

SCHEME ADVISORY BOARD COMMENTARY ON THE UPDATED LEGAL OPINION FROM NIGEL GIFFIN KC DATED 13 JANUARY 2025

Introduction

1. The full updated legal opinion can be found on the [Legal Opinions and Summaries page](#) of the Board's website.
2. The advice is a substantial document at 36 pages in length and expands on the previous advice in several areas, for example:
 - In clarifying how the fiduciary duty owed to employers differs from that owed to scheme members (paragraph 19)
 - How far administering authorities are required to consider environmental, social and governance (ESG) factors in decision making, and state this within the Investment Strategy Statement (ISS) (paragraph 37)
 - A reminder of the need for administering authorities to apply the policies set out in their ISS when making investment decisions, and the need to keep the ISS up to date (paragraphs 43-44)
 - Some discussion of the implications for ESG policy where administering authorities have devolved the implementation of their investment strategy to pools, while confirming that they may not be able to delegate the strategy-setting duty itself to the pool company (paragraphs 46-51)
 - The requirements around consulting members and how their views can be considered when deciding how and which ESG factors are applied (paragraphs 38-42 and 56-62).
3. The Secretariat have been asked to produce the following note which summarises their understanding of the main content of the opinion.
4. It represents the views of the Secretariat based on their current understanding of the law and policy. It should not be treated as a complete and authoritative statement of the law, and readers may wish, or will need, to take their own legal advice on the interpretation of any particular piece of legislation quoted. No responsibility whatsoever will be assumed by the Board or the Board Secretariat for any direct or consequential loss, financial or otherwise, damage or inconvenience, or any other obligation or liability incurred by readers relying on information contained in this note.

Main conclusions

5. The main conclusions of the [previous opinion](#) are reaffirmed in the revised opinion:
 - (i) An administering authority, although not strictly a trustee, owes fiduciary duties both to scheme employers and to scheme members
 - (ii) Those duties are broadly similar to those that arise as a matter of public law.

- (iii) "ESG" issues or non-financial factors can be taken into account when making investment decisions, where to do so would not involve significant risk of financial detriment to the fund and where there is good reason to think that scheme members would support the decision.
 - (iv) An administering authority must not prefer its own particular interests to those of other scheme employers.
6. The updated advice takes account of:
- (i) The Law Commission report [Fiduciary Duties of Investment Intermediaries](#) (Law Com No 350, 2014)
 - (ii) the Supreme Court's [decision](#) in a challenge brought by the Palestine Solidarity Campaign against parts of the content of [investment guidance](#) issued by the Secretary of State ("the PSC case"),
- both of which reached similar conclusions to the initial advice.
7. The revised opinion also considers the LGPS Investment Regulations 2016 and the associated statutory guidance "Local Government Pension Scheme – Guidance on Preparing and Maintaining an Investment Strategy Statement". These were made after the previous opinion was issued.
8. The Supreme Court's conclusion in *PSC* held that the Secretary of State (SoS) was not entitled to use guidance to usurp the responsible investment role of the administering authority. The statutory power to give guidance could be used to address topics such as, for example, what factors the administering authority should take into account when formulating its policy but could not dictate the substantive conclusions which the authority should reach or prevent the authority from acting upon those conclusions.
9. However, after the *PSC* case was decided the Public Service Pensions Act 2013 has been amended to broaden the power of the SoS to make such scheme regulations as she considers appropriate in the area below (new text underlined below):
- "The administration and management of the scheme, including – (a) the giving of guidance or directions by the responsible authority [i.e. the Secretary of State, in the case of the LGPS] to the scheme manager [i.e. the administering authority] including guidance or directions on investment decisions which it is not proper for the scheme manager to make in light of UK foreign and defense policy".*
10. In the light of this amendment, it is very probable that the SoS could now lawfully issue new guidance to achieve the same effect as that challenged in *PSC*. However, in doing so she may need to change the Investment Regulations first.
11. As a fiduciary, the administering authority should not pursue its own views of what was or was not desirable or acceptable as an investment from an ESG perspective. It had to give effect to the wishes of scheme members about how

their pension funds should be invested, and consistent with a proper "pensions purpose".

