duty to take action to protect the interests of future generations, and why, as CEO of my own company, I must act in a way to ensure Aviva's own sustainability over the next 300 years!



Mark Wilson - CEO, Aviva

**“But some things do not change: the need for a company like us, as an insurer and investor, to have thoughtful strategic planning; to adapt to changing circumstances; to think in the long term; and to analyse carefully the opportunities and risks ahead, so we look after our customers and their families for the long term.”**



## Foreword Euan Munro

# An opportunity to shape a better future

I can see the real benefits of getting our capital flowing more easily across the single market.

This paper clearly sets out that we believe the current structure of the European, and global, economy is unsustainable.

We also believe that policy-makers have an unprecedented opportunity to shape a better, more sustainable future for ourselves and our children. This will also enhance the long term financial value of companies, assets under management and entire economies. This is clearly critical for us as investors, and for our clients - citizens of our European countries.

Policy-makers have a duty to the well-being of current and future generations, as well as the values and environment in which we work and live. As asset owners and asset managers, we must do what we can to protect, and enhance, the value of assets owned by our clients.

This includes expecting our policy-makers to address the key sustainability challenges within our capital markets and the broader economy. Government inaction in this area will reduce the well-being of current and future generations.

That is why I welcome President Juncker's push for a capital markets union. I want to ensure that this is sustainable from the very beginning; that we show we have learned the lessons of the recent financial and economic crisis; and that it is embedded in the overall longer term EU2020 strategy, and beyond.

I am extremely proud that Aviva Investors already does a great deal across these areas to show that we can have responsible, sustainable capitalism, working and competing successfully with a long term perspective. For example, we have helped to prevent drilling in Virunga National Park in the Congo, a UN-protected area of scientific importance, through our dialogue with the company we were invested in.

I share Mark's vision that we seek to be regarded as good ancestors by future generations.

I am committed to use our influence as investors to work towards more sustainable capital markets within the European Union, and globally, because our economies are interconnected and interdependent. So I would urge others to engage in this capital markets union so that governments ensure the sustainability of the system they establish.



**Euan Munro - CEO, Aviva Investors**

This paper proposes a four-fold framework for policy-makers to harness the investment influence under sustainable capital markets:

- 1 to provide better information about companies
- 2 to reward long term success
- 3 for growth to be robust and sustainable; and
- 4 to increase responsible ownership.





**“We believe that policy-makers have an unprecedented opportunity to shape a better, more sustainable future for ourselves and our children. This will enhance the long term financial value of companies, assets under management and entire economies. This is clearly critical for us as investors, and for our clients.”**

Aviva is one of the largest pensions and insurance companies in the world. We manage over €300 billion of assets, making us a global institutional investor. Our history goes back more than 300 years to 1696. As both insurers and investors, we are accustomed to thinking about the long term.

Over the coming decades we see a new strategic risk to European and global economic growth from two sources:

1. Unsustainable economic activity that assumes unlimited natural resources. This creates a fundamentally flawed pricing system in capital markets.
2. Capital markets that are systematically short-term. This magnifies the problems associated with a flawed pricing system.

We are therefore very pleased to see the inclusion of sustainable economic growth and climate change among President Jean-Claude Juncker's ten priorities.

We believe that whilst good progress has been made by the EU institutions, there is more that can be done. To that end, the purpose of this paper is to make specific suggestions to EU policy-makers to help them ensure that the opportunity is not missed to put capital markets and economic growth onto a more sustainable and integrated basis through a Sustainable Capital Markets Union (SCMU).

To tackle these challenges there are four broad areas of policy action required:

### 1 Better information, better companies, better growth

The more of the right information that is available to investors about companies, the better the investment decisions.

### 2 Reward for long term success not failure

Short-termism remains in incentives for those in the financial sector. We need to align incentives with long term performance and sustainability.

### 3 Capital for sustainable growth

Aviva believes growth has to be robust and sustainable. EU policy-makers can help create that environment.

### 4 Increasing responsible ownership

Increasingly, we are all owners of companies through our pensions. It is crucial we all understand how our money is used to influence and encourage responsible investment.



Over €300 billion

of assets managed, making us a global institutional investor

## Aviva's background on the issue

### Why does a Sustainable Capital Markets Union matter?

There is no doubt that there are currently strong political pressures for economic growth in the EU area. Policy-makers are charged with the substantial task of ensuring that the best conditions for capital flow are achieved whilst at the same time ensuring that mistakes that led to the financial crisis are not repeated. It is also clear that public trust in the current capital markets is still at a historical low point.

