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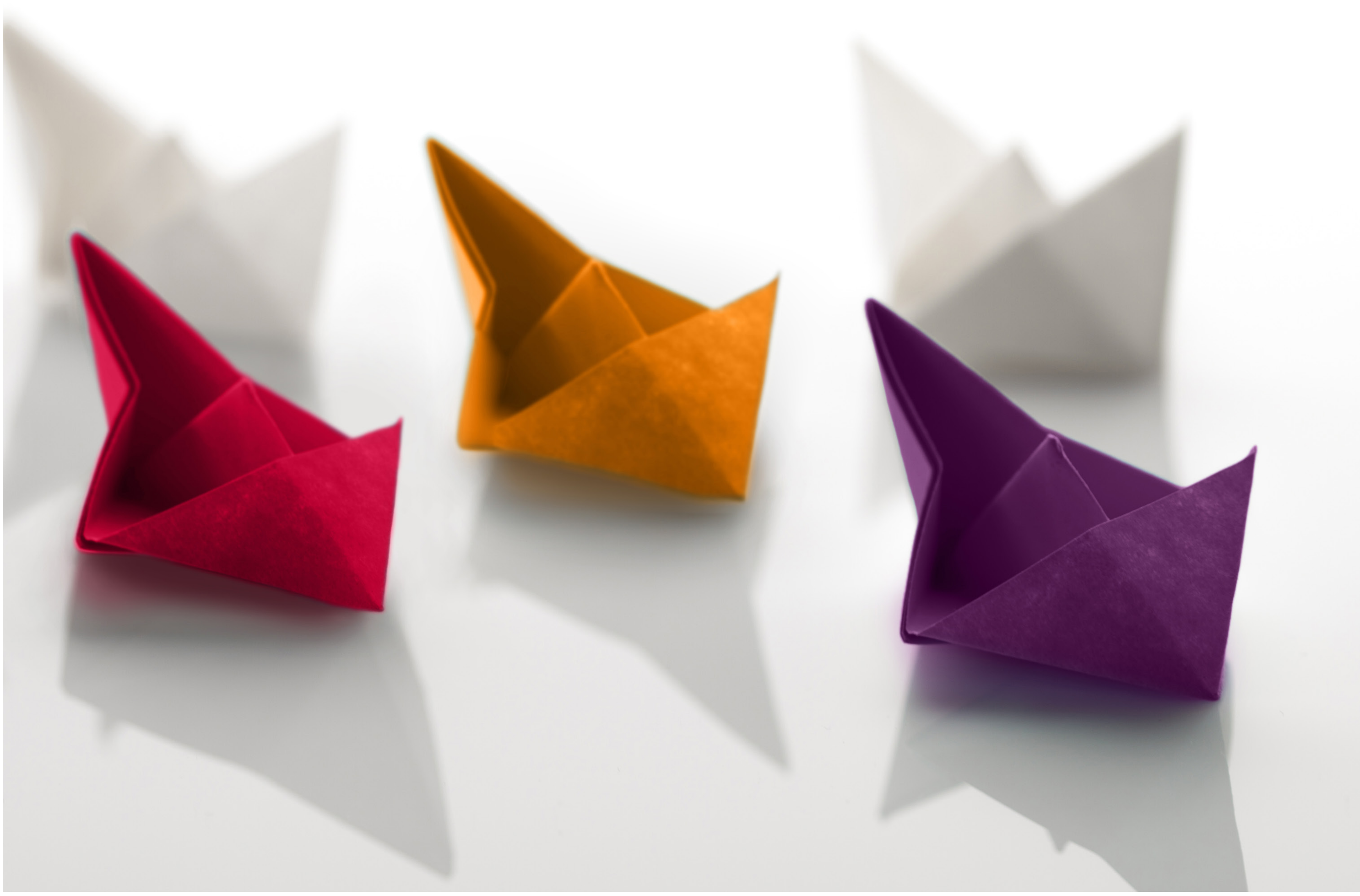
Finance & investment briefing

