

Pension Fund Engagement

Chances and Limitations

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Abstract

In this paper the growing salience of what is called ‘pension fund engagement’ is critically assessed by means of a reconstruction of the failure of the Swedish Wage Earner Funds. The outcome of this assessment is sobering. Even under optimal political conditions pension savings proved to be too unwieldy to have any impact on the ownership structure of large publicly quoted corporations.

Apparently the logic of funded pension arrangements is such that the chances for active engagement are minimal, largely explaining the marginal amount of pension savings actually invested in socially responsible ways. The second part of the paper is an exercise in institutional design. I propose a Fund for Economic Development, financed from the surpluses of regular pension funds, and largely organized as a ‘classic’ venture capital provider, as an alternative form of engagement. In this manner, so I argue, the fiduciary duties of regular pension funds can be taken seriously, while at the same time there will be sufficient mass behind the construction of an alternative investment infrastructure, including reconstructed concepts of ‘risk’ and ‘return’, that in the long run the monopoly of the mainstream financial industry on the definition of economic rationality stands a chance to be broken. As such, this attempt squarely stands within the tradition of ‘realist utopianism’.

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1. Introduction

Since worldwide pension savings have now reached the incredible amount of \$ 12 trillion, labour unions, academics, progressive voluntary associations, politicians, contributors and beneficiaries, investors and policy makers are increasingly studying ways to use these masses of capital to contain the growing political power of multinational corporations and to force them to pursue social and environmental goals that are currently not on the menu of the conventional financial industry. In the literature this is called ‘pension fund engagement’, and its growing popularity is related to the regulatory vacuum state retrenchment has left in its wake on the one hand and the recent surge in corporate misbehaviour on the other.

In general, pension fund engagement comes in three shapes: advocacy, screening and targeted investment. Advocacy is based on the voice rights of shareholders, while screening implies the use of the exit rights of ‘owners’. In the case of targeted investment the pension fund adopts the role of the venture capitalist and becomes an active investor.

In this paper I investigate the chances and limitations of these modes of engagement. I do so by means of a historical detour around the Swedish Meidner Funds of the late 1970s. I argue that their failure was due to a ‘logic of funding’ that is usually not recognized as such by advocates of pension fund engagement. This logic severely limits the ability of pension funds to pursue unconventional investment policies and largely explains the limited magnitude of the capitals thus invested. This is not to dismiss pension fund engagement offhand. Rather it is a reason for diminished expectations. However, diminishing expectations is not equal to no expectations at all. In the second part of the paper I propose to construct a parallel financial infrastructure, financed from a small percentage of the surplus value of pension funds only, with the aim to set up alternative investment opportunities and address the current deficit in this regard. Due to its parallel nature, such a structure would interfere only marginally with the conventions of the financial industry and hence would not collide with the logic of funding. Doing so, I hope to convince the reader that ‘real utopias’ are possible after all.

2. A New Politics of Ownership?

The idea that pension savings, being ‘deferred wages’, should be invested in ways that promote the long term interests of workers and citizens rather than hurt them, has a long pedigree within the socialist movement, ranging from Fritz Naphtali’s ‘Wirtschaftsdemokratie’, Gleitze’s ‘Sozialfund’ and Rudolf Meidner’s ‘Wage Earner Funds’ to the capital gains sharing-plans that were discussed within the Dutch and Danish social-democratic parties in the mid-1970s. After two decades of near silence on this topic, a growing number of progressive movements and academics, as well as some mainstream investment managers, have started to investigate the chances to use pension funds to initiate a ‘new politics of ownership’. These investigations have resulted in proposals that range from the detailed and well researched to the wild and fanciful.¹

What they have in common, though, is a measure of optimism that has everything to do with the nature of their intentions. This is indicated by the fact that none of the authors pays attention to the constraints that follow from the objectives of funded pension systems, or what I have called elsewhere the ‘logic of funding’ (Engelen 2003a). A better understanding of this logic, so I contend, is urgently required, for it would redirect the energy of progressive organizations and advocates away from fruitless attempts to replace orthodox investment strategies with unorthodox ones towards supplementary strategies, like the one presented in the second part of this paper.

I start with a reconstruction of the Swedish Wage Earner Funds, one of the few actual attempts to socialize capital and an excellent example of the conflicting logics of funding on the one hand and of pension fund engagement on the other, to highlight what is at stake.

2.1 Swedish Wage Earner Funds

Background

The Swedish Meidner-plan has been one of the few post-war attempts to socialize capital in order to give workers a say over strategic decision-making within the corporation. The premise that political democratisation in the form of universal suffrage and social democratisation in the form of universal social rights ought be complemented with economic democratisation, has a long pedigree in the Swedish social-democratic movement (Sassoon 1996: 707; Tilton 1991: 39-69). The reason why this took the form of so-called wage earner funds has to do with the way in which the Swedish

¹ See, in alphabetical order, Blackburn 1999; 2002; Clark & Hebb 2003; Dymski et al. 1993; Hirst 1994; Hutton 1995; Fung et al. 2001; Gamble & Kelly 1996; Pollin 1995.

system of industrial relations coped with the growing tension during the post-war period between a policy of coordinated wage restraint on the one hand and increasing growth differentials between industries on the other.

In a situation of full employment and universal wage solidarity, growth differentials between industries either result in windfall profits or in 'grey' wage raises and hidden inflation. The obvious solution is of course to dump the policy of wage solidarity across industries as such and link wage growth to intra-industry productivity growth or even to productivity growth at the firm level. However, that would imply increasing wage inequalities. Moreover, it would mean the dissolution of an instrument of macro-economic management that could be regained only in exceptional circumstances.

Instead, the Swedish social-democrats opted for a strategy, developed by the union economists Gösta Rehn and Rudolf Meidner, that kept to the moral principle of 'equal pay for equal work' and remained wedded to the institution of central wage negotiations between employers and workers. The solution for the tension between central wage agreements and growing profit-differentials between industries was sought in basing wage negotiations on median productivity growth-figures. In this manner two birds could be killed with one stone, for it ensured both a prudent and solidaristic wage development, and enforced an incremental rationalization of the Swedish economy. Firms that were less productive than the median corporation suffered higher wage costs than they would be able to bear in the long run, while firms with above average productivity rises were rewarded with lower wage costs.

It was clear from the outset that such an economic policy had to be complemented with an active labour market policy. To facilitate a smooth reallocation of capital between industries, the government attempted to cushion its effects on workers by supporting them with placement services, schooling and training programs, migration subsidies and public housing facilities. However, this left the problem of above average profits unaddressed. This was primarily perceived as a moral issue. Why would productivity gains need to fall toward capital rather than labour? But it was also a prudential problem. For what would detain the employer from disbursing these gains as 'grey' wages? That would not only endanger the goal of a solidaristic wage policy, but also that of economic rationalization. Hence to avert that possibility the Swedish government needed an instrument that would preclude consumptive expenditures and would guarantee productive uses. In the original plan of Rehn and Meidner this instrument consisted of a high real profit tax, combined with a number of specialized investment funds that would allocate these taxes according to parametrical and institutional requirements among targeted firms against below-market interest rates (Pontusson 1992: 57-79; 1994: 24-27; Sassoon 1996: 203-206).

From the second half of the 1970s onward, this instrument started to display shortcomings. First, the creation of new jobs in growth industries appeared to be insufficient to equilibrate the loss of employment in brownstone industries. As a result of worldwide market liberalization and

deregulation the competitive pressure on the exporting industries rapidly increased. Both greenfield and brownstone industries reacted with increasing their capital intensity, an accelerated closure of inefficient factories, defensive mergers and increased foreign direct investment. Hence the policy promise of full employment became ever harder to fulfil, which forced the government to expand employment in the public sector substantially (Pontusson 1992: 105-111).

Moreover, the Swedish economy was hit hard in the late 1960s by a wave of wildcat strikes and other forms of labour unrests. These disturbances had to do with three challenges: (i) dissatisfaction with the policy of involuntary wage solidarity; (ii) a growing discontent with the effects of the increasing Taylorisation of production as a result of the enforced modernization of the Swedish economy, and (iii) a gradual displacement of employment from industry to services and within industry from executive tasks to planning tasks. These changes in the job structure implied a change in the balance of power between blue-collar unions and white-collar unions (Pontusson 1992: 165-167).

To counter these challenges the social-democratic unions pursued a broad democratisation program that was meant to deflect spontaneous labour protests, to empower labour unions at the level of the work floor, to guarantee union involvement in central wage bargaining, and to serve the post-materialist interests of white collar workers in order to co-opt white collar unions. The legislative success of this program was immediate. From 1972 to 1976 the social-democratic party was able to pass a large number of Acts establishing minority representation of workers in the board of directors, extensive prerogatives for health and safety officers, more protective dismissal procedures and a co-determination act which obliged employers to negotiate with workers over each and every decision that touches upon worker interests (Pontusson 1992: 161-185; 1994: 27-28).

Wage Earner Funds

In the wake of these successes the congress of social-democratic unions decided in 1976 to push for Meidner's plan to oblige firms to emit equity on parts of their yearly profits and hand these over to so-called 'wage earner funds'. The underlying capital would remain with the firm. Only the titles would change hands, in order to let workers share in the capital gains and give worker's representatives more say over the strategic decision making of the firm. At the core of this proposal was thus the distinction between control rights and use rights.² The use rights were for the firm, while the control rights would fall to the workers.

² According to legal realists and other critical legal theorists, property rights consist of a bundle of rights, more particularly: use rights, control rights, transmission rights, disposition rights, transaction rights, etc. — which do not automatically accrue to the 'owner' (Hohfeld 1916; Honoré 1961; Kay 1997). In complex societies a growing number of objects of ownership simply do not fit the liberal mould; a state of affairs that is further complicated by the rise and transformation of the welfare state (Reich 1978; Grey 1980). Rights and

As such, this plan was nothing out of the ordinary. Not only were there clear historical precursors, ranging from the German ‘socialization-debates’ of the 1920s and more specifically Naphtali’s ‘Wirtschaftsdemokratie’ (Naphtali 1924; Novy 1974) to Gleitze’s ‘Sozialfonds’ (Gleitze 1969), in other European countries social-democratic parties played around with more or less similar ideas. In the Netherlands and Denmark for example, social democratic parties experimented with capital gains distribution schemes (Dercksen 1985; De Kam & Vermeend 1985; De Beus & Koelble 1995). Moreover, Meidner’s plans clearly belonged to a category of proposals for reallocating property titles, along which employee shareowner plans or ESOP’s also have to be counted. These were actually discussed by the Swedish labour movement and ultimately rejected for being too individualistic (Stephens 1979: 190-191; Tilton 1991:232). For in the case of ESOP’s the entitlements fall to the individual worker. Not only did this run counter to the solidaristic premises of the Swedish labour movement, ESOP’s also provide only limited possibilities for gaining real influence over corporate decision making due to well-known collective action problems (Engelen 2000).

