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Dear Mr Koufou

Consultation on changes to the Investment Regulations following the Law Commission's Report 'Fiduciary Duties of Investment Intermediaries'

Legal & General Investment Management (LGIM) is one of the largest investors in the UK with £499billion of assets under management (as at 31 December 2014). We manage assets for more than 3,000 clients making us one of the largest asset managers for pension funds in the UK.

We welcome the review by the Department for Work and Pensions (DWP) on the changes to Investment Regulations following the Law Commissions Report on Fiduciary Duties discussing the difference between financial and non-financial factors and the role that a stewardship can play when taking decisions about investments.

Our submission to the questions in the consultation follows this letter. We are available to discuss any of the issues highlighted in this submission.

Yours sincerely

Sacha Sadan
Director of Corporate Governance

Response to Questions

(1) How could regulation 2(3)(b) of the Investment Regulations be amended so that it more clearly reflects the distinction between financial and non-financial factors.

Firstly, whilst we appreciate the Law Commission is trying to distinguish between financial and ESG issues, we believe that the term ‘non-financial factors’ does not describe the issues being discussed. This is because it is clear that ESG issues are financially material and therefore should not be separated from what is deemed to be financial factors.

We believe the term ‘non-traditional financial factors’ is a more appropriate label to describe ESG issues. This term provides better guidance and understanding for trustees to consider other financial issues that are not within their traditional scope.

Secondly, at LGIM we believe that companies that demonstrate good ESG practices and have sustainable business policies will generate superior financial benefits for our clients. We do not see this as simply an ‘add on’ service. We are committed to providing long term investment solutions for our clients through investment strategies such as index-tracking and liability driven investments.

However, many long term issues are not easily quantifiable. In addition, due to confusion around the law and duties of trustees in examining non-traditional financial factors, it is difficult to examine these issues in a consistent and transparent manner.

Therefore, we believe that the Investment Regulations should clarify the role of trustees when taking in to account ESG and non-traditional financial issues on a permissive basis. This flexibility in the law will provide more comfort to Trustees to discuss these factors more openly (including with their advisors) without a rigid codification in law on their fiduciary duties.

(2) Do you agree that amending the Investment Regulations to require trustees to comply with the current requirements in the Stewardship Code or explain why they have not done so, is the most appropriate way to implement the Law Commission’s recommendation? If not, what approach would be more appropriate to encourage trustees to consider their approach to stewardship?

Whilst LGIM is supportive and is a signatory of the UK Stewardship Code, we do not believe that it goes far enough in encouraging Trustees to promote the long-term success of companies in which they invest.

We believe the Investment Regulations should require trustees to have a more robust policy on stewardship and disclose how these responsibilities are being discharged. This may also involve different parts of the investment chain (e.g. investment consultants) to assess investment managers during the selection process and judge which manager is best to exercise this policy.

The policy may define stewardship objectives such as encouraging their managers to engage collaboratively with other investors on companies or assess long term socio-economic trends that impacts on their clients’ portfolio.

Therefore, whilst the ‘comply or explain’ approach in the UK Stewardship Code provides one way for Trustees to consider their approach to stewardship; we would like to see a stronger requirement in the Investment Regulations for the development of a robust policy on this issue.

(3) What steps would trustees need to take to comply with any amendments to the Investment Regulations, as set out Chapter 2? What, if any, costs would be involved in meeting any new requirements?

Any amendments to Investment Regulations may take time to be embedded in to policies on investment and stewardship. Therefore, sufficient time should be given to pension funds to ensure that these are discussed appropriately and acted upon without being burdensome.

In addition, any costs of implementation should be judged against the opportunity cost of not implementing appropriate regulatory frameworks over the long term. At LGIM, it is our responsibility is to protect the interest of our clients' assets. Examining material impacts of ESG on a company's bottom line is part of this role. Our approach, which combines financial analysis with ESG is applied across all asset classes and is part of our investment philosophy.