

## Advisory Council Chair Cover Note

This cover note is to be read in conjunction with:

- [PRI Governance Review – Draft Scope](#)
- [PRI Governance Review - Recommendations](#)

### PRI governance review aims and principles

The aim of this review is to assess what governance structure the PRI should adopt to best facilitate the fulfilment of its Mission. In doing so, we must balance the interests of different signatories and ensure that decision making processes about the PRI's mission, direction, strategy, finances and operations are transparent, accountable to signatories, efficient and fit-for-purpose. The governance structure and processes determine – internally and externally – how effectively the organisation operates, and how it serves the needs of signatories and stakeholders.

Six principles have guided us in the review:

- **Mission.** The governance structure should facilitate the engagement of all signatories in the PRI's mission to advance the Principles and the development of a more sustainable global financial system for the benefit of society.
- **Simplicity.** The governance structure must be straightforward to administer and easy to describe, with clearly articulated roles and responsibilities.
- **Transparency.** The requirements and process for communicating governing body decisions to signatories and stakeholders must be transparent.
- **Accountability.** Lines of responsibility must be clear and those within the governance structure must be answerable to signatories.
- **Practicality.** The governance structure must meet the practical requirements of the organisation.
- **Representation.** The governance structure must retain an asset owner-majority and must include all categories of signatory.

### PRI governance context

In early 2005, the then UN Secretary-General, Kofi Annan, invited a group of the world's largest institutional investors to join a process to develop the Principles for Responsible Investment. A 20-person Investor Group drawn from institutions in 12 countries was supported by a 70-person group of experts from the investment industry, intergovernmental organisations and civil society. Since the Principles were launched in April 2006 at the New York Stock Exchange, when there were 76 founding signatories, the PRI has grown rapidly to today over 1,200 signatories, of all sizes and types. As a testament to this growth, in 2007, 106 signatories reported on their

implementation of the Principles, whereas in 2014, 814 signatories reported, publicly disclosing for the first time how they are managing their investments in line with the Principles. Within eight years of being established, the PRI has grown to be *the* global initiative driving the implementation of responsible investment.

During this growth the PRI Initiative has undergone a number of changes. Between 2007 and 2010, the PRI's financial and legal affairs were run from the Foundation for the Global Compact. Due to signatory growth and increased operational activity, the PRI Association, a company limited by guarantee (a not-for-profit), was established in 2010 with a governance structure made up of an asset owner-majority Advisory Council directly elected by signatories, an Association composed of the asset owner members of the Advisory Council, and an Association-appointed fiduciary Board of Directors. This governance structure was established to enshrine asset owner predominance and increase operational effectiveness, whilst including a high level of operational oversight and management support from the Board for an organisation that was still very young. The PRI also transitioned from voluntary to mandatory fees over this period, improving financial stability and increasing operational capacity within the PRI Association.

As the PRI grows, signatories are demanding more transparency, accountability and simplicity within the PRI governance structure. I fully concur with this view. At the same time, the elements that have contributed to the PRIs strong growth and success must be preserved and strengthened.

The predominance of asset owners and the UN partnership has remained integral to the success and Mission of the PRI since its foundation. The PRI was established as an asset owner led organisation, from the launch of the Principles, and asset owners continue to work with investment managers and service providers to implement the Principles and responsible investment practices. The power and usefulness of the PRI is amplified when all signatories - asset owners and non-asset owners - work together in pursuit of responsible investment. But the PRI will not work at all unless it stays relevant and useful to asset owners.

This is why the review has not considered whether asset owners should remain pre-dominant in the PRI's governance structure, nor whether non-asset owner signatories (investment managers and professional service providers) should be excluded from being signatories or from being involved in PRI governance. Having an elected, asset owner led peak governance body that is geographically representative and includes all signatory types, and representing the views of signatories, is a practical and effective means of delegation from a c.1260 strong signatory base that is growing, providing the remit is well defined and the body is accountable to the signatories. The review has considered the *extent* to which asset owners should predominate and *how* this predominance is best enshrined and exercised to ensure representation for other categories of signatory.

