6th May 2025

Joint submission by ShareAction, the Impact Investing Institute and ClientEarth
Written evidence to the Work and Pensions Select Committee for their session on 14th May 2025:
"MPs to examine boosting pension funds' UK investment"

1. This is a joint submission by ShareAction, the Impact Investing Institute and ClientEarth.

2. ShareAction is a UK registered charity working to build a financial system that serves our planet and its people. ShareAction works to define the highest standards for responsible investment, mobilising investors to take action to improve labour standards, tackle climate change and the biodiversity crisis, and address global health issues. We have strong relationships with financial regulators, government departments, investors and asset owners including UK pension schemes.

3. The Impact Investing Institute is an independent, non-profit organisation working to transform capital markets, so they support a fairer, greener, more resilient future. We see impact investing as an effective way to achieve that transformation, so we work to accelerate its adoption in the UK and globally. We work across the market to develop innovative solutions that help private finance address societal challenges, and we grow the field of impact investing by building expertise across financial markets. We work with investors and their advisers to move more effective capital for the benefit of people and the planet, and we advocate for regulation and policy that allow the impact investing market to thrive.

4. ClientEarth is an international non-profit environmental law organisation headquartered in the UK. In the Accountable Finance initiative, we are lawyers focussed on the legal implications of climate change and biodiversity-related financial risks and impacts for market participants, including pension funds.

5. In principle, we are not opposed to encouraging investment in the UK and of enabling pension schemes to invest in the UK. This should help drive UK growth and is usually popular with pension scheme members, for example where local government pension schemes invest in local initiatives that boost the local economy.

6. We would like greater clarity on what Government means by the term 'UK investment'. This should not necessarily mean investing in firms that are listed in the UK, some of whom have negligible numbers of UK employees; nor should it equate to investing abroad via investment in asset managers or private equity firms domiciled in the UK. We consider that the concept of 'UK investment' should be investment targeted at *economic activity* in the UK, especially given this Government's commitment to kickstarting economic growth and raising living standards in every part of the UK.

7. We consider that **clarification of fiduciary duty** and **regulation of strategic asset allocation advice by investment consultants** would both be helpful levers for encouraging UK investment for the reasons outlined below and would both be more acceptable to pension schemes than current threats to mandate UK investment.

Clarifying the law on fiduciary duty

8. In recent months the Government has threatened to mandate in law levels of investment by pension schemes in the UK if they do not do so voluntarily. The Government is exploring whether to introduce new legal powers through the Pension Schemes Bill this summer.

9. Making such investment mandatory faces significant opposition from UK pension schemes. There are concerns that any such legislation could cut across fiduciary duty and the purpose of the trust and lead to conflicts in investment decision-making by requiring decisions which are not in savers' financial interests.

10. We are working with leading pensions lawyers on legal drafting to clarify the law in relation to fiduciary duty. Our proposed drafting provides for the consideration of the impacts of pension schemes' investments on financial systems, the economy, the community and the environment and also on members' and beneficiaries' standards of living.

11. Our proposal does not involve making investments mandatory or a change to the proper purpose of a trust and it would not fetter the discretion of pension trustees. Our proposals are facilitating measures. Schemes would not be required by these proposals to invest in a particular way, but enabled to do so.

12. Our proposed change in the law could boost pension funds' UK investment in two key ways:

    a. First, by giving them permission to act on members' standards of living, it will allow trustees to consider members' and beneficiaries' wider interests - not just the value of their pot, or the monthly income stream, but their financial, physical, mental and social interests. This facilitates investments which include, but are not limited to, those providing local employment, housing, health, energy and transport infrastructure. It could also include indirect benefits such as investments which enhance the UK tax base, allowing the Government to cost-effectively - amongst other things - maintain public services and improve public infrastructure.

    b. Second, schemes can *choose* to act on the proposed duty to manage relevant system-level risks by making investments which deliver wider benefits to other parts of their portfolio - for example, homebuilding and the delivery of clean energy. In the UK, delivery of investments which boost economic growth could be of the scale to lift the substantial parts of the portfolio with significant UK exposure. This also aligns with principles in the UK Stewardship Code relating to identifying and responding to market-wide and systemic risks, including initiatives to promote well-functioning financial markets.

13. Our proposed change in the law has support from pensions trustees, pensions executives, pensions lawyers and investment consultants. We have adopted a consultative, iterative process for the drafting of our proposed change in the law and the wording has been presented to, and

tested with, a wide variety of stakeholders including at an event at Willis Towers Watson for over 100 participants and a recent roundtable at LCP.

14. We have presented our proposal to senior officials at HMT and DWP and we will be presenting our proposed change in the law to the Pensions Minister at a meeting on 15th May.

15. We consider that our proposal supports the Government's broader missions and programme of national renewal. For example, granting pensions schemes the freedom to invest specifically in community projects could support the mission to deliver local and regional growth, and to put place at the heart of its Modern Industrial Strategy. Encouraging schemes to invest in new infrastructure could support the mission to achieve energy security and clean power and to create new net zero jobs. And empowering schemes to prioritise investment in companies which treat their workers better or produce healthier products would support the mission to make work pay and tackle the root causes of ill health.

