UK to Mandate Consideration of Climate Change by Pension Fiduciaries in 2021

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On January 27, 2021, the United Kingdom's Department for Work and Pensions ("DWP") issued the draft regulation, The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 (the "Regulation"). The Regulation has been submitted for approval by Parliament and, assuming it is approved, would take effect on October 1, 2021. While pension plans in the United States are currently limited by a recent labor regulation to taking non-pecuniary environmental factors into account as a "tie-breaker" after considering pecuniary factors (which may also include environmental factors to the extent they are expected to materially influence the investment performance of a plan investment), and cannot take nonpecuniary factors into account at all in default funds, UK pension schemes (i.e., pension plans, DB and DC) with more than £5 billion in assets (initially, with the threshold dropping to £1 billion a year later) will be required to report on the financial risks of climate change in their portfolios.

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In supplemental draft guidance, the DWP explained that the Regulation would apply to pension schemes as well as master trusts and authorized schemes providing collective money purchase benefits. The Regulation would require that the climate change report would be due within 7 months of the end of each scheme year in which they are subject to the Regulation. The report would need to be linked to in the scheme's annual report and disclosed to members in annual statements.

Significantly, the supplemental guidance states that "Trustees [essentially, the functional equivalent of fiduciaries in the US] have ultimate responsibility for ensuring effective governance of climate related risks and opportunities" which are relevant to the pension scheme.

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In managing these risks and in creating the annual report, trustees would be required "as far as they are able" to undertake scenario analysis, obtain the scope of greenhouse gas emissions and other relevant data, use the data they obtain, use metrics that they agave calculate to help assess climate risk, and measure, annually, the performance of the pension scheme against any targets that have been set.

This guidance could be significant for US plan sponsors as it could serve as a blueprint for policymakers in other jurisdictions (such as the US Department of Labor) to require retirement plans to consider environmental concerns. This may be particularly true given the Biden administration's recent Executive Order calling for a review of the recent Department of Labor rule on the use of pecuniary and nonpecuniary factors in investing.

While the UK Regulation is not yet final, it seems likely to be finalized. And it could provide insight into what more progressive pension regulators are doing to encourage their retirement system to address environmental risks. In the US, where a conservative Department of Labor that sought to minimize the consideration of environmental factors is being replaced with more progressive officials, we anticipate seeing changes to related guidance. Even in the absence of new guidance, multinational companies with operations in both the US and the UK may start considering how the approaches by different jurisdictions to taking into account climate change in pension investing may impact their overall global pension investment and governance strategies, and whether or how they might be harmonized.

Multinational companies should continue to monitor US and UK regulators as they evaluate how pension fiduciaries should take into account environmental, social and governance factors for their pension investing, and the impact those may have on helping workers obtain a secure retirement. If you have any questions, please contact David Powell, Kevin Walsh or your regular Groom attorney.

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