The PRI is an investor initiative in partnership with the United Nations Environment Programme (UNEP) and the United Nations Global Compact (UNGC). The preamble to the Principles specifically mentions the wider remit of the PRI initiative:

*As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to*

*varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society.*

The PRI continues to work in close collaboration with our UN partners (for example, the UNEP FI Property Working Group; the UN Global Compact's ESG Investor Briefings; the Sustainable Stock Exchanges Initiative undertaken in partnership with the UNGC, UNEP FI, and UNCTAD; the UNISDR RISE initiative; the UN Caring for Climate Program; as well as contributing to the UN Secretary General's Climate Change Summit and the UN Climate talks in Paris in 2015). Under the current constitution, the UN is integral to the PRI and the UN will continue to be integral in any revised PRI governance structure.

## Ten recommendations

The first phase of the review was a fact-finding exercise. The independent advisor undertook desk-research; performed a peer review; considered feedback from the signatory survey and governance scope; reviewed minutes from meetings; conducted a limited number of focused interviews; and carried out a legal review.

Based on this work, the independent review put forward ten recommendations for signatory consultation:

### Structure

1. **Single Governing Body:** The dual Council / Board structure is merged into a single governing body, the PRI Board.
2. **Advisory role of the UN:** The UNGC and UNEP will continue to attend the PRI Board as senior advisors on a permanent basis.
3. **Independent Chair:** The Chair will not represent any of the signatory groups and will be an independent position.
4. **Fewer standing committees:** Board committees should be formed to facilitate governance and fiduciary responsibilities. They should be kept to a minimum and the seats will be restricted to Board members.
5. **Unambiguous control:** All Board members, with the exception of the UN, but including the Chair, will be the sole 'Members' of the Company.

### Process and Performance

6. **Clear responsibilities:** Clear terms of reference, lines of accountability and delegated authorities should be defined for the Chair, the Board of Directors, the committees and the Managing Director.
7. **Signatory involvement in governance:** Signatories will have certain matters reserved for their endorsement.
8. **Board member continuity:** Board members should provide continuity in governing the PRI and be accountable to signatories. The role of Alternates will be removed.
9. **Maintaining the skill level of the Board:** The current eligibility requirement for the PRI Board, i.e. those holding current CEO / CIO / Board director / trustee positions, will be extended to include retired or ex-CEOs / CIOs / Board directors / trustees.

10. **Formal Board reviews:** The Board will carry out a formal review process on an annual basis, evaluating both Board function, committee structure and individual member performance.

In the independent report every recommendation is supported by high level details and rationale, guided by five principles of good governance identified by Carnstone.

## The Chair's comments to the recommendations

The Advisory Council considered the report from Carnstone and its recommendations carefully at its meeting on 2 July. Although there were differing views on some issues, the Advisory Council was in broad agreement with the recommendations for the changes to the PRI governance structure. During the 2 July meeting we focused our discussion on the details of the recommendations. I would like to take this opportunity to highlight to signatories implications and questions around those details and ask signatories to reflect on these within their feedback during the forthcoming consultation period. The reflections and specific questions from the Advisory Council to signatories will also be included and clearly marked within the online questionnaire.

### Recommendation 1: Single governing body

There was a consensus that a single governing body is the most effective governance model for the PRI going forward. In its discussions, the Advisory Council focused on term limits, the size of the governing body, and means to achieve diversity.

- The **size of the governing body**, the Board, has to be viewed in totality, taking into consideration the balance of signatory category representation and diversity, including geographic representation. The proposed structure within the report maintains the same signatory *balance* on the new Board as the current Advisory Council, of (9) asset owners to (4) non-asset owners, elected by the respective signatory categories, in addition to the Chair and the two UN representatives. Recommendation one states that the Board can function well with the current number of members but there is an argument for reducing the size of the governing body to increase effective decision making. At the meeting, we discussed an alternative proposal, with a total of 7 asset owners and 3 non-asset owners, in addition to the Chair and the two UN representatives. In both scenarios there would still be a substantial asset owner majority. We see merit in both proposals and will make a final assessment based on feedback from the signatories.
- The new Board does require **diversity**, the question is how to achieve that diversity. The PRI seeks a mix of relevant skills, competence, and diversity of perspectives which may include diversity of geographical origin, language, culture and gender. The means to maintaining a geographic requirement are not prescribed within the recommendations. The PRI is a global organisation and the concern is that by removing mandated geographic positions there will not be a diverse geographic representation. However the current rules prescribe a rigid geographic diversity that can limit the range of candidates. The Advisory Council is seeking feedback from signatories on the importance of a geographically diverse PRI Board. If important, how does the PRI try to ensure that diversity:
  - mandated geographic region positions within the signatory categories (the current rules); or
  - having quotas but only distinguishing between developed and emerging market positions; or
  - no fixed quotas at the signatory category level but a minimum requirement for emerging

