THE FIDUCIARY CASE FOR ADDING TWO BRIGHTON & HOVE CITY COUNCILLORS TO THE EAST SUSSEX PENSION COMMITTEE

Summary:

Climate change is *the* major long-term threat to the East Sussex Pension Fund. Failure to support effective action to address this threat is therefore a clear violation of the Pension Committee's fiduciary duty.

Because of their central role in driving climate change, fossil fuel companies need to be singled-out in the Fund's approach to climate risk. Yet, despite repeated calls from Brighton & Hove City Council (BHCC) for it to do otherwise, the Committee has continued to promote and defend a failed policy of 'engaging' with fossil fuel companies that isn't fit for purpose.

The Fund should be focussing on engaging with policymakers (rather than with fossil fuel companies, as shareholders), pressing them to take the national and international actions necessary to address the climate crisis. Crucially, these actions will need to include across-the-board measures to rapidly phase out fossil fuels from the energy sector. Instead, the Fund's current approach is, in effect, providing cover for fossil fuel companies' ongoing attempts to block and slow-down effective climate action.

This is a governance problem for two reasons:

1. According to the 2014 Law Commission report 'Fiduciary Duties of Investment Intermediaries':

   'Where the purpose of a trust is to provide a pension, trustees will generally act in their beneficiaries' best interests by exercising their investment power to generate ***the best realistic return over the long term, given the need to control for risks****.'* (emphasis added)[1]*; and*

2. Residents of Brighton & Hove have no democratic oversight over the local government pension scheme in the same way that other residents of East Sussex have.

Expanding the Pension Committee to include Councillors from Brighton and Hove (eg. by adding two Councillors from BHCC) would help to address this failure by restoring full democratic oversight of the fund and increasing the diversity of perspectives present on the Committee to ensure the long term interests of fund members are given due consideration in light of the impending climate emergency.

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1 *Fiduciary Duties of Investment Intermediaries, Law Commission*, 2014, page 128, https://www.lawcom.gov.uk/app/uploads/2015/03/lc350_fiduciary_duties.pdf. The same report noted: (a) that 'there is no impediment to trustees taking account of environmental, social or governance factors where they are, or may be, financially material.' (p. 112); and (b) that the need to control for risks: 'is a question of broad judgment rather than mathematical formulae – and must be judged at the time of the decision, not in hindsight.' (p. 93).

Main body:

'THE ONLY REAL PATH TO PROTECT LONG-TERM INVESTMENT VALUE AND RETURNS'

Climate change is *the* major long-term threat to the East Sussex Pension Fund.

Indeed, according to the investor initiative Climate Action 100+ (CA100+), of which the East Sussex Pension Fund is a member:

'If left unchecked, [physical and transition] climate risks will threaten investors' long-term ability to sustain value and generate ongoing returns for their beneficiaries over decades. But because of the scope and size of these climate risks to the global economy ... climate change entails 'unhedgeable' risk for investment portfolios. ***That means action to cut emissions and avoid the worst impacts of climate change is the only real path to protect long-term investment value and returns.'*** (emphasis added)[2]

Failure to take effective action to address this threat is therefore a clear violation of the Pension Committee's fiduciary duty, as spelled out in the 2014 Law Commission report 'Fiduciary Duties of Investment Intermediaries':

'Where the purpose of a trust is to provide a pension, trustees will generally act in their beneficiaries' best interests by exercising their investment power to generate ***the best realistic return over the long term, given the need to control for risks****.'* (emphasis added)[3]

Because of their central role in driving climate change, fossil fuel companies need to be singled-out in the Fund's approach to climate risk.

Indeed, fossil fuels are the largest source of anthropogenic greenhouse gas emissions in the world: the fossil fuel industry and its products accounted for 91% of global industrial Greenhouse Gases (GHGs) in 2015, and about 70% of all anthropogenic GHG emissions.