The choice for collective asset procurement via wage earner funds was based on four considerations. First, it would to strengthen the solidaristic wage policy by skimming off excessive profits. Second, it would correct increasing wealth inequality. Third, it was perceived to stimulate productive investments. And fourth, it would give workers a greater say over corporate decision-making. In the original plan, all firms of more than 50 workers were obliged to emit new share issues worth 20 per cent of gross annual profit. Local unions would observe the control and income rights of these shares until the workers’ share would have surpassed 20 per cent of the total capitalization of the firm. If that threshold were reached, the control rights would be looked after by dedicated investment fund that would be governed jointly by employers and workers. It was estimated that if firms booked an annual profit of ten per cent, half of the stocks of a firm would be owned by the wage earner fund within a period of 35 years (Meidner 1978: 59; Pontusson 1992: 186-219; 1994: 29; Tilton 1991: 228-235; Sassoon 1996: 706-713).

It never got that far. In three rounds of negotiations the architecture of the plan was substantially softened. The emphasis was shifted from redistribution to stepped up investment; the goals of co-determination and control had to be combined with those of pension savings and profit maximalisation; capital accumulation through profit sharing was supplemented with accumulation through pension levies; the handing over of new property titles was replaced by an ordinary profit tax which was used to buy existing equity; these taxes would not be based on gross profits but on real profits, i.e. profits after interest on debts and inflation; instead of one central fund the ownership titles were to be handled by 24 local funds; the management of the funds would not be

obligations are widely distributed, emptying the notion of the ‘owner’ of most of its defining content (Engelen 2002).

appointed by local unions but would be elected by the participating workers; and finally, only firms with more than 500 workers would fall under the Act.

In 1983 five regional funds were set up for a period of seven years. These funds were modelled after the so-called ‘fourth’ pension fund that was set up in 1973 on behalf of the blue-collar union federation and was the sole public pension fund that was allowed to hold stocks. This meant in practice that though the five wage earner fund did have the license to buy, own and sell stocks, these investments were subject to the same restrictive rules that were applicable to the ‘fourth’ pension fund (Pontusson 1992: 191, 198). Hence, they were forbidden to practice their control rights actively; they were not allowed to gain a minority share of more than eight per cent; they had to conform to the prudent man-rule;³ and they were obliged to contribute three per cent of the value of their assets annually to the national system of supplementary pension provision (Pontusson 1992: 196-198, 205, 209-210).

After seven years the total value of the public shares in possession of the wage earner funds amounted to a meagre seven per cent of the total capitalization of the Stockholm stock exchange. In 1992 the ultimate winding down took place of what had been applauded in 1976 as a radical step towards a socialist economy. In March 1991 the social-democratic government had presented a proposal to realign the architecture of the Swedish pension system with the inherited practice and to do away with the organisational and functional distinctions between the wage earner funds and the different public pension funds. The underlying assets were to be reallocated among five brand new public pension funds that were supposed to contribute equally to the coverage of the national pension liabilities.

To deflect an imminent electoral defeat the social-democratic party opted for a confrontational strategy and added that only 40 per cent of these assets had to be invested in government bonds, implying that the rest — 260 billion kroner or almost half the total capitalization of the Stockholm stock exchange — could in principle be invested as the fund’s managers saw fit (Pontusson 1992: 200). The strategy failed and the social democrats had to endure their worst electoral results in 44 years. The next year, the centre-right Boldt-coalition pursued the institutional restructuring the social democrats had planned, but sharpened the investment restriction; the new funds were obliged to invest 60 per cent of their assets safely, that is in domestic governments bonds. Thus the idea to

³ The “prudent man” concept was legally established when Harvard College lost a suit in 1830 against an investment manager, Francis Amory. Harvard College sued Amory for bad faith when he lost 40 per cent of the assets entrusted to him in risky manufacturing and insurance stocks... The “prudent person” or “prudent man” rule, which was codified in the Employees Retirement Security Act (ERISA), takes the Amory principle and modifies it somewhat by requiring a fiduciary to manage funds with the “care, skill, prudence, and diligence that a prudent man in a similar situation would apply”. The prudence standard was thus shifted from a reference to how fiduciaries would manage their “own affairs” to how other professional investment managers would behave under similar circumstances’ (Barber & Ghilarducci 1993: 314).

use pension savings as a lever to gain workers' control over firms was finally buried (Davis 1995: 98).

2.2 Structural Explanations for a Failed Experiment

As any planning failure, the floundering of the Swedish wage earner funds too has to do with a combination of a number of (contingent) constraints. Pontusson and others mention the lack of public support; the lack of social democratic control over the press; the complexity and opaqueness of the organizational set-up of the wage earner funds; the disagreement between the blue collar union federation and the social democratic party over form, strategy and goal of the funds; and finally the inability to forge broad interest-coalitions around the wage earner funds (Stephens 1979: 191; Tilton 1991: 232-233; Korpi 1983: 234-235; Meidner 1993; Pontusson 1992; 1994; 1997; Sassoon 1996: 485ff., 711ff.; Ryner 1999).

However, in my view their failure is also due to the fact that these funds were ultimately designed to function as more or less regular pension providers. Hence, their failure contains a valuable but sobering lesson for each and every proposal to pursue social and ecological objectives through pension fund engagement. For the failure of the Swedish wage earner funds has as much to do with structural constraints as with the contingent constraints mentioned above.

Pension Fund Democracy

To come to grips with these structural constraints, the following considerations have to be kept in mind. The first consideration has to do with the extent of internal democracy. If you want progressive output from pension funds, you will first have to ensure progressive input. Hence questions arise regarding the organization of collective decision making within the fund. What is the composition of the board? What are its rights and prerogatives? To whom are board members accountable? Ideally, boards consist of an equal number of representatives of both workers and employers and have ultimate determination rights over investment decisions. In the Netherlands that is legally proscribed, both in corporate funds and in multi-employer funds. In the US however, equal representation is allowed for multi-employer funds only. Corporate pension funds are taken to fall under the *dominium* of the employer. Hence, the employer has fiduciary duties only and is not obliged to share prerogatives with worker representatives. The implication is that American workers have voice over less than 8 per cent of their 'deferred wages' (Ghilarducci 2001: 165).

In Sweden too pension funds are legally required to grant workers equal or near equal representation on the board of trustees. Even though there are thus substantial formal control rights for workers, in practice this does not seem to have had much impact on the investment

strategies of the wage earner funds. Nor has it resulted in a more ‘politicised’ investment practice than those of conventional investors, neither in terms of professed investment goals nor in terms of actual investment practices. The Swedish wage earner funds have comported themselves primarily as investment manager and only rarely as advocates. While eschewing corporate involvement, the funds’ managers appeared to have followed three dominant rules of thumb: risk diversification, long-term commitment, and blue chip investments. Within these constraints, the funds aimed to maximize capital gains. As such, the actual investment behaviour of the wage earner funds was indistinguishable from that of conventional investors.⁴ How come? To answer that question further considerations need to be invoked.

Legal Requirements

Even if internal democracy is formally guaranteed, effective advocacy is not. Whether assets can be transformed in voice depends on the institutions of corporate governance, the ownership structure of the firm in question, as well as the absence or existence of legal investment restrictions.

The first condition is fairly obvious. Whether getting access to the annual shareholders’ meeting is in fact a first step towards gaining control over the corporation, depends crucially on its legal rights and responsibilities. National corporate governance regimes differ widely with regard to the *complexity* of the corporate governance regime as well as with regard to the *locus* of control.

Complexity has to do with the number of forums within the corporate political structure,⁵ while the locus of control refers to the structuring of the functional relations between the different forums. Some corporate governance regimes put the board of directors at the corporate political pinnacle, while in others the general shareholders meeting or even the board of supervisors occupies this

⁴ Of course, this raises pressing questions about the effectiveness of urging for greater worker representation among pension fund boards as a solution to the paradox of large pensions funds and small benefits.

According to Ghilarducci this paradox is due to five ‘leakages’: (i) low coverage of workers; (ii) ‘contribution holidays’ for sponsors; (iii) inflation; (iv) fees and inefficiencies; and (v) speculative investment (Ghilarducci 2001: 162). In the light of the Swedish and Dutch experiences, one could expect worker representation to plug the first four leakages but to leave the fifth one unaddressed. In other words, worker representation might well be a necessary condition for pension fund engagement, but it surely is not a sufficient one.

⁵ The Dutch and German regimes of corporate governance, for instance, consist of a works councils and a supervisory board, next to a board of directors and a general shareholders meeting. In the German case workers even have direct access to the board of supervisors — reserving up to half the seats for worker representatives — and, in some cases, to the board of directors as well (Lane 1989; Streeck 1992: 137-168; Müller-Jentsch 1995). A complex system allows for a much more sophisticated architecture of interrelated rights and responsibilities, enabling the legislator to give each interest its optimal forum and each forum its optimal jurisdiction. Under simple regimes of corporate governance, such as the American, which has only two political forums — the board of directors and the shareholders meeting —, no such opportunities are available (Engelen 2002).

position. Under influence of the shareholder ideology a tendency can be observed in many corporate governance regimes to shift the locus of control from the supervisory board to the shareholders meeting, opening up opportunities to politicise them (Engelen 2002).

As such, it need not surprise that pension fund activists have pushed a more shareholder friendly regime of corporate governance. As O'Connor notes, public pension funds have been instrumental in bringing about 'the shareholder revolution' of the 1990s by speaking up for corporate bylaw amendments, more transparent CEO-compensation and written consent in the case of proxy voting. As such pension fund activism has been key in the battle against anti-takeover measures and for a well-functioning 'market for corporate control' (O'Connor 2001).⁶

The second condition is fairly obvious too. When ownership is widely dispersed it is much easier to build up a substantial minority stake than when property titles are closely held. If there is a sufficient spread of titles, as is generally the case in deep and liquid equity markets, a minority stake of 2 to 4 per cent suffices to gain leverage over the shareholders meeting and hence to get preferential treatment over other shareholders in the form of so-called 'investor's meetings' with the board of directors (Scott 1997).⁷

The total value of the capital accumulated by the Swedish wage earner funds has never crossed the threshold of 10 per cent of the total capitalization of the Stockholm stock exchange. Even though the legislator had been adamant in its stress on the rights and responsibilities of co-ownership, at the same time he had issued strict limitations on the share of total outstanding stocks these funds were allowed to own of any one firm, to wit 8 per cent. Hence, in theory the five wage earner funds, together with the 'fourth' pension fund, which was the only one that was allowed to take a maximum share of 10 per cent, could assemble up to a maximum of half of all outstanding shares of any one firm.⁸ However, in practice this required an ability to coordinate and fine-tune,

⁶ The issue whether this has been to the advantage of the long-term wealth creating capabilities of the firm is left unaddressed by O'Connor, turning her *laudatio* on 'labor's role in the shareholder revolution' into an uncritical apology for the shareholder ideology as such.