- market candidates within the election rules; or
  - no mandated geographic requirements but a call for nominations for a desired skillset or regional expertise as deemed required by the Chair / nominations committee; or
  - another mechanism.
- The proposal of a limit of two terms is challenged by the Advisory Council. A three term limit is considered appropriate to balance the need for both continuity and Board renewal, taking into consideration Board churn due to changes of role and the fact that the proposed Board is scheduled to meet three to four times per year. The Advisory Council is seeking signatory opinions on this before making a final determination.

### **Recommendation 2: Advisory role of the UN**

The UN has been widely consulted throughout the governance review and are in agreement with the proposed rule changes and advisory status on the board. The UN partners are important to the PRI and the Advisory Council agrees with the recommendation.

### **Recommendation 3: Independent Chair**

The Advisory Council supports the recommendation of an independent chair appointed by the elected Board, who does not represent any particular signatory category, but represents all signatories and acts for the benefit of the PRI initiative as a whole. We discussed an alternative option, whereby the Chair was nominated by the Board but elected by the signatories. There was broad agreement that this option has several serious drawbacks. If the election process is to have any meaning, the rules must also specify what would happen if signatories reject the Chair nominated by the Board. It is clear that this would imply a possibly long period of leadership vacuum – at great cost to the PRI. There is also the issue of removal of a Chair who is not functioning properly. It is reasonable to have symmetry in appointment and removal processes. The Board is in the best position to judge the performance of the Chair and should also have the possibility of removing him / her. This process would in practise be difficult if the Chair was elected by signatories and could only be removed by a signatory vote. At the same time, signatories retain the possibility to put forward resolutions on any issue – including removal of the Chair – so there would be a formal way of expressing lack of confidence in the Chair from signatories also when he / she is appointed by the Board.

The *in addition* recommendation to appoint a ‘*lead director*’, among the Board members, is a positive addition, to act as a contact if there are issues with the Chair and to assume the Chair’s responsibilities at meetings if the Chair is unavailable.

At the September SGM there will be further details for signatories on the Chair role and associated processes: the search and nomination process for a new Chair; the structure of a systematic Chair review process; and the process if there are issues with the Chair and a clear roadmap for a resolution.

### **Recommendation 4: Fewer standing committees**

The PRI Board should consider the appropriate number, remit and composition of the committees to ensure that the fiduciary Board is fit for purpose and undertaking all of its responsibilities in a diligent manner. As part of an effective delegation from the signatory base to the PRI Board, the

PRI Board should decide to change or amend committees as it sees necessary. The PRI Board should report to signatories on committee structure and composition, work plans and activities undertaken more thoroughly and transparently going forward.

#### **Recommendation 5: Unambiguous control**

This is a sensible proposal, supported by the Advisory Council, for reasons of effectiveness and more direct accountability. While we would disagree that there is formal “ambiguity” in the present setup, there is a consensus on the Advisory Council that the current structure can be overly complex in practice and historically has caused signatory confusion about roles and responsibilities.

In the proposed PRI Board all directors / Members act as individuals in a fiduciary role, are elected by one signatory category and represent the best interests of all the signatories, the totality of the PRI initiative, advancing the Principles and PRI mission. Members positions of the Company would include all Board members, not just asset owners as it is now.