12. As it was endorsed in *PSC*, the Law Commission approach to non-financial considerations can be regarded both as an authoritative statement of the general law and applicable to investment decisions made by LGPS administering authorities.
13. Lord Wilson said in *PSC* that LGPS funds represent "their [i.e. the members'] money". The money in an LGPS fund is not the members' money in a literal or legal sense. It is a fund held for the specific purpose of paying pension benefits to members and scheme employers also have a legitimate interest in the financial health of the fund, in particular, the contribution rates they are required to pay (or, on exit whether there is a surplus or a deficit). The views of scheme employers are relevant to the potential financial implications of ESG policies.
14. Central government has, via the Chancellor of the Exchequer's 2024 Mansion House speech, stated an intention to introduce a Pension Schemes Bill in 2025. The Bill could be a vehicle for amendments to primary legislation and could bring about such changes in administering authorities' investment duties as the government considers appropriate.
15. The [Fit for the Future consultation](#) proposes a new model of pooling from March 2026 (although one of the consultation questions invites comments on the viability of this timescale). The indicative timetable for pools to submit proposals for meeting the new requirements was by 1 March 2025.
16. The *PSC* judgment raises a considerable question as to whether it is currently lawful for pooling to be made mandatory. However, the government could mandate such requirements in the new Bill. Proposals in regulations could in principle be challenged if they were outside the powers conferred by the new legislation, or potentially on other public law grounds. However, until the detail of the Bill is known it is impossible to say whether there would be grounds for any such challenge.

What should administering authorities do about non-financial factors?

17. The revised opinion considers how far a clear dividing line can be drawn between financial and non-financial factors. It also provides advice on how an administering authority should apply the Law Commission criteria, what is meant by "significant risk of financial detriment" (the "financial criterion"), and by scheme member support (the "member support criterion"). It also looks at whether an administering authority is *obliged* to ask itself whether any, or any particular, non-financial factors should be considered
18. In his revised opinion, Nigel Giffin KC concludes that:
 - (i) An investment strategy ought to say something about ESG considerations, because the authority is required to state its policy on those matters. It could however state that the current policy is not to take any account of such considerations when making investment decisions. There are many other possibilities.

- (ii) All investment decisions should be consistent with the investment strategy for the time being in force. If the investment strategy has not identified how ESG will be considered, then it should not normally be taken into account without the strategy first being reviewed and amended.
 - (iii) When the authority comes to formulate or review its investment strategy (at least once every three years) it should give specific thought to what the policy on non-financial factors ought to be.
19. Funds should consult scheme members about the policy on the use of non-financial factors. That does not necessarily mean consulting all the individual members. Consultation could be directed to members generally or limited to representative bodies such as trade unions. It could be part of consultation on the overall investment strategy or done separately.
 20. In consulting, it would probably be helpful to consultees to be reminded of the existing policy and to explain the legal test for it being permissible to take account of such factors. Beyond that, some authorities might prefer simply to ask in an open-ended way for views on what the policy on using such factors should be; others might specifically canvass high level views on topical issues thought to be serious potential candidates for being made the subject of a policy; others might make specific proposals, and provide information about the reasons for them, or the authority's current assessment of their likely financial impact. Consultation could be conducted online.
 21. Employer interests are financial, so their views on the merits of a particular approach to non-financial factors are of only marginal significance, and an administering authority is not obliged to solicit such views.
 22. The triennial review of the investment strategy is a logical and convenient point at which to assess whether scheme member support exists for a particular policy. The authority must be open to reviewing the policy before the next 3-year deadline, but it will not normally be under any positive legal obligation to consider policy changes outside of its triennial cycle.
 23. Exceptional cases where it might be necessary to think in more detail about a request to review the policy early could include ones where a particular issue has only newly emerged as a significant concern, and/or where there is good evidence of a high level of member demand for action on a particular issue, or that the facts have changed very materially since the issue was last considered. Ultimately it is for the administering authority to judge whether early review of the investment strategy is appropriate.
 24. Although the function of making and reviewing the investment strategy is one that could in principle be delegated in the same way as other non-executive functions, not all the current investment pools would be permissible delegates (those structured as joint committees might be).
 25. If the Fit for the Future proposals are implemented, then the separation between formulation and implementation of the responsible investment strategy may

become a legal requirement. That will make the formulation of the strategy especially important.

26. The investment strategy might need, for example, to give a clear definition of the type of investments which are or are not to be made; where the policy is a negative one (i.e. not to invest in some specified category), whether it is calling for disinvestment from existing investments (and on what timescale, and within what parameters as to the disposal price).

Applying the financial criterion

27. When considering the “positive social impact” of an investment decision, the Law Commission report is clear that in making such decisions there cannot be a “risk of significant financial detriment” to the fund.
28. The “significant financial detriment” phrase seems to have been first used in this context by Sir Donald Nicholls V-C in *Harries v Church Commissioners for England* [1992] 1 WLR 1241. The underlying idea is that an administering authority ought not to be pursuing a policy which, for non-financial reasons, creates a realistic possibility of the fund suffering financial detriment which is material in the context of the fund’s size and nature. The likelihood of the financial disadvantage materialising, and its potential scale of impact if it does, are relevant to whether the policy is one which it is legitimate to adopt.
29. The advice emphasises that the administering authority does not balance the risk of significant financial detriment against the perceived strength of member support for a particular investment policy. Such risks should simply not be undertaken, on non-financial grounds, however much members might support it. It will normally be appropriate to obtain professional advice before an administering authority concludes that there is no such risk, although there may be particular cases where the absence of such risk is obvious.
30. Although there has been no ruling on precisely what level of perceived support is required, caselaw suggests that it would need to be something tantamount to consent given by the body of members as a whole. This would mean that there needed to be a very high proportion of members who would either positively support the reliance placed upon the non-financial factor in question, or at any rate have no objection to it. Administering authorities do not need to be convinced that there is no one amongst the membership who would object but if a non-financial factor is likely to be significantly controversial amongst members, then it would not be sufficient just to believe that a bare majority would support the decision.
31. Equally, if the vast majority of the scheme members simply had no opinion on a subject, one way or the other, then relying on that as a non-financial factor would seem to represent the administering authority (or the pension committee members) using the fund as a vehicle to advance their own personal views, which would not be a correct use of their fiduciary position.
32. An administering authority is not obliged to give effect to the widely held non-financial views of scheme members, even where they could. However, if it was