What we offer in our vision of the future is an opportunity for policy-makers to tackle those four pressures.

As well as looking at capital flows, we suggest creating conditions for economic growth on a sustainable basis, ensuring companies think about the long-term health of the economy, environment and citizens. We see a critical role for investors' stewardship (the way they interact with the companies they own) and the promotion of properly engaged investors in this debate. This moves us away from the corrosive short-termism that caused problems as wide-ranging as the financial crisis and climate change.

Finally, by bringing European citizens into the system with a better understanding of causes and effects, public trust can be rebuilt.

### Why does Aviva care about a Sustainable Capital Markets Union?

We believe that we have both a commercial interest and a duty to participate in this debate.

Our commercial interest is because climate change and other issues arising from unsustainable development will affect the way in which our business assesses risk. The assumptions we make underpin the insurance products that our industry provides, for example when property is affected by severe flooding. These sustainability changes potentially make significant proportions of the economy uninsurable, as they are too much of a risk. They therefore shrink the market we can work with.

In addition, the issues of good corporate governance and sustainable economic development have a clear material impact on the long term success of the companies and economies in which we invest. In short, it is in our customers' interests that companies and economies are sustainable.

Policy-makers have a duty to the well-being of current and future generations, as well as to the environment upon which we all depend. As asset owners and asset managers, we believe we and others in our industry have a legal duty to do what we can to protect and enhance the value of client assets. We think this includes helping policy-makers address the key sustainability challenges within our capital markets and the broader economy.

### What is our focus?

The focus of this paper is how the EU can promote more sustainable and responsible capital markets, with more engaged investors helping to support better governed companies that take a long term view on value creation.

We see the primary failure of the capital markets in relation to sustainable development as one of misallocation of capital. This, in turn, is a result of national governments' failure to act properly

to ensure that environmental and social costs are reflected in companies' profit and loss statements. As a consequence, the capital markets do not incorporate companies' full social and environmental costs.

Until these market failures are corrected through government intervention of some kind, it would be irrational for investors to incorporate such costs since they do not affect financial figures or appear on the balance sheet, thereby affecting companies' profitability. This means that corporate cost of capital does not reflect the sustainability of the firm.

The consequences of this are that unsustainable companies have a lower cost of capital than they should. This means that they are able to finance their activities more cheaply and so are unfairly more competitive than their more sustainable peers.

### What can be done?

We believe that policy-makers need both to change the pricing signals within the market and improve the readiness of the capital markets to integrate corporate governance and corporate sustainability issues.

With our proposals, however, we have chosen to focus more on market structure than on market prices.

These proposals on capital market structure do not replace the need for government actions to ensure that companies reflect the costs of the many external factors surrounding unsustainable economic development in their balance sheets. If the economy is to be moved onto a truly sustainable basis, then we would expect to see governments taking action to correct the many distortions in the pricing systems on fisheries, freshwater, climate change and natural resource depletion.

This is how sustainability issues become relevant to our corporate valuation work, and how our capital is put to work in the right places. This requires us, for example, to set standards, create fiscal measures such as carbon taxes, or set up market mechanisms such as carbon trading schemes that price the external factors and ensure that the negative factors are corrected. Other organisations such as the World Bank, the OECD and the Sustainable Development Solutions Network are already working in this area. This is why we focus more on the structure of markets and the systematic promotion of long term stewardship and engaged investors.

### Why should the EU institutions take on this role?

Many of our proposals can only work on an EU wide basis where co-ordination is needed to ensure that the changes made will work effectively. Cross-border engagement by investors is one such example.

The European Union institutions have a crucial role in being able both to legislate and use convening powers to ensure change. There is also a role for the EU to play on the international stage in ensuring change also happens globally such as at the G20 and UN level.



**These proposals on capital market structure do not replace the need for government actions.**

## Policy recommendations

### 1. Better information, better companies, better growth

Our recommendations fall into four broad areas and should be seen a basket of policy interventions that will act in concert to complement and reinforce each other - not a menu.

Information is the lifeblood of capital markets. If the information that market participants rely on is short-term and thin, then these are the characteristics that will define our market.

Bloomberg Data shows us that of 25,000 companies surveyed, 75% do not produce even one data point on sustainability information. We need more of this information, and we need it to be easily comprehensible to European citizens.