⁷ This is not to suggest that formal ownership is a sufficient condition for control, but merely that formal ownership is a necessary condition. In principle 'owners' have four avenues of control: (i) the general shareholders' meeting; (ii) representation in the supervisory board; (iii) informal consultation rounds such as irregular and informal 'investors' meetings'; and (iv) buy and sell decisions (Engelen 2000: 190). Here, only the 'voice'-option is relevant. Even though there is no access without property rights, the possession of property rights does not yet guarantee effective control, not even in the case of substantial minority stakes. For effective control is as much an effect of the informal networks among 'owners' as it is related to the possession of formal control rights (see Scott 1997).

⁸ In 1988, a 'fifth' pension fund was installed, largely modeled on the 'fourth'. At that occasion the investment restrictions of the five wage earner funds were reduced to 6 per cent per fund to keep their combined maximum at the earlier level.

which the funds either did not possess or did not want to exercise. Their combined portfolios contained only seven publicly quoted corporations in which they had a stake of over eight per cent. Of course, if ownership were sufficiently dispersed a small stake would suffice to gain a control. However, in Sweden share ownership is generally highly concentrated. Hence, most publicly quoted Swedish firms were ‘owned’ by at least one big ‘owner’ whose stake surpassed that of the combined workers’ funds with at least a third (Scott 1997: 152). As a result, the threshold of control was too high for the wage earner funds, limiting the practical value of share ownership to information gathering and gaining experience with the nuts and bolts of investment decisions, as well as getting acquainted with the national financial and economic elite. Compared to the real gains in terms of controlling rights of the co-determination act of 1976, this was a truly disappointing result (Pontusson 1992: 212).

Like Sweden, most states have issued legal investment requirements to protect pension funds from going bankrupt.⁹ These restrictions range from a 5 per cent limit on self-investment and prudent man principles in the Netherlands, the UK and the US — prohibiting pension funds both to invest more than 10 per cent of their assets into any one investment opportunity as well as to possess more than 5 per cent of the total value of the object of investment — to fairly elaborate restrictions on different asset categories in Austria, Denmark, Germany and Spain (EU 2000: 66ff). So, even if the conditions of democratisation and access to corporate decision-making are met, legal restrictions on block holding may still limit the ability of pension funds to flex sufficient financial muscle to influence corporate behaviour.

The logic of Funding

However, it is not clear that in the Swedish case these legal restrictions mattered much. The lack of mutual coordination as well as the gap between the actual and legally permitted minority stakes, indicates that the wage earner funds did not even try to gain maximum control (Pontusson 1992: 206). The explanation has to be sought, at least partly, in the objectives with which the funds were burdened. Apart from contributing to the restructuring and modernization of the Swedish economy, the funds were expected to yield ‘sufficient’ returns. However, the legislator had only specified the return requirements, while the restructuring part of the funds’ objectives was mentioned only under the abstract heading of ‘long term consequences’ (Pontusson 1992: 205). By

⁹ It is noteworthy that recently, due to a combination of increased equity investment and rapidly declining equity prices, the Dutch pension and insurance regulator has issued a statement in which pension funds are urgently required to bring their coverage up the parity, even if this means more sales of stocks. In a reaction the Dutch green party pressed the Dutch government to reintroduce legal investment requirements in order to ensure the long-term stability of pension savings. This is even more remarkable in light of the fact that the European directive on supplementary pensions did away with investment restrictions only after incessant pressure from the Dutch and British pension lobby.

keeping silent about the quantification, operationalisation and measurement of the funds' contribution to the modernization of the Swedish economy, the legislator provided worker representatives with insufficient juridical power to counter the dominance of the professional investment industry.

More important, in my view, has been the obligation of the wage earner funds to contribute annually 3 per cent of their assets to the public pension system. Together with the conventional financing formula of bilateral contributions — instead of a unilateral capital gains sharing-scheme — it meant the transformation of worker controlled investment funds in ordinary pension funds, conforming to the regular standards of the industry. This process was fortified by the attempt on the side of their designers to gain political and public acceptance of the workers funds, by the growing visibility and importance of stock markets as a result of the deregulation of capital markets in Sweden in the late 1980s, and by the competition among the workers funds themselves as a result of state-initiated bench marking (Pontusson 1992: 207-208).

In hindsight it is easy to conclude that conservative investment behaviour is to be expected of worker funds that have been turned into ordinary pension funds. For the 'logic of funding' is such that managing boards — however willing they may be to push for pension fund engagement — have every reason to follow conventional investment strategies and even hand over large chunks of investment decision making to the financial industry. This has everything to do with the conflicting objectives of pension funds. In general they have four objectives: the minimization of risks, the maximization of returns, the availability of sufficient liquidity, and the minimization of costs. These objectives serve the interest of the contributors and beneficiaries in a stable, secure and high pension. At the same time, they boil down to investment strategies that do not lend themselves easily to pension fund endearment.

This is obvious for the requirement to diversify risks. Since beneficiaries demand a stable and secure pension, fund managers do well to distribute assets over a large number of categories with complementary risk and return profiles, and hence to sacrifice 'social leverage' or 'democratic pressure' for guaranteed returns — with or without legal restrictions.

The same holds for the maximization of returns. Since surpluses are translated in lower employer contributions in the case of public and multi-employer pension funds, and in substantial pay-backs and/or lower contributions in the case of corporate ones, principals (the sponsoring corporation(s)) have an evident interest in creating an incentive structure to incite agents (trustees) to maximize returns and hence to invest in those asset categories that are perceived to reap the highest rewards. From the mid-1990s onward stocks were increasingly perceived as such. Hence, pension funds worldwide invested increasing shares of their total assets in public equity, both domestic and, in ever-larger measures, foreign equity, as long as it is 'blue chip'.

The combined effects of the requirements to minimize costs and to maximize liquid investment further fortify conventional investment behaviour. As I observed elsewhere (Engelen 2003a),

pension funds are subject to a life cycle during which the ratio of contributors and beneficiaries changes gradually. This results in a radical transformation of their risk profile and their investment strategies, turning committed, long-term owners increasingly into speculative investors. Driving this process is an increasing need for liquidity, forcing pension funds to invest in the most liquid markets and within these markets to buy the stocks of those corporations that have the largest daily 'free float'. Since sell-decisions influence prices, funds have every reason to forestall becoming prisoner of their own investments. Hence the preference for well developed asset markets and liquid investments. However, since 'blue chip' firms have a highly dispersed ownership structure, the minority stakes of institutional investors will generally be too small to be turned into voice while the exit-weapon is a priori unavailable.

Finally, there are strong economies of scale involved. Investment management is extremely costly, consisting of management fees, commissions, membership costs, exchange taxes, search and assessment costs, information costs, etc. The standardization of financial services is one way to keep these costs in check. However, standardization itself is only worthwhile if there is sufficient effective demand. As a result the cost advantage of conventional investment strategies is such, that most pension funds will decide against targeted investment and will choose for investment conventional asset categories, in particular 'blue chip' stocks and 'gilt edged' bonds.

2.3 Lessons

What was true for the Swedish workers' funds is true for contemporary forms of pension fund engagement. Contemporary forms of engagement consist of screening, advocacy and targeted investment. Advocacy is based on the direct leverage pension funds can have over corporate strategy by becoming a major stockholder. To use Hirschman's famous distinction: advocacy is based on voice rights. Screening is much more indirect and involves the use of social, moral and environmental criteria as 'investment screens'. Screening, in other words, is based on exit rights. Targeted investment, finally, requires a much more active stance of the pension fund in question. For in that case pension funds do not only initiate investment opportunities but commit themselves to become patient investors, more or less along the lines of the mythical venture capitalist, largely due to the illiquid nature of the investment (Fung et al. 2001). Despite the enthusiasm with which they are embraced, the magnitude of assets thus invested is still marginal, as are the measurable effects on corporate behaviour. I will address each of the modes of engagement in turn.

Advocacy

Despite a growing awareness among pension fund trustees of the consequences of their investment

decisions, their strategies are still mostly conventional and consist predominantly of investments in liquid stocks and bonds. In the US, which saw the birth of this type of pension fund engagement, pension funds, as noted above, have mainly used their voices to address issues of corporate governance, such as CEO compensation, corporate bylaw amendments, and limits on anti-takeover measures generally, according to a recent survey of labour-shareholder activism in the US (O'Connor 2001). Since the mid 1990s this type of pension fund activism has increasingly crossed the ocean and has turned large continental pension funds like the Dutch ABP and PGGM into powerful carriers of the shareholder ideology that is currently eroding the continental stakeholder regime, which is ironically viewed by many American critics as a paragon of progressivism (Blair 1994; Roe 1995; Blair & Roe 1999; Lazonick & O'Sullivan 2000).

Screening

Despite its popularity, screening too has proven to be too blunt an instrument to have a substantial impact upon corporate behaviour. Screening, having germinated from the counter-culture of the 1960s with its sympathy for sustainable growth and civil rights and its distaste for nuclear energy and the military-industrial complex, gained public notoriety in the 1980s as a result of its role in bringing down the South-African apartheid-regime. Currently a little more than \$ 922 billion is part of a socially responsible portfolio, or approximately 5 per cent of all capital under professional management in the US, while the screens themselves have become ever more fine-grained, ranging from tobacco, alcohol ('sin screens'),¹⁰ and weapons, to human rights, sweatshops, the environment as well as specific countries known for human rights abuses like Burma and Nigeria (Becker & McVeigh 2001: 46). Although no negative effects on investment returns have been observed (Becker & McVeigh 2001: 52-59; Bauer et al. 2002), neither have there been noticeable effects on corporate behaviour.¹¹ In that regard, screening is just as effective as consumer boycotts; only in the case of glaring offences of moral norms, catching the eye of public media, will the use of exit rights by investors (or for that matter consumers) affect corporate behaviour. Minor offences — or hidden offences — will remain unpunished. Moreover, the potential effects on corporate strategy, in the form of self imposed 'corporate citizenship charters', should not be overestimated. Without the 'shadow of hierarchy', social and environmental audits will largely remain public relations instruments and will continue to be contingent upon economic performance, the public attention and the visibility of its misbehaviour.

