

PRI RESPONSE TO THE LAW COMMISSION CALL FOR EVIDENCE ON INTERMEDIATED SECURITIES

ABOUT THE PRI

The Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI is a not-for-profit company with over 2,500 signatories (pension funds, insurers, investment managers and service providers) to the PRI's six principles with approximately US \$89 trillion in assets under management. 366 of these signatories, representing \$9 trillion, are based in the United Kingdom.

The PRI supports its international network of signatories in implementing the Principles. As long-term investors acting in the best interests of their beneficiaries and clients, our signatories work to understand the contribution that environmental, social and governance (ESG) factors make to investment performance, the role that investment plays in broader financial markets and the impact that those investments have on the environment and society as a whole.

The PRI will work to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

THE PRI'S POSITION

The PRI welcomes the Law Commission's project investigating problems arising from intermediated securities and dematerialisation.

The PRI's Principle 2 states: "We will be active owners and incorporate ESG issues into our ownership policies and practices". Active ownership is one of the most effective strategies available to investors to minimise risks and maximise returns. Voting is a crucial aspect of this, and thus the barriers presented by the current system of intermediation noted in the Commission's call for evidence are of serious concern.

The extent to which intermediation reduces the ability to reflect beneficiary preferences in how votes are cast may constitute a breach of fiduciary duty.¹ Understanding and incorporating beneficiaries' and savers' sustainability-related preferences, regardless of whether these preferences are financially material, is a fundamental aspect of fiduciary duty, and this extends to how votes are executed on savers' behalf. It is also an increasingly recognised aspect of good stewardship, as reflected in the revised Stewardship Code.²

There is good reason to believe that there is currently a disconnect between beneficiaries' preferences and how votes are cast on their behalf. For example, while climate change has been identified as a key issue among the British electorate³, a study by the Association for Member-Nominated Trustees (AMNT)⁴ found that over half of 42 UK fund managers did not have a voting policy setting out their approach to the issue.

The possibility for asset owners to split their vote when invested in pooled fund arrangements would be one solution to overcoming this disconnect; however, the current system of intermediation may obstruct this process. The PRI, together with AMNT and the UK Sustainable Investment and Finance Association (UKSIF), has commissioned research exploring this question.

The Commission has also sought evidence on the possibilities of technology such as distributed ledger technology with regards to this issue. The PRI has researched the implications of this technology for institutional investors and the financial industry, as set out in *Responsible Investment and Blockchain*.⁵ This notes numerous experiments and trials internationally in jurisdictions such as Estonia, Russia and the US State of Delaware to investigate the potential of blockchain technology regarding, for example, central share depositories and shareholder e-voting platforms.

Any questions or comments can be sent to emmet.mcnamee@unpri.org .

¹ <https://www.unpri.org/fiduciary-duty-in-the-21st-century-final-report/4998.article>

² <https://www.frc.org.uk/investors/uk-stewardship-code>

³ https://www.bsa.natcen.ac.uk/media/39251/bsa35_climate_change.pdf

⁴ <https://amnt.org/amnt-identifies-poor-transparency-in-fund-manager-voting-policies-and-practices/>

⁵ <https://www.unpri.org/sustainable-financial-system/responsible-investment-and-blockchain/2983.article>