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2 'The Business Case', Climate Action 100+, https://www.climateaction100.org/business-case (accessed 11 August 2021). Likewise, Mercers' 2019 report 'Investing in a Time of Climate Change - The Sequel 2019' concluded that: 'Advocating for and creating the investment conditions that support a "well-below 2℃ scenario" outcome... is most likely to provide the economic and investment environment necessary to pay pensions... over the timeframes required by beneficiaries.' (https://www.mercer.com/our-thinking/wealth/climate-change-the-sequel.html).
Recent modelling by ORTEC Finance and the Institute and Faculty of Actuaries concluded that in a 'failed transition' scenario (which sees global warming of approx. 4°C by 2100) global GDP would be 70% lower in 2100 than in the baseline pathway without the warming. They also found that such a scenario would lead to a 50% decline in Global equity returns by 2060. ('Climate scenario analysis: An illustration of potential long-term economic & financial market impacts', June 2020, https://www.actuaries.org.uk/system/files/field/document/IFoA%20Paper%202.pdf). In a similar vein, modelling by Swiss Re suggests that 'current likely temperature-rise trajectories, supported by implementation of [current] mitigation pledges' would lead to global GDP being 11 – 14% less in 2050 than in a world without climate change ('The economics of climate change: no action not an option', Swiss Re Institute, April 2021, https://www.swissre.com/dam/jcr:e73ee7c3-7f83-4c17-a2b8-8ef23a8d3312/swiss-re-institute-expertise-publication-economics-of-climate-change.pdf).

3 *Fiduciary Duties of Investment Intermediaries, Law Commission*, 2014, page 128, https://www.lawcom.gov.uk/app/uploads/2015/03/lc350_fiduciary_duties.pdf. The same report noted: (a) that 'there is no impediment to trustees taking account of environmental, social or governance factors where they are, or may be, financially material.' (p. 112); and (b) that the need to control for risks: 'is a question of broad judgment rather than mathematical formulae – and must be judged at the time of the decision, not in hindsight.' (p. 93).

And just 100 fossil fuel producers are responsible for 52% of all GHG emissions since the industrial revolution.[4]

Therefore, no approach to climate change makes any sense unless it singles out these companies and their actions for special attention. To put it crudely, the speed at which the umbrella industry decarbonises will have little or no impact on whether global warming is limited to 1.5°C. The speed at which the fossil fuel industries decarbonise (which in practice means phasing them out of the energy sector[5]) will be decisive.[6]

Significantly, the East Sussex Pension Committee has yet to publicly acknowledge this reality – at least in responses to questions from the general public.[7]

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4 'The Carbon Majors Database: CDP Carbon Majors Report 2017', Carbon Disclosure Project, July 2017, https://b8f65cb373b1b7b15feb-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/cms/reports/documents/000/002/327/original/Carbon-Majors-Report-2017.pdf?1499691240

5 The IEA's 'Net Zero' pathway still has fossil fuels contributing 20 percent of global energy supply in 2050. However, it can only permit this because it relies on unproven technology and unrealistic levels of land use (for carbon offsetting etc...) Fortunately, renewable energy is 'already more than capable of scaling up at the speed necessary to protect the climate, meet energy demands, ensure energy access for the poor, and support sustainable development', with the complete removal of fossil fuels from the energy sector by 2050: see 'Fossil Fuel Exit Strategy', June 2021, https://fossilfueltreaty.org/exit-strategy

6 In May 2021 the International Energy Agency (IEA) declared that if the world is serious about dealing with the climate crisis 'there can be no new investments in oil, gas and coal, from now – from this year' (IEA Executive Director, Fatih Birol, 'No new oil, gas or coal development if world is to reach net zero by 2050, says world energy body', Guardian, 18 May 2021, https://www.theguardian.com/environment/2021/may/18/no-new-investment-in-fossil-fuels-demands-top-energy-economist). Likewise, in February 2021 the Transition Pathway Initiative noted that: 'An almost complete and immediate stop in exploration and sanctioning of new oil fields would … be required to avoid locking in future oil production that would see temperatures exceed a 1.5°C increase' in global warming. ('The oil and gas industry will need to scale back much faster to limit warming to 1.5°C', Transition Pathway Initiative, 12 February 2021, https://www.transitionpathwayinitiative.org/publications/48?type=NewsArticle). However, while *necessary* for limiting global warming to 1.5°C, simply ending investments in new oil, coal and gas projects isn't by itself *sufficient* to limit global warming to 1.5°C. To achieve the latter the world will also need to 'actively wind down production from existing coal mines and oil and gas wells' – as 'emissions under a "no expansion" scenario are already 22% too high in 2025 and 66% in 2030 compared to a 50% chance of achieving a 1.5°C temperature target.' See 'Fossil Fuel Exit Strategy', op. cit.