There was strong support for the PRI being an asset owner led organisations in the recent signatory survey. The Advisory Council’s view is that the asset owner majority in the proposed governance structure, with the balance of 9 asset owners and 4 non-asset owners, retains the asset owner led focus of the PRI. However, as noted within the report appendix, special resolutions, that require a majority of not less than 75% of Members, would have to be passed by a combination of asset owners and non-asset owners, not just asset owners as it is within the current governance structure.

One central question for signatory consideration is whether the proposed structure with one governing body, a PRI Board, with strategic *and* fiduciary responsibilities would prevent candidates from signatory organisations from serving on the PRI Board. The PRI will be reaching out to different types of signatories in different geographic jurisdictions to test the legal advice received that there are no legal barriers to potential signatory candidates serving on the proposed PRI Board.

#### **Recommendation 6: Clear responsibilities**

Creating an effective PRI Board with clear responsibilities is crucial. The terms of reference, lines of accountability and delegated authorities need to be drafted and made available before signatories can have their final say on the proposed reforms.

#### **Recommendation 7: Signatory involvement in governance**

All signatories should remain associate members. The Advisory Council would like to hear from signatories if there are any barriers in their jurisdiction or organisation be being associate members. The PRI does not want to have dual classes of signatories.

Proposed matters reserved for endorsement by signatories include: election of the individual Board members for three year terms and approval of any changes to the mission or the Principles. Resolutions are also an important means for signatories to raise issues for the attention of the Board and signatory vote. The PRI needs to be responsive to signatories and



resolutions are an important mechanism.

The PRI currently has c.1260 signatories and growing. The proposed governance structure needs to be fit for purpose both now and going forward and a well-functioning institution should have real delegation from the signatory base to the Board and management. The budget, fees, committees (composition and remit) are for the decision of the PRI Board. There should be in depth signatory consultation processes around governance, strategy, long-term funding and significant changes to the fee structure, but the PRI Board should retain the right to the ultimate decision, consistent with its fiduciary role. There cannot be a scenario of binding votes for an ambitious work agenda and binding votes for inappropriate funding levels to resource such an ambitious agenda. The current governance consultation is an example of how the PRI would consult with signatories going forward.

As part of the effective delegation the PRI should report to signatories on its activities more thoroughly and transparently. In the 2013 Annual Report the PRI provided increased granularity around the budget details, the actions of the Advisory Council and committees and this trend will continue in the 2014 Annual Report.

#### **Recommendation 8: Board member continuity**

PRI Board members need to be accountable for their decisions and the PRI should publish the Board meeting attendance. All Board members would be expected to attend every *in person* Board meeting, with a minimum requirement to attend two out of the three *in person* meetings per year. The ability for Board members to be able to transfer their votes to the Chair or another Board member of the same signatory category by proxy is an important mechanism to try to ensure that every voice on the PRI Board is heard on important decisions.

Advisors can perform a valuable function for Board members. The proposed three or four in person meetings per year is a large time and work commitment and advisors can assist. The PRI also needs to ensure that language barriers, that advisors can mitigate, do not inhibit a diverse Board. On balance, most Advisory Council representatives agreed that advisors should not have the right to vote.

#### **Recommendation 9: Maintaining skill levels of the Board**

The Advisory Council considered that CEO / CIO / Board director / trustee position requirement was still relevant to guide the strategic success of the initiative and still important to have that high level C-suite engagement and champions to help mainstream responsible investment.

*Ex-CIO / CIO / Board director / trustee position candidates* have the applicable skillsets, experience, networks and time and could be a good addition to the pool of candidates. These candidates would still need to represent a signatory, be seconded by another signatory of the same category and voted for by the same certain signatory category. The Advisory Council is supportive of this suggestion and would like to get signatory feedback on the principle of proposal, rather than the technicalities of the surrounding rules.

## Recommendation 10: Formal Board reviews

This is a positive recommendation welcomed by the Advisory Council. As stated within the proposal, it is critical that any new single governance body is effective and assessed by an annual review. The ideal would be to have annual independent assessments but the review process needs to be appropriate for the size and resources of the PRI Association. The Board review would be by self-assessment, with the aim of an independent assessment once every three years.

### Further governance developments

Some elements of PRI governance are beyond this phase of the governance review, dependent upon signatory feedback, or beyond the scope of the current review.