June 2025

Sackers finance and investment experts take a look at current issues of interest to pension scheme investors



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Abbreviations

AIFMD: Alternative Investment Fund Managers Directive 2011/61/EU

BPA: Bulk purchase annuity

Climate Change Governance Regulations: the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021/839

DB: Defined Benefit

DC: Defined Contribution

ESG: Environmental, social and corporate governance

FCA: Financial Conduct Authority

FTC: Federal Trade Commission

HMT: HM Treasury

IGC: Independent Governance Committee

LDI: Liability Driven Investment

MA: Matching adjustment

NZAM: Net Zero Asset Managers

NZBA: Net Zero Banking Alliance

OTC: Over the counter

PASA: Pensions Administration Standards Association

PRA: The Prudential Regulation Authority

TPR: The Pensions Regulator

VFM: Value for Money

Finance & investment focus

Welcome to the second finance & investment briefing of 2025 – the sun may finally be shining.

In this issue, we look at the current ESG landscape and whether trustees may be impacted by the possible backlash being seen in the industry. We discuss what trustees might want to consider in relation to their ESG policies.

In the legal update section, we provide an overview of recent developments, including TPR's continued focus on growth, proposed changes to the regulation of asset managers and the PRA's speech on overseeing BPA growth.

> We also wanted to update you about an upcoming change to our briefings. Going forward, we will be merging the finance & investment briefing with the Quarterly briefing. This means that the finance and investment content you ordinarily receive will now be included within our general quarterly publication, so that all relevant content is easily accessible in one place. There is no need for you to take any action – the change will happen automatically.

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The ESG backlash?

Over the past few years, the issues surrounding climate change and pensions have continued to grow apace. Trustees now find themselves navigating a complex landscape that includes a myriad of regulations, associated guidance and industry initiatives. The challenges are multifaceted, encompassing not only the need to address climate-related risks and opportunities but also the broader implications of environmental, social, and corporate governance (ESG) factors.

UK pension scheme trustees have significant obligations and requirements in relation to ESG, and in the UK these responsibilities sit within a larger framework of ESG initiatives. The Government's Greening Finance Roadmap, launched in 2021, the UK Green Taxonomy and the expected review of the Climate Change Governance Regulations, all indicate that the UK Government remains committed to the climate change cause, with the intention to still reach its net-zero target by 2050.

But are we now witnessing an ESG backlash? Recent "anti-ESG" challenges, particularly from the US, might suggest that the landscape is shifting, once again.

A snapshot of the US

The recent change of government in the US has arguably catalysed further significant political division over the issue of climate change, and we have seen a recent wave of anti-ESG actions across the pond.

Earlier this year, a group of banks and asset management firms pulled out of the voluntary Net Zero Banking Alliance ("NZBA"), a UN-backed initiative aimed at aligning financial activities with the goal of net zero emissions by 2050, and the Net Zero Asset Managers ("NZAM") initiative. As a result, NZBA called for a vote on dropping the pledge to align assets with the Paris Agreement. In addition, following one recent departure, NZAM announced it was suspending activities, pending the outcome of a review "to ensure NZAM remains fit for purpose in the new global context".

A backlash in opinion also appears to be emerging in the US courts. It was held in January this year, by a federal judge in Texas in the case of *Spence v. American Airlines Inc.*, that the airline had breached one of its statutory duties to prioritise investment returns for savers by allowing its asset managers to vote in favour of ESG resolutions at shareholders' meetings. On its face, this appears markedly different to the position for trustees of UK pension schemes, where the current consensus is that it is **within** a trustee's fiduciary duty to consider financially relevant ESG factors when setting an investment strategy. Indeed, UK trustees have specific ESG legislative requirements covering, among other things, the statement of investment principles and climate reporting. It should, however, be noted that in the American Airlines case, ESG was generally considered a "non-pecuniary" factor, concerned with bringing about certain types of societal change, with the judge finding that an investment approach that "aims to reduce material risks or increase return for the exclusive purpose of obtaining a financial benefit" is *not* ESG investing. So, the case is perhaps a better illustration of the fact that we are "two countries separated by a common language", rather than having fundamentally different legal principles at play when it comes to fiduciary duties.

