

Supreme Court decision on LGPS Investment Guidance

This paper provides comment on the recent Supreme Court ruling on the Local Government Pension Scheme Investment Guidance. This paper is our understanding based on our thoughts and conversations with leading industry parties. However, we are not legal advisers and whilst we may comment on legal issues or legislation, our services do not constitute and are not a substitute for legal advice. It is recommended that you seek legal advice with respect to any legal matters.

Background

Under his statutory power, the Secretary of State for Housing, Communities and Local Government (MHCLG) issued Guidance on Preparing and Maintaining an Investment Strategy Statement (ISS) (“the guidance”). Under the LGPS (Management and Investment of Funds) Regulations 2016 (“the regulations”), LGPS administering authorities in England and Wales are required to follow that guidance when formulating their ISS.

The guidance directed how social, environmental or corporate governance considerations should be taken into account, and included two passages, which provoked a legal challenge led by the Palestine Solidarity Campaign Ltd:

- 1) “...the Government has made clear that using pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries are inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government.”
- 2) The second passage states that authorities “should not pursue policies that are contrary to UK foreign policy or UK defence policy”.

Supreme Court ruling

On 29 April 2020, the Supreme Court handed down its judgment, ruling against the Secretary of State. The court decided that by including these two passages in the guidance the Secretary of State had exceeded his statutory powers.

In his judgment, Lord Wilson concluded that the Government’s statutory “power to direct *how* administrators should approach the making of investment decisions by reference to non-financial considerations does not include power to direct... *what* investments they should not make”.

The Scheme Advisory Board met on 5 May 2020 and consideration of this ruling was on the agenda. The Government is also expected to respond to the ruling in the coming weeks.

Mercer view

This ruling will likely be disappointing to the Government, albeit one which it will have to accept. We believe that there will be a number of potential implications for LGPS Funds, and set out some of these below:

- **Increase in correspondence from campaign groups** – we believe that this ruling could see a significant increase in the volume of approaches that administering authorities receive from a range of campaigners, activists and pressure groups. There is a possibility that these groups will see this ruling as giving LGPS Funds a green light to pursue a range of divestment strategies, and will want to ensure that their particular area is included. In our view, Funds need to prepare themselves for this increase in interest, and ensure that they have the necessary governance and processes in place to manage it.
- In particular, **administering authorities should remain aware of the lawful requirements of the [guidance](#)**, including those regarding ESG. The guidance directs that Funds may take purely non-financial considerations into account (in addition to financial considerations), provided that doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.
- **Consider reviewing ISS and Responsible Investment policies** – whilst we do not believe that the existing guidance would have stopped any LGPS Funds from setting out their views as a Responsible Investor, any updated guidance from MHCLG will need to be reviewed in due course.
- **Role of central government in “guiding” LGPS investment strategy** – Lord Wilson held that Fund assets are not public monies, and the Supreme Court has now made it clear that responsibility for investment decisions rests with the administering authorities. This clarification is likely to be welcomed.
- **The Government’s response** – it will be interesting to see whether the MHCLG responds to this ruling, beyond deleting the unlawful passages from its guidance, given that this judgment cannot be appealed. Other matters concerning the Government at present may drive the timing of any response. We note that the [version](#) of the guidance currently published on gov.uk no longer includes the two passages that were ruled unlawful.

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