- **Election rules.** The election rules, dependent upon decisions on size, term and representation, will be developed following the proposals in September.
- **Governance of formal PRI Networks and the PRI voice.** These will be considered as part of the strategy review process.
- **Transition.** The review and recommendations has not considered the details of the transition from the current dual structure to the proposed single governing body, the PRI Board. If there is a broad approval from the signatory base of the single governing body, the main elements of an implementation and transition plan will be proposed at the SGM. The transition period and arrangements need to be fair, effective and efficiently implemented on a timely basis.
- **The role of management.** There also needs to be real delegation from the proposed PRI Board to the management and the role of the PRI Secretariat is largely absent from the report and recommendations. The PRI has more management capacity and expertise compared to five years ago, when the current governance structure was established. The terminology currently used is misleading, creating the impression that the Board is running the day-to-day organisation with the assistance of the *Secretariat*. In fact a *PRI Executive* runs the organisation under the guidance and supervision of the Advisory Council and Board, and from September the PRI will start using this terminology. The PRI Executive's function is still *supporting* and *galvanising* signatories to be better responsible investors and the proposal is that it reports to the PRI Board.

### Consultation plan

The consultation phase will start in mid-July and signatories have until 29 August to provide feedback on the governance recommendations. There are two key objectives of the consultation:

- **Ensuring Inclusion:** Enabling all signatories to have their say on the recommendations, regardless of their geographical location and appetite for engagement; and
- **Gathering Structured Feedback:** The value of the feedback received can only be realised if it is compiled and analysed in a structured manner.

There will be a range of channels to provide feedback: an online form; phone clinics; email; webinars; and signatory workshops. Submitting your comments through multiple channels will not lend additional weight to your views, but many of the consultation activities, e.g. webinars and in person meetings, will enable you to clarify details and form a better view of the rationale behind the recommendations before making your submission. You are welcome to submit views as an



individual organisation or as part of a group of signatories. For the consultation timeline and details on how to provide feedback see below and the [PRI Governance Review](#) page of the PRI website. I encourage all signatories to have their say on the review and initial recommendations.

#### *Online form*

The PRI encourages all signatories to provide structured feedback on the recommendations through the [online questionnaire](#). If you choose to make your written feedback publicly available it will be shared on the PRI website at the end of the consultation period. Feedback given with no permission to be made public will be only be disclosed in an aggregated, anonymised manner. Feedback will be disclosed in aggregate form to signatories, after PRI in Person in September. All responses will be collected in a database managed by the independent advisor. The online form submission window is from **16 July to 29 August**.

Each recommendation is accompanied by two questions: one soliciting quantifiable feedback enabling a statistical understanding of signatories' views, which in turn can be broken down by signatory category; and another one soliciting qualitative feedback, for example allowing respondents to elaborate on why they disagree / agree with a recommendation and potentially sharing comments on alternative options or implementation advice.

In addition, the recommendations will be accompanied by a qualifying statement, explaining why the particular recommendation was made and, where applicable, how it relates to concerns raised among PRI's stakeholders and existing good practice elsewhere.

The template outlined above is for the online consultation form, but insofar as possible the same structure will be used for webinars and in-person meetings in order to produce structured feedback.

#### *Webinars*

The webinars will be one hour sessions, as a minimum, where signatories will be taken through the recommendations and asked for feedback using the template above. Depending on the number of participants, feedback may be collected directly over the phone if numbers are low (<5) or, if numbers are higher, they will be asked to have the online form open next to them and input their views individually during or after the webinar. The webinars will be led by Carnstone.

Planned webinars:

- 29 July 08.00-09.00 (BST) and 17.00-18.00 (BST)
- 26 August 08.00-09.00 (BST) and 17.00-18.00 (BST)

To sign up for these webinars go to the [PRI Governance Review](#) page of the PRI website.