7 To date, members of the public have submitted the following question to Full Council meetings over 400 times: '*Does the East Sussex Pension Committee accept that, because burning fossil fuels is the key driver of global warming, the goals of the Paris Climate Agreement (to keep global warming to 'well below 2 °C', pursuing 1.5°C) cannot be achieved without the rapid alignment of the big fossil fuel companies with a 1.5°C pathway? By a 1.5°C pathway we mean one that: (a) yields a 50% or better chance of keeping global warming below 1.5°C; and (b) does so without assuming the future creation of global scale 'negative emissions technologies' (ie. ones that remove carbon dioxide from the atmosphere) that don't currently exist.'* The Pension Committee has yet to answer this question. See https://democracy.eastsussex.gov.uk/documents/b15215/Item%204-%20public%20questions%2013th-Oct-2020%2010.00%20Full%20Council.pdf?T=9; https://democracy.eastsussex.gov.uk/documents/b15365/Item%204%20-%20public%20questions%2001st-Dec-2020%2010.00%20Full%20Council.pdf?T=9; https://democracy.eastsussex.gov.uk/documents/b15572/Item%204%20-%20public%20questions%2009th-Feb-2021%2010.00%20Full%20Council.pdf?T=9; https://democracy.eastsussex.gov.uk/documents/b15908/Item%2015%20-%20Public%20questions%2025th-May-2021%2010.00%20Full%20Council.pdf?T=9

ENGAGING WITH FOSSIL FUEL COMPANIES: A FAILED POLICY

Brighton & Hove City Council (BHCC) has repeatedly called on the East Sussex Pension Committee to fulfil its fiduciary duty by making a public commitment to divest the East Sussex Pension Fund from fossil fuels: first in April 2017[8], then in again in October 2020[9] and for a third time this February.[10]

It has yet to receive an adequate response from the Committee.

Instead, the Committee has continued to promote and defend a failed policy of 'engaging' with fossil fuel companies that simply doesn't work.

In a written response to questions from the public to the October 2020 Full Council meeting the Chair of the Pension Committee claimed that the Fund's current approach of 'engaging' with oil and gas companies 'has made substantial demonstrable progress over the last 3 years in persuading major companies, including a number of oil and gas majors like BP, to more seriously address the energy transition'[11].

However, while it is true that several large fossil fuel companies have garnered a considerable amount of publicity for their climate or 'net-zero' 'ambitions', the reality is that these all fall far short of what is required if we're to avoid catastrophic climate change ('the only real path to protect long-term investment value and returns' – CA100+).

Indeed, despite many years of such 'engagement' **not a single major oil company is aligned with a 1.5°C pathway.**[12] [13]

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8 https://present.brighton-hove.gov.uk/mgAi.aspx?ID=56672

9 https://present.brighton-hove.gov.uk/mgAi.aspx?ID=81285

10 https://present.brighton-hove.gov.uk/documents/g10367/Printed%20minutes%2003rd-Feb-2022%2018.30%20Council.htm?T=1&CT=2

11 https://democracy.eastsussex.gov.uk/documents/b15215/Item%204-%20public%20questions%2013th-Oct-2020%2010.00%20Full%20Council.pdf?T=9