¹⁰ For some, apparently, 'sin' is not something to eschew but rather to embrace. September 3rd 2002 saw the birth of 'Vice Fund', an investment funds that specializes in investments in controversial industries such as tobacco, arms, alcohol etc. The claim is that investing in 'sin funds' makes good prudential sense for such funds tend to be less prone to business cycles, while investments in the arms industry after 9/11 is sure to bring handsome returns (www.vicefund.com).

¹¹ Admittedly, these are ever so much harder to measure.

Targeted Investment

In a sense, targeted investment is the activist counterpart of passive screening, for screens merely tell you which liquid investment opportunity to select or avoid, while targeted investment implies a much more activist stance, in fact suggesting that pension funds take over the role and function of venture capitalists. In other words, whereas screening is basically an alternative investment *strategy*, targeted investment ideally concerns the identification and even construction of alternative investments *products*. These products can be of a territorial or a functional nature, ranging from community and infrastructural investments to investments in small and medium sized enterprises (SME's) and sustainable development. What is uniting these products is their non-tradable nature. In other words, there are no well-developed markets for these investments. As a result, investments tend to be small. For instance, community investing, the big issue in the US and the UK where state retrenchment has left many local communities underfunded,¹² receives only \$ 5.4 billion from a total of \$ 2,159 billion (Becker & McVeigh 2001: 46). And even though many pension funds are increasingly directing capital to intermediate green and ethical funds, in part because of fiscal incentives, the amounts tend to be negligible, while the intermediate funds are grappling with a dearth of available investment opportunities, highlighting the difficulties of alternative investment strategies in general and of targeted investment in particular.

There are good cost-related reasons for that. First, the size of unconventional investment objects tends to be small, raising the costs of investment per unit. Second, determining the risk and profit-profiles of alternative asset categories requires a thorough economic knowledge of the object in question rather than mere financial knowledge. The financial industry focuses only on financial indicators and does hardly at all invest in fundamental research. The assessment of alternative investments will thus have to take place outside the well-known research circuits and requires the setting up of an alternative research network or infrastructure, which is difficult and costly. Third, alternative investment opportunities do not fall from heaven but have to be recognized, nurtured and supported and constructed, more or less along the lines of what 'classic' venture capitalists do (Kenney 2000). This requires a local scouting and assessment network — consisting of accountants, lawyers, bank officials, chambers of commerce and industry, labour unions, employer organizations and universities — as well as personalized and informal contacts, and entrepreneurial skills rather than financial engineering ones (Bygrave & Timmens 1992; Mason & Harrison 2002). If such an infrastructure is not available, it has to be set up *de novo*. Once again, a difficult, time-consuming and hence costly enterprise (Minns 1980: 78-125).

¹² See Clark (2000) for the UK, and Calabrese (2001) and Zanglein (2001) for the US. Note that Calabrese reports on alternative investment products, financed by American union pension funds, with a value of only \$ 18 billion (!), mainly in construction and some in private equity placement.

2.4 Reconstructing 'Risk' and 'Reward'

Apparently, pension savings do not lend themselves easily for engagement, in whatever form. Because they are in fact 'deferred wages', pension funds see themselves obliged, for good moral and prudential reasons, to invest prudently, that is minimize risks, maximize returns, minimize costs, and ensure sufficient liquidity. Given these objectives, it is only reasonable that trustees delegate their decision-making tasks increasingly to professional financial service providers. Setting up alternative research facilities, or even, in the case of targeted investment, scouting and support facilities, is too difficult, too time-consuming and hence too costly. At the same time, their fiscal and juridical status works against an organizational transformation from 'guardians' of pension savings into active allocators of credit, a traditional banking function. For these reasons, pension funds are hardly calibrated to contribute to investment planning, industrial policies, regional development, economic restructuring and promoting sustainable production systems. That is, if it is certain that investments in those projects is substantially more risky and considerably less rewarding than conventional investments.

Crucial in this respect are four questions: what is 'reward', what is 'risk', what is 'substantial' respectively 'considerable', and finally: who decides how risk, reward and moral, social and ecological criteria should be weighed? Of course, questions like these touch upon the technical side of the investment industry, and deal with accountancy rules, supervision, the role of the financial press, measurement techniques, different modes of value assessment, mathematical portfolio management techniques and underlying theoretical conceptions of financial markets. While in large measure an unintended product of large-scale collective processes, the close ties between nation-state formation and the development of statistical measurement conventions and techniques clearly demonstrate the constructivist nature of these conventions, suggesting opportunities for reconstruction and redesign (Alonso & Starr 1987; Donzelot 1979; Ewald 1986; Kula 1986; Porter 1995; Scott 1998; Scott et al. 2002). By applying existing regulations in new ways or by introducing new regulations, the state and other governing organizations might be able to change the weight of conventional criteria of portfolio management in favour of social and ecological criteria (Williams 1999).

The current division of managerial labour obstructs the development of such an investment strategy. Given the 'logic of funding', pension fund management is highly interwoven with the mainstream financial industry, implying that financial values predominate over social and ecological ones and that 'financial engineering' overshadows 'company-building' (Mason & Harrison 2002). This is fortified by the mandates of external fund managers — broadly: prudent management according to the rules of the profession — and the investment techniques they wield. For these techniques are based upon the so-called 'efficient market theory' which assumes that 'security prices

at any time “fully reflect” all available information’ (Fama 1970; 1991) and hence proclaims that outside intervention in the allocation of property titles is either futile (for profitable investment projects will attract capital anyway) or perverse (for enforced investment in non-profitable projects deflects capital away from profitable investment opportunities). However, the upshot is that the interests of the contributor are put on a par with those of the speculator and are in turn equated with the maximisation of the price earnings ratio (see, critically, Barber & Ghilarducci 1993: 303-304; Dyckman 1986; Henwood 1997: 161-170; O’Sullivan 2000: 170-171, 205-207).

There are at least three reasons to reject these equations. First, ‘real’ markets, rather than the ideal market of neoclassical theory, abound in irrationalities such as ‘noise, fads, and bubbles’ (Kindleberger 1978), which point towards the insight that market transactions and their price determining effects are social structured, even in the case of highly developed markets like stock, option and money markets (Knorr-Cetina & Bruegger 2002; McMillan 2002; Abolafia 1997; Henwood 1997; Baker 1984).

Second, the proposition that equity markets are perfect if prices ‘fully reflect’ all available information hinges on a big ‘if’ indeed. Instead, it is much more sensible to start from the premise that in real markets — because of insufficient or asymmetrical information, opportunism and uncertainty — imperfections are rife. Stiglitz and Weiss, for instance, have argued that banks practice ‘credit rationing behaviour’ to overcome information asymmetries, especially in the case of new, small or innovative firms. Even firms that are willing to pay the real costs of borrowing will thus be denied access to capital, implying that underinvestment of certain type of activities is much wider spread than the efficient market theory allows (Stiglitz & Weiss 1981). More generally, numerous studies have identified huge geographical and functional ‘gaps’ in the capital markets, leaving areas as well as industries cash poor. For example, Martin for the 1980s (1988, 1992) and Mason & Harrison (2002) for the 1990’s have convincingly shown that the geographical distribution of ‘classic’ (rather than ‘merchant’) venture capital in the UK is highly skewed towards the South East, an observation that is closely related to the spatial constraints inherent to the nature — personal and informal — of the investor relation.¹³ More widespread is the observation that small firms have difficulty financing their growth because of insufficient ‘retained earnings’ and lack of external capital due to information asymmetries (OECD 1998; Godley & Ross 1996). Hence, a strong case can be made for targeted investment to cover these ‘gaps’ in capital markets.

Finally, in complex societies like ours individuals perform a multitude of roles. They are at the same time worker, consumer, citizen, family-member, father, mother, child, voter, etc. From these different capacities follow distinct interests, which generally harmonize but which from time to time will collide. It is obvious that equating such a plurality of interests with the one-dimensional interest of the fictional speculator is reductionist to say the least. Doing justice to these plural interests

¹³ More on the distinction between ‘classic’ and ‘merchant’ venture capital below.

requires a transformation of the conventional techniques of investment management into more pluralistic ones. This in turn demands changes in governmental supervision, professional standards, accountancy rules, statistical techniques, audit formats as well as different systems of data-collecting and processing (cf. Nederlands Normalisatie-instituut 1996; Cahill et al. 1989; Blackburn 1999: 47-48). It is obvious that the technical problems only start here (Miller 1991; 1996; Miller & O’Leary 1993; 1994; Barber & Ghilarducci 1993: 305-312).

But even if morally, socially and ecologically reconstructed conceptions of ‘risks’ and ‘returns’ are widely available and broadly accepted, the overriding goal of a pension fund continues to be the provision of a stable and secure pension. Hence the most that can be expected from such a political process of reconstruction will be a dampening effect on the speculative, short-term orientation of contemporary equity markets. In no way will it be a once and for all panacea for the ‘collateral damage’ of current investment practices. In other words, even under an ‘enlightened regime’ many pension funds will continue to abstain from active engagement in either its advocacy variant or its targeted investment variant. Not only because of lack of expertise, data and means, but primarily because it is outside their functional mandate. In my view, that is the most important lesson from the Swedish Meidner Funds. Even unionists turn willy-nilly into *homini economicus* when they take the seat of the institutional investor.

3. Building a Fund for Economic Development

As I said in the introduction: diminishing naive expectations is not the same as nursing no expectations at all. Much is wrong with the current organization of capitalist production, so constructive proposals for reconstruction are urgently required. Screening, advocacy and targeted investment by pension funds are three ways to do so. However, given the logic to which pension funds are subject these alternatives will remain limited at best. What is needed, in my opinion, is an institutional facility that could incrementally provide the mass — if only through ‘demonstration effects’ (Hood 2000) — that is required to construct a viable set of alternative investment opportunities based on reconstructed ‘risk’ and ‘reward’ profiles. In this section I propose such a facility under the heading of a fund for Economic Development (FED). The idea behind this proposal is simple enough. Instead of letting sponsors use the surplus value of pension funds to stack their own coffers, either directly or indirectly via ‘contribution holidays’, funds will be legally required to transfer a substantial percentage of these surpluses to the FED to invest in the ‘socially and ecologically sustainable’ investment goals of the fund. In this way most capital will remain invested in conventional asset categories, allowing pension funds to fulfil their prudential obligations by means of the services of the conventional financial industry, while a much smaller

stream of capital will fund an alternative financial infrastructure where economic experimentalism will be practiced, ultimately generating the instruments necessary to unlock the conventional investment industry from its current hegemonic position.