Of potentially wider reach, however, might be how antitrust laws in the US are applied. In 2022 Lina Khan (then chair of the Federal Trade Commission ("FTC")) wrote an opinion piece in the Wall Street Journal ("ESG Won't Stop the FTC") stating: "Some in corporate America seem to think that the FTC won't challenge an otherwise illegal deal if we approve of its ESG impact. They are mistaken. The antitrust laws don't permit us to turn a blind eye to an illegal deal just because the parties commit to some unrelated social benefit." This article was quoted in a Texas case in late 2024 (of which we are still awaiting judgment) which saw the Attorney Generals of 11 states (including Texas) suing BlackRock, State Street and Vanguard claiming they used their collective voting power in coal production companies to violate antitrust laws by reducing coal output, thereby increasing energy prices for US consumers and producing "cartel-level profits". The details of the case are complex and, of course, hotly contested, but it serves as a reminder of the debate that can be had around the intersection between ESG and various jurisdiction-specific corporate laws.

The ESG backlash? cont.

Despite this possibly growing opposition, pension funds in the US are potentially barricading against this backlash. The NY times has suggested that there has been a step up in support of ESG principles and funds are arguably more engaged with asset managers on climate goals, with some US funds shifting to European asset managers, who are possibly more focused on climate change goals. Does this suggest that pension funds are not so swayed by political priorities, but rather the need for their investments to provide long-term sustainable returns for people who might not retire for many decades, keeping climate risks at the forefront of their minds?

That is not to say that opinion is not also shifting in Europe. Political pressures and the challenging economic environment have had their part to play in a possible slowing by some companies in taking climate action. In February 2025, the EU Commission set out a new package of proposals "to simplify EU rules" in relation to sustainability and EU investments. This "Omnibus Simplification Package" introduces amendments and clarifications to key sustainability regulations to streamline reporting.

What does this mean for UK pension trustees?

While the UK Government's current central mission is economic growth, climate remains on the UK agenda. By way of example, the Government has maintained its manifesto promise in respect of North Sea oil, committing to not issuing "new licences to explore new fields". And, although the Heathrow expansion is to go ahead with the aim of kickstarting economic growth, the new runway must be "delivered in line with our legal, environmental and climate obligations". Concurrently, the conflicting perspectives from the US seem unlikely to go away any time soon. So where does this leave UK pension schemes that have exposure to the US market?

In February 2025, the People's Pension, one of the UK's largest pension funds, withdrew £28bn assets from State Street, a US firm that was its only asset manager. In its place, Amundi, Europe's largest asset manager, and Invesco have been appointed in a step towards "achieving greater alignment with The People's Pension's stewardship approach and priorities". Perhaps this is an indicator of commercial resilience in the UK in preserving the ESG targets and ambitions, despite opposing US views.

In general, we would expect UK pension trustees to be well insulated from the above-mentioned potential issues. In relation to the exercise of fiduciary duty, it is domestic law that would apply to UK pensions schemes, and therefore the American Airlines case would have no precedent here.

What next?

The political landscape continues to change, and it is too early to say whether any backlash is here to stay. It may be that we are entering an era of "greenhushing", where companies retain their policies on ESG but are less vociferous about doing so. Whilst we wait to see how things play out, trustees can use the time to take stock of their own positions. Trustees may wish to ask themselves:

- do they understand how their fiduciary duties are applied to the trustees' investment policies and incorporation of ESG (including stewardship), and
- whether their policies are properly reflected in their appointed managers' investment objectives and policies (including stewardship). This may be as much about ensuring that managers are not overreaching on ESG as whether they are going far enough. ESG may mean different things in different jurisdictions so trustees should always focus on the substance of the manager's investment strategy (and whether this is aligned with a UK trustees' understanding of ESG as a financially material factor), rather than the label.