12 A September 2020 analysis by Oil Change International concluded that 'not a single climate plan released by a major oil company comes close to aligning with the urgent 1.5ºC global warming limit' (*Big Oil Reality Check: Assessing Oil and Gas Company Plans*, Oil Change International, September 2020, http://priceofoil.org/2020/09/23/big-oil-reality-check). In November 2021 the Transition Pathway Initiative declared that: 'Three oil and gas firms – Occidental Petroleum, TotalEnergies and Eni – have set emissions reduction targets which are ambitious enough to reach net zero by 2050 and to align with TPI's 1.5°C benchmark.' (see https://www.transitionpathwayinitiative.org/publications/92.pdf?type=Publication). However, this analysis: (a) 'solely relies on declarations from companies and does not consider facts and figures. This means that even if companies put forward unrealistic ambitions, the TPI benchmark will build on it anyway'; and (b) 'disregards the critical importance of short and medium term emission reduction to avoid immediate acceleration of climate change.' (see 'The TPI benchmark: misleading approach, dangerous conclusion', Reclaim Finance, December 2021, https://reclaimfinance.org/site/en/2021/12/06/the-tpi-benchmark-misleading-approach-dangerous-conclusion). For example, oil and gas major TotalEnergies 'is credited as 1.5°C-aligned because the company reaches TPI's emission intensity target in… 2047. Each year before that, TotalEnergies is above TPI's pathway, thus emitting too much GHG in the atmosphere and contributing to the overshoot of our short-term carbon budget. By 2035, TotalEnergies' emissions under its own scenario will already be more than 33% higher than if it aligned from now on with the 1.5°C pathway provided by the TPI.'

13 A few more illustrations:
(1) In 2019 the oil and gas industries were forecast to spend $4.9 trillion over the next decade on new oil and gas fields – none of which is compatible with limiting warming to 1.5°C ('Overexposed: How the IPCC's 1.5℃ report demonstrates the risks of overinvestment in oil and gas', Global Witness, April 2019, https://www.globalwitness.org/en/campaigns/oil-gas-and-mining/overexposed/);
(2) While BP and Total have declared 'Net Zero' goals for 2050, neither 'goal' actually covers all of the company's owned production and global product sales. For example, BP excludes its stake in Rosneft

And of course, time is running out. As the chair of the International Energy Agency announced in May 2021:

'We are approaching a decisive moment for international efforts to tackle the climate crisis – a great challenge of our times … [the] gap between rhetoric and action [on climate action] needs to close if we are to have a fighting chance of reaching net zero by 2050 and limiting the rise in global temperatures to 1.5 °C.'[14]

ENGAGING WITH FOSSIL FUEL COMPANIES: PROVIDING COVER FOR BIG OIL

The Committee's current policy – shrinking the Fund's exposure to fossil fuel companies down to something like 0.5% of the Fund while refusing to make a public divestment commitment – is effectively providing cover for these companies' ongoing attempts to block and slow-down effective climate action.[15]

As academics Dario Kenner and Richard Heede have noted, 'what the executives and directors [of companies like BP, Shell, Exxon and Chevron] have in common is a desire to maintain demand for oil and gas, and to defend their company's social license to operate'[16].

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from its Net Zero goal, even though this makes up around a third of BP's global production volume. Likewise, Total's goal fails to include end-user ('scope 3') emissions for its customers outside Europe. ('Absolute Impact 2021: Why oil and gas "net zero" ambitions are not enough', Carbon Tracker, May 2021, https://carbontracker.org/reports/absolute-impact-2021/);

(3) None of Shell, Equinor, Repsol, Occidental, Conoco-Philips, Chevron and Exxon have made any commitment to absolute emissions reductions by 2030 (meaning that they could actually increase their emissions during this period without breaching their 'goals'). This despite the fact that CO2 emissions from oil and gas must fall by at least 44% and 39% by 2030 respectively if we're going to limit global warming to 1.5°C. (See 'Big Oil Reality Check', op. cit., p.7 and 'Analysis: Why coal use must plummet this decade to keep global warming below 1.5°C', CarbonBrief, 6 February 2020, https://www.carbonbrief.org/analysis-why-coal-use-must-plummet-this-decade-to-keep-global-warming-below-1-5c);

(4) Even where companies have net zero 'goals', these remain 'heavily reliant on a range of unproven technologies to mitigate emissions, impacting their credibility'. For example, 'Eni and Shell's plans involve a combined 140Mt/CO2 of carbon dioxide removal per year through afforestation, effectively implying a forest larger than Bulgaria, and potentially nearly as large as Spain.' As Carbon Tracker note: 'This is a huge land area needed to address just 0.3% of current average emissions (41.5Gt/CO2 per year).' ('Absolute Impact', op. cit.)