The EU institutions have acted decisively so far to agree the Non-Financial Reporting Directive. This requires large companies to report on or explain sustainability issues such as the environment and human rights. This is an excellent step forward and extremely welcome. Three actions now need to be taken to ensure that this policy is effective:

1. As a matter of some urgency, it is crucial that this legislation is finalised through EU level 2 technical measures, with guidance being made available as soon as is possible to the over 6000 companies in scope across Europe. Otherwise they will not know how to prepare to avoid the negative consequences of any future impact assessment;
2. It is also important to ensure that this information is embedded in long term investment analysis so as to ensure that conflicts of interest and market inefficiencies in analysing this information are overcome (see below); and
3. Robust and authoritative benchmarks of corporate performance in the area of environmental, social and corporate governance (ESG) performance should be constructed, with the results being made available to the public. Our fear is that the key performance information conducted in this area will have to be purchased and therefore only available to those that can afford it. This is undemocratic and will render the Non-Financial Reporting Directive less influential, as civil society will not have the resources needed to understand and analyse the information of the performance of lagging companies.



**Information is the lifeblood of capital markets. If the information that market participants rely on is short-term and thin, then these are the characteristics that will define our market.**

**Detailed policy suggestions:**

● **Investment banks** should be required to include a view on a company's performance on corporate governance, corporate sustainability, culture and ethics when they make recommendations to investors regarding their Buy, Sell and Hold recommendations.

If they are not required to do so, our experience to date suggests that the conflicts of interest in this sector of the capital markets will encourage them not to comment on this information for fear of losing lucrative corporate clients and thus discouraging companies to act in a sustainable way.

● **Fund managers** should publish a report to their clients showing how they have considered sustainability when voting.

Fund Managers with more than €8 billion under management should - on a comply or explain basis - publish a report to their clients explaining how they have behaved as good stewards of their clients' money and how they have considered sustainability in their voting decisions at Annual Stewardship Meetings with their clients. This will encourage fund managers to consider this data in their voting decisions.

● **Investment consultants** should be required to include an analysis of how well corporate governance, corporate sustainability, cultural and ethics issues are integrated into investment decisions by fund managers in their recommendations of which fund manager to select.

Investment consultants are very powerful and advise on trillions in assets, typically in large pension schemes, and yet they are poorly understood. While there are some exceptions - such as Mercers and Towers Watson - they generally neglect to examine

properly how fund managers analyse corporate governance, corporate sustainability, cultural and ethical issues when investing. They also tend to overlook how effective fund managers are as owners - or stewards - of companies when promoting better performance in these non-financial areas.

Investment consultants advising on more than €8 billion in assets under management should also be required to report to their clients annually on how well they think fund managers are performing in this area, or again, explain why they have not done so. This would encourage fund managers to consider this data when investing, and to behave as better stewards of other people's money.

● **Proxy voting agencies**, who are instructed to vote on behalf of investors, should be encouraged to explain their rationale for their voting decisions to companies and investors.

Proxy voting agencies also have significant potential to sway how ownership influence is exercised via the voting process, as they advise a substantial portion of the market at shareholder meetings. Furthermore, requiring them to consider ESG performance in their voting recommendations would help to ensure that this information is embedded in the ultimate voting decisions.

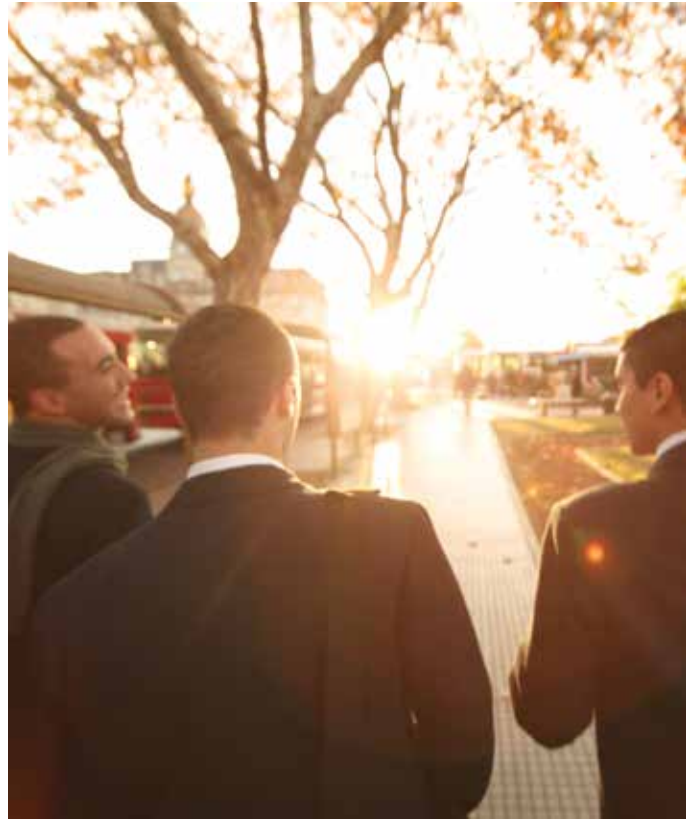
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## Policy recommendations