positively demonstrated that there was widespread support amongst members for a particular approach and that this was a particularly pressing concern amongst members and that there did not appear to be significant opposition to such a policy, the authority might need to ask itself specifically whether effect should be given to that concern, and to have at least some legitimate reason if it decided not to act upon it. The range of legitimate reasons might, however, be wide – they could include, for example, practical difficulties in formulating and implementing the precise policy to be followed.

33. The most obvious way to gauge member opinion is through the statutory consultation on the investment strategy. However, the views of trade unions, other employee representatives or Councillor understanding of scheme members' views may be relevant. Councillors are elected to represent their local communities and will no doubt have their own understanding of scheme members' opinions and their strength. It is a subtle distinction, but elected members need to be careful in doing so not to just give effect to their own views about what is morally or socially right.
34. Formulation of the investment strategy is, like most local authority functions, subject to the public sector equality duty. Administering authorities should therefore have regard e.g. to the need to protect community cohesion in appropriate cases.

The distinction between financial and non-financial factors

35. The Investment Guidance, and to an extent the caselaw, tend to assume that there is a sharp divide between financial and non-financial factors when it comes to decision-making. The revised opinion considers two specific areas where this distinction may not be so clearly drawn.
36. The opinion suggests that the targeting of economic growth, either in the local or the national economy is likely to represent a non-financial factor, so that the normal financial and member support criteria will need to be satisfied.
37. The climate crisis, on the other hand, may be considered a particular and pervasive systemic financial risk. It has the potential to cause economic disruption so profound that no pension scheme, whatever its specific investments, could hope to escape the adverse impact upon its ability to fund its commitments to pay benefits (or the cost in contributions of doing so). This view is clearly summarised in (for example) [*Climate scenario analysis: an illustration of potential long-term economic and financial market impacts*](#), produced by an Institute and Faculty of Actuaries (IFoA) working party in collaboration with Ortec Finance Ltd. Page 7 of the paper states:

“Climate change will almost certainly fundamentally impact how economies perform as a whole. It will affect macro-economic variables such as GDP growth, and in turn have significant influence over the resulting performance of asset classes and industry sectors. Since the risks associated with climate change are systemic in nature, they will affect all assets to some extent and so cannot be avoided completely through careful selection of investments.”

38. That means that action could be held to be financially motivated even if the intention was to encourage behavioural change by relevant undertakings, rather than to avoid the risk that specific assets will represent a poor investment.
39. The opinion suggests that in such circumstances, if a pension scheme believes that its divestment from fossil fuels would contribute towards encouraging the energy sector to leave such fuels in the ground, and that this will in turn contribute towards keeping climate change under control, then that could be regarded as promoting the long-term financial health of the pension fund, and not simply because of a political or moral belief that it is wrong to jeopardise the earth's environment.
40. Any decision to divest on such grounds as opposed to more conventional financial analysis would need to be properly reasoned and evidenced. The authority would also need to ask itself whether it could realistically influence how the undertakings in question behaved. It would also need to ask why divestment would be more effective than other measures, like stewardship or engagement. An authority may use its judgement about how it deals with "fossil fuel risk", subject to that judgement being a reasonable one in the public law sense.
41. Government guidance [Governance and reporting of climate change risk](#) (DWP, June 2021) already suggests that trustees' legal duty to consider financially material matters extends not just to the kinds of financial risks which might affect investments, but also to how action to address climate change "might contribute positively to anticipated returns or to reduced risk.". Similar arguments can be found in the climate risk guidance contained in CIPFA's [Managing Risk in the LGPS](#).
42. If an authority obtains advice from a suitably qualified advisor, and that advice contains no suggestion that the authority ought to think specifically about climate risk, then not having done so is unlikely to be a breach of the authority's public law duty of reasonableness (certainly if the authority has asked that the advice should cover any climate-related financial risks). On the other hand, an authority which is professionally advised that it should consider or act upon particular risks, yet fails to do so, is likely to be in a position of some difficulty if challenged.

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