(5) In March 2021 the *Economist* set out to assess the impact of the CA100+ investor initiative using a portfolio of 100 large emitters that were not engaged by CA100+ but which roughly matched the CA100+ firms in terms of sectors and regions represented. They found little difference between the two groups, in terms of commitments made, concluding that '$50trn-worth of investor pressing does not seem to result in much change'. ('The Impact of Green Investors', Economist, 27 March 2021, https://www.economist.com/finance-and-economics/2021/03/27/the-impact-of-green-investors).

14 'Net Zero by 2050: A Roadmap for the Global Energy Sector', International Energy Agency, May 2021, https://iea.blob.core.windows.net/assets/4482cac7-edd6-4c03-b6a2-8e79792d16d9/NetZeroby2050-AroadmapfortheGlobalEnergySector.pdf.

15 In March 2019, Influence Map – whose research CA100+ use for their Net Zero Benchmark – published research which found that the five largest publicly-traded oil and gas majors (ExxonMobil, Royal Dutch Shell, Chevron, BP and Total) had invested over $1bn of shareholder funds on misleading climate-related branding and lobbying since the 2015 Paris Climate Agreement. According to their report, these efforts were 'overwhelmingly in conflict with the goals of this landmark global climate accord and designed to maintain the social and legal license to operate and expand fossil fuel operations.' ('How the oil majors have spent $1Bn since Paris on narrative capture and lobbying on climate', Influence Map, March 2019, https://influencemap.org/report/How-Big-Oil-Continues-to-Oppose-the-Paris-Agreement-38212275958aa21196dae3b76220bddc). Such activity is ongoing, see eg. 'How a powerful US lobby group helps big oil to block climate action', Guardian, 19 July 2021, https://www.theguardian.com/environment/2021/jul/19/big-oil-climate-crisis-lobby-group-api.

16 Dario Kenner and Richard Heede, 'White knights or horsemen of the apocalypse? Prospects for Big Oil to align emissions with a 1.5C pathway', Energy Research & Social Science, 17 March 2021, https://www.sciencedirect.com/science/article/pii/S2214629621001420

The never-ending process of ‘shareholder engagement’ and its associated greenwash plays into this:

*‘**When BP, Shell and others talk of net zero, they are trying to stay part of the decision-making process. They want to be in charge of the transition as much as possible so they can slow it down – that is the whole point of trying to convince society to trust them** … It can’t be just about what Shell is doing or BP. It must be industry-wide. And should be about acting on climate science and phasing out oil and gas in line with a 1.5°C target’ (emphasis added).*[17]

ENGAGING WITH POLICYMAKERS: THE MISSING ALTERNATIVE

As Kenner and Heede suggest, when it comes to fossil fuel companies, engaging with policymakers - rather than shareholder engagement – should be the Fund's main focus, with the Fund actively pressing for national and international action to rapidly phase-out the fossil fuel industries in line with what the science requires.

Noting that ‘going through the investment process is a bizarre place to try to create social impact in the first place’, Tariq Fancy - formerly BlackRock Inc.’s chief investment officer for sustainable investing - has observed that:

‘Systemic problems such as a global pandemic or climate change – require systemic solutions. Only governments have the wide-ranging powers, resources and responsibilities that need to be brought to bear on the problem’.[18]

Yet to date the Fund appears to have done very little in the way of public policy engagement. At its February 2022 meeting, the Pension Committee couldn't even agree a proposal for it to call on the UK Government to stop licensing new oil and gas fields (in line with what the International Energy Agency says is necessary if we're going to limit global warming to 1.5ºC).

A public commitment by the Fund to divest from fossil fuels – as repeatedly called for by Brighton & Hove City Council - would greatly enhance the Fund’s credibility in pressing policymakers for effective climate action.

Moreover, investigations by two major financial management firms, BlackRock and Meketa, have ‘separately concluded that **investment funds have experienced no negative financial impacts from divesting from fossil fuels. In fact, they found evidence of modest improvement in fund return** ...’[19]

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17 ‘Oil firm bosses’ pay ‘incentivises them to undermine climate action’, Guardian, 15 April 2021, https://www.theguardian.com/environment/2021/apr/15/oil-firm-ceos-pay-is-an-incentive-to-resist-climate-action-study-finds

18 ‘BlackRock hired me to make sustainable investing mainstream. Now I realize it’s a deadly distraction from the climate-change threat’, Globe and Mail, 25 March 2021, https://www.theglobeandmail.com/business/commentary/article-sustainable-investing-is-a-deadly-distraction-from-actually-averting. Fancy came to the conclusion that, when it comes to climate change, ESG is actually functioning as a “deadly distraction”, like giving wheatgrass to a cancer patient: ‘medically harmless; but if that wheatgrass convinces the patient to delay chemotherapy, it’s a complete disaster.’