Rationales

There are five rationales behind this proposal. The first is moral in nature. Since pension savings are ‘deferred wages’ and serve to guarantee the long-term welfare of contributors, these contributions can legitimately be required to take the interests of future pensioners seriously. That means that pensioners should not only be seen as *rentiers*, but also as consumers, fathers, mothers, grandparents, husbands, wives, citizens, etc. This is what is called a ‘life course framework’ by demographers (Elder 1994; Hogan 1981; Mayer & Tuma 1990; Willekens 1999). Current pension arrangements, with their excessively short-term investment orientation, fail to do that.

The second has to do with the ‘public’ nature of pension savings. The huge fiscal subsidies granted to pension funds provide an excellent legitimation to toy with the governance structure of pension funds more generally. In the Netherlands corporate and industrial pension funds are established as ‘foundations’. As such, they have an explicit non-profit orientation and are exempted from profit taxes as well as capital gains taxes. Moreover, individual contributions are exempted from income taxes. Only when these ‘deferred wages’ are being dispensed as ‘pensions’ do they fall under income taxes. However, given the lower incomes of most pensioners, the level of taxation is generally much lower. Hence, the supplementary pension system of the Netherlands is heavily subsidized by the state. The same is true for the US and the UK, where annual fiscal subsidies are being estimated at \$ 100 billion and pound 12-17 billion respectively.

The third has to do with the nature of pension surpluses. These are perceived to be fuzzy in two respects. In general, surpluses refer to the positive difference between current assets and expected contributions on the one hand and current and expected future liabilities on the other. As such, the exact delineation of surpluses or deficits hinges crucially on a number of potentially controversial financial and demographic assumptions. Hence in principle there is widespread leeway for manipulation and obstruction. However, most national regulatory regimes contain fairly detailed prescriptions with regard to both actuarial methods and assumptions, resulting in remarkably uncontroversial determinations of overfunded or underfunded pension funds (Bennett 1994: 11-14).

The second respect in which pension surpluses can be called ‘fuzzy’ has to do with their ownership. Basically the issue is whether surpluses are owned by the fund itself, by the sponsor, by the contributors or by beneficiaries. In the first case the surplus is viewed as an extra buffer to absorb the uncertainties within the demographic and financial assumptions underlying the determination of surpluses in the first place. In the second case the reasoning is as follows. Since

sponsors are legally required to cover deficits in case of underfunding, sponsors hold the obverse ownership rights to surpluses should these occur. In the third case it is maintained that pension assets are ‘deferred wages’ and hence that the exact level of contributions should be calibrated in such a way that future liabilities will be met, no more and no less. Since surpluses indicate that contributions have been too high it follows that employees should receive a contribution holiday. In the last case too the surplus is viewed as being owned by ‘workers’. However, given the fact that most schemes are at best inflation indexed instead of wealth indexed, implying a steady decline in the financial positions of beneficiaries vis-à-vis contributors, beneficiaries make a compelling moral case for using these surpluses to enhance the quality of the pension scheme (Bennet 1994: 15-33).

In view of the huge controversies surrounding decisions in favour of any of these latent ‘owners’, there is much to be said for a policy initiative that takes the ‘fuzzy’ nature of these surpluses seriously, skims of a substantial percentage of them and redirects them towards investments which can claim to serve truly public or common interests. I will have more to say on this issue below.

The fourth rationale has to do with the dual structure of the proposal. By taxing only pension surpluses, the process of generating sufficient returns to cover current and future liabilities is largely left untouched. As such, this proposal bears great similarities to the strategy of ‘partial socialisation’ that was debated within the German socialist movement in the 1920s (Novy 1974: 221-223). This strategy was based on the perceived inefficiencies of market allocations and the expectation that the introduction of elements of social planning within the productive sphere would ultimately render the planned parts of the economy more efficient than the capitalist parts and would thus out compete them.¹⁴

The similarities with the proposed FED have to do with the expectation that alternative investment practices will in the long run prove to be more rewarding than conventional investments and will thus increasingly be perceived as the more sensible thing to do, not only by financial professionals but also by the public at large. The hope is that the financial mainstream will tether towards ‘reconstructed’ risk and return criteria as soon as the number of participants and the amount of capital of the alternative investment circuit reaches a certain threshold.

The differences have to do with a much more sophisticated perspective on markets than was available to the Austrian-Marxists and German socialists of the early 1920s. Instead of taking planning per se as a viable alternative to market allocation per se, the FED is based on the insight that markets are institutions in their own right, which are open to premeditated institutional design and which have different behavioural effects pending their layout. According to this perspective it makes sense to argue for more just markets, implying markets which (i) feature a fairly equal distribution of market power, (ii) provide relatively easy entrance and exit, both at the supply and the demand side, and (iii) induce agents to take account of the long term effects of their actions (Engelen 2001a; Krippner 2002). As such, many contemporary financial markets score low on all

¹⁴ See in this respect Otto Bauer’s notion of ‘Fehlrationalisierung’ (Bauer 1931)

three criteria. The FED aims to create a subset of financial markets, which score better on these dimensions of justice, both with regard to market power, the issue of entry and exit, and with regard to long terms effects. Hence, rather than replacing markets by planning, this proposal aims to fortify the allocation of capital by markets by targeting the cannibalising and self-eroding elements of current market behaviour (Toporowski 2000).

The fifth rationale, finally, is closely related and has to do with the observation that institutional investors in general and pension funds in particular are generally unwilling to participate in investment opportunities that lack easy exit. This is of course precisely the point of my claim that pension funds operate under a constraining logic. Since the rationale of the liquidity preference of institutional investors is overwhelming, incentives will have to be substantial to overcome this preference, as is demonstrated by the experience of the EU Seed Capital Fund where financial incentives were insufficient to entice investors to participate (Murray 1994; 1998). Given the fact that pension funds have good reasons to be unwilling to redirect substantial parts of their capital to unconventional investment strategies voluntarily — even when these are heavily subsidized —, there are strong empirical as well as moral arguments to make contributions mandatory. For reasons of political expediency, it makes sense to turn the implementation of the FED into a two-pronged procedure, consisting of a first step during which pension funds are incentivized to contribute voluntarily, while using the second step of mandatory contribution along the lines sketched here as a stick to ensure compliance.

3.1 The Requirements of Funding

Much of this paper is dedicated to a description of the structural impediments of pension fund engagement. In particular I stressed the ‘logic of funding’, i.e. the combined requirements to maximize returns and liquidity, and to minimize costs and risks, that are inherent to each and every funded pension arrangement. I also emphasized the extreme costliness of unconventional, non-standardized investment and the difficulty of gathering the required information and expertise. And, finally, for a proposal to be realistic, issues of political strategy have to be addressed, such as: who are the winners? Who are the losers? How can the latter be compensated? How should the gains and losses of transition be distributed? Hence the question is: how does the FED fare in these regards? In the following subsections I will deal with each of these issues in turn, starting with the requirements of funding and ending with the requirements of realism or political strategy.

On the requirements of funding I can be brief. For as I said above, the FED is designed in such a fashion as to make maximal use of the sophistication of the conventional financial industry to satisfy the prudential criteria of profit maximization, risk diversification, liquidity and cost

minimization. This is ensured by using only the surpluses of pension funds as a source for mandatory contributions to the FED. Moreover, in its final version the FED would take size and maturity of the fund into account when determining the precise level of taxation. Given the ‘fuzzy’ nature of these surpluses it makes sense to tax them rather heavily with a rate of, say, 50 per cent. Such a percentage would represent a substantial amount of capital, while still allowing individual pension funds to cover financial and demographic contingencies over and above their actuarial obligations.

If the transfers from fund to sponsor during the second half of the 1990s are anything to go by, the amount of capital controlled by the FED could have been substantial by now. For according to estimates Dutch corporate pension funds transferred a total amount of circa 3 billion euro in 1998. In 1999 this amounted to approximately 1 billion euro, while in 2000 a total of 1.67 billion euro was transferred. Due to rapidly declining capital gains on equity during the last two years, surpluses have gradually melted away, which would have resulted in a gradual drying up of the capital inflow. Incidentally, that points to an other attractive property of this proposal, namely that its burden is only felt when it doesn’t matter much, i.e. during periods of boom, while during periods of bust no taxes are levied since no surpluses will be booked, giving funds all the leeway they need to live up to their fiduciary obligations.

Of course, this requires a greater degree of transparency about size, composition, and returns on investment, structure of the portfolio, actuarial assumptions and methods from the side of pension funds than is currently available to preclude strategic manipulation. Hence more extensive and detailed disclosure obligations will have to be included in the constitutive charter to qualify for tax-free status. If funds choose to refrain from doing so, they could be punished with a more heavy-handed fiscal regime.

The obvious advantage of a strategy of ‘partial socialisation’ is precisely that it is partial, implying that the mainstream system of accumulation and allocation is left untouched, while at the same time infusing a second, alternative system of accumulation and allocation with sufficient capital to reach the critical threshold needed for standardization and the economies of scale this implies. Hence, the level of the transferable sum appears to be crucial. It has to be high enough to allow the FED to have any wider impact, while at the same time being low enough to allow mainstream pension funds to fulfil their fiduciary obligations unhindered. Whether a tax of 50 per cent satisfies these requirements is open for debate.

Determining surpluses is always controversial, as the experiences of the original Swedish ‘wage earner funds’ as well as those with the determination of ‘excess profits’ as a basis for ‘capital gains sharing’-plans in the Netherlands demonstrate (Dercksen 1985). In both cases, however, the controversy was not due to a lack of workable assumptions and methods but rather to a multitude of them. Apparently, this did not hinder normal accountancy practices, but merely became one as soon as conventional accounting categories were being used for redistributive ends. While in

‘normal’ situations pragmatical consensus apparently trumps ideological disagreements, in ‘abnormal’ ones it is precisely the other way around. Hence, strategies will have to be found to ‘depoliticise’ the issue and turn it into the ‘technical’ affair it normally is. How to co-opt potential adversaries, is an issue that will be addressed below under the heading of realism.

3.2 The Problems of Unconventional Investment

As I noted above, the problems of unconventional investment are twofold: first, its costs can be prohibitive — due to the absence of standardized investment objects and their small scale — and second, its information base is generally precarious. I will address these issues in that order.

Costs

Despite its persuasive appearance, the cost constraint does not have to be a decisive argument against unconventional investment. First, there is no reason why the FED would have to generate the same returns as conventional pension funds. Since the determination of the annual capital transferred from fund to FED is based on surpluses only, the transferred amount could fall under a different, less demanding set of requirements, for it would not have to contribute to the stock of capital that is used to cover current and future liabilities.

Second, post-war experiences with public investment banks have demonstrated that one can’t have it both ways; these banks either *supplement* market allocation and hence have to put up with lower financial returns (Pontarollo 1983), or they have to satisfy mainstream financial requirements and hence *replace* conventional market allocation (Minns 1980: 78-102; Eliasson & Ysander 1983).