Legal update

TPR continues its focus on growth

On 28 March 2025, TPR published Nausicaa Delfas' speech on pensions regulation and growth, which set out how TPR intends to lead in key areas designed to "protect savers, enhance the system and innovate in the interests of savers". Key points include:

- **increasing value –** the new VFM framework, which TPR sees as "an attempt to refocus competition on what should matter – outcomes" is expected to be set out in the Pension Schemes Bill. TPR wants to help trustees to look across the market to "see what good looks like" and for all schemes to be able to consider the full range of investment options
- **enabling productive investment –** TPR believes that pensions are "uniquely placed" to consider long-term returns, and "urges" the industry to consider what more can be done in this area, particularly around transparency in performance and associated charging structures, and
- **supporting market innovation –** TPR is planning to develop an innovation framework and criteria to trial new ideas, with the aim of launching a hub to test a variety of innovation services with the market "by the autumn".

These comments come as TPR has published its letter to the Government outlining "measurable commitments" to "significantly boost business confidence, improve the investment climate, and foster sustainable economic growth", which are consistent with TPR's remit.

Proposed changes to regulation of asset managers

On 7 April 2025, HMT announced that it is consulting on changes to the rules governing Alternative Investment Fund Managers. Much of the UK's asset management regulation is derived from EU legislation, including the alternative investment fund managers directive ("AIFMD"). The Government is proposing to repeal AIFMD's "firm-facing legislative requirements" and, where appropriate, for the FCA to replace those legal provisions in its rules. The FCA is also considering changes to its existing AIFMD rules.

The consultation is accompanied by an FCA call for input, which seeks to give stakeholders a chance to comment on the proposals before the FCA develops detailed rules and guidance for consultation.

Both the consultation and call for input close on 9 June.

PASA publishes updated guidance on data readiness for buy-ins and buy-outs

On 9 April 2025, PASA published an updated version of its guidance on data readiness for buy-ins and buy-outs. It offers practical support for trustees and administrators and should be read in conjunction with PASA's 2023 guidance.

The new version offers a "deeper insight" into the data elements that insurers usually consider significant for ensuring a smooth and successful transition process. Insurers expect trustees to focus on providing data that is as complete, accurate and up to date as possible. The principles in the guidance can also be applied to schemes exploring alternative endgame options.

PRA speech on overseeing growth in the bulk purchase annuities sector

On 30 April 2025, the PRA published a speech given by Executive Director, Gareth Truran on overseeing growth in the BPA sector. Mr Truran talks about the current work of the PRA against the backdrop of BPA deals being "at near record levels" that are "widely forecast to remain high". The speech focuses on three aspects: supporting investment, maintaining resilience and improving transparency.

Points of interests, include:

- **MA reforms –** the PRA has a dedicated MA permissions team to facilitate faster engagement with insurers. Insurers are using this new flexibility to include assets with highly predictable cashflows in the MA, with more examples now relating to the UK
- **maintaining resilience –** the PRA highlights the importance for the sector to safely absorb the high volumes of new BPA business projected, and is aware of potential risks that may arise if structures and features are not managed effectively. As the global risk outlook evolves, insurers need to consider the implications for credit conditions and their investment portfolios
- **solvency triggered termination rights –** these are becoming more common in the BPA buy-in market and allow pension schemes to terminate a buy-in arrangement if an insurer's solvency position breaches a predefined threshold. This can impact the sensitivities of an insurer's balance sheet and introduce new risk management challenges. Insurers are expected to consider potential issues for their portfolios in stress situations and have mechanisms in place to address them, and
- **stress testing –** a new approach to stress testing plans so as to be more transparent, publishing both sector-wide and firm specific stress test results for the largest UK life insurers. In designing the new tests, the Bank of England sought input from pension scheme trustees, as well as others, on the information they would find helpful to understand insurer resilience. The aim is to publish the first results by the end of 2025.

Sackers

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Sackers is the UK's leading commercial law firm for pension scheme trustees, employers and providers. Over 70 lawyers focus on pensions and its related areas, including Sackers finance and investment group, a team of lawyers who provide cutting-edge advice on all aspects of pension scheme finance and investment.

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