### 2. Reward for long term success not failure

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One of the underlying causes of the financial crisis in 2008 was the incentive structure throughout the markets. The incentives focused too many market participants on short-term profits. They looked only so far as the next quarterly earnings, at the expense of paying attention to the longer-term fault lines that were emerging. This short-termism still needs to be addressed.



**One of the main sources of market inefficiency is an excessively short-termist view among market participants. For example, the close and frequent monitoring of fund management performance by pension fund trustees can result in fund managers feeling pressured into maintaining high levels of short-term performance relative to the benchmark to retain funds.**



**Detailed policy suggestions:**

● **Investment consultants' fee structures** should be aligned with the long-term performance of the funds that they advise upon.

We believe that the current structure of consultant incentives encourages changes between fund managers that are too frequent. This is because the consultant will receive considerably more in fees for running a new tender process, than for being retained as an advisor.

● **Fund manager bonuses** should be based both on an evaluation of the fund manager's long-term ability to generate investment returns as well as a view on how they are performing as stewards of capital.

An evaluation of stewardship performance is routinely overlooked. In addition, further realignment of incentives to the long term performance of the fund will encourage investments in companies creating long-term sustainable growth, which will be good for the European economy. The EU should commission detailed research in this area to establish an appropriate performance benchmark in relation to stewardship and long term investing.

● **Executives on stock exchanges** should also be rewarded for their work in ensuring that the companies that list on their exchanges are well governed and sustainable - and sanctioned when this work is poor.

Currently, the remuneration of many executives on stock exchanges is predominantly focused on earnings per share or total shareholder return. This encourages too much focus on high frequency transactions. While it is appropriate to reward the creation of shareholder value, we believe it is also appropriate for remuneration committees to reward good practices by executives when promoting good corporate governance and corporate sustainability.

● **Investment bank research** paid for from commission charges should not be banned but harnessed to encourage sustainable investment.

Instead of potentially banning the use of commission for research, legislation should stipulate that all investment bank research needs to disclose the corporate governance and corporate sustainability factors considered by the analyst in making an investment recommendation on a particular company. This would increase corporate accountability in this area and produce better investment research. This would, in turn, support longer term and more sustainable investment decisions by fund managers.

● **Fund managers** should be required to allocate at least 5% of the research commission budget to ESG research from sell-side brokers, or explain why they have not done so. This would reward sell-side brokers for conducting this analysis, further building the small but influential market in this area.

● **Companies** should be required to report to the markets less frequently but on the wider set of issues including governance, sustainability and culture set out in the Non-Financial Reporting Directive.

This would stop the obsessive drive for quarterly results that companies are strongly focused on. It would allow those companies to begin to think more long term in their outlook.