This does not imply that alternative demands — social, ecological and economic — ought to trump financial ones automatically and hence that the FED would not have to be subjected to cost covering profit requirements at all. Public investment banks without a profit requirement in their mandate have historically proven to become either gullible charities who simply squander other people’s money or state instruments good at ‘backing losers’ rather than ‘picking winners’ (De Jong & Spierenburg 1983; De Grauwe & Van de Velde 1983).

Hence, the profit requirements of the FED have to be substantial enough to cover operational costs and ensure independence from state agendas, while being low enough to provide starters and ‘antelopes’ with an entry to capital they would not have possessed otherwise. To this must be added that access to seed capital is not the main obstacle to economic maturity; getting access to capital to finance growth is (OECD 1998). This implies that economic development is not so much a matter of lowering prudential requirements, but rather of repackaging them. Similar to the customized financial packages investment banks offer their high-grade corporate clients, growing firms could be

provided with financial instruments that are made to the measure of their highly individual needs. Hence, loans could embody different tradeoffs between returns and commitment over time, by varying the dimensions of yields, capital gains, repayment of principal and term intelligently.

Information

The precarious information-base of unconventional investments poses two problems; first, the problem of investment identification — how to identify promising investment opportunities and bring them into contact with the FED — and second the assessment problem — how to assess the growth potential of unconventional starters and the creditworthiness of non-standard debtors? The hard issue is that we are looking for profitable investment opportunities that nevertheless fall outside the conventional system of capital allocation. The implication is not only that the FED will have to wield diverging criteria of profitability (see above) and has to have access to entrepreneurial skills, but also that the FED will be unable to use conventional networks for the allocation and distribution of capital, for example those of commercial banks.

In principle, three solutions are available. The most obvious one is cooperation with existing financial service providers who, for reasons of a diverging ownership structure or an explicit ideological orientation, wield deviant performance criteria and possess aberrant networks. Savings banks, cooperative banks and state banks have historically played a crucial economic function by providing forms of credit that for a variety of reasons were unattractive to private banks (Verdier 2000a; 2000b). In a large number of European regions these types of financial service providers are still part and parcel of the micro and meso-corporatist networks that buttress the ‘cooperative competition’ for which these regions are famous (Cooke & Morgan 1998; Deeg 1999). However, their existence is increasingly endangered. Mergers and acquisitions have created financial conglomerates that provide the complete gamut of financial services, leaving less room for specialists. Moreover, because of economies of scale, specialists have increasingly been subjected to cutthroat competition, forcing them to cut costs and raise income. And wherever governments have come to the aid of these banks, as in Germany, European competition policy has cracked down hard on these attempts, arguing that it gave some an unfair advantage (Deeg & Lütz 2000). In the Netherlands these developments have resulted in a gradual dilution of the functional walls between different financial activities, in fact resulting in a loss of diversity that is being applauded by most observers of the financial industry as the triumph of ‘universal banking’. At the same time, however, new ideologically based initiatives have sprung up in the form of social and ecologically responsible banks. However, their size is still much too small to solve the problems of unconventional investment.

The second solution is simply to buy the required expertise. This can be done in two ways. First, by selecting and hiring asset managers and other intermediaries in a one by one fashion. However, this solution is not devoid of problems. For it implies that these managers have to be poached from

other financial service providers, which, in view of the bonuses this requires, can be a costly affair. Moreover it is uncertain whether hiring the right managers will also mean buying the right networks, for that is what makes these managers valuable to begin with. In other words, money won't buy you loyalty. For that you also need prestige and reputation. It is a safe bet that the reputation of regular investment banks within the mainstream financial industry will for a long time exceed that of alternative institutions.

The second way to buy expertise is by taking over an existing organisation with expertise in this field. Here the danger is that the acquired organisation proves to be a Trojan horse, turning it into a form of external management according to conventional criteria. However, in both cases the chances are that what you are actually buying will be 'the analytical, financial engineering, deal-making and transaction and closing skills' that are in abundant supply in the conventional financial industry and not the 'company forming, building and harvesting skills' that you really need (Mason & Harrison 2002: 430).

The third solution, finally, is difficult to accomplish but has the advantage that it entails an organisational scheme, which, if only for its deviance, guarantees to shelter it from the intellectual and institutional dominance of the financial industry. It boils down to the construction of a multi-layered organisational structure allowing for a division of tasks and duties over formally independent but functionally dependent units, which is based on the principle of subsidiarity: jurisdictional competencies ought to be devolved to the lowest possible level of aggregation. Which level should deal with which type of decision depends on the knowledge required, the degree of interested commitment of the agents involved, and the specific function the forum in question fulfils within the organizational decision structure as a whole. Nevertheless, the presumption of devolution implies that the burden of proof lies on the side of those who want to shift responsibilities upward rather than downward.

In general, parametric decisions should be made at the pinnacle of the organization, for these types of decisions consist of balancing general interests, criteria and sources of knowledge. Since these are intrinsically 'political' decisions, depoliticising the issues by distancing advocates from the interests they are representing in fact helps to enhance the effectiveness of the decision making process. This is much easier to accomplish at the central level. Moreover, lack of situated knowledge does not matter much, since abstract, codified knowledge suffices to make these categorical decisions. Instead, day-to-day decision-making does require situated knowledge, while the more pragmatic nature of these decisions limits the need for depoliticisation strategies. Moreover, since local decision makers act within the parameters laid down by central decision making, they do possess the right measure of jurisdictional liberty to act autonomously while at the same time being subjected to a sufficient degree of *ex post* control to preclude manipulation and favouritism.

In concreto, such a scheme would consist of a central fund where administration and parametric

decision-making takes place, combined with a small number of regional and sectoral entities where day-to-day assessment and management is done. In this manner economies of scale — joint administration — can be combined with the advantages of devolution and smallness, i.e. flexibility, diversity and the use of local knowledge. To prevent hierarchical control and coordination, which would do away with these triple advantages, central administration and decentral handling should be kept distinct legally. Otherwise central decisions will often trump local needs and requirements. On the other hand, to guarantee some ‘shadow of hierarchy’ control *ex post* should take the form of contracts, rewarding capital disbursement within the parameters laid down centrally with lower interests while punishing violations with higher rates. Finally, to ensure that investment opportunities are in fact identified, regional and sectoral funds will have to set up local networks consisting of representatives from industries, local governments, universities and labour unions. These representatives, together with managers from both local and central funds, could form advisory boards to steer the firm through rough waters and ensure the long-term profitability of the investment, just like venture capitalists do.

Of course, these solutions are non-exclusive. If the objectives of the FED are interpreted broadly — ranging from economic decentralisation, innovation and local and regional economic development to encouraging sustainable production and high-performance work places — there is much to be said for an organisational structure that keeps these objectives as distinct as possible, to prevent a self-defeating battle for scarce means. One way to do so is by mandating the board of trustees of the central fund to earmark specific capitals for specific goals,¹⁵ and to mould the allocating apparatus to the properties of the goals themselves. For instance, assessing credit applications for experiments with sustainable production methods by large and middle-sized firms, or for that matter with high performance work practices, is a task that is best conducted along the lines of the first or the second solution. However, as soon as credit allocation is part and parcel of a sectoral or regional modernisation or restructuring program the third solution seems more suited, for in that case a mix of financial and entrepreneurial skills is needed instead of merely financial ones.

Generally, the shape of the organization should depend on the locus of initiative. Applied to the earlier examples, this means that in the first case intermediation, assessment and allocation can take fairly conventional shapes. Not so in the second case, where the initiative is the FEDs, requiring a hands-on approach by sectoral and regional funds. Centrally, the input is restricted to parametric assessment according to the ‘reconstructed’ notions of profitability the FED wields for all its investments. It is obvious that the costs of investment rise exponentially as soon as the locus of

¹⁵ To overcome the rigidities of budgeting *ex ante*, a system of periodical assessment could be introduced centrally. The commission who would conduct these evaluations would have to be composed as broadly as possible, to ensure that its decisions reflect as many relevant interests as possible and are based on the maximum amount of relevant information.

initiative shifts from the outside to the inside. To diminish the temptation of passivity, internal and external reporting should be geographical or sectoral instead of categorical.

This may sound farfetched but is in fact largely similar to the structure of the venture capital industry as it has arisen in most countries. For in that case too proximity is guaranteed by delegating the responsibilities of day to day management to local venture capital firms who possess the required mix of skills and are well-embedded within local networks, while categorical management is undertaken by regional or national venture capital funds, staffed by managers with skills that are much more geared towards financial management (see figure 1.). The crucial difference between the venture capital industry and the FED is simply that under the latter sponsoring is mandatory rather than voluntary. Otherwise, the organisational make up is identical.

[Figure 1. about here]

Since the venture capital industry is not without problems itself, the implication is that these are problems for the FED too. It is customary within the literature on venture capital to distinguish between two forms of venture capitalists, i.e. 'classic' and 'merchant' venture activities. Merchant activities are primarily aimed at management buy-outs and buy-ins, ownership changes, and corporate restructurings, focus on larger firms, and hence require conventional financial management skills. These types of venture capitalists are mostly located in the larger financial centres and have increasingly become intertwined with the mainstream financial industry. Classic venture capital, on the other hand, seeks to finance entrepreneurial opportunities, which promise substantial growth, but which fall outside the scope of conventional credit provision for reasons of high uncertainty, intangibility of assets and non-existent secondary asset markets. Hence, classic venture capital activity is long term, committed and entrepreneurial in nature. It requires hands-on advice, constant coaching and grooming, and a willingness and ability to invest social and human capital next to financial capital to turn the venture into a success (Bygrave & Timmons 1992).

Since it is investment in new types of productive activities, rather than in reorganizing existing production, that we are primarily interested in, it is pertinent to ask which type of venture capital activity predominates. If the situation in the UK is anything to go by, it is obvious that the inroads the conventional financial industry has made within the branch of venture capital provision has radically changed the nature of the latter industry, for, as Mason & Harrison observe, '[s]ince the late 1980s, the UK venture capital has become progressively more geared to investing in [management-buy-outs] and [management-buy-ins]'. An increase that 'has been at the expense of investments in seed capital, start-up and early stage ventures', or the 'classic' venture function (Mason & Harrison 2002: 435). So, updating on Martins observation that venture activity was highly unevenly distributed in the UK, Mason & Harrison conclude that although aggregate figures do indeed show a more even distribution for the 1990s, once these figures are broken down for classic

and merchant activities it becomes apparent that the distribution of classic venture capital still follows the pattern identified by Martin in the 1980s.