16. A copy of our draft legislative changes has been provided to the Committee. We can also provide the following explanatory documents on request:

    a. Draft Keeling Schedules: these schedules show how the proposed changes would be incorporated into the text of existing legislation.
    b. Legal commentary on the proposed wording: this is an 8-page document aimed primarily at lawyers, explaining in more detail the rationale for particular drafting points.
    c. Q&A document: this is a 20-page document aimed primarily at pension trustees, pensions executives, pensions lawyers and other advisors, and explains (for example) why the law needs clarifying, why existing guidance is insufficient, and how the proposed wording will help pension schemes consider more investment in the UK.

17. Should the Committee wish to see any of the above documents or discuss our proposed change in the law please contact claire.brinn@shareaction.org in the first instance.

Why guidance on fiduciary duty is helpful but not sufficient

18. We note that there are several sources of potential guidance in this area, including recent papers and legal opinions. These are all useful but they do not have legal weight and trustees would be (understandably) wary in acting in reliance upon them.

19. The Financial Markets and Law Committee paper ("the FMLC paper") published last year is intended to provide a general explanation for trustees of the legal position and the uncertainties and difficulties that exist. The recent opinion commissioned by NatWest Cushon from Eversheds ("the Cushon opinion") provides a view on the extent to which schemes can take into account members' standard of living when making investment decisions. The Cushon opinion has not been published in full as it is legally privileged.

20. Both the FMLC paper and the Cushon opinion are very welcome papers. However they are not legally binding and they do not cover all of the areas covered by our legislative proposals.

21. The Government has said in a written question and answer on 24 April that it welcomes the FMLC paper. However, even in the event that the Government went further than this in endorsing either or both the FMLC paper and the NatWest Cushion opinion, they would still not be legally binding and so could not give schemes which acted on them protection from challenge, or ensure that schemes which were reluctant to follow them did so. The Courts can only rule on the letter of the law, and are not bound by interpretation of the law by other bodies, or endorsements from Ministers or Regulators.

22. DWP/HMT/TPR could issue guidance. The difficulty with standard (technically "non-statutory") guidance issued by Government or The Pensions Regulator is that it is not binding. A scheme could therefore not defend its investment decisions with complete confidence by reference to guidance, particularly where the legal position is somewhat unclear (as highlighted by the FMLC report).

23. Statutory guidance, which trustees must "have regard to", is likewise insufficient on its own to give much-needed clarity in this area. In practice, "have regard to" means following, or explaining where they have done something different. However, our understanding is that Government currently has no powers to issue statutory guidance with the scope required and (as with non-statutory guidance), such guidance would not be binding on trustees.

The regulation of investment consultants

24. Last year, ShareAction wrote to HM Treasury[1] urging the regulation of investment consultants. We noted that on numerous occasions over the last ten years the Financial Conduct Authority and the Competition and Markets Authority have called for investment consultants to be brought within the FCA's regulatory perimeter, as has the Work and Pensions Committee itself following its inquiry into the LDI crisis.[2]

25. Under section 36(3) of the Pensions Act 1995, pension scheme trustees "must obtain and consider proper advice on the question of whether the investment is satisfactory". Pension schemes are therefore explicitly legally required to seek advice and – because of the legal risk of doing otherwise – will follow this advice.

26. Despite the fact that this advice is required by law it is only regulated to a limited extent. Investment consultancy services which are not regulated activities include advice on investment strategies, manager selection and asset allocation.

27. Advice on strategic asset allocation is one of the most important aspects of investment consultancy advice:
    a. Strategic asset allocation determines the assets within a pension scheme portfolio, including the percentage of asset to be invested in the UK;

[1] https://shareaction.org/policies/hm-treasury-should-expedite-the-regulation-of-investment-consultants

[2] House of Commons Work and Pensions Committee Report on Defined benefits pensions with Liability Driven Investments", HC 486, 23 June 2023, Paragraph 10 and paragraphs 100-105 https://committees.parliament.uk/publications/40563/documents/197799/default/

b. Strategic asset allocation is a key determinant of the likely returns of the pension scheme; and
c. Strategic asset allocation can also influence markets in general (for example, the widespread adoption of the LDI approach).

28. Given the general importance of strategic asset allocation advice it seems illogical and unjustifiable that this service is not regulated. Furthermore, given the Government's current focus on expanding asset allocation and encouraging pension investment into UK assets, the issue of strategic asset allocation will become increasingly important.

29. Relative financial performance has been a key factor causing UK pension schemes to invest outside the UK. It is well-documented and widely acknowledged that US shares in particular have significantly outperformed UK shares in the 2010s and especially in the 2020s. It is therefore objectively justifiable that (at least until recently) more UK pension fund money has been invested into US stocks (for example, the "Magnificent Seven") than into UK equities.

30. Investment consultants' influence over strategic asset allocation by UK pensions schemes is crucial to investment decisions. It is reasonable to consider that the advice of investment consultants has resulted in pension capital being moved out of UK assets over the last decade in particular.

31. We consider that (in addition closing an acknowledged regulatory gap that the Committee itself has previously raised concerns about) the regulation of strategic asset allocation advice would give comfort to pension schemes to invest in a wider range of assets in the UK. In particular, private equity and other longer-term investments tend to be more risky and have a more uncertain and potentially a more volatile profile. Such assets will certainly have a different risk-return profile to the investments normally made by the majority of pension schemes. Regulation and oversight of advice on strategic asset allocation should help mitigate some of these risks and encourage pension schemes to have more confidence in investing in a broader range of assets.

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