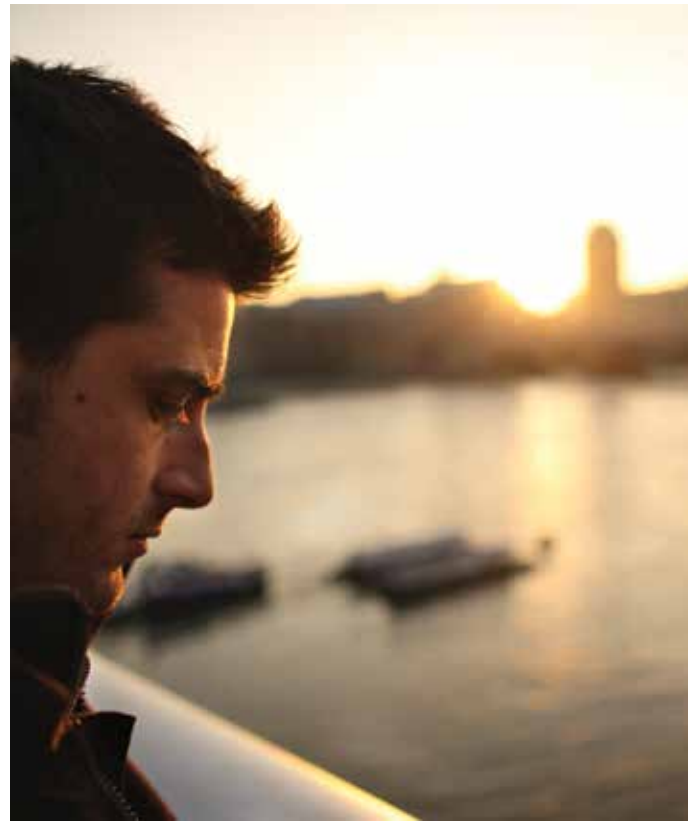
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## Policy recommendations

### 3. Capital for sustainable growth

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At Aviva we believe that there is significant potential for sustainable growth to be created through a capital markets union. EU policy-makers, in conjunction with actors such as the European Investment Bank (EIB) and European Central Bank (ECB), can work to develop a framework for growth through a sustainable capital markets union (SCMU) that includes:



#### Regulation

Regulatory changes that can unblock and expand the use of Europe's capital markets for investment in long-term sustainable infrastructure and enterprise, for example:

#### Standards

Standards and labelling for investors to allow easier comparison and analysis of investments in - amongst others - SMEs, infrastructure investment, public-private partnerships and Green bonds;

#### UCITs

EU standards on SME investment could also facilitate the creation of an Undertaking for Collective Investment in

Transferable Securities (UCITs) style retail product as well as institutional investment;

#### Centralise

Centralised resources such as infrastructure pipeline websites so that potential investors can easily access information on projects that require funding as well as standardised information on credit-worthiness of SMEs;

#### Frameworks

There is a significant regulatory disincentive against investing in unlisted equity, regardless of associated risk. EU policy-makers could address this by providing suitable regulatory

frameworks to support low risk equity investment (for example equity investment in infrastructure / equity investment without leverage).

#### Finance and investment

The use of the EIB to provide joint financing with institutional investors to boost growth through public-private partnerships;

#### Debt purchase

The ECB to consider in its mandate of purchasing debt whether it can orientate its purchases towards more sustainable investments and encourage demand in any new

types of securities markets created to support SMEs.

It is also crucial that the highest level of policy-makers work more closely with those at the highest level of the financial sector who have the power to mobilise investment for growth. In order to secure this capital, we need more planning and research for the future. For example, the International Energy Agency estimates that incremental investment in the energy sector alone will need to reach around \$1 trillion a year from 2012-2050 in order to keep global warming below two degrees Celsius.

**Detailed policy suggestions:**

● **The EU should explore** critical regulatory changes that could unblock and expand the use of Europe's debt capital markets for investment in long-term sustainable infrastructure and enterprise.

● **There is a significant lack** of standardisation of terms for SME investments/loans. EU policy-makers could address this by providing frameworks that, where achievable, create standardised terms/EU standards that will help facilitate investment into SMEs;

● **Once standardised terms** have been created for SME investments and loans it is foreseeable that a UCITS style product investing in these areas could be created through an EU label.

● **Creating centralised information** banks for funding have proved successful in many areas, from attracting institutional investment through to crowd-funding. The EU can do more to bring together those that need funding and institutional investors. This could include creating "pipe-line" websites where projects are listed with terms and funding requirements for investors to review. It is also crucial that information on SMEs' credit is standardised and made more widely available for investors to be able to lend directly.

● **To take the market further** and deliver its full potential for sustainable development, critical policy issues are emerging for the 'green bonds' market, including common standards to ensure market integrity, tax incentives to encourage inflows and credit enhancement to enable institutional allocations. Efforts to restart "good securitization" should crucially incorporate the sustainability dimension.

Globally, the spotlight is growing even brighter on the world's largest asset class – the US\$100trn bond market, which provides essential financing for governments and corporates to fund long-term investment. Governments, for example in Brazil and India, are upgrading their fiscal & regulatory incentives to encourage investments in 'infrastructure bonds' – and the EU's Project Bond initiative has considerable potential for expansion. A potential pillar of this is the green bond market which raises ring-fenced financing for investments in clean energy and resource efficiency. Global 'green bond' issuance has so far reached USD24bn in 2014, compared with USD11bn for the whole of 2013. As Aviva we have also worked with the UK's Green Investment Bank which helps create public-private partnership investment into infrastructure. This is worth exploring at an EU level.