According to Mason & Harrison this has everything to do with the preference of institutional investors, notably pension funds, for investments that provide easy exit and fall within the reach of conventional investment consultants. In general, that is more the case with merchant venture activities than with classic ones. Moreover, merchant activities do not come with the same proximity constraints as classic activities. The latter, because of their committed and active nature, require co-location of capital provider, coach and advisor, and venture. Whereas the purely financial nature of the relation between investor and venture in the case of merchant venture activities, allows the investor to remain at a geographical distance from the object of investment (Mason & Harrison 2002: 435, 443).

Recent attempts by the British government to stimulate institutional investors to redirect capital from merchant to classic venture activities by setting up so-called Regional Investment Funds (RIF), which match private investments with public money, indicate that addressing these issues will not be easy. According to Mason & Harrison four issues in particular stand out. First of all the liquidity preference of large investors. It is not clear whether the matching scheme is enough enticement for pension funds to become involved voluntarily. There are good reasons to doubt that. Second, the lack of classic venture capital skills, including the lack of the institutional infrastructure needed to provide a venture capital-friendly environment (Kenney 2000). Third, the long-term financial viability of the RIFs. Given the inability to overcome large investors' liquidity preference, the RIFs are due to remain small, resulting in high costs per unit of investment, making the funds vulnerable on a number of accounts: (i) because of a lack of ability to diversify; (ii) because of an inability to provide follow-on money, either because of a lack of capital or because of diversification requirements; (iii) because of an inability to 'harvest' and to build a 'track record' that might attract institutional investors. Fourth, because of a lack of viable investment opportunities (Mason & Harrison 2002: 445-446).

Not all of these problems are relevant here, for the mandatory nature of the FED addresses both the first and the third issues, while the organizational structure of the FED is such that the regional and sectoral outposts have a mandate to incorporate as many knowledgeable outsiders as possible. In particular, the local networks consisting of representatives from industries, local governments, universities and labour unions which the regional and sectoral funds will have to set up, are explicitly meant to ensure that investment opportunities are in fact identified and that potential entrepreneurial skills are in fact available. For it is obvious that the venture capital industry does not have a monopoly on these skills and that good coaches and advisors are not born but can be made. It is hoped that this goes a long way to dispel the qualifications of Mason & Harrison.

3.3 The Requirements of Realism

The final and most intricate issue is that of political tractability. Since institutional arrangements are temporary compromises between contending groups, each and every proposal for institutional redesign implies a more or less serious infringement upon vested interests. In other words, institutional change involves real costs, either of a financial, mental, emotional or habitual nature. Hence, the feasibility of a proposal for institutional change depends crucially on the identification of winners and losers, the nature of the costs involved as well as credible attempts to reimburse losers (Engelen 2001b: 152). In this particular case, three broad categories of interests can be identified, i.e. (i) sponsors, in particular large corporation; (ii) pension funds; (iii) contributors and beneficiaries; and (iv) the financial industry, especially insurers and commercial banks. I will address each in turn.

Corporate Sponsors

Although there is widespread acceptance that pension savings should be looked at as deferred wages, this does not extend to pension fund surpluses as we have seen, in particular those of single-employer or corporate pension funds. In the second half of the 1990s corporate pension funds in the Netherlands and elsewhere have increasingly yielded to the ownership claims of sponsors and have used their surpluses to grant sponsors ‘contribution holidays’ and/or substantial capital transfers. These refunds have not remained uncontested, however, especially since the bust of the equity markets has gradually eroded the financial positions of most pension funds. Though most legal claims of beneficiaries and contributors against these restitutions have been rejected, a good case can still be made against exclusive corporate ownership of pension surpluses.

Since contributions and capital gains are exempted from taxation, the accumulation of capital is in part publicly financed. As such, the state can claim potential voice over the uses of these surpluses. Moreover, there is a glaring inequality a propos the status of these surpluses, between multi and single-employer pension funds. In the first case, the link between sponsors and fund is much more indirect, standing in the way of restitutions (though not of contribution holidays), while in the second case the financial fates of sponsor and fund are perceived as being identical, allowing for restitutions during good times and obliging sponsors to refund during bad times. These practices thus boil down to a preferential treatment of large firms over SME’s. Consequently, the FED-scheme reveals a long-standing fissure within the class of capitalists, allowing for cross-class alliances that enhance the possibility to overcome the resistance of corporate sponsors.

The third argument against corporate ownership of pension surpluses has to do with the common interest in a vibrant, innovation-enhancing economic environment, requiring the ready availability of a number of crucial production factors such as loyalty, commitment, trust, qualifications and competencies, networks of cooperation, etc (Streeck 1992: 1-40). Since these

factors have definite public goods-properties, market relations result in an undersupply of these goods. As such, 'beneficial constraints' are needed to force rational agents to forsake short-term gains and take the long-term effects of their behaviour into account (Streeck 1997). Like collective bargaining, minimum wages, co-determination, works councils and vocational training, the FED too would represent such a 'beneficial constraint', in this case a constraint on the ability to buy conventional investment products in an attempt to stimulate beneficial investments in sustainable production opportunities.

Even though many large firms possess the means to create 'islands of order in an ocean of chaos', in most cases the internalisation of transactions this implies is set in motion by a low trust environment. Since trust lowers transaction costs, large firms too will be able to externalise transactions and hence to cut upon the organization costs entailed in building hierarchical pyramids. Hence, investing in the 'redundant capacities' of a specific locality is in the long-term interest of large firms too. Big corporations thus should explicitly be invited to aid the construction of local investment networks to enhance their geographical embeddedness. Moreover, part of the capital of the FED should be made available to large firms too, for instance to finance experiments with integrated chain management and sustainable production, or to invest in high performance workplaces and the high quality of labour these imply. To prevent large firm dominance it makes sense to earmark specific percentages of capital for specific categories of firms and to insist upon a matching formula for the largest ones.

Contributors and Beneficiaries

The main interest of both beneficiaries and contributors is a high, stable and secure pension. As such, redirecting some savings, if only half of pension surpluses, away from the conventional investment industry goes against the grain of workers' interests. However, these interests are less monolithic than it appears. For both in situations of underfunding and overfunding beneficiaries come into conflict with contributors. In situations of underfunding, deficits can be translated either in higher contributions (from both workers and employers) or in less favourable benefit conditions. In the first case the burden falls upon contributors, in the second on beneficiaries. In situations of overfunding, surpluses can be distributed either to beneficiaries in the form of better conditions or to contributors in the form of contribution holidays.

The only way out of this predicament is to emphasise that all contributors will ultimately be beneficiaries too. If the formulation of preferences can be kept at a distance from immediate interests and if participants can be stimulated to take a life course perspective, the clashing preferences for lower contributions and higher payments stand a chance of being reconciled. In fact, the Dutch legislator has given pride of place to the intergenerational solidarity that pension

funds embody, by stressing that the trustees are legally obliged to serve the interests of all parties, even though only contributors have access to the board of trustees.¹⁶

However, adopting a life course perspective would need to entail not only the inclusion of all parties involved, i.e. contributors and beneficiaries, but also of all relevant interests and preferences of those parties. For the participant is not merely a contributor who has a contractual claim on a defined benefit as soon as he or she reaches a certain age, but is also an employee, a consumer, a household member, a family member, an inhabitant of a specific neighbourhood, a citizen, etc. This diverse set of identity constituting roles and functions give rise to a pluralistic set of interests and preferences, which go beyond the level of contribution payments and the quality of the insurance conditions. Given such an encompassing life course perspective, participants also have an interest in securing long term wealth and welfare generating capabilities, which guarantee the sustainable fulfilment of his needs and desires as well as those of his neighbours, colleagues, friends and children.¹⁷ To fulfil these needs and desires investment strategies are required that go beyond mere profit maximization and risk minimization (Barber & Ghilarducci 1992: 308-309).

That is exactly what the FED tries to do. By supplementing conventional investment opportunities with the construction of a framework for alternative ones, the FED incorporates the objective need for sustainable development while acknowledging the legitimacy of the interest in high, stable and secure pensions delivered through the conventional channels. Moreover, the moral appeal to contributors and beneficiaries to assume a life course perspective will only be persuasive if there is an institutional arrangement embodying it. Obliging pension funds to reserve half of their surpluses for investment through the FED in the long term wealth and welfare generating capacities of the local economy is a policy measure in which the brute social fact of inter- and intragenerational interdependence, and the ‘moral community’ that it buttresses, comes clearly to the fore.

The Financial Industry

There is a tight link between pension funds and the financial industry. Over their life cycle pension funds become increasingly dependent on the services of the financial industry in an attempt to maximize their objectives, while the financial industry itself becomes increasingly addicted to the continuous inflow of capital provided by pension savings (Engelen 2003a). Some even go so far as

¹⁶ Interestingly, since the global stock market crash has severely endangered the financial ‘health’ of Dutch pension funds, this is increasingly perceived as insufficient, especially by pensioners’ organisations. Currently the introduction of representatives from beneficiaries within the board of trustees in a tripartite way is seriously discussed — and in some cases even voluntarily practiced — as a remedy for speculative behavior and too generous paybacks to the sponsoring corporation.

¹⁷ See Bader (1987) for a description of a strategy to ally ‘duties’ and ‘interests’ via long-term consequences, in the context of class alliances.

to suggest that the accumulation of pension savings sets in motion a gradual process of asset inflation, in its course transforming the incentive structure firms face, turning them into veritable ‘rentier capitalists’, ultimately resulting in the instalment of a discrete regime of accumulation described as ‘financialisation’ (Toporowski 2000; Boyer 2000; Minsky 1992).

However, fissures mark the financial industry, like the capitalist class at large, too, allowing for a divide-and-rule strategy that could enhance the feasibility of the FED. First, there are the interests of the pension industry itself to be considered. Whether a pension fund can be seen as an autonomous economic agent with a freestanding interest depends upon the nature of its relation with its sponsor. For in the case of private corporate sponsors there will generally be a high degree of congruence between fund and sponsor. In the case of public and multi-employer sponsors, on the other hand, the distance between fund and sponsors is much larger. Hence trustees of the latter will be more liable to perceive the imposition of investment requirements — either those directed at categorical asset allocation or, as in the case of the FED, at the management of proceeds from earlier investment — as an outside infringement on their fiduciary duties,¹⁸ than will trustees of the former, who will tend to equate the interests of the fund with those of the sponsor.

