

U.N. Drafts Principles for Responsible Investment



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Socially responsible investing (SRI) strategies serve as the foundation for a new United Nations initiative, the Principles for Responsible Investment (PRI). Launched last week at the New York Stock Exchange with 32 institutional investors representing \$2 trillion as signatories, the Principles gained another 18 institutional investors -- doubling the assets represented to \$4 trillion -- at the recent European launch in Paris.

"These Principles grew out of the understanding that while finance fuels the global economy, investment decision-making does not sufficiently reflect environmental, social, and corporate governance considerations -- or put another way, the tenets of sustainable development," said U.N. Secretary-General Kofi Annan. "Developed by leading institutional investors, the Principles provide a framework for achieving better long-term investment returns and more sustainable markets."

Citing the lack of a framework as the primary obstacle to integrating environmental, social, and governance (ESG) considerations into the investment decision-making process, Secretary-General Annan proposed the development of the Principles in early 2005. The U.N. Global Compact and the United Nations Environment Programme Finance Initiative (UNEP FI) coordinated the convening of an "Investor Group" of 20 institutional investors from 12 countries to draft the Principles. Another group of stakeholders representing investors, governmental and intergovernmental agencies, nongovernmental organizations (NGOs) and academics supported the work of the Investor Group from April 2005 to January 2006.

The Investor Group developed six overarching Principles, underpinned by 35 possible actions, to guide institutional investors and asset managers in practicing responsible investment. The Principles include integrating ESG issues into investment analysis, practicing active ownership and proxy voting, seeking ESG disclosure by companies, promoting uptake of the Principles, collaborating with other signatories, and reporting on progress of implementation of the Principles.

The Principles target "large, diversified institutional investors that operate within a traditional fiduciary framework." The Principles specifically require signatories to apply the Principles across the entire organization, preventing organizations from claiming signatory status based on limited SRI fund offerings or isolated ESG practices. This provision requires organizations to embrace SRI strategies across the board, though the Principles promote shareowner engagement and active voting while discouraging exclusionary screening based on ESG considerations.

"Through their focus on engagement, not divestment, the Principles represent a major milestone in our efforts to root global business in universal values to achieve a more sustainable global economy," said Georg Kell, executive head of the Global Compact.

Signatories fall into three categories: asset owners, investment managers, and professional service partners. Asset owners include some of the largest state pension funds, such as the California Public Employees Retirement System (CalPERS), the New York State and Local Retirement Systems, and the Connecticut Retirement Plans and Trust Funds (CRPTF). Other asset owners include the Universities Superannuation Scheme (USS) in the U.K., the Caisse des Depots et Consignations (CDC) and the Fonds de Reserve pour les Retraites (FRR) in France, and the Canada Pension Plan Investment Board.

"The United Nations, for its part, must practice what it preaches," said Secretary-General Annan. "Therefore, I am also pleased to announce that the U.N. Joint Staff Pension Fund, with nearly \$30 billion in assets, is signing on to these Principles."

The U.N. had come under criticism for promoting responsible investment while not enacting it with its own investments, so its signing of the Principles adds a significant imprimatur to the initiative.

"We at Innovest are delighted to see the adoption of the U.N. Principles by so many large and influential investors -- we're optimistic that this represents a significant sea-change, and will enrich the mainstream investment process considerably," said Matthew Kiernan, chief executive of Innovest Strategic Value Advisors. Kiernan has been critical of U.N. inaction on implementing responsible investment for its own pension fund in the past. "Inevitably, however, as with any undertaking of this scope, the devil will be in the details of how each signatory actually breathes real life into the Principles in its investment practices."

The Principles address this potential shortcoming, though may fall short of solving it.

"There are no legal or regulatory sanctions associated with the Principles [as they] are designed to be voluntary and aspirational," according to the Principles website. "There may be reputational risks associated with signing up and then failing to take any action, but the commitments are, for most signatories, a work in progress and a direction to head in rather than a prescriptive checklist with which to comply."

"The initial focus is on innovation, collaboration and learning by doing," the website continues. "As the project develops over time, the Board will consider how signatories can monitor and report on progress."

The launch of the Principles represents their first phase, with the second phase focused on promoting adoption of the Principles by additional investors, gathering resources to support implementation, and facilitating collaboration among signatories.

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