● **Two preliminary policy actions** are required for a green Asset Backed Securities (ABS) and Covered Bonds purchase programme to be a possibility for the ECB in the future. First, creating the market requires standards and labelling that make it easy for investors to identify which securities are green. Secondly, aggregation facilities will be necessary to pool together fragmented renewable energy and energy efficiency projects.

The European Central Bank can be a powerful actor in sustainable investment. The aforementioned move could be advanced specifically through the recent announcement by the European Central Bank purchases of Asset Backed and Covered Bonds which could be better aligned with the EU's low-carbon goals. This would help to reduce the risks of environment and climate change shocks that introduce unwanted stress on finance and banks. However, the green deal flow is not currently sufficient to cover the sums in discussion. Individual banks might not be able to have the necessary amount of green loans of a given type to do this – meaning a public-private partnership between fund managers and a publicly sponsored facility might be necessary. The EIB's proposed Renewable Energy Platform for Institutional Investors (REPIN) is an exciting idea that could help address this issue.

● **A high-level EU forum** should be created for the chief executives of leading financial institutions in the EU and the EU finance ministers to work together on new ways to raise and underwrite capital and infrastructure projects.

There are many bilateral and national meetings that occur in this area but the convening power of the European Union should be harnessed to ensure that decision makers are able to work collectively together to remove barriers to investment.

● **All EU Governments** should be required to develop national capital-raising plans informing the Commission how they intend to finance the delivery of a zero-carbon economy and meet, for example, the UN Sustainability Goals.

Intergovernmental organisations have traditionally been good at sourcing public financing but not yet as successful in leveraging private finance. If we are to raise this money in an efficient, effective and sustainable manner, we collectively need the international community to develop a well-considered international capital-raising plan that coordinates national plans and includes a view on the money that can be raised via infrastructure investment, project finance, corporate debt, foreign direct investment, equity investment as well as sovereign and Multilateral Development Bank debt.

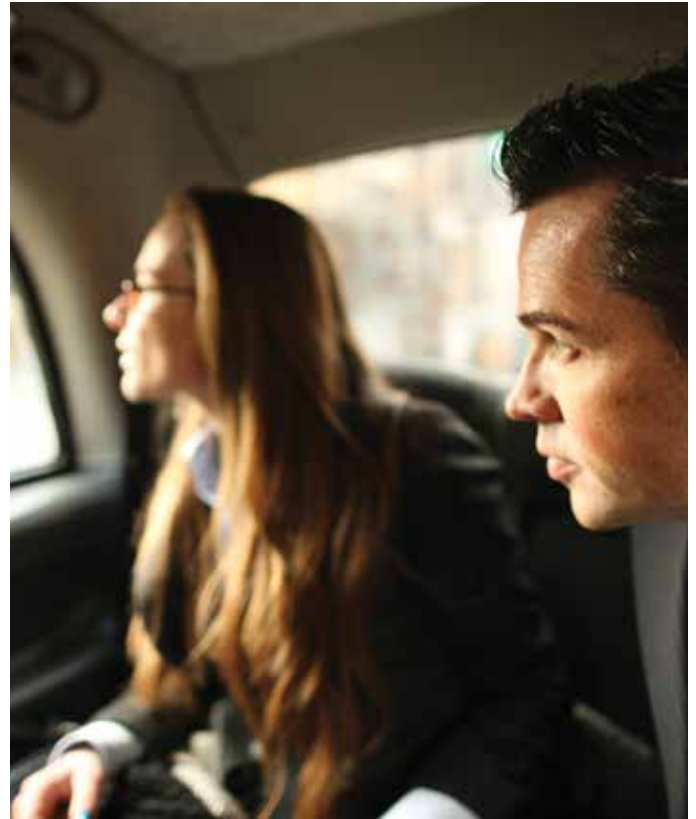
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## Policy recommendations

### 4. Increasing responsible ownership

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The ability of capital markets to influence companies into acting sustainably originates from the ownership rights they have through equities in those companies. As a recent example, Aviva investors, with other investors, helped to prevent drilling in Virunga National Park in the Congo - a UN protected area of scientific importance - through dialogue with the company using the investors' voting rights as a persuasive measure.



