Supreme Court decision in *Palestine Solidarity Campaign*: LGPS investment guidance on foreign policy and defence issues held unlawful

The Supreme Court has today given judgment in *R (Palestine Solidarity Campaign Ltd and another) v Secretary of State for Housing, Communities and Local Government* [2020] UKSC 16.

By a majority (Lady Hale, Lord Wilson and Lord Carnwath; Lady Arden and Lord Sales dissenting) the Court has allowed the claimants' appeal against the decision of the Court of Appeal, and restored the ruling made by Sir Ross Cranston at first instance.

Both parties were represented throughout the proceedings by members of 11KBW: **Nigel Giffin QC** and **Zac Sammour** appeared for the claimants; **Julian Milford QC** appeared for the defendant.

The case concerned one aspect of the guidance on investment strategy statements issued by the Secretary of State to Local Government Pension Scheme administering authorities. The relevant regulations require an authority's strategy to be "in accordance with" such guidance.

The issue leading to the dispute was about the taking into account of non-financial factors in the making of investment decisions (that is, "ethical investment"). The guidance uncontroversially stated that such factors could be taken into account, provided that doing so would not involve significant risk of financial detriment to the scheme, and that the authority had "good reason to think" that scheme members would support the decision to do so. But it went on to stipulate that it was inappropriate to pursue boycotts, divestment and sanctions "against foreign nations and UK defence industries", other than where formal government sanctions and the like were in place. The "summary of requirements" in the guidance stated that authorities "should not pursue policies that are contrary to UK foreign policy or UK defence policy".

The majority of the Supreme Court has now held that these passages in the guidance were unlawful. This was on the basis that the claimants' *Padfield* challenge succeeded – in other words, although the guidance may have fallen within the literal wording of the Public Service Pensions Act 2013 and the Regulations made under it, it was nonetheless made for a purpose falling outside those purposes for which the relevant powers could properly be exercised.

Lord Wilson (with whom Lady Hale agreed) put this primarily on the basis that a power to direct how the making of investment decisions should be *approached*, did not include power to direct *what* investments should or should not be made. He also characterised the relevant guidance as having been made "for entirely extraneous reasons", namely in "an attempt to enforce the government's foreign and defence policies", and suggested that this may have resulted from a misconception on the Secretary of State's part, relating:

> ". . . both to the functions of scheme administrators in relation to investment decisions and . . . to the identity of those to whom the funds should properly be regarded as belonging."

Specifically, Lord Wilson considered it inaccurate both to regard administering authorities as "part of the machinery of the state . . . discharging conventional local government functions", and to regard the scheme funds as "public money". Rather, they arose from the contributions of employees, and of employers as an element of employees' remuneration – so the fund "represents [the employees'] money", and administering authorities rightly regarded themselves as "quasi-trustees who should act in the best interests of their members".

Lord Carnwath held, similarly, that although guidance need not be limited to purely procedural or operational matters, it must respect "the primary authority of the statutory authorities as `quasi-trustees' of the fund". He upheld the claimants' submission that:

> "Whilst the Secretary of State was entitled to give guidance to authorities about how to formulate investment policies consistently with their wider fiduciary duties, he was not entitled . . . to make authorities give effect to [his] own policies in preference to those which they themselves thought it right to adopt in fulfilment of their fiduciary duties."

By contrast, the minority of the Court considered that the legislation *was* wide enough to permit guidance dealing with the extent to which non-financial considerations could be taken into account, and specifically that it permitted the Secretary of State to take into account "wider considerations of public interest" as perceived by him, so as to ensure that the right balance was struck "between the public interest and the interests of fund members", and to "delineate the functions of central government in relation to the fund". The minority accepted that scheme pensions were earned by its members, but considered that the public interest was also engaged by virtue of the relevant authority's duty to make good any deficiency in the fund.

The Supreme Court has effectively now endorsed the analysis contained in the Law Commission's report on *Fiduciary Duties of Investment Intermediaries* (Law Com No 350), and its applicability to LGPS administering authorities. Accordingly, with much attention currently being paid to the use of ESG (environment, social and governance) criteria in investing, authorities, pension scheme members and other stakeholders may well find themselves focusing in future upon the practical application of the Commission's two threshold criteria for taking account of non-financial factors – when can trustees and authorities conclude that there is good reason to think that scheme members would share the relevant concern, and when will taking account of such matters risk "significant financial detriment"? What is the role in this context of the public sector equality duty, to which the minority judgment briefly alludes?

More generally, both the majority and minority judgments provide further insight into the application of the *Padfield* doctrine, and indeed the division of judicial opinion which has characterised this litigation demonstrates that it will often not be easy to know exactly when and how wide statutory words should be regarded as subject to implicit limitations.