19 ‘Major investment advisors BlackRock and Meketa provide a fiduciary path through the energy transition’, Institute for Energy Economics and Financial Analysis, 22 March 2021, https://ieefa.org/major-investment-advisors-blackrock-and-meketa-provide-a-fiduciary-path-through-the-energy-transition/.

ENHANCING THE COMMITTEE THROUGH EXPANSION

Expanding the East Sussex Pension Committee to include adequate representation for Councillors from Brighton & Hove (eg. by adding two Councillors from BHCC to the existing five[20]) would enhance the Pension Committee's ability to act in the best financial interests of the Fund's beneficiaries by:

(a) increasing the diversity of perspectives present on the Committee (eg. Brighton & Hove City Councillors are unlikely to share the view, often voiced in Pension Committee meetings, that fossil fuel companies are 'part of the solution' to the climate crisis, bearing in mind their stated support for divestment from fossil fuel assets.);

and

(b) ensuring that the Fund finally makes a public commitment to divest from fossil fuels and begins the process of aggressive engagement with policymakers, pressing them for effective climate action ('the only real path to protect long-term investment value and returns' - CA100+).

ADDRESSING THE ACCOUNTABILITY DEFICIT

Finally, such an expansion of the Committee would also address a fundamental deficit: the Fund's lack of democratic accountability to a large chunk of its membership.

Brighton & Hove City Council employees make up 26.9% of the membership of the East Sussex Pension Fund[21] and, together with BHCC as their employer, contribute 31.9% of annual contributions to the Fund.[22] The figures for *all* members from active participating Brighton-based employers would be higher still.[23]

Yet, Fund members who live in Brighton & Hove (unlike those who live in the rest of East Sussex) currently have no democratic means of holding the Pension Committee to account.

If they believe that the Pension Committee is failing in its fiduciary duty then there is currently no way in which these members (unlike their fellow members in East Sussex) can vote to alter the Committee's composition (eg. by changing the political balance on East Sussex County Council). Currently, these Fund members are not even officially permitted to raise questions about the Fund in Full Council meetings or to petition the Council for

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20 Note that (2/7) = 28.6% is almost precisely the proportion of the Fund's membership that are current or former employees of BHCC (26.9%) – see note 21 below.

21 As at 31 March 2020 BHCC had 20,677 members in the scheme (active, deferred and pensioner) out of a total of 76,792 (https://www.whatdotheyknow.com/request/727793/response/1742970/attach/html/2/Response%20all%20information%20to%20be%20supplied.pdf.html and 'East Sussex Pension Fund Annual Report and Accounts: 2019-2020', p.3, https://democracy.eastsussex.gov.uk/mgConvert2PDF.aspx?ID=33539).

22 For the financial year ending 31 March 2020, BHCC's employers' and employees' pension contributions totalled £41.561m (see page 130 of https://www.brighton-hove.gov.uk/sites/default/files/2020-12/Statement%20of%20Accounts%202019%20to%202020.pdf). For the same financial year the total annual contributions to the East Sussex Pension Fund linked to active employees were £130.421m (see page 110 of https://www.eastsussex.gov.uk/media/17241/escc-statement-of-accounts-2019-20-including-audit-opinion.pdf).

23 For example, Brighton University made £7.8m in contributions to the Fund in 2019/20 (see page 56 of https://tinyurl.com/univbrighton2019-20). If we add these to the £41.561m in contributions (employer and employee) from BHCC then we get a figure of £49.361m, amounting to 37.8% of annual contributions to the Fund.

redress. The only democratic option available to them is to lobby Brighton & Hove City Council, who have no seat on the Pension Committee. Herein lies the problem.

In effect, **the current set-up makes BHCC employees (and other Brighton-based members) second-class members of the Fund, with fewer rights than those based in the rest of East Sussex**.