What has to be kept in mind in this regard is the preferential fiscal status of pension funds. This does not only imply that part of the asset accumulation of pension funds is ‘public’ in nature, but also that the state is privileging some financial service providers, in this case pension funds, over others, i.e. merchant banks, commercial banks, savings banks, insurers, mutual funds etc. Especially since pension funds are providing ever more services and are increasingly entering financial markets that used to be the dominion of private financial service providers, the preferential fiscal treatment of pension funds by the state has more and more become a cause of complaint, especially for insurers, whose field of operation is increasingly penetrated by huge pension funds while the ‘market’ for pension provision is in turn highly regulated and guarded.¹⁹

The legitimacy of the differential treatment of insurers and pension funds stands or falls with the ability of the Dutch government to keep the markets separate. However, upholding the walls

¹⁸ In fact, the privatisation of the largest public Dutch pension fund, the ABP, in 1994, was largely set in motion by the announcement of the Dutch government in 1991 to skim 22 billion euro surplus from the ABP to finance infrastructural investments. This caused huge uproar among the small community of Dutch institutional investors and ultimately resulted both in the privatisation of the ABP and, as a kind of compromise, the establishment of a so-called ‘industrial facility’, a revolving fund set up by the Department of Economic Affairs and financed by a small number of Dutch banks, pension funds and the state itself. The facility started in 1993 with a total capital of nearly \$ 400 billion. In 1996 only two firms had applied for a loan under the facility. In 2001 the facility was abolished.

¹⁹ Pressured by Dutch insurers the Dutch government has recently installed a so-called ‘Pension Fund Conglomerate Committee’, which is to determine what the core business of pension funds is and which additional activities they may undertake.

between these markets is increasingly becoming controversial. A case in point, discussed by Clark (2003), is the recent ruling by the European Court of Justice (ECJ) ON the compatibility of pension fund exclusiveness over the Dutch pension market with EU competition policy. The ECJ maintained that the requirements of competition had to be weighed against requirements of economic and social cohesion and ruled that neither the tax advantages of Dutch pension funds nor their exclusive rights to provide pension is in fact a breach of European competition law. As such, the ECJ adhered to a broad version of competition policy, according to which competition is merely a means to the ends of market integration, social cohesion and other objectives enshrined within the Treaty of Rome (Clark 2003). However, there is no guarantee that next time the ruling will be similar, especially if Dutch practices are perceived to stand in the way of an integrated European-wide financial market, as some in the Dutch pension industry fear.

The point is that this particular constellation provides an excellent opportunity to coerce unwilling pension funds into a more supporting stance towards the FED. By offering pension funds the guarantee to continue their preferential fiscal treatment against the increasing complaints of insurers, and even against European pressures, in exchange for legislative support, the Dutch state could create the momentum that is needed to carry such a legislative project.

On the other hand, the activities of the FED itself imply new infringements on the territory of other financial service providers, in this case those of investment banks, for disbursing productive capital to firms and aspiring entrepreneurs is a classic bank function. Hence, banks will be among the most outspoken adversaries of the FED, as they historically have been a *propos* similar looking initiatives. Even though the investment criteria used by the FED are explicitly designed to divert excess funds into localities, sectors and business opportunities that are currently not serviced by the conventional financial industry, and are hence by definition preserved from the charge of unfair competition, the many precautionary measures surrounding the establishment of state investment companies in Europe in the 1940s and 1950s demonstrate that formal arguments like these will be insufficient to deflect the complaints of commercial banks. Hence, many charters contained an explicit prohibition to tread on the turf of commercial banks (Hindley 1983). In some cases, distributing the shares of the company between state, commercial banks and institutional investors, who were also granted equal control rights in the jointly managed board of trustees, largely deflected the worries of the financial industry, (De Jong & Spierenburg 1983: 63-64).

Since the FED is supposed to be a facility that aims to break the investment hegemony of the conventional financial industry, cooptation strategies like these are unavailable. The ability of the FED to realise its unconventional goals depends crucially not only upon the absence of state control but also on its ability to stay outside the sphere of influence of mainstream financial service providers. Participation of mainstream financial institution in the ownership structure or control structure of the FED is for this reason undesirable. Apparently proponents of FED-like facilities have only moral arguments to overcome the objections of adversaries from the financial

industry. And, as we know, moral arguments have only a weak motivating force, especially if there are strong prudential counter arguments. Hence, state voluntarism seems to be the only solution to tip the balance in favour of pension-financed economic development and restructuring.²⁰

However, there is more to this than meets the eye. As I have already mentioned, the financial industry is far from homogeneous. For despite increasing market integration financial institutes are still very much nationally based, implying a potential conflict of interest between ‘insiders’ and ‘outsiders’. A case in point is the increasing number of clashes between the requirements of EU competition policy and historically grown national and regional investment practices. And as I mentioned above, spokespersons for the Dutch pension industry are concerned that the lack of awareness on the side of EU-policy makers for the Dutch distinction between life insurance and pension provision might result in a form of European pension harmonization that could erode the distinct ‘identity’ of Dutch pension funds. But not only international and interregional differences matter in this respect, so do intranational differences. Most developed economies have established different financial organisations for different goals, which are characterised by distinct ownership and control structures and wield diverging investment standards and criteria. Just like American Savings & Loans differ hugely from Wall Streets major investment banks, so do German savings banks, cooperative banks and commercial banks (Deeg 1999). The local embeddedness of the former two types of banks have made them into the interfaces *par excellence* between local SMEs and local savers, while the large commercial banks, almost all of them located in the Financial centre of Frankfurt, mainly serve large publicly quoted German corporations.

It is obvious that such a structured landscape of different legal banking mandates generates different institutional interests, which could be manipulated by the central government to create fissures within the financial industry that enlarge her strategic maneuvering space and allow her to lessen the autocratic nature of her intervention. However, divide-and-rule strategies will by definition never overcome all objections; they merely breaks a collective of potential adversaries up into smaller units. Since someone is going to get hurt the central government will ultimately have to fall back upon her legislative monopoly and will have to legitimate her intervention by paternalist means, the moral validation of which is grounded in a reasoned balance between moral, prudential and realist requirements. That is what ‘real utopianism’ is all about (Bourdieu 1998; Wright 1995a: ix-xiv; Bader & Engelen 2003).

3. Conclusion

²⁰ Perhaps this type of logic explains the fact that one of the few successful examples of pension-financed economic restructuring is to be found within authoritarian Singapore (Asher 1993: 155-158).

Despite the enormous growth of pension fund assets, especially during the 1990s, and despite the fact that these assets represent workers' savings, raising expectations of a quick and imminent 'socialisation of capital', the alternative investment strategies captured here as 'pension fund engagement' are marginal to the conventional financial industry and represent only small percentages of total assets. This has not deterred progressives to place great hope on the political opportunities created by glaring cases of corporate misbehaviour and rapidly falling equity prices to enforce a paradigm shift upon the financial industry in general and the pension fund industry in particular.

In this paper I argued that these hopes are largely misplaced. A reconstruction of the Swedish mid-1970s attempt to use pension savings as a mechanism for 'encroaching control' over publicly quoted firms, demonstrated that even in the best of circumstances such attempts are destined to fail. The lessons I derived from the Swedish Wage Earner Funds boiled down to the following. Because pension savings are 'deferred wages', pension funds see themselves obliged, for good moral and prudential reasons, to invest prudently, that is minimize risks, maximize returns, minimize costs, and ensure sufficient liquidity. Given these objectives, it is only reasonable that trustees delegate their decision making tasks to professional financial service providers, offering standardised and hence cheap investment 'products'. Setting up alternative research, scouting and support facilities, is too difficult, too time-consuming and hence too costly too. At the same time, the fiscal and juridical status of pension funds works against an organizational transformation from 'guardians' of pension savings into active allocators of credit, a traditional banking function. For these reasons, pension funds are hardly calibrated to contribute to investment planning, industrial policies, regional development, economic restructuring and promoting sustainable production systems. In other words, the 'logic of funding' largely explains why the amount of assets allocated to 'social responsible investment' is so limited.

Given this state of affairs, a more sober approach to pension fund engagement, its chances and limitations, is urgently required. However, soberness is not identical to fatalism. Identifying the lack of clear, distinct, workable and largely uncontroversial criteria for socially and environmentally sustainable investment as one of the main bottlenecks for the mainstreaming of social responsible investment, I proposed the install a complementary mechanism, financed from pension fund surpluses, to provide the mass that is required to standardize alternative investment categories and minimize its costs while at the same time starting to address the most glaring 'gaps' within real existing capital markets. I argued that such a Fund for Economic Development, as I labelled it, would answer most of the objections that screening, advocacy and targeted investment run into. First of all because the ability of pension funds to fulfil the requirements of funding would remain unharmed, since the FED could only claim surplus savings. Second, because the FED was explicitly designed to mimic the organisational features of the venture capital industry in order to be able to do what it set out to do in the first place, namely allocating capital to economic ventures that are

not supplied by the conventional financial industry. The only difference being the mandatory nature of the inflow from pension fund to venture capitalist. And third, because a number of current developments — having to do with European market integration, issues of competition policy, and the conglomeration tendency within the financial industry — provide the political opportunity to push for mandatory arrangements such as the one proposed here.

It is evident that this proposal is primarily directed to a European audience, and in particular a Dutch one. As such, it can be objected that the ‘realism’ of this proposal might be obvious for a Dutch audience, although even that can be debated, but that for a, say, American audience its ‘utopian’ overtones are overwhelming. In other words, proposals such as these, despite being garbed in a universal idiom, clearly betray distinct institutional, organisational and political presuppositions and conditions.

I won’t deny that, though I want to stress that proposals for institutional redesign, even though conditioned by distinct spatio-temporal coordinates, can contain lessons for other times and localities. It is obvious that the growing attention for the potential regulatory possibilities of pension fund engagement by American scholars, activists and practitioners is born from the increasing inability of progressives to impact the legislative trajectory. As such, voluntarism seems to be the only political pressure instrument available. From this perspective, proposals that count on state intervention must strike one as truly utopian, in the naive sense of the word.

Although as a general assessment of the political chances of progressive ideals within the American legislature this is surely overly pessimistic — see the current discussion in the US on the mandate of the Securities and Exchange Commission (SEC) and whether it encompasses the right of the SEC to enforce ‘social disclosure’ requirements (Williams 1999; 2002) — it remains the case that voluntary measures have a higher chance to succeed in the US than legislative ones. However, even under adverse political conditions like those in the US, ‘conceptualised’ lessons can be drawn from the FED-proposal described in this paper. For in that case, the American corrective will probably consist of turning its mandatory nature in a voluntary arrangement. Or to be more specific, union governed pension funds could, through coordinated action, set up an alternative investment facility, mimicking the organisational model of the venture capital industry, to enhance the mass of capital available for targeted investment and subsequently create the momentum that is needed to set in motion the collective learning process that has to be behind the construction of alternative standards for ‘risk’ and ‘return’.

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