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New QC legal opinion confirms pension fund trustees' legal duty to assess climate risk

On 2 December 2016, ClientEarth published a legal opinion from two UK barristers, including a leading pensions QC, confirming that pension funds that fail to consider climate risk could be exposing themselves to legal challenge.

Summary of the legal opinion

The opinion (by Keith Bryant QC and barrister James Rickards) explores trustees' obligations under common and statutory law and concludes that where climate risks carry material financial implications for fund performance, trustees must take those risks into account in their investment decisions. The authors make clear that this is "beyond reasonable argument" and that failing to do this "would not be proper exercise" of trustees powers.

What does this mean for pension fund trustees?

The opinion means that pension fund trustees can no longer ignore climate risk. It clarifies beyond doubt that pension fund trustees are legally required to take climate risk into account where it could present financial risks to the fund's investments.

The opinion also stresses that:

- The risk does not need to have an immediate impact on investment return before it needs to be considered - longer term financial risks must also be considered; and
- If the issue of climate risk is raised with trustees (for example by pension fund members) the trustees are legally required to turn their minds to the issue and consider whether it is financially material (provided it is not "obviously fanciful").

This means that pension fund trustees must now grapple with the issue of climate risk and - at the very least - consider whether it is financially material. If, having considered the evidence, they find that it is financially material, they *must* take it into account in their decision-making.

Is climate change actually a financially material risk for pension funds?

There is now abundant evidence available to demonstrate that climate change is a financially material risk for pension funds. BlackRock, the Economist Intelligence Unit, leading investment consultants Mercer, the FSB, the Bank of England and the Cambridge Institute for Sustainable Leadership have all recently put out papers warning of the financial risks of climate change, including the risks to pension funds. Trustees must consider this evidence. Those who ignore it are leaving themselves open to legal challenge.

But what can pension trustees do to manage climate risks?

There are a number of guides and tools available to pension fund trustees to help them assess and manage climate risks. These include "Climate Change Investment Solutions: A guide for

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Asset Owners" from the Institutional Investors Group on Climate Change (IIGCC), and Mercer's series of papers¹ on climate change. The IIGCC's guide recommends that trustees:

- Evaluate the evidence;
- Integrate climate change into their investment beliefs and investment policies;
- Explore actions for measuring and managing the risks both within the existing asset allocation structure and through evolving the asset mix over time;
- Reduce carbon intensity of existing assets and explore opportunities for investment in low carbon assets; and
- Take action to reduce vulnerability of existing assets.

Simple steps that pension fund trustees might consider are (1) adding climate change to their risk register, (2) adding climate change to their Statement of Investment Principles, (3) discussing climate change risk with both their investment consultants and their asset managers, and (4) taking steps to ensure the fund's shares are being voted effectively on climate change issues. Taking steps like these should help to ensure that trustees are not susceptible to legal challenge.

What does this mean for pension fund members?

The opinion is a major step forward in protecting pension savers' money from climate change risks. Pension fund members who are concerned about the risks climate change poses to their savings should contact their pension funds to draw their attention to this new legal opinion. Organisations like ShareAction can provide advice and support to pension fund members who want to engage with pension funds on this issue.

When pension fund members raise the issue of climate change with their pension funds, this new legal opinion confirms that the trustees have, at the very least, a legal duty to consider the evidence and decide whether the risk is financially material. If, on considering this, the trustees conclude that climate change is a financially material risk (as the papers referred to above demonstrate), then the trustees are legally required to take the risk into account in their investment decisions.

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¹ "A climate for change: A trustee's guide to understanding and addressing climate risk" (2005); "Climate Change Scenarios – Implications for Strategic Asset Allocation" (2010); "Investing in a time of Climate Change" (2015)