Demand for good stewardship is low. There are three reasons for this.

- 1 The so-called free-rider problem i.e. good engagement by one investor benefits all holders of the stock.
- 2 Levels of financial literacy are low and individual investors generally do not think to ask.
- 3 The small minority of investors that do think about these issues are neither able to access consistently the required level of information they need on how their capital is being put to work, nor how their influence is being used at company annual general meetings.

These issues magnify and reinforce each other. A lack of informed demand leads to a significant underinvestment in stewardship by fund managers. Consequently, shareholder democracy has become dysfunctional.

**We believe all Member States should have compulsory financial literacy in national curricula.**

**Detailed policy suggestions:**

● **Guidance** should be introduced to encourage Member states to make sure financial literacy on the structure of the capital market and the role of the individual in promoting shareholder democracy is a key component of the national curriculum in education.

Countries such as the UK are now working towards ensuring financial literacy is mandatory in the national curriculum. We believe that encouragement from the EU for all Member States in this area would be a positive move allowing citizens to understand better the stake they have in the financial system.

● **The EU** should act so that all EU Governments ensure that all national governance codes promote the integration of sustainable development into corporate governance mechanisms such as audit, internal control, remuneration and board succession for companies.

By ensuring that governance codes include these requirements, it will mean that companies are taking decisions that are sustainable and long-term throughout the management layers.

● **The EU** should act to ensure that all EU Governments develop national Stewardship Codes that promote voting and engagement.

The experience of the UK Stewardship Code in this regard has been very positive.

● **An EU stewardship standard** should be built for asset managers that can be used by institutional asset owners as well as individual investors and their advisors to ascertain whether certain minimum standards and procedures in stewardship are being adhered to by an asset manager.

Such a standard could be modelled on the successful EU Eco-management and Audit Scheme (EMAS), which paved the way for ISO 14001. It would be voluntary and management systems based. This would allow asset owners to assess easily which asset managers are well positioned to exercise responsible investment and stewardship commitments.

● **The EU** should integrate long term sustainability factors in the mandates of the financial stability board and other supervision agencies.

This will allow these factors to be considered as part of the DNA of the financial markets. It will allow these agencies to consider build-ups of bad practices in these areas as systemically important and therefore materially relevant to companies, rewarding good behaviour and warning about bad behaviour.

● **There could be enforcement** measures of investor stewardship codes, with sanctions such as a vote on the stewardship statement at annual stewardship meetings.

This will ensure that the chain of accountability extends between the intermediaries from the company to the end beneficiary.

● **Clauses on responsible investment**, culture and governance should be inserted into fund management contracts to ensure legal accountability for performance transparency.

Such clauses may reference national Stewardship Codes, the Principles for Responsible Investment and/or the International Corporate Governance Network principles, and require annual performance reporting.

● **Fiduciary duty** (legal requirements) should be clarified so that all intermediaries are aware of their Environmental, Social and Governance (ESG) duties to clients and the end beneficiaries.

We believe that it is important that long-term sustainable development be incorporated into the legal duties of market participants including, in particular, the fiduciary duty of asset owners and the duty of care of asset managers and investment consultants. This is an area that the Kay review and the associated review by the Law Commission in the UK have examined in some detail with some poor progress that could be built upon at the EU level.

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## Conclusion

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We need policy-makers to ensure that the culture within financial services is one where each agent works to promote the interests of their clients rather than their own.

A combination of regulatory intervention and soft guidance can be used to help ensure that all the incentives in the capital markets are for companies to act in the interests of the long-term sustainability of the economy.

By ensuring that financial incentives are aligned, transparency is created so that the European public is engaged and so that growth measures are targeted towards sustainable investment. This will create a sustainable capital markets union that will be robust enough for the future.

Some of this will require greater government intervention, particularly around the regulation of investor delivery of responsible ownership. Elsewhere, a more light-touch approach will be required to help shift culture towards the long-term. In this way, capital markets can become the primary facilitator of sustainable growth.

While much has been done in the EU on this agenda, there is a long way yet to go before we have transparent, accountable and integrated capital markets – a vital strand of the capital markets union.

This is a large and complicated area and we appreciate that some of these recommendations are very technical in nature. We would be happy to go into greater depth. Contact details overleaf.



**2014**

Aviva's Sustainable  
Capital Markets  
Union Manifesto

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