#### *Network / regional workshops*

Network / regional workshops will be in person meetings, typically arranged on the back of already planned gatherings, hence some of the meetings taking place either side of the official consultation window. The consultation session will run for an hour, as a minimum, and will be structured around the online form. As is the case with webinars, participants may be asked for

feedback directly which will then be aggregated and submitted through the online form. Or, if the number of participants is >5, they may be asked to have the online form open next to them and provide feedback on an individual basis. The workshops will be run by the PRI Managing Director, Advisory Council representatives or the independent advisor and conveners will be fully briefed by the independent advisor in advance.

Planned workshops / in person events:

- Melbourne (8 July)
- Sydney (16 July)
- London (17 July)
- Paris (17 July)
- New York (31 July)
- San Francisco (August, TBC)
- Rio de Janeiro (7 August)
- London (late August / early September, TBC)
- Montreal (4 September)
- Copenhagen (8 September)
- Oslo (9 September)

To sign up for these workshops go to the [PRI Governance Review](#) page of the PRI website.

#### *Email*

Throughout the consultation phase, signatories will be able to email through questions and concerns, both regarding the process as a whole and relating to technical issues with the feedback channels. Questions submitted by email will go to the independent advisor. The email address will be [consultation@arnstone.com](mailto:consultation@arnstone.com). Email window: 16 July – 5 September

#### *Phone clinics*

Lastly, signatories can submit feedback and ask questions by phone. Signatories wishing to you this option can book a 30-minute slot on one of two dates in July and August. Bookings will take place using [consultation@arnstone.com](mailto:consultation@arnstone.com). The phone will be manned by the independent advisor. More dates can be added if it proves a popular option.

Planned clinics: 24 July and 22 August, bookable 30-minute slots between 08.00-20.00 (BST).

Throughout the consultation period, you can submit views and ask questions about the process by contacting [consultation@arnstone.com](mailto:consultation@arnstone.com). As always, you can also contact the PRI on [info@unpri.org](mailto:info@unpri.org) with general signatory enquiries.

## **Presentation and implementation**

After the consultation period has closed on 29 August, I will review signatory feedback with the Advisory Council's Governance Committee, PRI Executive team and the independent advisor before making a final recommendation about any changes to the PRI's governance structure.

The structure will be presented to the Advisory Council at their next meeting on 22 September and to signatories at the **Signatory General Meeting at PRI in Person, in Montreal, on 24 September**. For signatories that cannot attend the SGM in person, the session will be webcast and **two webinars have been scheduled for 30 September**. After these presentations there will be opportunities to provide further feedback.

From October, the PRI will focus on communicating the proposed governance structure, the reasons for the proposed changes and the implementation plan, plus drafting any necessary amendments to the Articles. Under the current rules, any changes to PRI Association's Articles and / or the Administrative Rules relating to the Advisory Council and signatories require the support of asset owner-elected Advisory Council representatives and asset owner signatories:

- PRI Association's Articles of Association may only be amended by a special resolution of PRI Association's members (being the asset owner members of the Advisory Council and the Chair of the Advisory Council), as required by the UK Companies Act 2006, and subject to fulfilment of the additional conditions imposed by Article 42.1 of the Articles, if applicable, as mentioned in the next sub-paragraph.
- By virtue of Article 42.1, changes to the Articles affecting the composition of the Advisory Council (Article 23.3) and the Principles (as set out in the Schedule to the Articles) may only be made (i) with the consent of a simple majority of signatories who are asset owners voting on the amendment in question, such consent to be given by way of an electronic poll held in accordance with the rules and byelaws made pursuant to Article 41, and (ii) in accordance with any other requirements specified in those rules and byelaws.
- The Administrative Rules Relating to the Advisory Council and signatories may only be amended (i) by a special resolution of the PRI Association members, or (ii) by a resolution of the Advisory Council passed by a majority of the asset owner elected members, the Chair of the Advisory Council and the UN members of the Advisory Council, taken together as one group. (Article 41.2 of the Articles and Rule 9 of the Administrative Rules.)

While asset owner signatories within the current rules have the formal voting rights, in parallel with the asset owner vote and as part of the presentation and implementation phase, the PRI will have a process to gather in a structured way the opinion of non-asset owners. If a majority of non-asset owners express significant discontent with the proposed governance revisions, the PRI will reconsider further and seek to address, within reason, the non-asset owner concerns.